



FUTTERMAN DUPREE  
DODD CROLEY MAIER<sup>LLP</sup>

## Federal Equity Receiverships in Enforcement of Statutory and Constitutional Claims

*California Receivers Forum*

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Martin H. Dodd

Mr. Dodd has served as an equity receiver appointed by the federal courts in several securities fraud cases and has represented equity receivers in both the state and federal courts. Since 2006, he has represented the receiver for the California prison health care system, appointed by U.S. District Judge Thelton E. Henderson in *Plata v. Schwarzenegger*. In addition to his receivership practice, Mr. Dodd has 26 years of experience representing companies, government entities and individuals in commercial, employment, product liability and toxic tort cases in the state and federal trial and appellate courts. He has particular expertise in corporate and partnership dissolution, fiduciary litigation, public entity litigation and civil rights and employment disputes. Mr. Dodd is also a trained mediator and has mediated a wide range of disputes, including real estate, commercial, personal injury and employment matters.

Mr. Dodd was a founding partner of Futterman Dupree Dodd Croley Maier LLP. For many years, he was a partner in the San Francisco law firm of Marron Reid LLP. He began his legal career as an associate with Graham & James in San Francisco in 1982. Mr. Dodd received his B.A. (with Highest Honors) from the University of California, Santa Cruz in 1974, an M.A. from Harvard University in 1977 and his J.D. from the University of California, Berkeley (Boalt Hall) School of Law in 1982. He is a member of Order of the Coif.

**I. INTRODUCTION**

**II. CIRCUMSTANCES IN WHICH FEDERAL EQUITY RECEIVERS MAY BE APPOINTED**

**A. Pre-1950**

**B. Modern era**

1. Remediating statutory violations (e.g., offering fraud under Securities and Exchange Act)
2. Remediating constitutional violations in state and local institutions
  - a) Courts have whatever powers are necessary to remedy constitutional violations
  - b) But there are additional considerations where state and local authority implicated
    - (1) Courts must be mindful of interests of state and local officials in managing their own affairs
    - (2) The remedy must be the least possible adequate to the end proposed and no lesser alternatives are presented
    - (3) E.g., statutory limits: Prison Litigation Reform Act
3. Authority to appoint receiver
  - a) Generally
    - (1) Federal law governs appointment of receivers in federal court even in diversity actions
    - (2) Decision to appoint a receiver is within discretion of district court; may be based on one or more of a variety of factors, and no one factor is dispositive (See *Canada Life Assurance Co. v. LaPeter*, 557 F.3d 1103, 1110 (9th Cir. 2009)(listing factors)
  - b) Receivers in cases involving statutory violation
    - (1) Appointment of receivers to remedy statutory violation “derives from the inherent power of a court of equity”

to fashion effective relief" (*SEC v. Wenke*, 622 F.2d 1363 (9th Cir. 1980)) and is not dependent on a statutory grant of authority

- (2) Compare appointment in bank and S&L failures (FIRREA)
4. In constitutional cases, courts employ balancing test for appointment of receiver (See, e.g., *Plata v. Schwarzenegger*, 2005 U.S. Dist. LEXIS 43796, \*66-\*67 (N.D. Cal. 2005))
- a) Most important factors:
    - (1) Grave and immediate threat or actuality of harm to plaintiffs
    - (2) Use of less extreme measures of remediation have been exhausted or prove futile
  - b) Other factors that may be considered
    - (1) Whether continued insistence that compliance with prior orders would lead to confrontation and delay
    - (2) Whether there is a lack of leadership to turn the tide within a reasonable period of time
    - (3) Whether there is bad faith
    - (4) Whether resources are being wasted
    - (5) Whether a receiver is likely to provide a relatively quick and effective remedy

### III. SCOPE OF RECEIVER'S AUTHORITY

- A. **Consistent with broad scope of federal courts' remedial powers, orders governing receivers can be very broad**
- B. **The federal equity receiver does not merely "stand in the shoes" of the entity in receivership**
  1. Receiver is court's agent implementing equitable relief
    - a) E.g., *SEC v. American Capital Investments, Inc.*, 98 F.3d 1133 (9th Cir. 1996); *Gaskill v. Gordon*, 27 F.3d 248 (7th Cir. 1994)

- b) E.g., status of prison medical care receiver
- 2. Compare receiver appointed under FIRREA (E.g., *O'Melveny & Myers v. FDIC*, 512 U.S. 79 (1994))

#### **IV. SPECIAL RULES AND DEFENSES AVAILABLE TO FEDERAL EQUITY RECEIVERS**

##### **A. Administration of the estate**

- 1. 28 U.S.C. 754
  - a) Permits jurisdiction over property in other districts
  - b) Procedure for acquiring jurisdiction under Sections 754
  - c) 10-day rule and reappointment of receiver (See *SEC v. American Capital Investments, Inc.*, 98 F.3d 1133 (9th Cir. 1996); *SEC v. Vision Communications, Inc.*, 74 F.3d 287 (D.C. Cir. 1996); *Warfield v. Arpe*, 2007 U.S. Dist. LEXIS 12177 (N.D. Tex. 2007))
- 2. 28 U.S.C. 2001
  - a) Governs sales of real property in receiver's hands
  - b) Two-step process: appointment of appraisers and sale confirmation hearing
- 3. 28 U.S.C. 959(b)
- 4. Applicable rules
  - a) FRCP 66
  - b) Local court rules
    - (1) Northern District Civil L.R. 66-1 through 66-6
    - (2) Eastern District Civil L.R. 66-232

##### **B. Proceedings brought by the receiver**

- 1. Claims against third parties
  - a) Personal jurisdiction
    - (1) Provided there has been compliance with 28 U.S.C. §754, jurisdiction may be obtained via 28 U.S.C.

§1692 over persons in any district where receivership property is located (E.g., *Warfield v. Arpe*, 2007 U.S. Dist. LEXIS 12177, at \*31-\*34)

- (2) Other statutes may also provide for nationwide jurisdiction, e.g., 15 U.S.C. §§ 77v and 78aa (See, e.g., *SEC v. The Infinity Group, Co.*, 27 F. Supp. 2d 559 (E.D. Pa. 1998))

b) Subject matter jurisdiction

- (1) Claims, even if exclusively under state law, are ancillary to main action
- (2) No independent subject matter jurisdiction required (*SEC v. Wenke*, 783 F.2d 829, 837 n.9 (9th Cir. 1986); *Tcherepnin v. Franz*, 485 F.2d 1251, 1255-1256 (7th Cir. 1973); *Warfield v. Arpe*, 2007 U.S. Dist. LEXIS 12177, at \*18-\*20)

2. Summary proceedings

- a) Receiver may pursue recovery for the estate and litigate ownership of assets in summary proceedings so long as notice and opportunity to be heard are afforded to persons in possession of receivership property (*SEC v. Wenke*, 783 F.2d at 836-837; *SEC v. Universal Financial*, 760 F.2d 1034, 1037 (9th Cir. 1985))
- b) Formalities of plenary litigation not required
- c) Summary proceeding: "enables a receiver to consolidate all litigation concerning his receivership in a single district court and before a single district judge, and to avoid formalities that would slow down the resolution of disputes." *SEC v. Wenke*, 783 F.2d at 837 n. 9

3. Receiver remedial measures

- a) Remedies in fraud cases
  - (1) Constructive trusts
    - (a) Protects limited assets for defrauded investors from claims by creditors
    - (b) May provide protection against taxing authorities

(2) Disgorgement and “clawback” powers:

Receiver may seek disgorgement of receivership assets from third parties, even those not accused of wrongdoing, if the third parties have received ill-gotten gains and have no legitimate claim to the assets (E.g., *SEC v. The Infinity Group*, 27 F.Supp. 2d at 563)

(3) Distribution plans

b) Remedies in constitutional cases

(1) Generally

(2) Waivers of state law

**C. Special procedural and substantive defenses in claims against receivers**

1. Removal to federal court

a) 28 U.S.C. §1442(a)(1),(3)

b) See *Gay v. Ruff*, 292 U.S. 25 (1934) and *Ely Valley Mines, Inc. v. Hartford Acc. & Indem. Co.*, 644 F.2d 1310 (1981)

2. Subject matter jurisdiction: *Barton v. Barbour*, 104 U.S. 126 (1881)

a) *Barton* doctrine: permission of the appointing court must be obtained before a receiver may be sued in another court (E.g., *In re Crown Vantage*, 421 F.3d 963 (9th Cir. 2005); *Van Horn v. Hornbeak*, 2009 U.S. Dist. LEXIS 5701 (E.D. Cal. 2009); *Medical Devel. Internat'l v. CDCR*, 2008 U.S. Dist. LEXIS 108046 (E.D. Cal. 2008))

b) Compare 28 U.S.C. 959(a)

(1) Overruled *Barton* on its facts

(2) When does statute apply?

(a) Despite broad language, courts have severely restricted application

(b) E.g., *In re Estevez*, 165 Cal. App. 4th 1445, 83 Cal.Rptr.3d 479 (2008)

- (3) Limitation on enforcement of judgments against receivers entered in non-appointing court
  - c) Ninth Circuit test for whether permission to sue the receiver should be granted (*In re Crown Vantage*, 421 F.3d 963 (9th Cir. 2005); *In re Kashani*, 190 B.R. 875 (9th Cir. BAP 1995))
    - (1) Whether the acts or transactions relate to the carrying on of the business connected with the property of the estate.
    - (2) If approval from the appointing court appears necessary, do the claims pertain to actions of the receiver while administering the estate?
    - (3) Do the claims involve the individual acting within the scope of his or her authority under the statute or orders of the bankruptcy court, so that the receiver is entitled to quasi-judicial or derived judicial immunity?
    - (4) Are the proposed plaintiffs seeking to surcharge the receiver; that is, seeking a judgment against the receiver personally?
    - (5) Do the claims involve the receiver's breaching her fiduciary duty either through negligent or willful misconduct?
  - d) Courts retain equitable authority to enjoin or stay proceedings against receivers without regard to Section 959(a) (*SEC v. Wenke*, 622 F.2d 1363, 1369-1370 (9th Cir. 1980); *Diners Club, Inc. v. A.J. Bumb*, 421 F.2d 396, 399-401 (9th Cir. 1970))
3. Quasi-judicial immunity from suit
- a) Immunity, if applicable, is absolute
  - b) Applies to decisions made in exercise of receiver's discretion while carrying out duties ordered by the court
    - (1) Most clearly applies if court has authorized the actions by order
    - (2) Does not apply to wrongs committed outside the scope of court-ordered authority



- (3) E.g., *New Alaska Devel. Corp. v. Guetschow*, 869 F.2d 1298 (9th Cir. 1989)
- (4) Consider possible impact of *Antoine v. Byers & Anderson, Inc.*, 508 U.S. 429 (1993)
- c) Failure to allege lack of immunity renders claims subject to dismissal

4. Appeals from receivership-related orders

- a) Appeals from interlocutory orders permitted in limited circumstances under 28 U.S.C. §1292(a)(2)
- b) Turnover orders may not be appealable until conclusion of the action (*FTC v. Overseas Unlimited Agency, Inc.*, 873 F.2d 1233, 1235 (9th Cir. 1989); *SEC v. American Principal Holdings, Inc.*, 817 F.2d 1349, 1350 (9th Cir. 1987). Compare *Canada Life Assurance Co. v. LaPeter*, 557 F.3d at 1108-1109 (turnover order included within order appointing receiver immediately appealable under Section 1292(a)(2))