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Receivers: Immunity and Its Limits

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More is required than honesty; a receiver is a fiduciary, he undertakes to care for the property and manage it for creditors, to act with assiduity and with reasonable competence.

In re C.M. Piece Dyeing Co., 89 F.2d 37, 40 (2d Cir. 1937).

In 1991, a plenary session of the National Association of Insurance Commissioners added a new section to the Insurers Rehabilitation and Liquidation Model Act (the "Model Act"): Section 9, Immunity and Indemnity of the Receiver and Employees. Section 9 provides that insurance company receivers and their employees [2] are immune from suit and liability in both their personal and official capacities. The concept of immunity has its basis in a larger goal – the efficient administration of the receivership. As courts have long recognized, without immunity, receivers could become "a lightning rod for harassing litigation." *Kermit Constr. v. Banco Credito Y Ahorro Ponceno*, 547 F.2d 1, 3 (1st Cir. 1976). Such an environment could dissuade qualified candidates from serving as receivers:

To subject citizens serving as public officers to suit and trial in every instance in which their good faith but mistaken actions caused injury to another "would dampen the ardor of all but the most resolute, or the most irresponsible, in the unflinching discharge of their duties."

Elder v. Anderson, 23 Cal. Rptr. 48, 53 (Cal. Ct. App. 1962) (quoting *Gregoire v. Biddle*, 177 F.2d 579, 581 (2d Cir. 1949) (Learned Hand, J.)).

Subsection B of Section 9 of the Model Act sets out the parameters of the immunity afforded:

The receiver and his employees shall have official immunity and shall be immune from suit and liability, both personally and in their official capacities, for any claim for damage to or loss of property or personal injury or other civil liability caused by or resulting from any alleged act, error or omission of the receiver or any employee arising out of or by reason of their duties or employment; provided that nothing in this provision shall be construed to hold the receiver or any employee immune from suit and/or liability for any damage, loss, injury or liability caused by the intentional or willful and wanton misconduct of the receiver or any employee.

Many states have enacted, as part of their insurance insolvency statutes, Section 9 or a similar immunity or indemnity provision to protect receivers. [3] Even without, or prior to, such codification, courts have afforded protection for acts or omissions performed in the capacity as a receiver.

This protection for receivers – whether common law or statutory – is often invoked when the receiver files suit on behalf of the estate and a defendant lodges affirmative defenses or counterclaims that are directed at the receiver, not the estate. For example, in *Foster v. Rockwood Holding Co.*, 632 A.2d 335 (Pa. Commw. Ct. 1993), the Pennsylvania Insurance Commissioner, in her capacity as liquidator of Rockwood Insurance Company, brought suit against the former officers and directors of the insolvent insurer's holding company, seeking to recover more than $140 million in losses suffered by the insurer. The defendants' answers included several affirmative defenses directed at alleged actions or omissions of the Commissioner, such as failure to mitigate damages and negligence.

In analyzing the propriety of the district court's decision striking the affirmative defenses, the court drew a distinction between the affirmative defenses relating to the Insurance Commissioner's actions prior to her appointment as statutory receiver and those defenses relating to actions taken in the Commissioner's capacity as liquidator. As to the former, the Commissioner and Insurance Department were entitled to sovereign immunity by statute. *Id.* at 339 (citing 4 Pa. Cons. Stat. §§ 8521-8528). As to the latter, the *Foster* court determined that, as a liquidator, the Commissioner was entitled to immunity based on the purpose of Pennsylvania's insurance insolvency statute to protect the "public good" and the

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[2] Section 9 immunity does not extend to attorneys, accountants, auditors, and other professionals that the receiver retains as independent contractors.

[3] *See* Colo. Rev. Stat. Ann. § 10-3-514.5 (West 2004); Conn. Gen. Stat. Ann. § 38a-909 (West 2003); Fla. Stat. Ann. § 631.392 (West 2003); Ga. Code Ann. § 33-37-8.1 (2003); 215 Ill. Comp. Stat. Ann. 5/202 (West 2003); Ky. Rev. Stat. Ann. § 304.33-115 (2003); Md. Code Ann., Ins. § 9-205 (West 2004); Md. Code Ann., Cts. & Jud. Proc. § 5-410 (West 2004); Mo. Rev. Stat. §§ 375.650, 375.1166, 375.1182 (2004); Mont. Code Ann. §§ 33-2-1392, 33-2-1393 (2003); Nev. Rev. Stat. § 696B.565 (2004); N.C. Gen. Stat. § 58-30-71 (2003); Okla. Stat. tit. 36, § 1937 (2003); Or. Rev. Stat. §734.144 (2001); R.I. Gen. Laws § 27-14.3-9 (2003); Tex. Ins. Code Ann. § 21.28 (Vernon 2003); Utah Code Ann. § 31A-27-110 (2003); Wash. Rev. Code Ann. § 48.31.115 (West 2004); W. Va. Code § 33-10-39 (West 2003); Wis. Stat. Ann. § 645.08 (West 2003). Some states that do not have an immunity provision within their insurance insolvency code have a general statutory immunity for the discretionary acts of public employees. *See, e.g.*, Alaska Stat. § 21.06.165 (2003); Cal. Gov't Code § 820.2 (2004).

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statutory powers of the liquidator. *Id.* at 338. The court reasoned that the liquidator had the statutory "power to institute proceedings against [and recover damages from] the officers and directors of the insurer for any wrongdoing committed by those individuals which resulted in harm to the insurer" and that this power "should not be encumbered by an examination in court of the correctness of any specific act of the Insurance Commissioner in its receivership." *Id.* The court further found that forcing the liquidator to defend acts of regulatory conduct would frustrate the overall purpose of protecting the public and result in inefficiency and delay. *Id.* at 338-39. The court also noted that the "defendants should not be permitted to assert regulatory negligence to offset their own alleged culpability." *Id.* at 338.

The court analogized the propriety of this *de facto* immunity for the liquidator to the "no duty" rule that protects a bank receiver from an avalanche of suits:

The rule that there is no duty owed to the institution or wrongdoers by the FSLIC/Receiver is simply a means of expressing the broad public policy that the banking laws creating the FSLIC and prescribing its duties are directed to the public good, and that every separate act of the FSLIC as a receiver in collecting assets is not open to second guessing in actions to recover damages from wrongdoing directors and officers. If there is no wrongdoing by the officer or director, there can be no liability, but if wrongdoing is established, the officer or director should not be allowed to set up as a defense a claim that would permit the detailed examination of the FSLIC's action as receiver.

Id. at 337-38 (quoting *Fed. Sav. & Loan Ins. Corp. v. Burdette,* 718 F. Supp. 649, 664 (E.D. Tenn. 1989)). Thus, even absent explicit statutory immunity, the *Foster* court found that the purpose of the insolvency statute necessitated some level of immunity for the receiver for conduct in the course of the receivership.

A receiver taking over the affairs of an insolvent insurance company faces a monumental challenge. Without immunity from suits alleging that the receiver should answer personally for the good faith decisions and actions she takes in managing the estate, the efficient management of the estate could be jeopardized. Accordingly, courts and legislatures have recognized that receivers are entitled to at least some immunity, although they have placed certain limitations on the extent of the immunity afforded.

Limits on Immunity – Intentional or Wanton and Willful Misconduct

Immunity under Section 9 of the Model Act or under similar statutes is limited: a receiver and her employees have "no immunity for damages caused by intentional or wanton and willful misconduct." Based on this concept, courts will allow affirmative defenses and actions to be asserted against receivers where the requisite level of conduct is asserted. For example, a federal court denied the West Virginia insurance commissioner's motion to strike affirmative defenses that were directed to the commissioner's conduct as receiver and regulator because the defendant had alleged gross misconduct. *Clark v. Milam,* 152 F.R.D. 66 (S.D.W.V. 1993).

The *Clark* court rejected the commissioner's argument that affirmative defenses of comparative negligence, laches, waiver and estoppel, avoidable consequences, failure to mitigate, comparative assumption of risk, and unclean hands were "inconsistent with the doctrine of sovereign immunity." *Id.* at 71. Since the immunity provided by the West Virginia statute explicitly "does not reach 'acts or omissions which are malicious or grossly negligent,'" the court reasoned that the West Virginia Insurance Commissioner's qualified immunity is narrower than sovereign immunity. *Id.* [4] The court observed that "[a]lthough perhaps unlikely, it is theoretically possible Defendants could mount proof at trial establishing Plaintiff was malicious or grossly negligent in his activities as receiver." *Clark,* 152 F.R.D. at 71. Accordingly, the court allowed the affirmative defenses to stand. *Id.* However, because the court was troubled by the "shotgun approach" used by the defendants in selecting affirmative defenses, the court noted that it would consider sanctioning the defendants if it became clear the defendants had asserted any frivolous defenses. *Id.*

Similarly, the Missouri Supreme Court held "that the immunity provided to a deputy receiver for an insurance receivership…is conditioned upon actions taken in 'good faith' and it was error to dismiss a petition alleging the deputy receiver's actions were 'willful, wanton and malicious.'" *Avidan v. Transit Cas. Co.,* 20 S.W.3d 521, 522 (Mo. 2000) (en

[4] The statutory section in question is quite similar to Section 9 of the Model Act. The West Virginia statute reads:

No claim of any nature whatsoever that is directly related to the receivership of an insurer shall arise against, and no liability shall be imposed upon, the insurance commissioner…or any person or entity acting as receiver of an insurer, including surety, in rehabilitation, liquidation, or conservation as a result of a court order issued on or after the effective date of this article for any statement made or actions taken or not taken in the good faith exercise of their powers under law. However, this immunity shall not extend to acts or omissions which are malicious or grossly negligent. This qualified immunity extends to agents and employees of the receiver.

W. Va. Code § 33-10-39(a) (West 1990).

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banc). The statute at issue, Section 375.650.2, [5] provided two different immunities to the special deputy receiver. "First, he is allowed 'absolute judicial immunity.' Second, the statute also provides that the receiver 'be immune from any claim against [him] personally for any act or omission.' Both of these immunities, however, are conditioned upon his 'acting in good faith' in the performance of receivership functions." *Id.* at 525. At issue in *Avidan* were allegations by a former employee that the deputy receiver had acted in a willful, wanton, and malicious manner in violating the employee's civil rights under 42 U.S.C. § 1983. *Id.* at 525. The court held that it was error for the trial court to dismiss the plaintiff's civil rights claim because the plaintiff's allegations were not barred by statutory immunity – since such actions would exceed the good faith immunity provided by statute. *Id.*

Even where statutory immunity is granted to receivers, legislatures may restrict that immunity to cover only acts done in good faith or that are merely negligent as opposed to wanton and willful misconduct. This limitation ensures that incentives remain for receivers to act diligently and responsibly.

Limits on Immunity – Breach of Fiduciary Obligations

In a recent and lengthy opinion, the Missouri Court of Appeals held that a court overseeing the administration of a receivership of an insolvent insurance company has the power to surcharge a Special Deputy Receiver ("SDR") for breaching fiduciary obligations to the estate by overcharging for services. *McPherson v. U.S. Physicians Mut. Risk Retention Group,* 99 S.W.3d 462 (Mo. Ct. App. 2003).

In *McPherson,* the appellate court examined "the seeming tension between the statutory powers possessed by receivers to wind up insolvent insurance companies and the general supervisory powers of Missouri trial courts overseeing the administration of the receivership of these companies." *Id.* at 466. Specifically at issue was the supervisory court's order surcharging the special deputy receiver (the"SDR") for $771,752.95 in "damages" after an audit disclosed that the SDR had overcharged the receivership. *Id.* at 467. The *McPherson* court ultimately held that the trial judge should have recused himself, so the court reversed and remanded the case for trial before a different judge. However, the appellate court provided specific guidance for the new trial judge about the other issues raised in the appeal:

Several matters, however, need to be set out to aid the trial court in conducting the new trial; Judge Wells had the jurisdiction to order the audit [of the SDR's performance] which was presented for court approval; Wells had the authority to receive in evidence and accept the contents of the audit; in this insurance insolvency proceeding the trial court has jurisdiction to assess a reasonable surcharge against a special deputy receiver who has been afforded proper due process and discovery rights; Sauer, if she so chooses, may again present her claim for an increased hourly rate for unreimbursed time spent as SDR prior to April 29, 1999; the Receiver will not be allowed to recover the audit costs and the attorney's fees because of his admission during oral argument that the fees had not been requested, an admission that is binding under the law of the case.

Id. at 491.

The *McPherson* court held that the supervisory court had the power to impose a restitutionary surcharge, analogizing that power to "two inherent powers that courts definitely have. A court has the power to order a party who received money under a mistaken judgment to disgorge it…A court also has the inherent power to sanction bad faith litigation misconduct." *Id.* at 478. The appellate court reasoned that "disallowing a surcharge of the SDR would reduce the amount of recovery by creditors of USPM. Conversely, allowing a surcharge would signal to future receivers that they best pursue their responsibilities carefully and diligently." *Id.* at 480. Characterizing the overpayment as "unjustified fees," the court further reasoned that the surcharge was an appropriate method of obtaining restitution from the SDR for those fees, since the SDR's fiduciary duty to the estate obligated her to remit any overpayment. *Id.* at 480-81. *See also id.* at 484 ("As a fiduciary, [SDR] had a duty to exercise reasonable care, at a minimum.").

The SDR argued that the Missouri statutes "immunized her from liability for the acts and omissions upon which the

[5] Section 375.650.2 reads in full:

The receiver, special deputy receiver, commissioners and special masters appointed by the court, the agents and employees of the receivership and the commissioners and employees of the state of Missouri when acting with respect to the receivership shall enjoy absolute judicial immunity and be immune from any claim against them personally for any act or omission while acting in good faith in the performance of their functions and duties in connection with the receivership.

Mo. Rev. Stat. § 375.650. In Section 375.1182.5, the Missouri code also provides for immunity for acts or omissions in the performance of functions and duties in connection with a liquidation by the "director as liquidator" and for special deputies appointed by the director whose appointment is approved by the court. Section 375.1182.5 affords the same absolute judicial immunity as provided by Section 375.650.2, with the important difference that Section 375.650.2's "while acting in good faith" language does not appear in Section 375.1182.5. Section 375.650 applies to receivership proceedings initiated prior to August 8, 1991, while the broader immunity of Section 375.1182.5 applies to receivership proceedings initiated on or after that date. *Avidan,* 20 S.W.3d at 524-25 (interpreting Mo. Rev. Stat. § 375.1158.1).

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court based its surcharge because they were committed in the performance of her duties as liquidator of USPM." *Id.* at 482 (citing the aforementioned Missouri immunity statute for liquidators (*see* note 4, *supra*), Mo. Rev. Stat. § 375.1182.5). The court rejected this argument, stating,

[t]he purpose of the immunity statute is not to protect receivers (and, derivatively, SDRs) from court-imposed surcharges, but rather to prevent receivers (and SDRs) from becoming a lightning rod for harassing litigation. "[T]he receiver functions as an arm of the court by making decisions about the operation of a business that the judge otherwise would have to make." Immunity, then, is designed to ease compliance with judicial orders by barring third parties from hindering an agent of the court when the agent is complying with court orders, not when the agent evades the spirit of those very orders.

Id. at 482 (citations omitted). The *McPherson* court concluded that the SDR had "no immunity for acts beyond the scope of [her] authority." *Id.* at 483.

In sum, a receiver's fiduciary responsibilities to the estate are not obviated by the fact that the receiver has immunity for acts or omissions within the context of her responsibilities. Since failure to exercise reasonable care has the potential to damage third parties – in addition to damaging the estate – courts may conclude that statutory immunity does not apply to such acts or omissions.

Limits on Immunity – Acts Beyond Statutory Authority

Just as a receiver is not immune from suit based on breach of her fiduciary duty, a receiver is not immune from liability for acts taken outside the scope of a receiver's statutory duties. "The receiver functions as an arm of the court by making decisions about the operation of a business that the judge otherwise would have to make." *New Alaska Dev. Corp. v. Guetschow,* 869 F.2d 1298, 1303 n.6 (9th Cir. 1989). Accordingly, immunity serves to bar third parties from "hindering an agent of the court when the agent is complying with court orders, not when the agent evades the spirit of those very orders." *McPherson,* 99 S.W.2d at 482 (finding that there is no immunity for acts that are beyond the scope of the receiver's authority, such as acts that are not taken by a desire to further the interests of the insolvent insurer). The same reasoning applies when the receiver's acts go beyond the authority granted by statute – in other words, when the challenged action simply was not taken in the individual's capacity as a receiver.

For example, in *Executive Branch Ethics Commission v. Stephens,* the Kentucky Supreme Court examined whether a former insurance commissioner who subsequently served as deputy liquidator of a life insurance company estate was immune from an administrative action charging ethical violations in connection with his procurement of the appointment as deputy liquidator. 92 S.W.2d 69 (Ky. 2002). The court held that the relevant portion of the Kentucky insurance insolvency statute provides immunity "only to the liquidator or deputy liquidator because of any official actions they take regarding the liquidation proceedings …Immunity is not available to prevent an administrative agency from investigating that official for possible ethics violations." *Id.* at 74 (interpreting Ky. Rev. Stat. Ann. § 304.33-115). *See also Avidan,* 20 S.W.3d at 525 (reinstating a civil rights claim brought by former employee since allegations that deputy receiver acted in a willful, wanton, and malicious manner in violating the employee's civil rights, if proved, would not be a good faith execution of the deputy receiver's statutory duties).

Indemnification

Section 9 of the Model Act also provides that the receiver, if sued, will be indemnified out of the assets of the insurer for attorney's fees, expenses, settlements, and judgments. Any such payments are classified as an administrative expense and receive priority commensurate with that classification. Further, pursuant to Section 9, the "expenses incurred in defending a legal action for which immunity of indemnity is available" are to be paid "as they are incurred." If it is subsequently determined that the act, error or omission causing the damage did not arise out of or by reason of the receiver's duties or employment, or that the receiver's misconduct was intentional or willful and wanton, indemnification is not available. Accordingly, the Model Act states that in such case the indemnified receiver or employee is to repay the funds expended on his or her behalf.

Conclusion

Although rehabilitators and receivers have broad immunity for actions taken in performance of their official duties, there are limits to that immunity. A receiver is not immune from suit or liability for intentional or wanton and willful misconduct, nor is a receiver immune from liability for damages caused by the receiver's breach of her fiduciary duties to the estate. Further, the statutory immunity provided for receivers does not extend to acts that are outside the receiver's duties as a receiver. However, where a receiver is the target of a claim concerning acts taken on behalf of the estate, and done within her discretion as receiver, the costs of defense are generally paid out of the assets of the estate.

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