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Client Interview – Best Practices

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Michael Catrett

This presentation is dedicated to Michael Catrett.

Michael was suppose to be here with us today providing us all with his wealth of knowledge. He contributed to this project up until his untimely passing. Our condolences go out to his family and friends. The bankruptcy community will truly miss him.

Purpose of the Client Interview and Verifying the Client's Information

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To start a restaurant business, the Debtors obtained a line of credit for \$250,000. The Debtors operated the restaurant on leased premises. Ten years later, the restaurant was booming. Debtors obtained another loan for \$200,000 to purchase a vacant commercial lot to eventually build a strip center and relocate the restaurant, which was eventually paid in full. Debtors also obtained a \$400,000 construction loan to build their dream home. Debtors' home is completed and is worth \$900,000.

Purpose of the client interview and Verifying the client's information

The restaurant kept doing well until Hurricane Ike struck Houston and dealt a devastating blow to the business. As a result, revenues dropped drastically and Debtors could no longer service the line of credit and Debtors had to close the business. Wife now has a job earning \$50,000 per year and husband is unemployed. Bank sued Debtors on the line of credit and was granted a default judgment for \$150,000 a year ago, but has not commenced collection proceedings. Debtors also have \$100,000 of unsecured debt. They wish to keep their home and the vacant lot, which is now worth \$500,000. The Debtors also have a pending insurance claim for damage on their home.

Purpose of the client interview and Verifying the client's information

1. According to these facts, what additional questions should be asked?
2. How should you verify the information provided by the prospective client?
3. Should the Debtors file for bankruptcy protection? Chapter 7 or Chapter 13?
4. If the vacant lot is contiguous to their home, would this fact change your recommendation?
5. What should you advise the Debtors as to the insurance claim?

Purpose of the client interview and Verifying the client's information

Let's assume the Debtors, concerned about the judgment creditor, sell the vacant lot and use the sales proceeds to pay-off the loan on their homestead.

1. Should they file for bankruptcy?



Pitfalls to Watch-Out For

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Pitfalls to Watch-Out For

Six months ago, Ms. Davis, an elderly women, became a widow. She has been receiving calls from collection agencies that according to her have been “ugly” to her. One night unable to fall asleep due to her medicine, she watches an infomercial claiming that bankruptcy will stop these people from calling her. She Googles bankruptcy and schedules an appointment with Alice, the attorney.

Ms. Davis shows up with her personal assistant to her initial consultation with Alice the attorney. Ms. Davis is a shareholder of her deceased husband’s corporation, ABC Corp. Although not ever involved in the operations of ABC, she is fully aware of the operations of the corporation and wants to take control of the business and defend vigorously pending litigation. For convenience and due to her physical condition, she wants an attorney that will represent both her and ABC Corp. At the same time, she wants to liquidate assets to pay her creditors. She has a hard time hearing and takes medications, primarily painkillers. Her assistant helps her carry her bag of prescriptions and helps her move around. Ms. Davis says her only equity interest in any business is that in ABC Corp. Before the consultation, Penny the paralegal pulls a Texas Secretary of State report listing Ms. Davis as a shareholder in other active corporations. All corporations have been profitable and own unencumbered assets.

Pitfalls to Watch-Out For

1. Should the personal assistant be allowed in the conference room with Ms. Davis?
2. Is Ms. Davis competent to consult with Alice the attorney? Would her medications impair her judgment and ability to comprehend?
3. Should Alice the attorney represent both Ms. Davis and ABC Corp?
4. In light of the circumstances and as part of due diligence, should Alice the attorney run additional public reports on Ms. Davis and the affiliated entities?
5. How do you determine Ms. Davis' goals?
6. If Ms. Davis files for bankruptcy, should she list her shareholder interests in ABC Corp. and the other corporations? Are these interests generally capable of being claimed as exempt?

Pitfalls to Watch-Out For

During a follow-up consultation, Alice the attorney finds more wrinkles in Ms. Davis' case:

Through a warranty deed, Ms. Davis' mother transferred property to her. She expressly instructed Ms. Davis to hold the property and transfer it once her sons were of majority. Three years ago, Ms. Davis transferred the property from herself to one of the companies. She subsequently pledged the property as collateral for a loan. The company failed and the collateral was foreclosed upon. Because of this foreclosure transaction, one of her sons has refused to speak with her since last family reunion. Ms. Davis secretly keeps up with him on Facebook.

1. What should you warn Ms. Davis about?



Pitfalls to Watch-Out For

For years her husband paid most of the household bills out of one of the companies' bank accounts – mortgage, utilities, and vehicle payments. Ms. Davis continues to do so without reporting it on her taxes.

1. What should you recommend to Ms. Davis?
2. Are there any concerns with priority claims?
3. Do these accounting practices give the companies' creditors any basis to assert any claims against Ms. Davis' bankruptcy estate?

Pitfalls to Watch-Out For

Ms. Davis' other son has been in and out of rehab several times. Out of concern for his wellbeing after she passes, she set up a spendthrift trust for his benefit. The trust documents list no assets as the initial corpus of the trust. Ms. Davis states that the trust now has \$3M which she has transferred into it.

1. What should you warn Ms. Davis about?
2. Should she file for bankruptcy?

Pre-Bankruptcy Planning

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Pre-Bankruptcy Planning

Mr. and Mrs. Jones have been sued by a creditor and have decided to seek advice about filing for bankruptcy. They are internet savvy and have done research on their own before coming into your office. At the consultation, Mr. and Mrs. Jones tell you they know that they want to file a Chapter 7 and they are willing to do whatever it takes to qualify. Upon review of their income, expenses, and assets; you indicate that they may not “pass” the means test. Additionally they only owe about \$20K on their home and it is worth \$120K. They have \$20K in the bank and another \$5K in Canadian dollars in a safe deposit box that they keep “just in case.” Mr. Jones explains that he is an AC repairman and since it is summer he works a lot of overtime but barely gets 40 hours during the winter. He also indicates that he has a car that is about 7 years old which needs replacing. He also explains that he knows a car payment may make a difference in his qualifications for chapter 7 (remember – he likes the internet).



Pre-Bankruptcy Planning

1. Should you advise Mr. and Mrs. Jones to finance a new car before filing?
2. Should you advise Mr. and Mrs. Jones to wait to file until his summer pay has “fallen-off” of the 6 month means test window?
3. Should you advise Mr. and Mrs. Jones to spend down the \$20K in the bank?
4. Should you advise Mr. and Mrs. Jones to pay-off their homestead with their non-exempt cash before filing?
5. Should you advise Mr. and Mrs. Jones to purchase a new vehicle with their non-exempt cash because the car will be exempt property under Texas law?
6. Should you advise Mr. and Mrs. Jones to take the Canadian Dollars and give them to charity?

Pre-Bankruptcy Planning

Additionally, Mrs. Jones has a partnership with Mr. Garcia, ABC Cell Phone. The partnership has not been profitable. Mrs. Jones personally guaranteed all partnerships debts. The partnership's assets consist of cell phone inventory, fixtures, a computer, and a register. Mrs. Jones' cousin is the sole member in XYZ Cell Phone, LLC, which is not currently operating. He opened it at the urging of Mrs. Jones who promised to "partner-up" with him and help him with its future cell phone retail operations. Mrs. Jones would like to personally guarantee a lease for XYZ Cell Phone before her credit reflects a bankruptcy. She would also like to sell the assets of ABC to XYZ before the filing of the Chapter 7 and split the income with Mr. Garcia because neither of them have been able to pay themselves for several months.

Pre-Bankruptcy Planning

1. Should you advise Mrs. Jones to personally guarantee the lease for XYZ before she files for Chapter 7?
2. Should you advise Mrs. Jones to sell the assets of ABC to her cousin and pay herself and Mr. Garcia with the proceeds as back wages before filing the Chapter 7 for ABC?
3. Should the partnership file for bankruptcy?
4. Should you represent the Joneses and the partnership?

Preparation of Management, Key Employees, and Exit Strategy

The newly minted CEO of Braco, Inc, a company that manufactures baby products, comes in to discuss a potential bankruptcy filing. The company and the former CEO mutually agreed to part ways after the company recalled a stroller that caused the death in hundreds of infants and the former CEO's missteps in connection with the recall negatively impacted their image with the public and press. The company is now a defendant in at least a dozen lawsuits in several different states. The public backlash has resulted in a drastic decrease in sales. As a result, the company is unable to meet their obligations to the secured lenders, who have not yet sent a demand letter and notice of default. However, the lead bank for the syndicate indicated that such a notice was coming if an accommodation was not worked out in the next seven to ten days. At least three of the company's key vendors have asked for a meeting to discuss invoices that are over 45 days past due. An aggressive credit manager for Baby Bratz, a vendor that regularly files involuntary bankruptcy petitions against account debtors, threatened to coordinate with at least two other vendors in forcing the Company into bankruptcy if Baby Bratz was not paid first, even before payroll, taxes, and the secured creditors. Baby Bratz is owed approximately \$115,000.

Preparation of Management, Key Employees, and Exit Strategy

The current CEO has also learned that the company was behind in withholding taxes. The current CEO has been in the position for only 6 months and knows little or nothing about the company. Since she joined the company, the CFO and the Controller have also left. Consequently, the current management team does not have a lot of knowledge or background about the company. The CEO indicated she would like a release in any plan of reorganization for herself and her management team. Notwithstanding the negative publicity the company suffered lately, the CEO is confident that the company's image could be resuscitated and there is significant value in intellectual property in the company. Further, a friend of hers who is a successful turnaround specialist recommended to her, for free, that she consider abandoning certain lines of products, especially the ones that causes injuries, in exchange lower risk products that are very high demand that can be manufactured with slight modifications to existing equipment.

Preparation of Management, Key Employees, and Exit Strategy

1. Does the company need to file bankruptcy?
2. Should the company pay off Baby Bratz first? In this connection, you learned that Baby Bratz enjoys chairing creditors' committees.
3. What can the company accomplish with a bankruptcy filing?
4. Should the company consider hiring the turnaround specialist? Is there any PR advantage to doing so? Is that something to suggest to the banks in negotiations?
5. Should the company file Chapter 7 or Chapter 11?

Preparation of Management, Key Employees, and Exit Strategy

Business Preparation: CEO has decided to file, but is not sure how much cash is needed. You explain that cash is necessary and she is now asking how to accumulate cash given the Company's financial predicament.

1. How important is cash?
2. Can the company stock pile cash in preparation of filing? If so, how does it do so?
3. Does that the company need to contact their lenders before filing?

Preparation of Management, Key Employees, and Exit Strategy

Legal Preparation: CEO is concerned about how to pay for the attorney fees in connection with the bankruptcy. She is requesting a budget and a guarantee of the length of time in the case.

1. What kind of fees will be involved?
2. How much control does the firm have over fees?
3. How much control does the firm have over the length of the case?
4. What other professionals would the company need to engage besides attorneys?