35th Annual Jay L. Westbrook Bankruptcy Conference

Austin, Texas

November 17–18, 2016

Pre-Bankruptcy Planning: Pigs, Hogs and Great Ideas That Weren't

My Grandmother's rule—"Say it out loud first and if you want to slap yourself, it ain't a great idea"—as lawyers we should know when to slap ourselves. Discuss the strange tales and law applicable to the prickly field of pre-bankruptcy planning, including a lawyer's duties and how to keep your head.

Presenter:

Louis M. Phillips

KELLY HART PITRE
301 MAIN STREET, SUITE 1600
BATON ROUGE, LA 70801

Written Materials Prepared By:

Amelia L. Bueche
Louis M. Phillips

KELLY HART PITRE
301 MAIN STREET, SUITE 1600
BATON ROUGE, LA 70801

CONSUMER

Generally, pre-bankruptcy planning refers to the process whereby a debtor facing significant claims protects his or its assets. Ethical rules require attorneys to seek the lawful objectives of their client through reasonably available means permitted by law. Bankruptcy planning can be legitimately used to deter litigation by reducing the size of the client's assets; providing incentives for a creditor to seek an early and cheap settlement; and protecting and preserving assets. But while some degree of bankruptcy planning is acceptable—and perhaps required—"there is a principal of too much."[1] As summed up by one court, when a pig becomes a hog it is slaughtered; and the bankruptcy court has the primary duty to distinguish hogs from pigs.[2]

Distinguishing legitimate pre-bankruptcy planning from abusive pre-bankruptcy planning is a necessarily fact intensive inquiry. While there are common means available inside and out of bankruptcy to attack these transactions, whether the transactions will be unwound or the debtor or attorney punished almost always depends on the debtor's motive for the pre-bankruptcy planning transaction.

I. NON BANKRUPTCY & BANKRUPTCY ACTIONS AVAILABLE TO ATTACK HOG-ISH PRE-BANKRUPTCY PLANNING

Attorneys advising clients on pre-bankruptcy planning means should be cognizant that these transfers can be attacked outside of bankruptcy and in bankruptcy. Generally, whether the pre-bankruptcy planning strategy withstands legal scrutiny depends on whether the court determines that the strategy was executed with fraudulent intent. A successful attack could unwind the transaction, punish the debtor, and/or penalize the attorney. Therefore, it is important to anticipate challenges to pre-bankruptcy planning.

---

1 *Matter of Swift*, 3 F.3d 929, 931 (5th Cir. 1993)(citing *In re Zouhar*, 10 B.R. 154, 157 (Bankr. D.N.M. 1981)).

2 *Id*.

A. Outside of Bankruptcy

Asset protection or pre-bankruptcy planning can be attacked even if the client never files for bankruptcy through fraudulent transfer statutes. Texas has adopted the Texas Uniform Fraudulent Transfer Act (TUFTA). It provides that:

> (a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or within a reasonable time after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:
>
> (1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or
>
> (2) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
>
> (A) was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
>
> (B) intended to incur, or believed or reasonably should have believed that the debtor would incur, debts beyond the debtor's ability to pay as they became due.[3]

Generally, a four-year statute of limitations applies to fraudulent transfer claims in Texas, but this is subject to discovery rules.[4] That means if a doctor transfers large sums of money to trusts of his children, someone bringing a malpractice claim against the doctor would have four years to file a fraudulent transfer action to unwind the gift, unless the gift was not disclosed in which case the claimant would have an additional year after the gift was reasonably discoverable.

Texas's statute sets forth several non-exclusive statutory "badges of fraud" that courts examines to determine if the debtor had the requisite actual intent to defraud. Specifically, § 24.005(b) of TUFTA provides that consideration may be given, among other factors, to whether (A) the transfer was to an insider; (B) the debtor retained possession or control of the property transferred after the transfer; (C) the transfer was concealed; (D) before the transfer was made, the debtor had been sued or threatened with suit; (E) the transfer was of substantially all the debtor's assets; (F) the debtor absconded; (G) the debtor removed or concealed assets; (H) the value of the consideration received by the debtor was

3 Tex. Bus. & Com. Code Ann. § 24.005 (Vernon 2006).

4 Tex. Bus. & Com. Code Ann. § 24.010 (Vernon 2006).

Title search: Pre-Bankruptcy Planning: Pigs, Hogs and Great Ideas That Weren't