

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH CAROLINA

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MAY 24 1999
BRENDA K. ARGOE, CLERK
United States Bankruptcy Court
Columbia, South Carolina (6)

IN RE:

Southern Textile Knitters, Inc.,

Debtor.

Robert F. Anderson, Trustee,

Plaintiff,

v.

Samuel H. Simchon, Levy Simchon, Rebecca
Simchon, Oded Simchon, Renee Simchon,
Southern Textile Knitters of Greenwood, Inc.,
STK de Honduras Sewing, Inc., Excel Dyeing
and Finishing, Inc., Center Point
Construction, Inc., and Old Fort Industrial
Park, LLC,

Defendants.

C/A No. 98-07203-W

Adv. Pro. No. 99-80026-W

JUDGMENT

Chapter 7

ENTERED
MAY 24 1999
K.K.M.

Based upon the Findings of Fact and Conclusions of Law as recited in the attached Order of the Court, the Plaintiff's Motion for Partial Summary Judgment is granted in part to the Third Counterclaim and denied in part. The First and Second Counterclaims asserted by the Defendants in their capacities as shareholders, officers or directors of the Debtor corporation are hereby severed and stayed subject to further Order pending the determination of the other claims and issues in this adversary proceeding.


UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina,
May 24, 1999.

CERTIFICATE OF MAILING

The undersigned Deputy Clerk of the United States
Bankruptcy Court for the District of South Carolina hereby certifies
that a copy of the document on which this certificate appears
was mailed on the date listed below to:

MAY 24 1999

Griffin
Gleason
Cauthen

DEBTOR, DEBTOR'S ATTORNEY, TRUSTEE 5 CCS to JW

KELLEY MORGAN

Deputy Clerk

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Southern Textile Knitters of Greenwood, Inc.,
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and Finishing, Inc., Center Point
Construction, Inc., and Old Fort Industrial
Park, LLC,

Defendants.

ORDER

Chapter 7

ENTERED
MAY 24 1999
K.K.M.

THIS MATTER comes before the Court upon the Motion for Partial Summary Judgment filed by the Plaintiff Robert F. Anderson, the Chapter 7 Trustee ("Trustee") in regards to the Counterclaims asserted by the Defendants against him in his capacity as Trustee. Based upon the pleadings submitted by the parties including the Motion for Partial Summary Judgment, the Objection to the Motion for Partial Summary Judgment, the accompanying affidavits and the arguments of counsel, the Court makes the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

On January 26, 1999, the Trustee filed this adversary proceeding alleging the following

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causes of action: (a) turnover under 11 U.S.C. §542,¹ (b) preferential transfer under §547, (c) fraudulent transfer under §548, (d) post-petition transfer outside the ordinary course of business under §549, (e) breach of fiduciary duty, (f) piercing of the corporate veil of the Debtor Southern Textile Knitters, Inc. (“STK” or “Debtor”), (g) aiding and abetting, (h) common law conversion, (i) fraudulent transfer under South Carolina Statutory Law, (j) civil conspiracy, (k) subordination of claims under §510, and (l) an accounting.

The Defendants filed Answers to the Complaint as well as Counterclaims against the Trustee alleging (a) the negligent handling and loss of an asset of the estate, specifically an insurance claim, (b) the negligent and unjustified delay by the Trustee in distributing the proceeds of the sale of collateral to SouthTrust Bank N.A. (“SouthTrust”), and (c) the Trustee’s intentional interference in the contractual relationship between Samuel H. Simchon and Amplicon Financial, Inc. (“Amplicon”) alleging that the Trustee continues to seek to enforce a Settlement Agreement against Amplicon and Samuel H. Simchon even though the Settlement Agreement between Amplicon and STK has been deemed rejected pursuant to § 365.

The Trustee filed the within Motion for Partial Summary Judgment taking the position that (1) he enjoys judicial immunity because his actions were pursuant to Orders of the Court, (2) his Complaint was filed in his official capacity and he should not be sued in his individual capacity in this adversary proceeding, (3) the automatic stay applies to prohibit the Counterclaims and (4) that the Defendant shareholders do not have standing to assert these Counterclaims. The Defendants filed an objection to the Motion primarily asserting that the

¹ Further references to the Bankruptcy Code, 11 U.S.C. § 101 *et seq.*, shall be by section number only.

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Motion was premature at this time as the parties had not had a full and fair opportunity to conduct discovery. At the time of the hearing, the Defendants were waiting for the Trustee's response to their initial discovery requests, which deadline had been extended by agreement of the parties. Additionally, at the time of the hearing, the deposition of the Trustee and the Trustee's accountant were scheduled for the following week.

CONCLUSIONS OF LAW

The Trustee seeks dismissal of the Counterclaims initially because they seek personal liability against the Trustee and are not brought against him in his official representative capacity, the capacity in which he initiated the Complaint.² However, at the hearing on the Motion for Partial Summary Judgment, counsel for the Defendants stipulated that all of the Counterclaims were being asserted against the Plaintiff in his official capacity as the Chapter 7 Trustee. Therefore, based upon this stipulation, the Trustee's Motion on these grounds is resolved by separate Order. Additionally, at the hearing, counsel for the Defendants agreed that the Counterclaims would not to seek recovery from assets of the bankruptcy estate. This stipulation appears to have resolved the Trustee's Motion based upon the violation of the automatic stay and is also addressed in a separate Order. With the parties' agreement, the remaining grounds for the Motion for Partial Summary Judgment are whether the Trustee's actions are protected by judicial immunity in so far as they were based on Orders of this Court and whether the Defendants as shareholders of the Debtor lack standing to raise these Counterclaims. Considering the

² Paragraph 56 of the First Amended Answer and Counterclaim states in part that "[t]he Trustee should be held personally liable for his negligent actions without court authorization", Paragraph 57 states in part that "[t]he Trustee should be held personally liable", and Paragraph 95 states in part that ". . . the Trustee should be held personally liable for the damages caused by the intentional, grossly negligent, willful and negligent actions."



arguments and based largely on the fact that discovery in this adversary proceeding is not complete, the Court must deny the Trustee's Motion in part and grant the Motion in part.

Initially, while a Chapter 7 Trustee may enjoy certain immunities while acting within the scope of his official duties, that immunity is lost when a Trustee acts outside the scope of his official duties in the absence of jurisdiction. "The immunity of the trustee is not absolute . . . , if a trustee is acting under the direct orders of the court, there is immunity. In the absence of an explicit court order, however, a factual issue may arise regarding whether the trustee has acted within her authority." Yadkin Valley Bank & Trust Co. v. McGee, 819 F.2d 74, 76 (4th Cir. 1987).

Plaintiff argues that as trustee, he has "quasi-judicial immunity from damages." Mullis v. United States Bankruptcy Court, District of Nevada, 828 F.2d 1385, 1390 (9th Cir.1987) appeal dismissed, cert. denied, Mullis v. United States Bankruptcy Court, 486 U.S. 1040, 108 S.Ct. 2031, 100 L.Ed.2d 616 (1988). However, a trustee "loses his immunity if he acts in the clear absence of all jurisdiction." *Id.*

In re American Fabricators, Inc., 186 B.R. 526 (Bkrcty.M.D.Fl. 1995).

There is no explicit court Order in this case which addresses the subject matter of the First Counterclaim which alleges a failure to pursue an insurance claim as an asset for the estate nor is there an explicit Order under which the Trustee could assert judicial immunity to preclude an allegation of contractual interference which is alleged in the Third Counterclaim. The Second Counterclaim alleges a failure to contact potential buyers for estate assets and a failure to timely distribute proceeds of sale to a lienholder. While the Trustee was authorized to sell assets by an Order entered October 15, 1998 and to pay SouthTrust Bank, N.A. ("SouthTrust") by Consent Order entered February 5, 1999, the Court is reluctant to conclude at this time before the



Defendants have a full opportunity for discovery that the Trustee is immune from allegations of negligence based on a delay in distribution. For these reasons, the Motion for Partial Summary Judgment on these grounds must be denied; however, as discovery develops in this case and if circumstances warrant, the Motion can be refiled.

Additionally, the Court is reluctant to dismiss in full the Counterclaims at this time based upon the Trustee's argument that the Defendants lack standing. At least two of the Defendants asserting the Counterclaims, Levy Simchon and Rebecca Simchon, have filed proofs of claims against the estate as unsecured creditors and may have standing in that capacity to assert claims against the Trustee. Additionally, it appears from a review of the pleadings that at least one of the Defendants, Samuel H. Simchon, is asserting damages against the Trustee arising from his contingent liability as a guarantor of the Debtors' obligations. The Court is aware of at least one other Court from within the Fourth Circuit that has found that a Chapter 7 trustee owes a fiduciary responsibility to a guarantor.

The Court is unaware of any case that explicitly states that a Chapter 7 trustee owes a guarantor of the debtor's obligations any fiduciary responsibility; however by examining the Code and a related case it appears clear that a fiduciary duty does exist. The trustee does admit that he owes a fiduciary duty to creditors of the estate. See Memorandum in Support of Motion to Dismiss and Motion for Summary Judgment p. 10 (citing In re 2001 Cincinnati, Inc. VIP Clubs etc., 43 B.R. 6, 7 (Bankr.S.D.Ohio 1984)). The Code defines a "creditor" as being "an entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor". 11 U.S.C. § 101(10)(A). A "claim" is defined as being a "right to payment, whether or not such right is reduced to judgment, liquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured;". 11 U.S.C. § 101(5)(A). Even though Walker appears not to have been called upon to honor his guaranty, the generous definition of a "claim" allows contingent or unmatured liabilities to

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be considered claims. Accordingly, a guarantor who has not been called upon to honor his guaranty, may nevertheless still file a claim.

In re Southern International Company, L.P., 165 B.R. 815 (Bkrctcy. E.D.Va. 1994). Furthermore this Court has previously recognized the standing of a guarantor to object to the sale of property by a Chapter 7 Trustee and thus recognized that a guarantor may have a sufficient pecuniary interest under the standards of Willemain v. Kivitz, 764 F.2d 1019 (4th Cir. 1985). In re Indigo Fields, Inc., Case No. 90-00764-B (Bkrctcy. D.S.C. 2/12/92).

Finally, the Defendants may have standing to pursue the First and Second Counterclaims against the Trustee as shareholders of the Debtor. The general rule in the Fourth Circuit is that a Chapter 7 debtor only has standing if it can be demonstrated that he has a pecuniary interest in the distribution of his assets among his creditors.

The district court correctly determined that Willemain lacks standing to prosecute this appeal. In the analogous setting of whether an insolvent debtor may object to the allowance of claims against the estate, the leading and authoritative bankruptcy treatise as well as numerous tribunals have held that an insolvent debtor is not a party in interest and thus lacks standing because he has no pecuniary interest in the distribution of his assets among his creditors. See 3 J. Moore & L. King, Collier on Bankruptcy ¶ 57.17[2.1], pp. 275-277 (14th ed. 1977); 3 L. King, Collier on Bankruptcy ¶ 502.01[2] (15th ed. 1985). The Eighth Circuit succinctly stated the general rule:

Thus, since the bankrupt is normally insolvent, he is considered to have no interest in how his assets are distributed among his creditors and is held not to be a party in interest. [citations omitted] However, when it appears that, if the contested claims are disallowed, there may be a surplus of assets to be returned to the bankrupt, the bankrupt is considered to have standing to contest the claims.

Kapp v. Naturelle, Inc., 611 F.2d 703, 706-707 (8th Cir.1979). See also In Re Woodmar Realty Co., 241 F.2d 768, 770-771 (7th



Cir.1957); In Re Silverman, 10 B.R. 734, 735 (Bankr.S.D.N.Y.1981), aff'd, 37 B.R. 200, 201 (S.D.N.Y.1982); In Re Roberts, 20 B.R. 914, 916-917 (Bankr.E.D.N.Y.1982); In Re Lapointe, 39 B.R. 80 (Bankr.W.D.Ky.1984).

Applying the above principles to the setting before us, that is, whether an insolvent Chapter 7 debtor has standing to challenge the proposed sale of his primary asset, it becomes apparent Willemain lacks a pecuniary interest in this litigation.

Willemain v. Kivitz, 764 F.2d 1019 (4th Cir. 1985). This Court has recognized and applied that requirement of a pecuniary interest to establish standing in regards to a Chapter 7 debtor's objection to sale of property, In re Indigo Fields, *supra*, and in regards to a Chapter 7 debtor's objection to claims, In re Payne, 95-08343-W, (Bkrcty. D.S.C. 6/6/96) and In re Byrd, 89-03822-B, (Bkrcty. D.S.C. 1/15/92).

In opposition to the Motion, the Defendants assert that the Fourth Circuit, in In re Hutchinson, 5 F.3d 750, at 754 (4th Cir. 1993), has stated that a Trustee's fiduciary duties under § 704(1) extend to all "interested parties". This argument implies that "interested parties" is a broader group than the term "parties in interest" used in the statute and a group which includes shareholders of a debtor corporation. The Court disagrees. Upon consideration of the full opinion in Hutchinson, the Court concludes that the Fourth Circuit Court of Appeals did not intend to broaden the statutory language of § 704 but intended to use "interested parties" and "parties in interest" interchangeably.³

The question now before the Court is whether the Defendants as shareholders of the Chapter 7 Debtor corporation have a direct pecuniary interest in the distribution of assets to the

³ It has frequently been noted that the term "parties in interest" is not defined in the Bankruptcy Code. This led many courts, including the Fourth Circuit, to develop the pecuniary interest standard in order to determine whether there is party in interest standing.



creditors so as to provide them with standing to assert the breach of fiduciary duty claim against the Trustee alleged in the First and Second Counterclaims.

Initially, there has been no showing or even contention by the Defendant shareholders that absent the actions of the Trustee, which are the subject of their Counterclaims, there would be a surplus in the estate which would allow distribution to all creditors, payment of all administrative costs, and still provide a distribution to the Debtor. The Debtor, as a corporation, has no right to exemptions in property of the estate. Therefore, under the Willemain standard, the Debtor itself does not have a pecuniary interest to allow it standing to object to actions of the Trustee in administering the estate. Secondly, even if the Debtor had standing, the Defendant shareholders, even if they hold 100% ownership of the Debtor, are not the alter ego of the Debtor, so as to establish their standing on the Counterclaims. In re Manshul Construction Corp., 223 B.R. 428 (Bkrcty. S.D.N.Y., 1998). Also see: In re F.A. Delleastochastic, Inc., 121 B.R. 487 (Bkrcty. E.D.Va. 1990) (Chapter 7 corporate debtor did not have standing to seek order allocating payments to IRS first to trust fund liability, but which recognized that real parties in interest were debtor's responsible persons who would otherwise be personally liable for trust fund taxes); In re I & F Corporation, 219 B.R. 483 (Bkrcty. S.D. Ohio 1998) (Chapter 7 corporate debtor did not have standing to object to claims because estate was not solvent and debtor neither asserted any right to distribution nor contested its lack of pecuniary interest in case); In re Drost, 228 B.R. 208 (Bkrcty. N.D. Indiana, 1998) (Chapter 7 debtor did not have standing to object to abandonment unless estate is solvent or there is reasonable possibility that debtor would receive a distribution of any surplus); In re Martin, 201 B.R. 338 (Bkrcty. N.D.N.Y., 1996) (Chapter 7 debtor did not have standing to file an action against the Chapter 7 trustee for breach of fiduciary

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duty and other wrongs if prospect of surplus and distribution to debtor was speculative and debtor's actions were to impede administration of the estate).

In his Motion, the Trustee relies solely upon the holding in In re Slack, 164 B.R. 19 (Bkrcty. N.D.N.Y. 1994). In that case, the Court granted summary judgment for the trustee due to the Chapter 7 debtor's lack of standing to sue the trustee for alleged negligence in failing to obtain insurance on the only assets of the estate. These assets were subsequently destroyed by fire, leaving no payment to the nondischargeable tax claims in the case. The Court held that the debtor failed to establish that if the assets had been insured, assets would have exceeded liabilities so as to provide for a surplus distribution to the debtor in the case. The Court also held that the debtor had not claimed any exemption in the assets destroyed by the fire.

What distinguishes this case from the above analyses of standing in bankruptcy cases, is that in this proceeding, the Trustee has asserted at least two causes of action which would render these Defendants, as shareholders, officers, or directors, personally liable for the debts of the Debtor. In the Fifth Cause of Action, the Trustee, pursuant to § 544(b), asserts an action for breach of fiduciary duty by these Defendants as corporate officers and members of the Board of Directors of the Debtor. In the Sixth Cause of Action, the Trustee seeks to pierce the corporate veil and hold these Defendants personally liable as shareholders for the debts of the Debtor.

Therefore, an additional issue under the Motion for Partial Summary Judgment is whether this prospective personal liability to shareholders, officers and directors, as a result of this adversary action, provides these Defendants sufficient pecuniary interest in the administration of the case and resulting distribution to creditors to allow them standing in that capacity to assert the Counterclaims.

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This Court could not find any authorities on point to address this issue. However, in an analogous area, there is authority which indicates that a Chapter 7 debtor has a sufficient pecuniary interest to have standing to object to acts associated with the administration of the estate, if there has been a determination that the debts are not discharged because in that event the debtor remains personally liable for those debts and is directly affected by the distribution to creditors.

In McGuirl v. White, 86 F.3d 1232 (D.C. Ct. of Appeals 1996), the Chapter 7 debtors were found to have sufficient pecuniary interest for standing to object to administrative fees and expenses because the prior determination that their debts were not discharged caused them to be personally liable for the debts. The Court concluded that any reduction in administrative fees and expenses would allow greater payment to creditors, reducing such debts, and therefore the debtors' personal liability.

In its decision, the District of Columbia Court of Appeals distinguishes the case of SEC v. Securities Northwest, Inc., 573 F.2d 622 (9th Cir.1978). In Securities Northwest, a former shareholder and officer of a corporate debtor in a case under the Security Investor Protection Act was found not to have standing to appeal a final report and accounting made by the trustee which had determined the priority of payment of a tax claim on which the shareholder officer, as a responsible person under the tax laws, was also personally liable.⁴ The Court found that the shareholder officer did not have "a sufficiently direct and immediate interest in the proceeding". The Ninth Circuit stated that although the shareholders' interests were "indirectly pecuniary", his

⁴ The shareholder complained that had the claim of the IRS been given a higher priority, it would have been paid from the estate and eliminated the shareholders personal liability.

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interests were “remote and consequential rather than direct and immediate”.

In McGuirl, the Court held that the debtors’ interest in maintaining as large an estate as possible for purposes of paying creditors after the bankruptcy proceeding was not remote and consequential and that the relationship between reducing the administrative expenses and the debtor’s ultimate post bankruptcy personal liability was direct. McGuirl, supra at 1235.

In the matter before the Court, unlike in McGuirl, there has not yet been any determination of personal liability by the Defendants as shareholders, officers or directors. Secondly, the Defendants’ assertions of facts in the First and Second Counterclaim have little connection with the factual basis of the Complaint against the Defendants. Third, it has hereinabove been determined that three of the four Defendants already have standing in other capacities to assert the Counterclaims. Finally, this Court is aware of the Fourth Circuit Court of Appeal’s admonition regarding the recognition of standing in bankruptcy cases:

Courts consistently have noted a public policy interest in reducing the number of ancillary suits that can be brought in the bankruptcy context so as to advance the swift and efficient administration of the bankrupt’s estate. This goal is achieved primarily by narrowly defining who has standing in a bankruptcy proceeding . . . In certain instances, courts relax the general rule that only the Chapter 7 trustee has standing before the bankruptcy court and grant standing to certain other interested parties. Courts should be chary about granting such dispensations, however, as lax rules which liberally allow parties with some interest in the bankruptcy proceeding, such as a Chapter 7 debtor, to contest a proposed course of action, or to appeal an adverse decision, are too likely to generate “protracted litigation” that ultimately served the interest of neither the debtor’s estate nor the creditors. See In re Thompson, 965 F.2d 1136, 1145-56 (1st Cir.1992). Stricter rules, on the other hand, have the salutary effects of advancing the estate’s “timely administration,” In re Bowman, 181 B.R. 836, 844 (Bankr.D.Md.1995), and shielding the courts from “the needless multiplication of lawsuits.” In re Wells, 575 F.2d 329, 331 (1st

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Cir.1978); see McGuirl v. White, 86 F.3d 12232, 1235 (D.C.Cir.1996) (discussing the need to avoid “overwhelm[ing] bankruptcy courts with claims by the many parties indirectly affected by bankruptcy court orders”).

In re Richman v. First Woman’s Bank, 104 F.3d 654, 656-657 (4th Cir. 1997).

Therefore, for all of these reasons, the Court, pursuant to Bankruptcy Rule 7021, chooses to sever and stay the Counterclaims asserted by the Defendants in their capacity as shareholders, officers and directors pending the determination of the allegations of the Complaint which seek to impose personal liability on the Defendants in those capacities. The Trustee’s Motion for Partial Summary Judgment as to these Counterclaims against the Defendants in those capacities shall also be stayed.

The Third Counterclaim asserts an intentional interference with contract and does not assert a breach of fiduciary duty. As presently asserted, the Third Counterclaim does not benefit nor directly affect the Defendants in their capacity as shareholders, officers and directors. A review of the contract which is the subject of the Third Counterclaim indicates that Samuel H. Simchon individually is a party to the contract but that Levy Simchon, Rebecca Simchon, and Oded Simchon are not parties to the contract. Therefore, Levy Simchon, Rebecca Simchon and Oded Simchon do not have standing to maintain the Third Counterclaim and the Motion for Partial Summary Judgment is granted as to them.

For all of these reasons, the Trustee’s Motion for Partial Summary Judgment is granted in part to the Third Counterclaim and denied in part as stated hereinabove. The First and Second Counterclaims asserted by the Defendants in their capacities as shareholders, officers or directors of the Debtor corporation are severed and stayed subject to further Order pending the

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determination of other claims and issues in this proceeding.

AND IT IS SO ORDERED.

Columbia, South Carolina,
May 24, 1999.


UNITED STATES BANKRUPTCY JUDGE

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CERTIFICATE OF MAILING

The undersigned, Deputy Clerk of the
Bankruptcy Court for the District of Columbia,
certifies that a copy of the document
was mailed on the date listed below.

July 24 1999

Griffin
Cawthon
Gleissner

DEBTOR, DEBTOR'S ATTORNEY, OR CREDITOR

KELLEY MORSE
Deputy Clerk