

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF SOUTH CAROLINA

98-07203-W
11-3-99

IN RE:

Southern Textile Knitters, Inc.,

Debtor.

Robert F. Anderson, Trustee,

Plaintiff,

v.

Samuel H. Simchon, Levy Simchon,
Rebecca Simchon, Oded Simchon, Renee
Simchon, Hava 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, I.I.C, and Bay Island
Sportswear, Inc.,

Defendants.

Case No. 98-07203-W

Adversary No. 99-80026

ENTERED
AUG - 3 1999
K.K.M.

ORDER

Chapter 7

This matter comes before the court on the Motion of the Plaintiff, Robert F. Anderson, Trustee to compel Billy J. Garrett, Jr. to respond to questions at his deposition.

An involuntary petition for relief under Chapter 7 of the Bankruptcy Code was filed against the debtor, Southern Textile Knitters, Inc., on August 19, 1998. Relief was *subsequently granted and the Plaintiff was appointed to act as Trustee. The Trustee brought the instant action against the insiders of the debtor for the turnover assets pursuant to 11 U.S.C. § 542, the recovery of preferential transfers pursuant to 11 U.S.C. § 547, for the recovery of fraudulent transfers pursuant to 11 U.S.C. § 548, for the recovery of*

post-petition transfers pursuant to 11 U.S.C. § 549, for damages for breach of fiduciary duty, to pierce the corporate veil, for damages for aiding and abetting the transfer of the debtor's assets, for conversion, for fraudulent transfers pursuant to South Carolina Code § 27-23-10, for civil conspiracy, for subordination of claims, for an accounting, and for the collection of monies due to the estate.

The witness, Billy J. Garrett, Jr., is a member of the South Carolina Bar. Mr. Garrett served as corporate counsel for the debtor beginning July 1, 1997 and continuing at least until after the involuntary petition was filed against the debtor. Mr. Garrett also represents the defendant, Samuel Simchon, in ~~the~~ several ~~the~~ matters ^(gmv) currently pending in other courts. Mr. Garrett has also represented Mr. Simchon's wife, the defendant, Renee Simchon. Finally, Mr. Garrett has represented the defendant, Southern Textile Knitters of Greenwood, Inc. (STK Greenwood). Mr. Garrett has admitted ^{now} he has conflicts of interest *in connection with this action.* (gmv)

In his complaint, the Trustee alleges that the debtor, under the control of the defendant, Samuel Simchon, transferred approximately \$940,000.00 in inventory to Samuel Simchon who subsequently transferred the inventory to a company owned by Mr. Simchon, the defendant, STK Greenwood. The Trustee alleges that the transaction constituted a fraudulent transfer, and a preference.

The Trustee questioned Mr. Garrett regarding the matters in which he currently represents the defendants. The Trustee also questioned Mr. Garrett regarding his conversations with the debtor's president, Samuel Simchon, regarding the formation of STK Greenwood, and conversations he had with Mr. Simchon regarding the transfer of inventory to STK of Greenwood. The witness, at the request of the defendants, Samuel

Simchon and STK Greenwood, refused to answer the Trustee's questions on the grounds that the information was protected by the attorney/client privilege.

The Court of Appeals for the Fourth Circuit has adopted the following test for the application of the attorney/client privilege:

The privilege applies only if (1) the asserted holder of the privilege is or sought to become a client; (2) the person to whom the communication was made (a) is a member of the bar of a court, or his subordinate and (b) in connection with this communication is acting as a lawyer; (3) the communication relates to a fact of which the attorney was informed (a) by his client (b) without the presence of strangers (c) for the purpose of securing primarily either (i) an opinion on law or (ii) legal services or (iii) assistance in some legal proceeding, and not (d) for the purpose of committing a crime or tort; and (4) the privilege has been (a) claimed and (b) not waived by the client.

United States v. Jones, 696 F.2d 1069, 1072 (4th Cir. 1982).

It is well established that the Trustee has the authority to waive the debtor's attorney/client privilege so that corporate counsel may fully answer questions. In *Commodity Futures Trading v. Weintraub*, 105 S.Ct. 1986 (1985), the court held as follows:

In seeking to maximize the value of the estate, the trustee must investigate the conduct of prior management to uncover and assert causes of action against the debtor's officers and directors. See generally 11 U.S.C. Sections 704(4), 547, 548. It would often be extremely difficult to conduct this inquiry if the former management were allowed to control the corporation's attorney-client privilege and therefore to control access of the corporation's legal files. To the extent that management had wrongfully diverted or appropriated corporate assets, it could use the privilege as a shield against the trustee's efforts to identify those assets. The Code's goal of uncovering insider fraud would be substantially defeated if the

debtor's directors were to retain the one management power that might effectively thwart an investigation into their own conduct. See generally *In re Browy*, 527 F.2d 799, 802 (CA7 1976) (*per curiam*).

At or about the time the inventory was transferred, Mr. Garrett was representing both STK Greenwood and the debtor. Since Mr. Garrett was representing both parties to the transaction, neither can claim attorney/client privilege. *Garner v. Wolfenbarger*, 430 F.2d 1093 (5th Cir. 1970), cert. den. 401 U.S. 974, provides that when "the same attorney acts for two or more parties having a common interest, neither party may exercise the privilege in a subsequent controversy with the other." Since Mr. Garrett was representing the debtor, Samuel Simchon, and STK Greenwood, none of the parties may assert the privilege.

The most well known exception to the attorney/client privilege is the so called crime-fraud exception. See *In re Andrews*, 186 B.R. 219 (Bankr. E.D.Va. 1995); *In re Rigby*, 199 B.R. 358 (Bankr. E.D.Tex. 1995); *In re Diamont v. Sheldon L. Pollack Corporation*, 216 B.R. 589 (Bankr. S.D.Tex. 1995); and *In re Cumberland Investment Corporation*, 120 B.R. 62/ (Bankr. D.R.I. 1990). In order to circumvent the attorney/client privilege on the basis of fraud, the Trustee must make a *prima facie* case by demonstrating one or more "badges of fraud" is present.

In the current case, there are several such badges. There is an insider relationship between the debtor, Mr. Simchon, and Southern Textile Knitters of Greenwood, Inc. Mr. Simchon owns all the stock and is the president of Southern Textile Knitters of Greenwood, Inc. Mr. Simchon and several other members of his family own all the stock of the debtor and Mr. Simchon was the president of the debtor.

The transfer of the inventory took place no more than three months prior to the filing of the involuntary petition. Close proximity in time to insolvency and litigation are both recognized badges of fraud.

The nature of the transaction has been secreted by Mr. Simchon. At his Bankruptcy Rule 2004 examination, he indicated that the transfer of inventory was a contemporaneous exchange. However, the cancelled check and the invoices submitted by the Trustee indicate that the transaction was not contemporaneous.

The debtor continued to have possession of the transferred inventory after the alleged transaction had taken place. Finally, the defendant, STK Greenwood took over the debtor's location, customers, employees, and telephone number.

It is not necessary that the Trustee prove intent to defraud at this time. However, the Trustee has established a *prima facie* case by demonstrating one or more badges of fraud.

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that the Trustee's Motion to Compel is granted. The witness, Billy J. Garrett, Jr. shall answer the questions the Trustee has posed.

August 2, 1999


UNITED STATES BANKRUPTCY JUDGE

CERTIFICATE OF MAILING

The United States District Court for the District of South Carolina hereby certifies that a copy of this document, which is being mailed, was mailed on the date listed below to:

AUG 23 1999

*Constance
Gleason
Beal
And
UST*

DEBTOR, DEBTOR'S ATTORNEY, TRUSTEE

KELLEY MORGAN

Deputy Clerk

RECORDED

99 JUL 29 AM 10:42

DISTRICT OF SOUTH CAROLINA