UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF SOUTH CAROLINA

IN RE: Southern Textile Knitters, Inc., Debtor.	C/A No. 98-07203-W Adv. Pro. No. 99-80026-W
Robert F. Anderson, 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 Pointe Construction, Inc., Old Fort Industrial Park, L.L.C., Hava Simchon and Bay Island Sportswear, Inc. Defendants.	**JUDGMENT** Chapter 7

Based upon the Findings of Fact and Conclusions of Law as recited in the attached Order of the Court, the Court grants Defendants' Motion for Sanctions pursuant to Fed. R. Bankr. P. 9011 by Old Fort and denies Defendants' Motion for Sanctions pursuant to Fed. R. Bankr. P. 9011 and For Reimbursement of Costs Pursuant to Fed. R. Bankr. P. 7068 by STKG, Renee Simchon, and Center Pointe. The Court also denies the Trustee's request that his expenses and attorney's fees incurred in opposing Defendants' Motion be awarded pursuant to Fed. R. Bankr. P. 9011(c)(1)(A).

John E. Waites
UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina,
August 17, 2000.

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CERTIFICATE OF MAILING

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THIS MATTER comes before the Court upon the Motion for Sanctions pursuant to Bankruptcy Rule 9011 and For Reimbursement of Costs Pursuant to Bankruptcy Rule 7068 (the "Motion") by Southern Textile Knitters of Greenwood, Inc. ("STKG"), Renee Simchon, Center Pointe Construction, Inc. ("Center Pointe"), and Old Fort Industrial Park, LLC ("Old Fort") (collectively "Defendants"); filed with the Court on March 15, 2000. In the Motion, Defendants request sanctions pursuant to Fed. R. Bankr. P. 9011 against the Trustee, Robert F. Anderson, and his counsel, Anderson & Associates, P.A., for their continued pursuit of the following contentions: (1) the allegation that Southern Textile Knitters, Inc. ("Debtor") was insolvent during the ninety-day period prior to the filing of the bankruptcy petition and all claims that include insolvency as a necessary element; (2) the allegation that Debtor's inventory, valued at

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approximately $2.4 million, was misappropriated and all claims based upon that contention; and (3) all claims against Old Fort. Renee Simchon and Center Pointe further request that they be reimbursed for the costs incurred in preparing for trial pursuant to Fed. R. Bankr. P. 7068.

On April 3, 2000, Anderson & Associates, on its behalf and on behalf of the Trustee, filed an Objection and Request for Expenses and Attorneys Fees (the "Objection"). In the Objection, the Trustee requested that his expenses and attorney's fees incurred in opposing Defendants' Motion be awarded pursuant to Fed. R. Bankr. P. 9011(c)(1)(A). Based upon the pleadings filed in this matter, considering the evidence presented, and hearing the arguments of counsel at the hearing on the Motion; the Court makes the following Findings of Fact and Conclusions of Law pursuant to Fed. R. Civ. P. 52, made applicable in bankruptcy proceedings pursuant to Fed. R. Bankr. P. 7052.[1]

FINDINGS OF FACT

1. On August 19, 1998, an involuntary petition for relief under Chapter 7 of the Bankruptcy Code was filed against Debtor. Debtor consented to the relief sought, which was ultimately granted on September 10, 1998.

2. On September 10, 1998, Robert F. Anderson was appointed to act as the Trustee in the case. On October 23, 1998, the Trustee was authorized by the Court to employ Anderson & Associates to represent him in legal matters and to hire George W. DuRant as his accountant.

3. On January 26, 1999, the Trustee commenced this adversary proceeding against certain of

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[1] The Court notes that to the extent any of the following Findings of Fact constitute Conclusions of Law, they are adopted as such; and to the extent any Conclusions of Law constitute Findings of Fact, they are so adopted.

the defendants with the filing of an initial Complaint. The initial Complaint was then twice amended, once on February 1, 1999 and then again on July 6, 1999. The Second Amended Complaint asserts the following causes of action against various defendants in the case: (1) turnover of assets pursuant to 11 U.S.C. §542[2]; (2) preferential transfers pursuant to §547; (3) fraudulent transfers pursuant to §548; (4) post-petition transfers pursuant to §549; (5) breach of fiduciary duty; (6) piercing the corporate veil; (7) aiding and abetting; (8) conversion; (9) fraudulent transfers pursuant to South Carolina Code §27-23-10; (10) civil conspiracy; (11) subordination of claims; (12) accounting of assets; (13) rent due by STK de Honduras; and (14) money owed by Hava Simchon.

4. The Trustee and Defendants filed cross-motions for Summary Judgment as to many of these causes of action. By Order entered December 20, 1999, the Court granted summary judgment in favor of STKG, Renee Simchon, Center Pointe, and Old Fort on some of the causes of action asserted in the Second Amended Complaint, leaving the following causes of action to be tried on the merits: First Cause of Action (turnover of assets pursuant to §542); Second Cause of Action (preferential transfers pursuant to §547); Third Cause of Action (fraudulent transfers pursuant to §548); Fourth Cause of Action (post-petition transfers pursuant to §549) as it relates to STKG; Seventh Cause of Action (aiding and abetting); Ninth Cause of Action (fraudulent transfers pursuant to South Carolina Code §27-23-10) as it related to Renee Simchon, Center Pointe, and STKG; and Twelfth Cause of Action (accounting of assets) as it related to Center Pointe, Old Fort, and STKG.

5. On January 3, 2000, Defendants provided notice to the Trustee and his counsel of their

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[2] Further references to the Bankruptcy Code shall be by section number only.

intent to move for sanctions if the Trustee continued the pursuit and refused to withdraw the following contentions and claims within twenty-one (21) days:

(a) The allegation that Debtor was insolvent during the ninety-day period prior to the filing of the bankruptcy petition and all claims that include as a necessary element Debtor's insolvency.
(b) The allegation that Debtor's inventory with a value of approximately $2.4 million was misappropriated and all claims based upon the contention that there was a misappropriation of Debtor's inventory.
(c) Preference, fraudulent conveyance, Statute of Elizabeth claims, and all other claims against Old Fort despite the Trustee's acknowledgment that Old Fort had not received any transfer from Debtor.

6. Despite the Notice provided on January 3, 2000, the Trustee pursued the first two allegations set forth above at the trial on the merits. While the Trustee did not argue the causes mentioned in the third allegation set forth above at trial, he never withdrew the causes nor did he respond to Defendants' Notice by informing Old Fort that he was no longer pursuing those causes.

7. At the conclusion of the Trustee's case-in-chief at the trial on the merits, Defendants moved for Judgment on Partial Findings pursuant to Fed. R. Civ. P. 52(c), made applicable to bankruptcy proceedings pursuant to Fed. R. Bankr P. 7052, on all of the causes of action pending against them.

8. By a ruling announced at trial and Order of March 13, 2000, the Court granted the Motion for Judgment on Partial Findings as it related to Old Fort; therefore, all causes of action asserted by the Trustee against Old Fort were dismissed with prejudice. The Motion was granted because at trial the Trustee acknowledged that he was not aware of any transfers to Old Fort and further informed the Court that he was then only seeking an accounting from Old Fort.

9. By a ruling announced at trial and Order of March 13, 2000, the Court also conditionally granted the Motion for Judgment on Partial Findings as it related to Renee Simchon and Center Pointe upon the completion of the turnover of the furniture and equipment alleged in the Complaint to have been transferred to the two defendants.

10. By a ruling announced at trial and Order entered on July 19, 2000, the Court granted the Motion on Partial Findings in favor of STKG as it related to the Fourth Cause of Action and the Twelfth Cause of Action.

11. In several Orders, the Court concluded that Debtor was solvent up to at least July 31, 1998.

12. On July 26, 2000, the Court entered an Order dismissing all the causes of action against the remaining defendants, Samuel Simchon, STK de Honduras Sewing, Inc. ("STKH"), and STKG; with the exception of the First Cause of Action (Turnover) as it relates to STKH and Samuel Simchon, the Eight Cause of Action (Conversion) as it relates to the equipment transferred to STKH, and the Thirteenth Cause of Action (Rent Due). In that Order, the Court noted that "[d]espite the fact that DuRant's analysis is logical, the Court finds that Defendants have offered a reasonable explanation which could account for the alleged misappropriated inventory" and concluded that the Trustee did not meet his burden to prove that inventory was being diverted over time. Furthermore, the Court found that Debtor was solvent at least until July 31, 1998; however, it concluded that, from the evidence introduced at trial, it was unable to conclude the exact date when any insolvency occurred.

13. On August 13, 1999, Renee Simchon and Center Pointe made an offer of judgment to the Trustee in which they offered "to allow judgment to be taken against them by the Plaintiff which judgment only will require the Defendants to return the inventory which the Plaintiff alleges was

transferred to Defendants in May of 1998." The offer was ultimately rejected by the Trustee.

CONCLUSIONS OF LAW

Defendants filed the Motion against the Trustee and his counsel requesting that their attorneys' fees and costs in defending against the Second Amended Complaint be awarded pursuant to Fed. R. Bankr. P. 9011 and further requesting that they be reimbursed for costs incurred by Renee Simchon and Center Pointe pursuant to Fed. R. Bankr. P. 7068.

1. Sanctions Pursuant to Fed. R. Bankr. P. 9011

Federal R. Bankr. P. 9011 serves, as a primary goal, to sanction an attorney, his or her law firm, or a client for conducting themselves in a manner which frustrates the purpose of the judicial system. The rule provides in pertinent part:

> **(b) Representations to the Court.** By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an attorney or unrepresented party is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances,--
>
> (1) it is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation;
>
> (2) the claims, defenses, and other legal contentions therein are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law;
>
> (3) the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery; and
>
> (4) the denials of factual contentions are warranted on the evidence or, if specifically so identified, are reasonably based on a lack of information or belief.
>
> (c) **Sanctions.** If, after notice and a reasonable opportunity to

> respond, the court determines that subdivision (b) has been violated, the court may, subject to the conditions stated below, impose an appropriate sanction upon the attorneys, law firm, or parties that have violated subdivisions (b) or are responsible for the violation.

A claim violates the requirements of Fed. R. Bankr. P. 9011 or Fed. R. Civ. P. 11 when

> "it 'has been interposed for any improper purpose, or where, after reasonable inquiry, a competent attorney could not form a reasonable belief that the pleading is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification or reversal of existing law."

In re Kilgore, C/A No. 98-08227-W (Bankr. D.S.C. 6/19/2000) (quoting United States v. International Brotherhood of Teamsters, 948 F.2d 1338, 1343 (2d Cir. 1991)). Subsection (b) of the rule imposes on parties a duty to conduct a reasonable inquiry prior to presenting a claim or defense to the Court. Courts have generally held that in order to determine whether a litigant has breached his or her duty to conduct a reasonable inquiry, they need to conduct an objective reasonableness test, "'asking whether such conduct is "reasonable under the circumstances."'" Allnutt v. Friedman (In re Allnutt), 1995 WL 222067 (D. Md. 1995) (quoting In re Burse, 120 B.R. 833, 836 (Bankr. E.D. Va. 1990)); see also, Lichtenstein v. Consolidated Servs. Group, Inc., 173 F.3d 17, 23 (1st Cir. 1999); Jones v. International Riding Helmets, Ltd., 49 F.3d 692, 695 (11th Cir. 1995) ("[A] court confronted with a motion for Rule 11 sanctions first determines whether the party's claims are objectively frivolous--in view of the facts or law--and then, if they are, whether the person who signed the pleadings should have been aware that they were frivolous; that is, whether he would have been aware had he made a reasonable inquiry . . . If the attorney failed to make a reasonable inquiry, then the court must impose sanctions despite the attorney's good faith belief that the claims were sound."); In re Kilgore, C/A No. 98-08227-W

(Bankr. D.S.C. 6/19/2000).[3]

Both Fed. R. Civ. P. 11 and Fed. R. Bankr. P. 9011 were amended effective in 1993 and 1997 respectively to make clear that the requirements of the rule place a continuing responsibility on the litigants to evaluate the plausibility of the claims. The 1993 Advisory Committee's notes to the amendments emphasize that:

> [A] litigant's obligations with respect to the contents of these papers are not measured solely as of the time they are filed with or submitted to the court, but include reaffirming to the court and advocating positions contained in those pleadings and motions after learning that they cease to have any merit. For example, an attorney who during a pretrial conference insists on a claim or defense should be viewed as 'presenting to the court' that contention and would be subject to the obligations of subdivision (b) measured as of that time.

Fed. R. Bankr. P. 9011 advisory committee's note. See, e.g., Turner v. Sungard Bus. Sys., Inc., 91 F.3d 1418, 1422 (11th Cir. 1996); Young v. Corbin, 889 F. Supp. 582, 585-86 (N.D. N.Y. 1995); Rodriguez v. Banco Central, 155 F.R.D. 403, 406-08 (D. P.R. 1994).

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[3] The Court recognizes that "the imposition of sanctions must be divorced from the ultimate disposition of the underlying action." R.K. Harp Investment Corp. v. McQuade, 825 F.2d 1101, 1103 (7th Cir. 1987). The rule was intended to prevent litigants from flooding the judicial system with frivolous claims that would unnecessarily increase the parties' fees and waste judicial time. However, the purpose of the rule is misused "when sanctions are sought against a party or counsel whose only sin was being on the unsuccessful side of a ruling or judgment." Gaiardo v. Ethyl Corp., 835 F.2d 479, 483 (3d Cir. 1987) ("'We caution litigants that rule 11 is not to be used routinely when the parties disagree about the correct resolution of matter in litigation. Rule 11 is intended for only exceptional circumstances.' Nothing in the language of the Rule of the Advisory Committee Notes supports the view that 'the Rule empowers the district court to impose sanctions on lawyers simply because a particular argument or ground for relief contained in a non-frivolous motion is found by the district court to be unjustified.'"); see also Trace Servs., Inc. v. American Meter Co., 141 F.R.D. 47, 48 (W.D. Pa. 1992); Mareno v. Rowe, 910 F.2d 1043 (2d Cir. 1990) ("[N]ot all unsuccessful legal arguments are frivolous or warrant sanction.").

In this case, Defendants claim that sanctions pursuant to Fed. R. Bankr. P. 9011 should be awarded against the Trustee and his counsel, not for the filing of the claims, but for the continued pursuit of the claims that Debtor was insolvent during the ninety-day period prior to the filing of the bankruptcy petition, that Debtor's inventory with a value of up to $2.4 million was misappropriated, and because the Trustee pursued claims against Old Fort despite the Trustee's acknowledgment that Old Fort had not received any transfer from Debtor.

The Trustee and his counsel filed an Objection initially arguing that Defendants' request for sanctions pursuant to Fed. R. Bankr P. 9011 was not procedurally proper in that the Motion *also made a request for costs pursuant to Fed. R. Bankr. P. 7068.* The Court finds that the Trustee is generally correct in that Fed. R. Bankr. P. 9011(c)(1) provides in pertinent part that "[a] motion for sanctions under this rule shall be made separately from other motions or requests and shall describe the specific conduct alleged to violate subdivision (b)." (Emphasis added); see also Glutzer v. The Prudential Ins. Co., 183 F.R.D. 632, 638 (N.D. Ill. 1999) (holding that request for Rule 11 sanctions was improperly made in that it was made in the response brief to a motion for summary judgment); Omega Sports, Inc. v. Sunkyong America, Inc., 872 F. Supp. 201, 203 (E.D. Pa. 1995) (holding that it was procedurally improper to include a request for Rule 11 sanctions along with a motion to remand). However, at least one court has noted that the procedural requirements emphasized in Fed. R. Civ. P. 11 and Fed. R. Bankr. P. 9011 do not prohibit combining a Rule 11 request with other sanction requests pursuant to other statutes. See *Ridder v. City of Springfield, 109 F.3d 288, 294 (6th Cir. 1997).* In Ridder, the Court noted:

> [Appellant] argues that Springfield's motion for sanctions was not 'separate' because Springfield moved for sanctions and/or attorney fees pursuant to Rule 11, 42 U.S.C. § 1988, and 28 U.S.C. §1927. We believe Springfield has filed a 'separate' motion for sanctions under the meaning of the rule. The drafters instruct that a

> 'separate' motion is one that is 'not simply included as an additional prayer for relief contained in another motion.' . . . As we understand it, this requirement is intended to highlight the sanctions request by preventing it from being tacked onto or buried in motions on the merits, such as motions to dismiss or for summary judgment. The requirement does not foreclose combining a Rule 11 request with other provisions regulating attorney behavior, such as §1988 and §1927.

Id. at 294 n.7. In this case, the Court finds that the combining of a request for sanctions pursuant to Fed. R. Bankr. P. 9011, coupled with a remedial request that costs be awarded against the Trustee for his rejection of Defendants' Offer of Compromise pursuant to Fed. R. Bankr. P. 7068, does not in itself violate Rule 9011. Therefore, an examination of the specific basis for the request for sanctions is necessary.

Defendants have first moved for sanctions based on the Trustee's contentions that $2.4 worth of inventory was misappropriated. Defendants argue that Samuel Lovell, the estate's liquidator, actually accounted for the inventory alleged to be misappropriated by conceding that the "missing inventory" had been sold by Debtor, was located at offsite processors, or sold by him pursuant to order of the Court. Furthermore, they argue that Debtor's certified public accountant, W.R. Garvin , and Samuel Simchon all accounted for the allegedly misappropriated inventory in their depositions and testimony at trial.

In support of the allegation of misappropriation, the report of George W. DuRant was introduced into evidence and DuRant further testified at trial regarding his conclusion that approximately $2.4 million in inventory was misappropriated by the corporation's insiders. DuRant started his analysis by determining that as of July 31, 1998, Debtor reported an inventory worth approximately $3,721,725. DuRant took into account the fact that the inventory was subsequently liquidated and that $324,105.56 was received from the sale. In conceding that the

Trustee's liquidation sales of $324,105.56 did not represent a true value of the inventory, DuRant restated the Trustee's sales consistently with the manner in which Debtor's records were maintained and concluded that the sales accounted for $1,322,652.92 in value. From those figures, and taking into consideration a sale of goods which took place in August of 1998 in the amount of $8,644, DuRant reached the conclusion that approximately $2,390,428 in inventory was unaccounted for. The testimony of the Trustee's accountant as well as the Trustee's argument that the inventory was misappropriated were rebutted at trial by Defendants who provided a different explanation for the discrepancies in numbers which the Trustee attributed to misappropriation. By Order entered July 26, 2000, the Court concluded that the Trustee did not meet his burden to prove that the equipment in question was diverted to Honduras and that it was "misappropriated." Considering the circumstances of this case, including the insider relationship of many of the defendants, the Trustee's allegations of misappropriation, while ultimately unsuccessful, were not unwarranted to take to trial.

Defendants have also moved for sanctions based upon the Trustee's continued advocacy of and lack of support for his allegation that Debtor was insolvent at the time of the transfers alleged in his Complaint since such insolvency is a necessary element of the causes of action. They argue that the Trustee's expert witness, George W. DuRant, a certified public accountant, testified during his deposition and asserted in his Accountant's Report that Debtor was solvent as of June 30, 1998. At the trial on the merits, the Court ultimately found that Debtor was solvent up to at least July 31, 1998.

Specifically, as to movant STKG, the Trustee asserted an improper transfer of inventory through Samuel Simchon and STKG to Debtor's customers. As part of his argument, the Trustee alleged that the relevant date for the transfer of inventory to Simchon and STKG was the date of

the ultimate sale by STKG to the customers; which, according to invoices introduced into evidence, took place between June 30, 1998 and September 11, 1998. While the Court declined to make such a finding, the determination of the actual transfer dates was litigated by the parties at the trial on the matter; therefore, certain causes of action were not completely precluded by the Trustee's pretrial evidence of Debtor's solvency. To a great decree, in asserting these claims the Trustee relied upon the analysis of his accountant, who is experienced in bankruptcy cases. The determination of causes of action regarding STKG ultimately hinged upon findings made by the Court at trial, which had been the basis of a rational dispute by the parties. Therefore, under the circumstances of this case, the Court finds that the Trustee's allegations of misappropriation of inventory and improper transfers against STKG were maintainable until trial and should not serve as a basis for sanctions under this Motion.

Additionally, the allegations of transfers to Renee Simchon and Center Pointe were resolved by the parties' agreement regarding the turnover of property and the Court's Order of March 13, 2000; therefore, as to these Defendants, the Court is not inclined to consider sanctions appropriate under this Motion. For these reasons, the Court concludes that the Trustee's allegations and contentions that $2.4 million worth of Debtor's inventory was misappropriated and that Debtor was insolvent during the ninety-day period preceding the filing of the petition do not warrant sanctions as to these Defendants.

Defendants also claim that the Trustee should be sanctioned pursuant to Fed. R. Bankr. P. 9011 for asserting claims pursuant to §547, §548, and S.C. Code Ann. §27-23-10 against Old Fort. As to these causes of action, the Second Amended Complaint is very general and does not indicate with specificity the defendants against whom or which the claims are sought. While the Second Amended Complaint does not expressly assert these causes of action against Old Fort, it

leaves the possibility open by claiming that Debtor transferred or caused to be transferred to certain named defendants, but adding the phrase "including but not limited to" in order to emphasize the possibility of other transfers against the remaining defendants, including Old Fort.[4] At his deposition conducted on May 20, 1999, when the Trustee was questioned about the relation of Old Fort to the transfer-based causes of action, he replied that he was unaware of any transfers at that time:

> Q. You haven't made a single allegation as it relates to a transfer to Old Fort Industrial Park. Is Old Fort Industrial Park a defendant for any of those Causes of Action?
> A. You haven't listed anything yet so I don't think so. But, I don't know.
> Q. So, as it relates to Old Fort Industrial Park those Causes of Action don't apply to them?
> A. At this point we don't know. But, if I find something I will amend to include it.

Despite this testimony, the Trustee objected to Old Fort's Motion for Summary Judgment based on a lack of transfers, even while admitting the lack of viability of other causes against it.[5]

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[4] For example, as to the Second Cause of Action pursuant to §547, the Trustee asserts that "[within one year before the filing of the petition commencing the case, the Debtor transferred or caused to be transferred to defendants, *including but not limited to* Samuel Simchon, STK Greenwood and Renee Simchon, property of the debtor including, but not limited to, the transfers above." (Emphasis added).

[5] In his Objection to the Motion of Southern Textile Knitters of Greenwood, Inc., Renee Simchon, Center Pointe Construction, Inc., and Old Fort Industrial Park, LLC for Partial Summary Judgment, filed with the Court on November 8, 1999, the Trustee stated:

> There are issues of fact regarding the Trustee's claim against Old Fort Industrial Park, LLC on the Trustee's First Cause of Action (Turnover), Second Cause of Action (Preferences), Third Cause of Action (Fraudulent Transfers Under Section 548), Fourth Cause of Action (Post-Petition Transfers), Tenth Cause of Action (Civil Conspiracy), and Eleventh Cause of Action (Subordination of Claims). The trustee is not seeking a recovery against Old Fort Industrial Park, LLC under the Fifth Cause of Action (Breach of

By Order of December 20, 1999, the Court sustained the Trustee's objection to Old Fort's Motion for Summary Judgment.[6] At the trial, the Trustee never introduced evidence relating to any transfers by Debtor to Old Fort, and Old Fort's name was not mentioned until Defendants moved for Judgment on Partial Findings at the end of the Trustee's case-in-chief. At that point, the Trustee acknowledged that he was unaware of any transfer to Old Fort; therefore, all causes of action, including an accounting, were dismissed by the Court as they related to Old Fort.

The question before this Court is whether the Trustee's failure to withdraw the claims against Old Fort or respond to the Notice of the request for sanctions pursuant to Fed. R. Bankr. P. 9011 presented to the Trustee on January 3, 2000, constitute a basis for sanctions under the rule if the Trustee did not argue for recovery under those claims at the trial. Prior to its amendments, Rule 11 did not impose a continuing duty on litigants to review the validity of their claims and withdraw ones that were initially valid but had proven to be frivolous. In accordance with the pre-amended rule, the District Court of South Carolina, in citing the Fourth Circuit case of Fahrenz v. Meadow Farm Partnership, 850 F.2d 207 (4th Cir. 1988) had concluded that "Fahrenz does not create a duty to withdraw properly signed pleadings, and sanctions may not be imposed under Rule 9011 in the absence of improperly signed pleadings." Cain v. Roe &

> Fiduciary Duty), Sixth Cause of Action (Piercing the Corporate Veil), Eighth Cause of Action (Conversion), Thirteenth Cause of Action (Rent Owed), and Fourteenth Cause of Action (Money Owed).
>
> . . .
>
> The Defendant's Motion for Partial Summary Judgment should be denied.

[6] The Court notes that the denial of summary judgment on the transfer-based causes of action asserted against Old Fort does not *per se* prohibit sanctioning pursuant to Fed. R. Bankr. P. 9011. See, e.g., Runfula & Associates, Inc. v. Spectrum Reporting II, Inc., 88 F.3d 368, 374 (6th Cir. 1996).

Assoc., Inc., C/A No. 4:95-3318-22 (D.S.C. 12/22/1995).

However, both Fed. R. Civ. P. 11 and Fed. R. Bankr. P. 9011 were amended in 1993 and 1997 respectively, and new provisions were included to clarify that litigants have a continuing responsibility to reevaluate their pleadings. See, e.g., Theodore C. Hirt, A Second Look at Amended Rule 11, 48 Am. L. Rev. 1007, 1015 (1999) ("A litigant's responsibility for such statements, therefore, is no longer completely 'static' in nature, but has become more of a continuing duty."). The amendments specify that a lawyer may be sanctioned under the rule "whether by signing, filing, submitting, or later advocating" a pleading or written motion. The added language in the rule thus specifies that the contents of the papers which are the subject of the Rule 11 sanctions are not only measured at the time of filing; rather, the amendments place on the litigants a continuing obligation and subject them to potential sanctions "for insisting upon a position after it is no longer tenable and by generally providing protection against sanctions if they withdraw or correct contentions after a potential violation is called to their attention." Young v. Corbin, 889 F. Supp. 582 (N.D. N.Y. 1995). The rule was also changed to include a "safe harbor" provision which gives alleged violators the opportunity to withdraw the challenged documents within twenty-one days to prevent the court's imposition of sanctions. Therefore, this Court notes that the holding of Cain v. Roe & Assoc, Inc., which constitutes precedent in this district but which was decided prior to the rule's amendments, has been impacted by the new provisions of Fed. R. Civ. P. 11 and Fed. R. Bankr. P. 9011.

The issue that has been presented to this Court is whether a litigant has a duty under the rule to withdraw or dismiss causes of action which are no longer plausible, or whether he or she is shielded from sanctioning by proceeding to trial on such causes of action while refraining to make any arguments as to the causes of action or defendants against which or whom a plausible

claim no longer exists. In this case, the Trustee argues that prior to receiving service of the Defendants' Motion for Sanctions he indicated, through counsel, that he was not aware of any transfers to Old Fort and further asserts that he did not advocate any claims for preferences, fraudulent conveyances, or Statute of Elizabeth claims against Old Fort after he was provided with a copy of the Notice on January 3, 2000. The Court rejects the Trustee's arguments and concludes that Fed. R. Bankr. P. 9011, as presently written, does not allow a litigant to maintain a claim, which was not initially frivolous, even while refraining from making any arguments or presenting any evidence as it relates to the specific claim. The Court believes that Fed. R. Bankr. P. 9011 was not designed to allow for such inappropriate conduct which only results in increased and unnecessary attorney's fees and costs and proves to be a waste of judicial efforts and time.

Even though precedent on this issue is limited, the cases seem to follow this reasoning and generally hold that, upon realizing through further discovery that a claim is no longer supported by law or facts, the litigant should modify or withdraw it or may face sanctions pursuant to the rule. In Young v. Corbin, 889 F. Supp. 582 (N.D. N.Y. 1995), for example, a prisoner brought a pro se action alleging that a prisoner official had violated the provisions of 42 U.S.C §1983. He claimed that the official had entered his cell, assaulted him, and destroyed plaintiff's books and other personal property. The defendant then filed a motion for summary judgment, which was properly served on the plaintiff and was ultimately granted. Following the service of the motion for summary judgment, the plaintiff did not contest any of the facts, nor did he make any attempt to conduct further discovery or modify his pleadings. The court noted that the plaintiff's allegations contained no evidentiary support in light of the fact that defendant was absent from work on the day the plaintiff claimed to have been assaulted and further observed that "plaintiff made no effort by way of further investigation or discovery to ascertain an

evidentiary basis, if any, for his allegations." Id. at 586. The court ultimately sanctioned the petitioner and concluded that "[i]n spite of over seven years in which to undertake discovery, and given full opportunity to modify his claims, plaintiff has failed to modify or *withdraw* his complaint." Id. (Emphasis added).

The court in Turner v. Sungard Bus. Sys., Inc., 91 F.3d 1418 (11th Cir. 1996) reached a similar conclusion. In that case, an employee sued his employer under Title VII for race discrimination and alleged that the employer had passed him over for a promotion and filled the vacant position with a white employee. The lawyer who initially represented plaintiff withdrew after the plaintiff expressed a desire to pursue the matter despite his lawyer's contrary advice. The plaintiff subsequently retained another lawyer to represent him in the suit. The defendant filed a motion for summary judgment; however, the plaintiff neither responded to the motion nor appeared at oral argument. In affirming the district court's award of sanctions against the plaintiff and his lawyer, the court noted:

> The district court found that (1) [the lawyer] knew from the moment he began representing Plaintiff that his claim was meritless, (2) at the pretrial conference, [the lawyer] represented that he had evidence to support [the lawyer]'s claim that the job at issue had been filled though no such evidence was ever presented to the court, and (3) after taking Zales' deposition, [the lawyer] had to know that the case was without a factual basis but *failed to dismiss it*, thereby forcing [the employer] (and the court) to expend time and money on a summary judgment motion. That the contentions contained in the complaint were not frivolous at the time it was filed does not prevent the district court from sanctioning [the lawyer] for his continued advocacy of them after it should have been clear that those contentions were no longer tenable.

Id. at 1422. (Emphasis added).

Finally, the case of Asllani v. Board of Edu., 150 F.R.D. 120 (N.D. Ill. 1993), despite

being a pre-amendment case, refers to the changes in obligations that will be implemented through the amendment of Rule 11. In that case, the court concluded that the complaint in itself did not violate the provisions of Rule 11 in that a reasonable inquiry had been conducted and the initial evidence warranted the claims asserted against the various defendants. What the court specifically focused on was the events following the initial complaint, and more specifically the letter that two of the defendants wrote to plaintiff to inform her that they were not involved in any of the actions which were the basis of the claims and further invited plaintiff to meet to discuss the matter. The plaintiff did not accept their offer and, as the court stated, "by failing to dismiss those defendants it indicated its intention to continue to sue them." Id. at 121. The court noted that the provisions of Rule 11 at that time only reached the filings in court and did not impose a continuing obligation; therefore, the motion filed by the defendants for Rule 11 sanctions was denied. However, the Court acknowledged that the proposed amendments to the rule would have changed the outcome of the case and further discussed the policy reasons for changing the rule to impose a continuing obligation:

> This court, for one, hopes that the amendments do become effective. Litigation is a very expensive process. The costs are multiplied when a party is seeking substantially the same remedy against a number of defendants and on the basis of a number of different theories, all of which depend upon essentially the same assumed factual circumstances. A party advancing a claim may have a reasonable basis for so claiming, only to find early on that she was mistaken--or, as in this case, being told that a party against whom the claim was advanced is prepared to sit down and demonstrate that she is mistaken. The defendants here were, as well, parties of very limited financial resources, and whatever resources had to be diverted for defending this actions came at the expense of substantive programs.

This Court is of the opinion that the Trustee cannot shield himself from sanctions under Fed. R. Bankr. P. 9011 by arguing that he did not advance any claims made against Old Fort

during trial. By failing to withdraw the allegations despite a knowledge of a lack of evidentiary support, the Trustee indicated that he was pursuing them, in essence, reaffirming them. The Court finds that the Trustee should have shielded himself with the "safe harbor" provision specified in the rule which allows for a twenty-one day period within which the plaintiff can withdraw any claim which has proven to be frivolous or not based in fact. The Trustee's failure to withdraw the transfer-based allegations against Old Fort, after he was served with a copy of the Notice on January 3, 2000, or to advise the opposing party of his position forced Old Fort to incur costs and fees in preparation for trial and caused unnecessary complications and use of judicial resources. Therefore, the Court finds that sanctions pursuant to Fed. R. Bankr. P. 9011 are appropriate as it relates to the continued assertions against Old Fort up to and including the trial of the matter. Considering the fees and costs incurred by Old Fort in this action as evidenced by its counsel's submission of May 23, 2000 and recognizing that deterrence is the primary goal of the rule, the Court finds that $1,000 is an appropriate sanction to be paid by Anderson & Associates to Defendant Old Fort.[7]

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[7] Even though Defendants did not request sanctions under 28 U.S.C. §1927, the Court notes that even if Anderson & Associates were not sanctioned pursuant to Fed. R. Bankr. P. 9011, the conduct at issue may still be sanctionable pursuant to §1927. Section 1927 of Title 28 provides that:

> Any attorney or other person admitted to conduct cases in any court of the United States or any Territory thereof who multiplies the proceedings in any case unreasonably and vexatiously may be required by the Court to satisfy personally the excess costs, expenses, and attorneys' fees reasonably incurred because of such conduct.

Section 1927 imposes on the litigants a continuing obligation to evaluate the proceedings and a constant responsibility "throughout the entire litigation to avoid dilatory tactics." United States v. International Brotherhood of Teamsters, 948 F.2d 1338 (2d Cir. 1991); Accent Designs, Inc. v. Jan Jewelry Designs, Inc., 827 F. Supp. 957, 972 (S.D. N.Y. 1993).

It is understandable that the Trustee, as a fiduciary in charge of investigating and recovering Debtor's assets for the benefit of the bankruptcy estate, brought this action. The factual situation of the case validly raised the Trustee's suspicion and placed on him a difficult burden to determine the propriety of the transfers between Debtor and related corporations and insiders, who generally are not eager to cooperate with or assist a Trustee. However, this Court discourages the "shotgun approach" to pleadings, "where the pleader heedlessly throws a little bit of everything into his complaint in the hope that something will stick." Rodgers v. Lincoln Towing Serv., Inc., 596 F. Supp. 13, 27 (N.D. Ill. 1984), aff'd 771 F.2d 94 (7th Cir. 1985); Weil v. Markowitz, 108 F.R.D. 113, 116 (D.C. 1985) ("Counsel should not be allowed to file a complaint first and thereafter endeavor to develop a cause of action."). The Court understands why the Trustee and his counsel filed this action and gave them, through discovery and in the defense of summary motions, significant deference to pursue the true facts. However, a trustee, like all litigants must, prior to trial on the merits, objectively evaluate the burden of proof which he bears and the existing evidence to support that burden, rather than bringing actions and relying on the pendency of trial in the hopes to extract a settlement with the opposing party to his advantage. The Court notes that, as the matter became more aggressively defended, the increasing animosity between the parties caused the Trustee to become more entrenched in his views of the alleged fraudulent conduct committed by Defendants, which in turn caused Defendants to become more critical of the Trustee's efforts. Such developments do not benefit any of the parties nor further the interest of justice; rather, they solely increase the attorney's fees and costs of the parties and waste judicial time. Rodriguez v. Banco Central, 155 F.R.D. 403, 406 (D.P.R. 1994) (quoting Cruz v. Savage, 691 F. Supp. 549, 556 (D.P.R. 1988)) ("There is a point beyond which zeal becomes vexation, the 'novel' approach to a legal issue converts to

frivolity and steadfast adherence to a position transforms to obdurateness.").

2. Offer of Judgment Pursuant to Fed. R. Bankr. P. 7068

Defendants' Motion also requests that the Trustee bear the costs incurred by Renee Simchon and Center Pointe pursuant to Fed. R. Civ. P. 68, made applicable to bankruptcy proceedings pursuant to Fed. R. Bankr. P. 7068. Fed. R. Civ. P. 68 was intended to encourage settlement and avoid litigation. The Rule provides in pertinent part:

> At any time more than 10 days before the trial begins, a party defending against a claim may serve upon the adverse party an offer to allow judgment to be taken against the defending party for the money or property or to the effect specified in the offer, with costs then accrued. If within 10 days after the service of the offer the adverse party serves written notice that the offer is accepted, either party may then file the offer and notice of acceptance together with proof of service thereof and thereupon the clerk shall enter judgment. An offer not accepted shall be deemed withdrawn and evidence thereof is not admissible except in a proceeding to determine costs. If the judgment finally obtained by the offeree is not more favorable than the offer, the offeree must pay the costs incurred after the making of the offer.

"The Rule prompts both parties to a suit to evaluate the risks and costs of litigation, and to balance them against the likelihood of success upon trial on the merits." Marek v. Chesny, 473 U.S. 1, 4 (1985). In his Objection to the Motion, the Trustee raised the question whether the offer in this case was proper under Rule 68. Among other things, the Trustee argued that Renee Simchon and Center Pointe failed to offer to pay the "costs then accrued," as Rule 68 requires. According to the explicit language in the rule and according to its interpretation by courts in various jurisdictions, the offer of judgment must meet certain requirements before a court may conclude that it was effective:

> First, it must be in the form of a written offer, served in accordance with Civil Rule 5, made applicable to bankruptcy cases by Bankruptcy Rule 7005. An offer contained in a pleading or motion

> will not suffice. Second, the offer must be for a specific sum mentioned in the offer. Third, the offer must include "costs then accrued." Absent conformity with each of these requirements, the offer will be deemed ineffectual.

10 Collier on Bankruptcy, ¶ 7068.02 (15th ed. rev. 1997) (footnote omitted). Courts have interpreted the rule strictly and have concluded that "to obtain the benefits of Rule 68 a defendant must follow its requirements." Cole v. Wodziak, 169 F.3d 486, 487 (7th Cir. 1999); Magnuson v. Video Yesteryear, 85 F.3d 1424, 1430-31 (9th Cir. 1996) ("Because [Appellant] did not serve its Rule 68 offer in compliance with Fed. R. Civ. P. 5(b) and did not offer good cause for its failure to validly serve the offer, we reverse the district court's award of costs to Appellant pursuant to Rule 68."); Grosvenor v. Brienen, 801 F.2d 944, 948 (7th Cir. 1986) (concluding that an oral offer of judgment made at the final pretrial settlement conference did not satisfy the requirements of Rule 68 and noting that "although Rule 68 does not specify that an offer of judgment be in writing, the requirement that the offer be served upon the plaintiff makes no sense unless it means that the offer must be written."); Conolly v. S.S. Karina II, 302 F. Supp. 675, 683 (E.D. N.Y. 1969) ("The tender mentioned in respondent's papers not only gave less notice than required under Fed. R. Civ. P. 68 and omitted 'costs then accrued,' but is in fact less than the amount of the judgment including interest."); see also Nordby v. Anchor Hocking Packaging Co., 199 F.3d 390, 393 (7th Cir. 1999) ("[A]mbiguities in Rule 68 offers are to be resolved against the offerors."); Nusom v. Comh Woodburn, Inc., 122 F.3d 830, 832 (9th Cir. 1997) (same).

In Marek v. Chesny, the Supreme Court was faced with the issue of whether the offer of judgment was proper pursuant to Rule 68 given the fact that it lumped petitioner's proposal for damages with their proposal for costs. Marek v. Chesny, 473 U.S. 1 (1985). Respondents

argued that an offer of judgment pursuant to Rule 68 must "separately recite the amount that the defendant is offering in settlement of the substantive claim and the amount he is offering to cover accrued costs." Id. at 5. The Court rejected respondent's argument and noted that the rule should not be read as requiring that defendant's offer of judgment specifically itemize the respective amounts being tendered for the settlement of the claim and for the separate costs incurred by the plaintiff. Id. at 6. The Court further concluded:

> [I]t is immaterial whether the offer recites that costs are included, whether it specifies the amount the defendant is allowing for costs, or, for that matter, whether it refers to costs at all. *As long as the offer does not implicitly or explicitly provide that the judgment not include costs, a timely offer will be valid.*

Id. at 6 (Emphasis added) (citation omitted).

In this case, Renee Simchon and Center Pointe's offer of Judgment stated that they "offer[ed] to allow judgment to be taken against them by the Plaintiff which judgment *only* [would] require the Defendants to return the inventory . . . which requirement will be the *only* relief to be granted Plaintiff under the Second Amended Complaint in regards to the Defendants." (Emphasis added). It is implicit in the language of the offer of judgment that costs incurred by the Trustee were not to be included and the Trustee's rejection thereof could have reasonably been based upon that deficiency. Therefore, the Court finds that, despite the fact that the ultimate judgment was not more favorable than the one offered by Renee Simchon and Center Pointe, the defendants's failure to meet the requirements of Rule 68 prohibits an award of costs against the Trustee.

It is therefore;

ORDERED that Defendants' Motion for Sanctions pursuant to Fed. R. Bankr. P. 9011 and For Reimbursement of Costs Pursuant to Fed. R. Bankr. P. 7068 by STKG, Renee Simchon,

and Center Pointe is denied.

IT IS FURTHER ORDERED that Defendants' Motion for Sanctions pursuant to Fed. R. Bankr. P. 9011 by Old Fort is granted, and Anderson & Associates shall pay to Old Fort sanctions in the amount of $1,000.

IT IS FURTHER ORDERED that the Trustee's request that his expenses and attorney's fees incurred in opposing Defendants' Motion be awarded pursuant to Fed. R. Bankr. P. 9011(c)(1)(A) is denied.

AND IT IS SO ORDERED.

UNITED STATES BANKRUPTCY JUDGE

Columbia, South Carolina,
August 17, 2000.