

UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION



IN RE:

Application of Gareth Howard Hughes)
and John C. McKenna, as Joint)
Provisional Liquidators of Carolina) Case No. 02 M 002
Reinsurance Limited, for an order)
compelling Charles Edelman to)
testify pursuant to subpoena.)

ORDER

The matter before the court is a motion filed by the Joint Provisional Liquidators of Carolina Reinsurance Limited to compel Charles Edelman to provide further deposition testimony. The motion to compel was heard on November 5, 2002. Marc J. Gottridge and Alan M. Ruley appeared on behalf of the Joint Provisional Liquidators and Ira S. Sacks and H. Arthur Bolick, II appeared on behalf of Charles Edelman.

MATTER BEFORE THE COURT

The deposition of Mr. Edelman was conducted on July 17, 2002, as part of the discovery that is being conducted in an ancillary case to a foreign proceeding that was commenced pursuant to § 304 of the Bankruptcy Code by Messrs. Hughes and McKenna as the Joint Provisional Liquidators of Carolina Reinsurance Limited, a reinsurance company incorporated under the laws of Bermuda. The ancillary case was filed in the United States Bankruptcy Court for the Southern District of New York. When the ancillary case was filed, an order was entered in the bankruptcy court in New York which provides that the Joint Provisional Liquidators "are

authorized hereby to engage in and compel discovery pursuant to the Federal Rules of Civil Procedure and the Federal Rules of Bankruptcy Procedure for purposes of assisting them to determine the nature of all claims and judicial proceedings pending or threatened against Carolina Re and its estate, the nature of Carolina Re's business and business transactions and to determine the nature and location of Carolina Re's assets. . . ."

Mr. Edelman resides within the Middle District of North Carolina and the subpoena for him to appear for the deposition was issued from this court, following which a deposition of Mr. Edelman was conducted within the Middle District of North Carolina. The motion to compel involves communications between officers of Carolina Re and Mr. Edelman, which Mr. Edelman refused to disclose during his deposition. The dispute regarding these communications involves whether the officers' assertion of the attorney/client privilege prevents the disclosure of the communications by Mr. Edelman.

The motion to compel is before this court pursuant to Rule 37(a) (1) of the Federal Rules of Civil Procedure which provides that an application for an order to compel disclosure or discovery from "a person who is not a party shall be made to the court in the district where the discovery is being, or is to be, taken."

F A C T S

Both parties rely upon the transcript of Mr. Edelman's

deposition as establishing the factual basis for their respective positions regarding the motion to compel. Therefore, the following relevant portions of the transcript are extracted for purposes of this order.

Carolina Re was incorporated in Bermuda. Except for a few shares owned by resident directors, the stock of Carolina Re **was** and is owned by Maurice Sabbah, Mr. Sabbah's wife and Kenneth Kornfeld. Messrs. Sabbah and Kornfeld were the principal officers of Carolina Re, were directors of Carolina Re and controlled Carolina Re. Mr. Edelman was vice president of Carolina Re, but was never an employee of Carolina Re, was never a director of Carolina Re and never owned any interest in the company.

During the entire time that he was vice president of Carolina Re, which extended from approximately 1984 until December of 2001, Mr. Edelman was employed by another corporation known as Fortress Re, as its general counsel. Fortress Re also is owned and managed by Messrs. Sabbah and Kornfeld. While serving as general counsel of Fortress Re, Mr. Edelman provided legal advice to Fortress Re, as well as to Messrs. Sabbah and Kornfeld, related to Fortress Re. In describing the context in which advice was provided to Messrs. Sabbah and Kornfeld, Mr. Edelman stated that the "persons who were officers of Carolina Re existed not simply in that sphere. They existed as individuals, they existed as persons affiliated and associated with Fortress Re. And those persons from time to time

asked me for legal advice in all those capacities and in others."

According to his sworn testimony, Mr. Edelman never provided legal advice to the Board of Directors of Carolina Re, never advised the Board to seek legal advice and never held the position of general counsel of Carolina Re, although he admitted that he did provide advice to two of the directors of Carolina Re, Messrs. Sabbah and Kornfeld. Mr. Edelman's testimony disclosed that Carolina Re, as a Bermuda corporation, had attorneys in Bermuda who provided legal services and advice to Carolina Re. However, Mr. Edelman testified that his only involvement with Carolina Re was as a lawyer and he admitted performing some legal services for Carolina Re. He testified that on some occasions he was assigned specific tasks for Carolina Re, such as determining why a Carolina Re filing with the authorities in Bermuda was not filed in a timely manner and to followup with the outside accountants to make sure that the filing was made, which he performed. As described by Mr. Edelman, matters were referred to him as they would be to an outside law firm, on an item or individual basis.

Mr. Edelman acknowledged receiving the waiver of the attorney/client privilege on behalf of Carolina Re from one of the provisional liquidators during his deposition. He understood the waiver to permit disclosure of communications regarding Carolina Re "[a]s long as it was people acting not in their personal interest, but rather in connection with their position as either agents or officers of Carolina Re."

According to Mr. Edelman he did not give **any** legal advice to officers of Carolina Re, but did give legal advice to directors of Carolina Re. The directors to whom he gave legal advice were Mr. Sabbah and Mr. Kornfeld.¹ However, Mr. Edelman testified that he "was providing any such legal advice to individual clients without reference to their being directors or shareholders of agents of Carolina Re." In giving such advice, Mr. Edelman "did not quantify whether I was giving somebody, to wit Mr. Sabbah and Mr. Kornfeld, legal advice as a director or shareholder, but rather treated them as individual clients, if you like." Mr. Edelman could not recall giving any legal advice to them as officers of Carolina Re.

In answering how he determined whether he was giving Mr. Sabbah and Mr. Kornfeld legal advice as individuals rather than as officers, Mr. Edelman stated that "it would depend on the nature of the legal advice involved." He then gave as an example, if one of them came to him and asked about whether they should sign a document, he would look at the capacity in which they were being asked to sign. If they were being asked to sign as a director, then he considered that he **was** giving advice to them as a director. He was then asked how he would make the determination if no document were involved and he answered: "I'm not sure there were

¹The testimony of Mr. Edelman does not reflect how or why Mr. Edelman determined that he was communicating with Messrs. Sabbah and Kornfeld as directors of Carolina rather than as officers of Carolina Re.

such occasions, that there wasn't a document involved."

When asked what advice he gave to Mr. Sabbah and Mr. Kornfeld on the occasions when he gave them legal advice, he was instructed not to answer, based upon the attorney/client privilege. Mr. Edelman concurred in such instruction, stating that the advice "is covered by the attorney/client privilege and can only be waived by the clients, to wit Messrs. Sabbah and Kornfeld as individuals." Mr. Edelman also was instructed not to answer a question asking him "in what areas did Mr. Sabbah seek personal legal advice" but was permitted to answer that some of those matters "did relate to Carolina Re" but was not permitted to answer in what way the advice related to Carolina Re. When asked who paid for the legal services that he rendered to Mr. Sabbah and Mr. Kornfeld in their personal capacities, he testified that nobody did. Mr. Edelman was permitted by his attorneys to testify that he had no recollection of giving legal advice to Messrs. Sabbah and Kornfeld on how to fulfill their duties- as officers of Carolina Re. However, he was instructed not to answer a question as to whether he ever gave them legal advice as to how to fulfill their duties as directors of Carolina Re. Mr. Edelman also was instructed not to answer questions as to whether Mr. Sabbah and Mr. Kornfeld ever asked him for advice relating to their defense against possible claims that might come out of the operation of Carolina Re. Finally, Mr. Edelman was instructed not to answer a question in which he was asked what he learned about

the payment of dividends by Carolina Re after the commencement of the insolvency proceeding involving Carolina Re.²

ANALYSIS

Under some circumstances, the attorney/client privilege may be available to corporate officials who obtain legal advice from the corporation's attorney. Thus, if corporate officials consult an attorney for the corporation regarding their personal liability unrelated to their role as corporate officials, the attorney/client privilege may be invoked by the corporate officials to prevent disclosure of such communications. See In re Citibank v. Andros, 666 F.2d 1192 (8th Cir. 1981). However, the situation changes when corporate officials consult corporate counsel regarding corporate matters or matters that are related to their roles as corporate officials.

Because a corporation can act and communicate only through its

²Although Mr. Edelman did not answer these questions, he did answer questions regarding matters which are being investigated by the Joint Provisional Liquidators. Thus, Mr. Edelman testified that he played no role in establishing the loss reserves for Carolina Re and was not consulted by Messrs. Sabbah and Kornfeld regarding whether the loss reserving practices of Carolina Re met appropriate legal standards. Mr. Edelman testified that he had no knowledge of Carolina Re paying dividends to its shareholders, had no discussions with Mr. Sabbah or Mr. Kornfeld regarding the payment of dividends and was not consulted for advice regarding Carolina Re paying dividends to its shareholders. Mr. Edelman also testified that he had no recollection of having any discussions with any one regarding the variance between the statutory basis of accounting and generally accepted accounting principles and whether such variance was material or presumed material. These answers suggest that, as a practical matter, compelling further testimony from Mr. Edelman may be of limited benefit.

agents, a corporation's privilege consists of communications by corporate officials about corporate matters and their roles and actions in the corporation. A corporate official thus may not prevent a corporation from waiving its attorney/client privilege with respect to discussions between corporate officials and corporate counsel regarding corporate matters. See In re Bevill, Bresler & Schulman Asset Mgt. Corp., 805 F.2d 120 (3d Cir. 1986). In applying this principle, the court in Bevill ordered the attorney to testify as to all communications between the attorney and the corporate officers about the corporation and the role and functions of the officers, but did not require the attorney to testify concerning communications about the officers' potential personal liability unless the communications also related to the business and assets of the corporation or the roles of the officers in the corporation. Id. at 123-24 . In discussing how to differentiate between the personal attorney/client privilege of an officer and that of the corporation, the court observed that "under existing law, any privilege that exists as to a corporate officer's role and functions within a corporation belongs to the corporation, not the officer." Id. at 124.

When a corporate official confers with and seeks the advice of the corporation's attorney, the default assumption is that the attorney represents the corporate entity, and it is the corporate official's burden to dispel that presumption. See In re Grand Jury

Subpoena, 274 F.3d 563, 571 (1st Cir. 2001). The following five-part test has been developed by the courts for determining whether a corporate official has carried the burden of dispelling this presumption and successfully established a personal claim of attorney/client privilege: (1) the corporate official must first show that he or she approached corporate counsel for the purpose of seeking legal advice; (2) the corporate official must show that when he or she approached corporate counsel, it was made clear that the corporate official was seeking legal advice in his or her individual' rather than in their representative capacity; (3) the corporate official must show that corporate counsel was willing to advise the corporate official in his or her individual capacity even though a possible conflict might arise; (4) the corporate official must show that his or her conversations with corporate counsel were confidential; and (5) the corporate official must show that the substance of the communications did not concern matters within the company or the general affairs of the company. Id. at 571. In accord Grand Jury Proceedings v. United States, 156 F.3d 1038, 1041 (10th Cir. 1998); United States v. Int'l Bhd. of Teamsters, 119 F.3d 210, 215 (2d Cir. 1997); Bevill, 805 F.2d at 125.

The dispute in this case involves communications between individuals who were officers and directors of Carolina Re and an attorney, who, though not actually employed by Carolina. Re,

sometimes functioned as attorney for Carolina Re. The dispute regarding these communications involves whether the individuals' assertion of the attorney/client privilege after the waiver of Carolina Re's attorney/client privilege by the Joint Provisional Liquidators prevents the disclosure of the communications between the individuals and the attorney.³

The initial issue is whether the default presumption arises with respect to communications that Mr. Sabbah or Mr. Kornfeld had with Mr. Edelman that were related to or concerned Carolina Re. The default presumption that an attorney is representing a corporation when the attorney gives advice to a corporate official applies where the attorney who is consulted is an attorney for the corporation at the time of the consultation. In the present case, Mr. Edelman argues that the default presumption is not applicable because he was never employed as corporate counsel for Carolina Re. While Mr. Edelman may never have been officially designated or employed as general counsel for Carolina Re, he admittedly did function as an attorney for Carolina Re on some occasions. In fact, the testimony was that his only involvement with Carolina Re was as a lawyer. Although Mr. Edelman was employed as general

³It is undisputed that to the extent that Carolina Re was entitled to invoke the attorney/client privilege regarding communications involving Messrs. Sabbah and Kornfeld, the privilege may be waived by the Joint Liquidators, which has occurred. Hence, Messrs. Sabbah and Kornfeld may not rely upon any attorney/client privilege that existed for Carolina Re prior to the waiver by the Joint Liquidator, and they do not claim to the contrary.

counsel by Fortress Re and paid by that corporation, both Fortress Re and Carolina Re were owned and controlled by the same shareholders, who also were officers and directors of both corporations. Mr. Edelman, of course, was consulted by those shareholders/officers/directors regarding matters related to Fortress Re. However, on other occasions, Mr. Edelman was consulted by those same shareholders/officers/directors regarding matters related to Carolina Re.⁴ In both situations, he responded with the requested advice or service and, therefore, at various times functioned as attorney for both companies. In describing his involvement with Carolina Re, Mr. Edelman stated: "With respect to Carolina Re in general, my only involvement was in response to solicited requests for action or advice. Matters were referred to me as they would be to an outside law firm on an item or individual basis." A reasonable inference from the testimony is that Mr. Edelman was acting as attorney for Fortress Re when he was

⁴In explaining his difficulty in answering a question as to whether an officer of Carolina Re ever consulted him for legal advice, Mr. Edelman stated:

"The problem is that persons who were officers of Carolina Re existed not simply in that sphere. They existed as persons affiliated and associated with Fortress Re. And those persons from time to time asked me for legal advice in all those capacities and in others. So when you say a person associated with Carolina Re or an officer of Carolina Re ever asking me for my legal opinion, the answer is yes. But it doesn't necessarily mean it had to do with Carolina Re." (P. 63).

consulted about matters related to Fortress Re and, in response, provided the requested legal services or advice regarding matters related to Fortress Re. Similarly, it is a reasonable inference that Mr. Edelman was acting as attorney for Carolina Re when he was consulted about matters related to Carolina Re and, in response, provided the requested legal services or advice. The record thus shows that Mr. Edelman's role when he was requested to perform services for Carolina Re or was consulted regarding matters related to Carolina Re was that of attorney for Carolina Re. The default presumption therefore arises as to such matters, and the question becomes whether Messrs. Sabbah and Kornfeld have made a sufficient showing to dispel the presumption that Mr. Edelman was representing Carolina Re at the time of communications with Messrs. Sabbah and Kornfeld related to Carolina Re.⁵ Answering this question involves examining the testimony of Mr. Edelman, since' the only evidence submitted in support of the attorney/client privilege claimed by Messrs. Sabbah and Kornfeld is the deposition testimony of Mr. Edelman. If such testimony is not sufficient to rebut the presumption, then the attorney/client privilege may not be invoked on behalf of Messrs. Sabbah and Kornfeld with respect to their communications with Mr. Edelman, regarding Carolina Re. Having

⁵Mr. Edelman was asked about communications that took place before Carolina Re came into existence. The court accepts the argument that the default presumption would not be applicable to such communications since Mr. Edelman would not have been acting as counsel for Carolina Re before it came into existence.

carefully weighed the testimony of Mr. Edelman, the court concludes that such testimony is insufficient to satisfy the five-part test discussed in Bevill and the other cases cited earlier and that Mr. Edelman therefore should be required to provide further testimony regarding the communications related to Carolina Be that have occurred between Mr. Edelman and Mr. Sabbah or Mr. Kornfeld.

It is, therefore, ORDERED, ADJUDGED AND DECREED as follows:

(1) Mr. Edelman is hereby ordered to be available for a further deposition and, except as provided in paragraph (2) below, shall answer fully and completely all questions regarding any communications between Mr. Edelman and Mr. Sabbah or between Mr. Edelman and Mr. Kornfeld regarding or related to Carolina Re, including any communications related to the business, assets or affairs of Carolina Re or related to the roles and functions of the officers and directors of Carolina Re, including Messrs. Sabbah and Kornfeld;

(2) Mr. Edelman shall not be required to testify to communications with Mr. Sabbah or with Mr. Kornfeld in which either Mr. Sabbah or Mr. Kornfeld sought legal advice from Mr. Edelman regarding their personal rights or liabilities unless such communications involved the business, affairs or assets of Carolina Re; and

(3) In the event of uncertainty on the part of Mr. Edelman as to whether communications are excepted from disclosure under

paragraph (2) above, Mr. Edelman may submit any such communications to the court for in camera inspection by the court.

This 10 day of December., 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge