



ORDERED in the Southern District of Florida on March 09, 2007.

**A. Jay Cristol, Judge
United States Bankruptcy Court**

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF FLORIDA**
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In re

Case No: 04-40306-BKC-AJC
Chapter 7 Proceeding

GERALD ZWIRN
SSN XXX-XX-4831

Debtor _____/

ORDER GRANTING MOTION TO STRIKE AMENDED SCHEDULE F

THIS CAUSE came before the Court on January 18, 2007 upon the motion to strike Debtor's Amended Schedule F filed by creditor Franklin Day (Day) (CP 163). The motion requests the Court strike Debtor's Amended Schedule F based on the Debtor's alleged bad faith related to its filing and based on the prejudice it causes to Day. Day asserts there is no economic purpose for the amendment, and the sole purpose for the amendment is to confer standing or party-in-interest status upon Joseph Passarelli (Passarelli), Debtor's former business partner, so that he may continue his litigation in

this Court against Day. The Court took the matter under advisement and instructed the parties to submit proposed memorandum decisions in support of their respective positions. Upon review of the submissions, the Court enters this opinion.

BACKGROUND

Debtor filed his voluntary petition under Chapter 7 of the Bankruptcy Code on November 2, 2004. At that time, the Schedule F filed identified 8 creditors with claims totaling \$3,566,395.00. Joseph Passarelli was not listed as a creditor in the originally filed Schedule F.¹ Schedule B of Debtor's initial filing identified an Accounts Receivable of "[n]otes totaling \$720,000 from several corporations and signed by Joseph Passarelli."

Approximately two years later, on October 27, 2006, the Debtor amended his Schedule F, adding Joseph Passarelli as a creditor. The description of Passarelli's alleged claim reads as follows:

Any alleged setoff or counterclaim against the two promissory notes in Schedule B, including claims for unpaid rents and sales tax or other matters arising out of the business relationship between Debtor and this creditor.

The amount of this alleged claim is stated as \$10,000. No date is provided for when this claim arose.

¹ Among the eight creditors listed by Zwirn is Day (for a judgment obtained by Day in 1999 in the amount of \$131,000) and W. Robert Curtis (for a claim of attorney's fees and costs in the amount of \$750,000). Both Day and Curtis filed Proofs of Claim. Later Zwirn would testify in a deposition taken by the Trustee that the primary reason he filed for bankruptcy was to get rid of the New York fraudulent action ("Well, I thought I never would get rid of Curtis [] unless I filed and wiped them out."). Excerpt of deposition transcript of Gerard Zwirn, March 2, 2005, pages 144-45, admitted as Trial Exhibit 31 on June 30, 2005, Adv. No. 05-1036.

Joseph Passarelli was not a creditor of this estate prior to the Debtor's amendment of Schedule F in October 2006. The record establishes that Passarelli never filed a Proof of Claim prior to the amendment, although he was fully afforded the opportunity to exercise this right,² and his attorney, Mr. Behar, did not file a Proof of Claim on behalf of Passarelli even after he was served with the Debtor's Amended Schedule F.

Notwithstanding the fact that he was not listed as a creditor or did not file a Proof of Claim in this case, Passarelli appeared during these proceedings to pursue the following:

A. On August 17, 2006, Passarelli filed a response in opposition to the Trustee's motion to approve a Stipulation he (the Trustee) had previously entered with Day allowing him to proceed with a judgment against Joseph Passarelli in the New York fraudulent conveyance action.

B. On September 20, 2006, Passarelli filed an Adversary Complaint and emergency motion seeking a Temporary Restraining Order on behalf of Joseph Passarelli. The Adversary Complaint named Day and his New York lawyer as defendants and claimed willful violation of the automatic stay by the continued prosecution of the New York fraudulent conveyance action against non-debtor Passarelli. The Temporary Restraining Order sought to restrain Day and his attorney from taking a judgment against Passarelli just days after this emergency motion was filed (ADV. CPs 1 and 2).

² Passarelli was represented sequentially by two New York attorneys beginning well before the Debtor's filing for bankruptcy on November 2, 2004. After the filing, both attorneys unsuccessfully sought to have the automatic stay afforded the Debtor herein extended to non-debtor Joseph Passarelli in a New York fraudulent conveyance case, an action that named the Debtor as a transferor and Passarelli as a transferee of a 1995 fraudulent conveyance.

C. On October 2, 2006, Attorney Behar noticed the deposition of Trustee Tabas seeking testimony on both his Stipulation with Day and the facts Passarelli alleged in his recently filed Adversary Complaint (ADV CP 20).

ANALYSIS

The threshold issue before the Court is whether it has discretion to disallow Debtor's amendment to Schedule F. Generally, the amendment process adheres to a rather "permissive approach". Federal Rule of Bankruptcy Procedure 1009 provides that a debtor may amend his schedules as a matter of course at any time before the case is closed. However, a court may deny leave to amend on a showing of the debtor's bad faith or of prejudice to creditors. *Matter of Doan*, 672 F.2d 831, 833 (11th Cir. 1982); *In re Green*, 268 B.R. 628, 655-56 (Bankr. M.D. Fla. 2001). Absent a showing of bad faith on the part of the debtor or prejudice to creditors, established by clear and convincing evidence, a court does not have discretion to deny a debtor's amendment to the schedules.

Bad Faith

Day seeks to strike Debtor's Amended Schedule F on the basis that the amendment was filed solely to provide retroactive standing to Joseph Passarelli in this bankruptcy case so that he may maintain his existing litigation against Day (and the Trustee) in this forum. Day argues that the absence of any other reason for the amendment constitutes bad faith. The Court agrees.

The timing of the filing of the amendment supports the proposition that the sole reason for its filing was to give legal standing to Passarelli. First, when Passarelli filed his objections to the Trustee's motion for this Court to approve his Stipulation with Day, the Trustee moved to strike the objection based on Passarelli's lack of standing and the

fact that he was not a party in interest. The Trustee cited to this Court its ruling in *In re E.S. Bankest, L.C.* for a definition of “legal interest” and for the proposition that the Court should not allow legal interests to be created as a litigation tactic. 321 B.R. 590, 594 (Bank. S.D. Fla. 2005). Likewise, on September 20, 2006, when Passarelli filed his Adversary Complaint against Day and his New York attorney, Day argued he had no legal interest in the main case, and lacked standing to bring this new action at this time. Finally, on September 29, 2006, when Attorney Behar noticed the deposition of the Trustee and sought the production of his files relative to the Stipulation with Day and the many issues related to the Adversary Complaint, the Trustee moved for a protective order arguing that Passarelli is not a party in interest and lacks standing. The Debtor’s amendment, following the filings and the colloquies in Court relative to the standing issue and party-in-interest status, emits a bad odor that does not pass the smell test, indicating that the amendment to Schedule F was filed for no other purpose than to provide standing to Passarelli so that he may prosecute his objection and other claims in this Court. Without such amendment, Passarelli would have no standing to object to the settlement in this case or to otherwise seek discovery or reap the protections of the bankruptcy laws.

The intended effect achieved by the Debtor’s Amended Schedule F is the creation of a legal interest for Passarelli and thus (i) his standing in this Court to object to a Stipulation between Day and the Trustee that would allow the continued prosecution of the New York fraudulent conveyance action, (ii) his standing to commence an Adversary Complaint against Day and his New York attorney in this bankruptcy case seeking a preliminary injunction, and (iii) his standing to take extensive discovery against the

Trustee. Without the Amended Schedule F, Passarelli would not be permitted to use the jurisdiction of this Court for these legal actions. Because Passarelli does not have standing without the amendment, its filing appears to be an act of bad faith intended as a litigation tactic in this case. The amended schedule has only one practical effect: it creates rights for Passarelli that otherwise would not exist.

The rule of this jurisdiction is that while a Debtor may generally amend his original filing without leave of Court, where an amendment is made in bad faith the Court may strike it. *In re Talmo*, 185 B.R. 637 (Bank. S.D. Fla. 1995). See also *In re Kauffman*, 299 B.R. 641 (Bank. S.D. Fla. 2003). When analyzing the possible bad faith basis of an amendment, the focus by the Court should be on the “debtor’s purpose.” *Talmo* 185 B.R. at 648. Here, the Court finds no economic purpose for the amendment. The only purpose served by the amendment is the creation of rights for Passarelli, the Debtor’s former business partner, so that he may continue his litigation in this Court. However, litigation between 2 non-debtor parties – one who was listed as a claimant and the other who has never appeared in the case as a claimant – is not permitted in this Court and neither is the Debtor’s attempt to circumvent the standing issue by the amendment. An amendment to a schedule will not be allowed where it does not appear that error or mistake was made or where the failure was unintentional or where the amendment if allowed will be of no value to the debtor. See *In re Powers*, 339 F.Supp. 1068 (W.D. Ark. 1972).

In this case, the Debtor and Passarelli have known each other since long before the Debtor filed his case. At no time prior to the standing issue being raised did either one of them record a claim by Passarelli against the Debtor. The Court gave the Debtor

the opportunity to explain the amendment; but instead of persuading this Court in its memorandum that the omission of Passarelli was inadvertent or unknown, the Debtor relied on the “permissive approach” to schedule amendments set forth in the Federal Rules of Bankruptcy. The Debtor’s argument suggests the Court rely on the docket in this case which simply shows that the Debtor added this creditor prior to discharge and complied with Rule 1009(a) of the FRBP and Rule 1009-1C of the Local Rules. This is not enough to rebut the evidence already of record which indicates the amendment to Schedule F was proposed for the improper purpose of conferring standing upon Passarelli.

Prejudice to Day

In addition to finding bad faith in the filing of the amendment, the Court finds Day has been prejudiced by the Debtor’s Amended Schedule F. Day proceeded against Passarelli in the New York action, relying upon the original filing of the Debtor which did not identify Passarelli as a creditor or as a person having any legal interest in the bankruptcy action. Day and his attorney expended hours of time at a great cost to Day seeking permission from the Trustee to continue the action against Passarelli as a non-debtor and non-creditor in the New York Action. Less than three weeks after Debtor filed, the Trustee indicated to Day that the stay did not apply to non-debtors and he was free to pursue them. It appears the Trustee, at that time, considered the New York action to be nothing more than litigation between two non-debtors. So too, the New York State Court took the same position as the Trustee [that the stay did not apply to non-debtors]. Based on the position of the Trustee and the decision of the New York Court, Day actively prosecuted the New York fraudulent conveyance action for the next two years.

The extent of that prosecution is presented to this Court by two affidavits submitted by Passarelli's own New York attorneys, Richard L. Aronstein, Esq. and Michael McQuade, Esq. Mr. Aronstein acknowledges that "[t]he purpose of []his affidavit is to describe to this Court the events that have occurred in the New York action since the commencement of the instant bankruptcy action." (ADV CP 3). Mr. Aronstein goes on to present 38 detailed paragraphs about the prosecution by Day and his defense of it which he states entails "no less than 72.5 hours in defending the New York action after November 2, 2004 – the date of the Zwirn bankruptcy filing." (ADV CP 3). Likewise, Mr. McQuade provided a detailed analysis of the extensive work he did in response to the prosecution by Day of the New York fraudulent conveyance action after Debtor's filing (ADV CP 4). From a review of the two affidavits, it appears that the litigation by Day against Passarelli as a non-debtor and non-creditor was extensive and continued for two years.

Thus, when Debtor amended his Schedule F two years after his initial filing and shortly after moving for an order of discharge, Passarelli was afforded new rights that completely changed the rights of Day as a creditor and completely changed his litigation posture. Not only has Day expended substantial sums for legal fees and costs, but he now must provide a defense in the legal actions taken by Passarelli in this Court. Prejudice is recognized as a basis for striking a debtor's amendment in the Southern District of Florida. In *Talmo*, sufficient prejudice was found to justify denying an amendment by a showing that the litigation posture of a party in interest was harmed. 185 B.R. at 645. When determining whether to deny an amendment based on prejudice to a creditor or party in interest, the focus of the Court is on the "effect" of allowing the amendment. *Id.*

Here, if the amendment is allowed, Passarelli would obtain the legal status of a creditor. This standing, conferred *only* by the Amended Schedule F, requires Day to defend litigation on three legal actions brought by Passarelli when he would not otherwise have to do so if standing were not conferred by Debtor's amendment. Clearly, this constitutes substantial prejudice to Day.

Other jurisdictions which have followed the rule of striking an amendment where it is prejudicial to a creditor offer some additional guidance. For example, in *In re Carley Capital Group*, the court offers a four-part analysis to determine the nature of the alleged prejudice. 138 B.R. 50 (W.D Wis. 1991). The court addressed whether an adverse party's rights will be prejudiced if the amendment is allowed, whether not allowing the amendment will cause undue hardship to a debtor who has acted in good faith, whether there is a reasonable excuse for not identifying the claim on the original schedule, and whether there is a reasonable excuse for the delay in seeking the amendment. *Carley*, 138 B.R. at 50. Under this four-part analysis, the Debtor's amendment must be stricken. Striking the amendment will cause no hardship to the Debtor given that he has obtained his discharge and Passarelli never chose to file a claim in the case, having had full knowledge of the bankruptcy filing. No reasonable excuse, actually no excuse at all, has been offered by the Debtor for not identifying Passarelli's claim at the time of the original filing and there has been no proffer as to why Passarelli was added as a creditor two years after his original filing.

CONCLUSION

The existence of bad faith and prejudice each provide an independent and sufficient basis to strike a debtor's amendment. "Bad faith is a separate ground for

disallowing an amendment to schedules, independent of the prejudice issue” and each is sufficient by itself. *Talmo*, 185 B.R. at 648. Here, there is clear and convincing evidence of both bad faith and prejudice relative to the filing of the Debtor’s Amended Schedule F. The Court is persuaded the filing of the amendment was accomplished for the improper purpose of conferring standing on Passarelli in this Court so that he may pursue litigation in this case.

The Court also believes the extreme prejudice to Day warrants striking the amendment, especially in light of it having no impact on the Debtor and little, if any, impact on the bankruptcy estate. The failure of the Debtor and his attorney to provide a reasonable excuse, or any excuse at all, for not including this claim in the original filing or providing a reasonable excuse, or any excuse at all, for why it took two years to list it, further strengthens this Court’s view that the filing is sufficiently prejudicial to Day and warrants being stricken.

For the foregoing reasons, it is

ORDERED AND ADJUDGED that the motion to strike Debtor’s Amended Schedule F filed by creditor Day (CP 163) is GRANTED and Amended Schedule F is STRICKEN and DISALLOWED.

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Copies furnished to:

W. Robert Curtis, Esq.
David B. Javits, Esq.
Brian S. Behar, Esq.
Joel L. Tabas, Trustee
Ariel Rodriguez, Assistant U.S. Trustee