UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

In re:	)	Chapter 13
	)	
James Thigpen,	)	Case No. 17 B 10161
	)	
Debtor.	)	Judge Jacqueline P. Cox

Order on Remand - Ruling on SSA
Motion for Relief from Automatic Stay (Docket 11)
Amended on April 22, 2019 Nunc Pro Tunc

This matter is before the court on remand from the District Court's September 30, 2018 order disposing of the Debtor's appeal.

The District Court ruled that the recoupment doctrine does not apply herein and for that reason retention of Thigpen's Old-Age, Survivors, and Disability Insurance ("OASDI") benefit to cover overpayments under another Social Security Administration ("SSA") program is subject to the automatic stay.

The District Court ordered that the Government's Motion for Relief from Stay be ruled on; this order does that.

The Automatic Stay

Filing a bankruptcy case operates as an automatic stay applicable to all entities of acts to collect or recover a claim against the debtor that arose before the commencement of the bankruptcy case. 11 U.S.C. § 362(a). The right of setoff allows entities that owe each other money to apply their mutual debts against each other, avoiding "the absurdity of making A pay B when B owes A." *Studley v. Boylston Nat. Bank of Boston*, 229 U.S. 523, 528 (1913). The setoff of any debt owing to the debtor that arose pre-petition against any claim against the debtor

is, however, stayed by the automatic stay. *Citizens Bank of Md. v. Strumpf,* 516 U.S. 16, 20 (1995) (Section 362 imposes a restriction upon when an actual setoff may be effected, not during the automatic stay). In *In re Quade*, 482 B.R. 217, 229 (Bankr. N.D. Ill. 2012) the court noted:

> "While the Bankruptcy Code preserves the right of setoff, 11 U.S.C. § 553, the express provisions of the automatic stay . . . make clear that no postpetition setoff is permissible without relief from the stay. 11 U.S.C. § 362(a)(7). Because no relief from stay has been granted with respect to this matter, no postpetition setoff should have occurred. Had such setoff occurred without relief from stay, the act would be potentially sanctionable under section 362(k) of the Bankruptcy Code. 11 U.S.C. § 362(k). Further, such an act would be void as a matter of law." (citations omitted).

A creditor wishing to retain funds it owes a debtor in bankruptcy may seek relief from the automatic stay under 11 U.S.C. § 362(d) which states that the automatic stay may be terminated, annulled, modified or conditioned for cause, including the lack of adequate protection of an interest in the property of such party in interest, or if the debtor does not have equity in such property and such property is not necessary to an effective reorganization. 11 U.S.C. § 362(d)(1) and (2).

The burdens of proof with respect to stay relief motions are provided for in section 362(g): "the party requesting such relief has the burden of proof on the issue of the debtor's equity in property and the party opposing such relief has the burden on all other issues." 11 U.S.C. § 362(g)(1) and (2).

The SSA has not shown that the automatic stay should be modified or terminated for cause or for lack of adequate protection. The confirmed modified plan provides for monthly payments to SSA; it has not been shown that the payment amount fails to provide adequate protection. With respect to whether the Debtor has equity in such property, the court finds that

the record does not include sufficient information to address this issue.

The court finds, however, that the property is necessary to an effective reorganization under chapter 13 of the Bankruptcy Code (the burden of proof of this falls on the Debtor) and notes that the SSA did not object to confirmation of the modified plan.

Res Judicata

As noted in this court's June 16, 2017 order at Docket 30 on the SSA's Motion to Confirm that the Automatic Stay Does Not Apply, etc., the parties have not raised the res judicata doctrine. Under that doctrine a final judgment on the merits bars further claims by parties or their privies based on the same cause of action. *Montana v. U.S.*, 440 U.S. 147, 153 (1979). To establish this defense a party has to demonstrate that (1) a final judgment on the merits was rendered by a court of competent jurisdiction; (2) that the claims raised in the subsequent action were identical to those decided in the prior action and (3) that the prior action involved the same parties or their privies. *Retired Chicago Police Association v. City of Chicago*, 7 F.3d 584, 591 (7th Cir. 1993).

The October 29, 2009 judgment in the criminal case is a final judgment on the merits regarding the Debtor's obligation to pay the restitution award at 10% of his monthly income. The SSA claim herein is based on the identical claim ruled on in 2009, the imposition and collection of the $49,327.17 restitution award. The parties are the same - the government and the Debtor.

The SSA is barred from re-litigating the terms under which the Debtor has to repay the obligation in issue. It could have asked the District Court in 2009 to order that all future benefits due to the Debtor be withheld until the obligation was satisfied.

Laches

Laches is based on the notion that those who sleep on their rights, lose them. It addresses delay in the pursuit of a right when a party must assert that right in order to benefit from it. For laches to apply the party asserting the defense must demonstrate an unreasonable lack of diligence by the party against whom the doctrine is asserted and prejudice arising therefrom. The SSA could have earlier sought withholding of all of the Debtor's benefits until the restitution award was satisfied and it could have objected to the plan before it was confirmed. The government chose to rely on the recoupment doctrine which the District Court has rejected.

The debtor can show prejudice. Either he supports himself by having part of his monthly benefit satisfy the SSA overpayment obligation as provided for in the confirmed plan, or have all of it satisfy the SSA overpayment obligation. Clearly, he would be prejudiced if required to forego the entire benefit. His Amended Schedule I of Income discloses that he has monthly income of a $968 SSA benefit and a $665 contribution from a son. Docket 24, p. 2.

Recoupment

Property subject to recoupment is exempt from the automatic stay. *United States v. Consumer Health Services of Am., Inc.,* 108 F.3d 390, 395 (D.C. Cir. 1997) (The recoupment exception depends on whether the creditor's and debtor's claims arise out of the same transaction. The recoupment doctrine exempts a debt from the automatic stay when the debt is inextricably tied up in the post-petition claim.). *In re B & L Oil*, 782 F.2d 155, 156 (10th Cir. 1986).

The Debtor received, via fraud, overpayments under the Supplemental Security Income program ("SSI") under Title XVI of the Social Security Act ("Act") while he is now receiving

OASDI benefits under Title II of that act. Section 404 of the act covers recovery of SSI benefits; section 1320b-17 of the act governs recovery of the benefits that the Debtor now receives. Section 1320b-17 allows the SSA to withhold funds without regards to a limit that applies to situations where the recipient is not at fault for the overpayment.

The District Court pointed out that the circumstances here are more analogous to cases where the parties' obligations arise out of different contracts, circumstances that typically do not give rise to a recoupment defense. *In re Thigpen,* 590 B.R. 810, 816 (N.D. Ill. 2018) (citation omitted).

The District Court noted that section 1320b-7 allows for cross-program cost recovery - permitting SSA to withhold OASDI payments to recover prior SSI overpayments while the statutes in *Consumer Health* and *Wernick* allowed withholding only where the prior and ongoing payments were made pursuant to the same program. *Id.,* (citing *Consumer Health,* 108 F.3d at 394; *Wernick,* 2016 WL 7212508, at *2).

The District Court concluded that the parties' obligations in this case do not arise under the same program or statute - the SSI program is administered by the states, whereas the OASDI program is administered by the SSA. It was also pointed out that the programs are funded separately, have different eligibility criteria and serve different populations. Payroll taxes fund the OASDI program while Congress appropriates funds from general revenue for the SSI program. For that reason the defense of recoupment does not lie. However, setoff is available.

Section 1320b-17 allows but does not require SSA to withhold the maximum amount of current benefits under one Social Security program to recover a past overpayment under another Social Security program, even where the overpayment arose from the recipient's fraud. For that

reason "SSA's withholding of Thigpen's OASDI benefits to recover its prior SSI overpayments is a setoff not a recoupment, and therefore that SSA's withholding is not exempt from the automatic stay." *Thigpen*, 590 B.R. at 818.

Setoff in Bankruptcy

The right of setoff is of equitable origin, designed to facilitate the adjustment of mutual debts. The Bankruptcy Code does not create a federal setoff right. It provides, however, that "this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor . . ." 11 U.S.C. § 553(a). The Supreme Court has held that "any right of setoff that a creditor possessed prior to the debtor's bankruptcy filing is not affected by the Bankruptcy Code." *Citizens Bank of Md.*, 516 U.S. at 20. Generally, Bankruptcy Code Section 506(a) provides that a creditor holding a valid right of setoff is to be treated as the holder of a secured claim to the extent of the amount subject to setoff. A creditor asserting the right to set-off in bankruptcy must establish that (1) it has a right of setoff under nonbankruptcy law and (2) this right should be preserved in bankruptcy under the Bankruptcy Code's setoff provision. However, trial courts have discretion to allow or disallow setoff. *In re Faasoa*, 576 B.R. 631, 638 (Bankr. S.D. California 2017). "Setoff will not be permitted when it would be inequitable or contrary to public policy to do so." *In re Hal, Inc.*, 122 F.3d 851, 854 (9th Cir. 1997).

The Bankruptcy Code recognizes the right to setoff where:

(a) the creditor holds a claim against the debtor that arose before the commencement of the case;
(b) the creditor owes a debt to the debtor that arose before the commencement of the case;
(c) the claim and debt are mutual; and
(d) the claim and debt are valid and enforceable.

11 U.S.C. § 553(a).

The SSA's claim arose in 2009 when the restitution provision was included in the judgment order resolving the criminal case; its claim arose pre-petition. The SSA owed the Debtor OASDI benefits before the bankruptcy case was filed; the SSA owed the Debtor benefits pre-petition.

The Bankruptcy Code does not define what mutuality means in the context of setoff of debts. That requirement mandates that the parties' claims be between the same parties and that they act in the same capacity. A claim against a bankrupt as an administratrix can not be set off against a debt owing to the bankrupt as an individual. *Allegaert v. Perot*, 466 F.Supp. 516, 518 (S.D.N.Y. 1978). A claim against a creditor for damages to property belonging to the debtor's assignee cannot be set off against the creditor's claim against the bankrupt estate. *Id.* Although the parties' claims arose under different programs, they are mutual as they arose between the same parties - the SSA and the Debtor, and in the same capacities, in that neither acted as a representative of others when the debts were incurred.

The debts are enforceable.

The Bankruptcy Code also requires that the obligations be owed in the same right, i.e., that joint obligations are not subject to setoff against separate debts.

Until February 2017, the SSA paid the Debtor OASDI benefits for several years without deducting amounts pursuant to the restitution order for the SSI overpayment. U.S. Memorandum in Support of Motion to Confirm that the Automatic Stay Does Not Apply to Recoupment, etc. (Docket 12, p. 3). This delay may justify a finding of laches.

Lack of Pre-Confirmation Objection

Where a creditor receives notice of the filing and contents of a debtor's chapter 13 plan, such notice satisfies the creditor's due process rights and the bankruptcy court's confirmation order binds the creditor who does not object pre-confirmation. *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010).

Bankruptcy Rule 3015(f) provides:

> An objection to confirmation of a plan shall be filed and served on the debtor, the trustee, and any other entity designated by the court, and shall be transmitted to the United States trustee, at least seven days before the date set for the hearing on confirmation, unless the court orders otherwise. An objection to confirmation is governed by Rule 9014. If no objection is timely filed, the court may determine that the plan has been proposed in good faith and not by any means forbidden by law without receiving evidence on such issues.

Federal Rule of Bankruptcy Procedure 3015(f).

On April 12, 2017, the SSA filed a Motion to Confirm that the Automatic Stay Does Not Apply to Recoupment or, Alternatively, for Relief from the Automatic Stay as a Setoff to its non-dischargeable debt against the Debtor. The District Court has ruled that recoupment does not lie herein.[1]

The Debtor filed his Plan the next day, April 13, 2017. Docket 13. A modified plan was filed on May 10, 2017. Docket 22.

The Debtor's Modified Plan proposed to pay the SSA 17.5% of its allowed amount, for a total of $6000 as a specially classified unsecured claim due to the restitution order. Modified Plan, Docket 22, Section E 7, page 3. The SSA did not object to the plan as allowed by Section

[1]A different District Judge has ruled that recoupment is not available in a similar situation. *See Johnson v. United States of America (In re Johnson)*, 586 B.R. 449 (N.D. Ill. 2018).

1324(a) of the Bankruptcy Code: "A party in interest may object to confirmation of the plan." It was understandably arguing that the automatic stay did not stay its recoupment obligation. However, the District Court has dispensed with that position, finding that recoupment does not lie herein.

Conclusion

The automatic stay will not be lifted. The movant has not shown that the Debtor lacks equity in the property in issue, his SSA benefit, nor has it shown that the property interest is not necessary to an effective reorganization. The SSA is protected while the monthly payments are being made toward the Debtor's non-dischargeable debt.

The court finds that it would be inequitable to now modify the automatic stay when the government could have sought 100% of the Debtor's future benefits at the 2009 sentencing on the criminal charge or pre-confirmation.

In the exercise of its discretion, the court denies the Motion for Relief from the Automatic Stay.

Date: March 20, 2019

ENTERED:

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Jacqueline P. Cox
United States Bankruptcy Judge