

RETHINKING RECOUPMENT: ARE WE REALLY SURE IT'S NOT A SUBSET OF SETOFF?

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INTRODUCTION

Recoupment can slice through the Bankruptcy Code¹ like a knife through butter. Stronger than setoff, recoupment has been held to be exempt from the automatic stay,² unregulated by section 553,³ and resistant to the avoiding powers.⁴ It derives this extraordinary power from case law that relies on its not being mentioned in the Bankruptcy Code. Unmentioned by the Code apparently means ungoverned by the Code. But this lack of express statutory recognition sometimes leads to inconsistent results. Two decisions last year emanating from the Kmart bankruptcy case demonstrate that there is a cost to recoupment's having no grounding in the Code: It was struck as an affirmative defense to a preference action.⁵ Although these decisions reached the wrong result, the basic thrust of their analysis seems undoubtedly correct: There is no place in the Bankruptcy Code for an unenumerated exception to preference liability.

Beyond the issue of preference liability, what place is there for an equitable doctrine that sometimes looks like a setoff and acts like a setoff but will not be restricted like a setoff? This article proposes that recoupment be considered as a species of setoff. This proposal is not offered merely as a way to deal with the problem of a missing preference defense. By treating recoupment as a special case of setoff, the courts can properly incorporate the doctrine within the confines of the Code, rather than tolerate an out-law that often seems to defy the Code's authority with impunity.

RECOUPMENT AND SETOFF: THE STANDARD VIEW

The Supreme Court has observed that the "right of setoff . . . allows entities that owe each other money to apply their mutual debts against each other, thereby avoiding 'the absurdity of making A pay B when B owes A.'"⁶ Section 553(a) of the Bankruptcy Code preserves and regu

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lates mutual, prepetition setoffs.⁷ The key feature in permissible setoffs is “mutuality.”⁸ This requirement not only ensures that setoffs are bilateral, rather than triangular or multilateral;⁹ it reinforces the conditions imposed under state law that the opposing obligations be between the same parties, acting in the same capacities, and in the “same right.”¹⁰ Typically, in a setoff, the mutual debts arise from different transactions.¹¹

In contrast, recoupment traditionally requires that the opposing demands arise from the same transaction.¹² Recoupment is thus viewed as being essentially a defense, a mechanism for determining the proper liability on a plaintiff’s claim.¹³ It has its origin in an equitable rule of joinder, permitting the adjudication in one action of countervailing claims that arise out of the same transaction.¹⁴ Its modern counterpart in federal practice is the compulsory counterclaim.¹⁵ Setoff, too, originated as a rule of joinder,¹⁶ the modern federal version of which is the permissive counterclaim.¹⁷ Because the demands in recoupment arise out of the same transaction, recoupment is viewed as not requiring setoff’s “mutuality.”¹⁸

In the typical recoupment case, the creditor has in some sense overpaid or overadvanced sums to the debtor.¹⁹ When the debtor then delivers goods or renders services expecting payment, the creditor “recoups” the prior overpayment or advance by not paying for the subsequently delivered goods or services.²⁰ To reach equitable results, the single transaction rule has been stretched to allow recoupment in bankruptcy cases involving the same “set of transactions.”²¹

The significant fact about recoupment for purposes of bankruptcy is that it is nowhere mentioned in the Bankruptcy Code. Because of the historical differences between setoff and recoupment, courts have felt unburdened by the Code’s regulation of setoff in dealing with the equitable doctrine of recoupment.²² Thus courts have felt free to hold that the automatic stay does not apply to recoupment²³ and neither do the avoiding powers.²⁴ Perhaps most important, courts generally hold that a creditor may use a prepetition overpayment or overadvance to recoup against a debtor’s postpetition delivery of goods and services.²⁵ In light of the power of this doctrine, courts have noted that, as an equitable remedy, recoupment should not be allowed when inequity would result.²⁶

KMART AND UNENUMERATED PREFERENCE DEFENSES

Last year’s *Kmart* decisions²⁷ provide the catalyst for the reexamination of the recoupment doctrine in bankruptcy. The background for these cases is simple: there are no facts to reckon with. *Kmart* sued to recover a preference, and the defendant filed an answer with several affirmative defenses, including setoff and recoupment. *Kmart* then

moved to strike some of these defenses as insufficient as a matter of law.²⁸ The bankruptcy court granted the motion in part, striking the setoff and recoupment defenses as not being either among the enumerated affirmative defenses in section 547(c) or what the court called “threshold defenses.” In the bankruptcy court’s view, “threshold defenses” bar recovery without considering the merits of the substantive claim for relief. They are either procedural, such as lack of jurisdiction, or otherwise prevent recovery, such as *res judicata* or release. Prior to striking the setoff and recoupment defenses, the court declined to strike the waiver and estoppel defenses as insufficient, considering them to be “threshold defenses.” These defenses were nevertheless struck as inadequately pleaded but leave to replead was granted.

The bankruptcy court granted Kmart’s motion to strike setoff and recoupment as affirmative defenses. It held that section 547(c) provides the exclusive affirmative defenses to the merits of a preference action.²⁹ The court reasoned that, under principles of statutory construction, when Congress enumerates exceptions to a general provision, additional exceptions may not be implied in the absence of a contrary legislative intent.³⁰ Setoff and recoupment are not enumerated defenses. The court also concluded that they are not “threshold defenses,” because they necessarily require an analysis of the parties’ underlying transactions that go to merits of the preference claim. Thus the bankruptcy court struck the setoff and recoupment defenses.³¹

The defendant sought leave to appeal to the district court. It argued that the district court should allow the interlocutory appeal³² because the defendant could satisfy the requirements applicable to interlocutory appeals from district courts to the courts of appeal, including “a controlling question of law as to which there is substantial ground for difference of opinion.”³³ The district court denied leave to appeal. It held that, on the controlling question of law at issue, there was no difference of opinion about whether section 547(c) provides the exclusive affirmative defenses to the merits of a preference action.³⁴

THE OVERLOOKED STATUTORY DEFENSE FOR SETOFF

Regrettably, neither the bankruptcy court nor the district court addressed an express statutory defense that applied to Kmart’s defendant. Section 553(a) clearly states: “Except as otherwise provided in this section and in sections 362 and 363 of this title, this title does not affect any right of a creditor to offset a mutual debt . . .” Thus section 547, the preference section, like all other sections of the Bankruptcy Code except for sections 362 and 363, is subject to the preservation of valid setoffs in section 553. That means that if a setoff is validly preserved under section 553, it cannot be avoided as a preference.³⁵ Therefore, a contention that

a claimed preference is actually a validly preserved setoff ought to be a proper defense, even though it is not enumerated in section 547(c) or considered to be a “threshold defense.”

IS THERE ANOTHER STATUTORILY-BASED DEFENSE FOR RECOUPMENT?

There is a frequently articulated defense, which has support in the case law, that a setoff is not a transfer.³⁶ This defense is based on the absence of the term “setoff” in the Bankruptcy Code’s definition of “transfer” in section 101(54),³⁷ and the statement in the legislative history that such absence was intentional for the purpose of making setoffs subject to other rules,³⁸ namely those set forth in section 553.³⁹ The statutory supremacy of validly preserved setoffs in that section makes this defense unnecessary for setoffs themselves. Nevertheless, it is worthwhile asking whether this defense is available for recoupment, since “recoupment” is likewise not mentioned in the definition of “transfer.” If a recoupment is not a “transfer,” then it cannot be avoided as a preference. Moreover, this defense is not an unenumerated affirmative defense; it negates one of the elements of the claim for relief.

In the normal sense of the word “transfer,” a typical recoupment does not qualify. This is because a typical recoupment is simply the refusal to pay the entire amount of a rendered bill. The refusal stems from either an overpayment of an earlier bill or some other overadvance. By not paying, nothing is transferred. Unfortunately, the ordinary understanding of things does not govern when there is a statutory definition of a term. Congress has defined “transfer” for purposes of the Bankruptcy Code, and this definition must be applied to recoupment in the context of a preference action.

Excluding the examples, the statutory definition is “every mode, direct or indirect, absolute or conditional, voluntary or involuntary of disposing of or parting with an interest in property.”⁴⁰ This definition, like all other unambiguous statutory provisions, must be construed in accordance with its plain meaning.⁴¹ Courts have no authority to enforce a principle of interpretation that is found solely in the legislative history and not in the statutory text itself.⁴²

With these interpretative injunctions in mind, it is difficult not to include recoupment-and setoff, too-within the plain meaning of “every mode, direct or indirect, absolute or conditional, voluntary or involuntary of disposing of or parting with an interest in property.” It is not the fact of nonpayment that constitutes the disposition of the property within the statutory definition. Rather, it is the debtor’s “involuntary . . . parting with an interest in property” that occurs when the debtor’s

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right to payment of a just debt is taken away by the recouping party.⁴³ This is more clearly seen in the context of setoff, because the Supreme Court has defined the steps that must be taken for a setoff to occur: “(i) a decision to effectuate a setoff, (ii) some action accomplishing the setoff, and (iii) a recording of the setoff.”⁴⁴ There seems to be little reason why the same three steps - decision, action, record - should not be applied to recoupment. Whether or not the same three-step process is required, something must happen to establish, at least so far as the creditor is concerned, that the parties’ accounts have been permanently adjusted. Indeed, it is the lack of permanent adjustment that the Supreme Court relied on in distinguishing a postpetition “administrative freeze,” which did not violate the automatic stay, from a postpetition setoff, which would violate the stay.⁴⁵ Whenever the creditor contends that a permanent adjustment of accounts has occurred, whether by setoff or recoupment, so does a “transfer.” There are no exceptions to the statutory definition, the discussion in the legislative history with regard to setoffs notwithstanding. Consequently, the defense that a recoupment is not a transfer must fail.

It should be noted that, although the definition of “transfer” has been reformatted by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, the part of the definition on which the above argument relies has not been changed.⁴⁶ And there are still no exceptions.

Since a recoupment is a transfer, the question remains whether the transfer satisfies all the elements of a preference. It seems fairly straightforward that the transfer is to a “creditor”⁴⁷ and that it is on account of “antecedent debt.”⁴⁸ The requirements of the transfers occurring while the debtor was insolvent⁴⁹ and during the preference period⁵⁰ present factual issues for which recoupment receives no special exemption. The best candidate for a recoupment defense is the so-called “greater percentage” test in section 547(b)(5).⁵¹ This requirement involves a comparison between the recovery that the creditor actually received on its claim from the transfer and what would have been distributed to such creditor in a hypothetical chapter 7 case had the transfer not been made. If the actual recovery is better than the hypothetical one, then this requirement is satisfied.

If the recoupment had not occurred, what would happen in a hypothetical chapter 7 case? The answer is not that the creditor would have paid the full amount claimed by the debtor. Rather, the same nonpayment of the debtor’s debt would have taken place. The difference is that the nonpayment would be temporary, a sort of “administrative freeze,” rather than represent an intentional decision by the creditor to make permanent adjustment of the accounts between the parties.⁵² The debt to the

debtor would still be owing, and the right to recoup would still exist postpetition. Therefore, under existing law, the recoupment could be accomplished postpetition against a demand for payment by the hypothetical chapter 7 trustee. The hypothetical recovery is therefore equal to the actual one, and the “greater percentage” test fails. The result, consistent with the Supreme Court’s dicta,⁵³ is that no preference has occurred.

The same analysis applies equally to a properly preserved setoff under section 553. Indeed, the argument is even clearer for such a setoff because, in the hypothetical chapter 7 case, section 542(b) permits the same postpetition setoff that might have been challenged as preferential had it occurred during the preference period.⁵⁴ Such analysis, however, is totally unnecessary for such setoffs, because section 553 “trumps” section 547.

IMPLICATIONS FOR RECOUPMENT

So far as the ability to use setoff and recoupment as defenses to a preference action is concerned, the *Kmart* decisions are clearly wrong. Nevertheless, these decisions highlight the problems in treating the uncodified doctrine of recoupment in bankruptcy. The problem with the courts’ analysis with respect to setoff is easily demonstrated. With respect to recoupment, revealing the decisions’ flaws requires a much more detailed examination. Yet, what is critical to bear in mind is that, despite their flaws, the analytical framework of these decisions is essentially correct. As a matter of statutory interpretation, except for the so-called “threshold defenses,” which do not involve analysis of the transaction complained of, there ought to be no exceptions to preference liability other than the ones that Congress put into the Code.

The notion of an uncodified, equitable exception to preference liability is reminiscent of the discussion that took place in the original *Deprizio* result.⁵⁵ All courts of appeals that addressed the issue determined that there could be no uncodified, equitable exception to insider preference liability for noninsiders.⁵⁶ The same result should obtain here. As the Supreme Court has stated with respect to “equitable arguments,” “whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.”⁵⁷

IS RECOUPMENT REALLY EXEMPT FROM THE AUTOMATIC STAY?

The *Kmart* decisions provide both a stimulus and an excellent analytic framework to examine a piece of received wisdom about recoupment that it is not subject to the automatic stay. This result seems to stem from two theories that distinguish recoupment from setoff. One is that recoupment is not a claim but instead a defense.⁵⁸ The other is that funds subject to recoupment are not viewed as property of the debtor’s estate or,

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stated differently, property in which the estate has no interest.⁵⁹ Nevertheless, these theories run into problems when confronted with specific provisions of the Code.

If recoupment is not a setoff, then the specific automatic stay provision addressed to setoff, section 362(a)(7),⁶⁰ does not apply. Nevertheless, two other provisions are implicated, and at least one of them is applicable. Section 362(a)(6) automatically stays “any act to collect, assess or recover a claim against the debtor that arose before the commencement of the case.”⁶¹ As demonstrated above, recoupment is a “transfer,”⁶² which requires the recouping creditor to make a permanent adjustment in the parties’ accounts. It is difficult not to consider this an “act,” which has been defined as “anything done, being done or to be done”⁶³ and “external manifestation of actor’s will.”⁶⁴ It is also evident that what is being recouped is a “claim.”⁶⁵ Consequently, so long as the claim is one that “arose before the commencement of the case,” recoupment, which is an “act” to “recover” a “claim,” is automatically stayed by section 362(a)(6).⁶⁶ It may also be an “act . . . to exercise control over property of the estate,” such property consisting of the debtor’s right to collect payment of its debt and therefore automatically stayed by section 362(a)(3).⁶⁷ The Supreme Court considered these two provisions as well in holding that an “administrative freeze” was not a stay violation. The determining factor for making these provisions inapplicable to the “administrative freeze,” just as it was for the provision forbidding setoff, was that the “freeze” was temporary.⁶⁸ Not so with a recoupment, which is intended to be permanent. Similarly, these provisions cannot be circumvented by viewing recoupment as a defense. However useful such treatment might be outside of bankruptcy, it cannot contravene the Code’s definition of “claim,” to which, as demonstrated in the notes accompanying the above discussion concerning avoidable preferences, recoupment clearly applies. While the assertion of a defense may not be stayed, an act to recover a “claim” clearly is.

The result is that the cases that hold that recoupment is exempt from the automatic stay are clearly decided incorrectly. Even though not mentioned by name in the automatic stay provision, a recoupment is an act to recover a claim. If that claim is a prepetition one, then recoupment is stayed.

WHY NOT A SPECIAL CASE OF SETOFF?

As set forth above, the lack of grounding for recoupment in the Code not only engenders bad results, it also encourages litigation to create or employ equitable exceptions to statutory directives. Since recoupment shares many, if not most, of the attributes of setoff, one may well ask why recoupment should not be treated as a special case of setoff. After all,

having countervailing claims arise from the same transaction (or set of transactions) is a special case of having countervailing claims (which may arise from the same or different transactions). Moreover, when opposing demands arise from the same transaction (or set of transactions) they satisfy all the criteria of “mutuality.” That is to say, they are necessarily bilateral, and they are between the same parties, acting in the same capacities, and in the “same right.”⁶⁹

Making recoupment subject to the same statutory provisions as setoff raises three substantial issues: the automatic stay, the avoiding powers, and the ability to traverse the petition date. As to the first, treating recoupments as setoffs certainly subjects them to the automatic stay.⁷⁰ This imposition, however, is not as severe as it may seem at first glance because relief from the automatic stay ought to be granted as a routine matter. No statutory change is needed to make the right to a recoupment qualify as “cause” for relief from the stay within the meaning of section 362(d)(1).⁷¹ This recognition of a new type of “cause” for relief from the stay is nothing more than the lifting of a barrier that was lowered only because of the decision to treat recoupments as a special case of setoffs. By limiting such “cause” to recoupments, no substantive change from existing law is accomplished. All setoffs do not immediately become eligible for stay relief, only the ones in the special case of recoupment. Procedurally, there is an incremental burden because the recouping party is compelled to seek court permission. Indeed, the Second Circuit partly based its decision to relieve recoupments from the automatic stay in the case of utility deposits as a matter of convenience, eliminating the transaction costs, and thus reducing the cost of utility service for consumers and businesses.⁷² The precise result reached in the Second Circuit for utility deposits has been codified in the 2005 amendment to section 366, which authorizes “a utility [to] recover or set off against a security deposit provided to the utility by the debtor before the date of the petition without notice or order of the court.”⁷³ For other types of recoupments, a similar result can be accomplished by the adoption of national or local bankruptcy rules standardizing and simplifying motions for relief from the stay to permit recoupment. A change in the rules of the Judicial Conference could also eliminate the fee for such stay-relief motions.⁷⁴ Thus no substantive change in the law has occurred, and the incremental transactional costs can be minimized. An additional advantage is achieved by allowing courts to prevent recoupment in those few cases in which the doctrine would be inequitable, for example, when the rights of secured creditors are implicated.⁷⁵

The stay relief procedure also permits recoupment across the great divide of the petition date. It must first be observed that, although section 553 preserves the validity of mutual prepetition setoffs, it does not

itself outlaw a creditor's use of a prepetition claim to offset a postpetition one by the debtor.⁷⁶ The section merely states that, other than sections 362, 363 and 553 itself, nothing in "this title," that is to say, the Bankruptcy Code, "affects" the right to offset mutual prepetition debts.⁷⁷ For cases in which one or more postpetition debts are involved, "this title" may affect the right of setoff. But what specifically in this title affects such right of setoff? The unsurprising answers are, principally, section 553(a), the automatic stay, and the avoiding powers.

The restrictions imposed by section 553(a) on the use of a creditor's prepetition claim to setoff against a prepetition debt owed to the debtor are three-fold: (1) the creditor's claim is disallowed; (2) the creditor's claim was transferred to the creditor by some entity other than the debtor after the petition or in the 90 days prior to the petition while the debtor was insolvent; or (3) the creditor's claim was incurred in the 90 days prior to the petition while the debtor was insolvent and for the purpose of obtaining a right of setoff.⁷⁸ The first of these is irrelevant to any difference between setoff and recoupment. The second and third of these cannot occur with respect to a recoupment, since the opposing claims arise out of the same transaction. Therefore, the recouping creditor's claim cannot have been transferred to the creditor by an entity other than the debtor and cannot have been incurred for the purpose of obtaining a right of setoff. Consequently, section 553(a) itself imposes no impediment to recoupment's crossing the petition line.

For validly preserved, mutual prepetition setoffs, the automatic stay precludes the effecting of a setoff that did not occur prepetition.⁷⁹ Nevertheless, in the absence of one of the three disqualifications of the creditor's claim discussed above, the right of setoff, though stayed, is treated in section 506(a) as a secured claim.⁸⁰ As such, it is entitled to adequate protection⁸¹ and, if it lacks such protection, relief from the stay.⁸² Thus, theoretically at least, the creditor gets to exercise his right of setoff or is protected against the diminution in the value of such right.⁸³

This analysis does not work if the creditor attempts to use a prepetition claim against the debtor to offset the debtor's postpetition claim against the creditor. The same automatic stay applies to the creditor. But, in this instance, the creditor does not get the benefit of secured status under section 506(a) because the creditor does not have "an allowed claim . . . that is subject to setoff under section 553."⁸⁴ In the absence of a secured position, the creditor has no basis to claim adequate protection and hence no right to relief from the stay when such protection is lacking. Under existing case law, this creditor has no special "cause" under section 362(d) that would require the stay to be lifted.⁸⁵ Thus the stay remains in place, and the creditor is relegated to a prepetition unsecured claim.

If instead the creditor uses a prepetition claim against the debtor to recoup against the debtor's postpetition claim against the creditor, the result is different. Once again, section 506(a) offers no aid to the creditor. But this time, under existing case law, this creditor has the substantive right to recoup across the petition divide. Therefore, such creditor does have special "cause" under section 362(d) to obtain relief to permit the recoupment. Having the court grant permission to effect the recoupment also insulates the recoupment from avoidance under section 549 because the transfer becomes "authorized . . . by the court."⁸⁶

One substantive change that comes from treating recoupments as a subset of setoffs is that recoupments become subject to section 553(b) avoidance, based on the "insufficiency" analysis contained in that section.⁸⁷ Section 553(b)(1) allows a trustee to recover from an offsetting creditor that improves its position during the 90 days prior to bankruptcy.⁸⁸ The amount by which the creditor's claim against the debtor exceeds the debtor's claim against the creditor is called the "insufficiency."⁸⁹ The smaller the insufficiency, the greater the percentage of the creditor's claim against the debtor available to be satisfied via setoff. If a creditor has a claim against the debtor, an insufficiency of zero means that the debtor's claim against the creditor is equal to the creditor's claim against the debtor, and the entire amount of the creditor's claim can be satisfied via setoff. Section 553(b) compares the insufficiency on the date of the setoff against the insufficiency that existed at the beginning of the period, if one did exist then, or at the first day during the period at which an insufficiency existed. If the insufficiency on the date of the actual setoff is smaller than the initial insufficiency during the 90 days prior to bankruptcy, the creditor taking the setoff has improved its position, and the trustee can recover the setoff to the extent of the difference between the insufficiencies.⁹⁰

Treating recoupments as setoffs allows for recovery from recouping creditors. This represents a change from existing law. Nevertheless, this change is less significant than it first appears. To the extent a setoff or recoupment is avoided, the creditor's claim against the debtor is restored as a prepetition claim. In the event the debtor does not continue operations postpetition, the creditor merely has a prepetition claim against the debtor. To the extent the transaction that was avoided was a setoff, that would be the end of the story. But recoupments, unlike setoffs, can traverse the petition divide. Therefore, the avoided recoupment, after appropriate stay relief, becomes eligible to be used anew against a postpetition claim by the debtor. Therefore, in a chapter 11 case in which the creditor continues to incur debt to the debtor, most attempts to avoid recoupments under section 553(b) would be less than useless.⁹¹ Unfortunately, in most chapter 7 cases,⁹² there is no way to rescue the avoided recoupment.

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Despite this result, considering recoupments to be a special case of setoffs makes sense because it reins in a rogue doctrine. It discourages parties and courts from importing common law doctrines to vary the results decreed by the statute. It reduces litigation costs and makes results more predictable and reliable.

CONCLUSION

The traditional notion that setoff and recoupment are distinct doctrines with separate regulations, one grounded in statute and the other in the common law, is misguided and leads to incorrect and inconsistent results. It is time to realize that having opposing demands that arise out of the same transaction is just a special case of having opposing demands, which may or may not arise out of the same transaction. Treating recoupment as a special case of setoff, and therefore regulated by section 553 of the Bankruptcy Code, eliminates litigation cost and uncertainty and bolsters the important jurisprudential result that an uncodified theory cannot be allowed to ride roughshod over a Congressional enactment. The special case of the same-transaction setoff can maintain its worthwhile substantive properties after receiving stay relief. The same-transaction setoff, also known as recoupment, can still be allowed when an ordinary setoff would not, even across the great divide of the petition date.

1. 11 U.S.C.A. §§ 101-1330. Unless otherwise specified, all references to the Bankruptcy Code are prior to the enactment on April 20, 2005 of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, 119 Stat. 23 (2005). The discussion contained herein is not expected to be affected by the changes to the Bankruptcy Code made by such Act.

2. *In re McMahon*, 129 F.3d 93, 96, 31 Bankr. Ct. Dec. (CRR) 865, Bankr. L. Rep. (CCH) P 77538 (2d Cir. 1997); *In re University Medical Center*, 973 F.2d 1065, 1079, 38 Soc. Sec. Rep. Serv. 482, 23 Bankr. Ct. Dec. (CRR) 628, 27 Collier Bankr. Cas. 2d (MB) 800, Bankr. L. Rep. (CCH) P 74791 (3d Cir. 1992) (rejected on other grounds by, *In re St. Johns Home Health Agency, Inc.*, 173 B.R. 238, 46 Soc. Sec. Rep. Serv. 52 (Bankr. S.D. Fla. 1994); *Matter of Holford*, 896 F.2d 176, 179, 20 Bankr. Ct. Dec. (CRR) 416, 22 Collier Bankr. Cas. 2d (MB) 1097, Bankr. L. Rep. (CCH) P 73294 (5th Cir. 1990).

3. *In re McMahon*, 129 F.3d 93, 97, 31 Bankr. Ct. Dec. (CRR) 865, Bankr. L. Rep. (CCH) P 77538 (2d Cir. 1997); *In re B & L Oil Co.*, 782 F.2d 155, 14 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 70964 (10th Cir. 1986).

4. *Reiter v. Cooper*, 507 U.S. 258, 265 n.2, 113 S. Ct. 1213, 122 L. Ed. 2d 604, Bankr. L. Rep. (CCH) P 75129A (1993), the Supreme Court said: "It is well settled . . . that a bankruptcy defendant can meet a plaintiff-debtor's claim with a counterclaim arising out of the same transaction, at least to the extent that the defendant merely seeks recoupment. Recoupment permits a determination of the just and proper liability on the main issue and involves no element of preference." [Internal quotation omitted].

5. *In re Kmart Corp.*, 318 B.R. 409 (Bankr. N.D. Ill. 2004) leave to appeal denied, 2004 U.S. Dist. LEXIS 19829 (N.D. Ill. Sept. 30, 2004) (second decision referred to in text) (contains substantive discussion).

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6. *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 18, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995) (quoting *Studley v. Boylston Nat. Bank of Boston*, 229 U.S. 523, 528, 33 S. Ct. 806, 57 L. Ed. 1313 (1913)).

7. 11 U.S.C.A. § 553(a); *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 18, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995).

8. See *U.S. Through Agr. Stabilization and Conservation Service v. Gerth*, 991 F.2d 1428, 1431, 24 Bankr. Ct. Dec. (CRR) 304, 29 Collier Bankr. Cas. 2d (MB) 23, Bankr. L. Rep. (CCH) P 75230 (8th Cir. 1993).

9. *Matter of Elcona Homes Corp.*, 863 F.2d 483, 486, Bankr. L. Rep. (CCH) P 72532 (7th Cir. 1988).

10. See, e.g., *In re Visiting Home Services, Inc.*, 643 F.2d 1356, 1360, 7 Bankr. Ct. Dec. (CRR) 712 (9th Cir. 1981); *In re County of Orange*, 183 B.R. 609, 616, 27 Bankr. Ct. Dec. (CRR) 435, 33 Collier Bankr. Cas. 2d (MB) 1604, 28 U.C.C. Rep. Serv. 2d 631 (Bankr. C.D. Cal. 1995); *Matter of O.P.M. Leasing Services, Inc.*, 68 B.R. 979, 986 (Bankr. S.D. N.Y. 1987); *Prudential Reinsurance Co. v. Superior Court*, 3 Cal. 4th 1118, 14 Cal. Rptr. 2d 749, 842 P.2d 48 (1992); *Matter of Consolidated Indemnity & Ins. Co.*, 287 N.Y. 34, 38, 38 N.E.2d 119 (1941). In bankruptcy, the notion of obligations being in the “same right” is sometimes used to prevent prepetition debts from being setoff against postpetition ones. *In re County of Orange*, 183 B.R. 609, 27 Bankr. Ct. Dec. (CRR) 435, 33 Collier Bankr. Cas. 2d (MB) 1604, 28 U.C.C. Rep. Serv. 2d 631 (Bankr. C.D. Cal. 1995); *In re Bay State York Co., Inc.*, 140 B.R. 608, 23 Bankr. Ct. Dec. (CRR) 57, 26 Collier Bankr. Cas. 2d (MB) 1520 (Bankr. D. Mass. 1992). Nevertheless, the notion that obligations are not in the “same right” has meaning outside of bankruptcy. For example, if a fund is established for a special purpose, it may not be used for a setoff outside that special purpose. The attempted setoff is stated not to be in the “same right.” *Matter of Consolidated Indemnity & Ins. Co.*, 287 N.Y. 34, 38, 38 N.E.2d 119 (1941).

11. *In re Malinowski*, 156 F.3d 131, 133, 33 Bankr. Ct. Dec. (CRR) 81, 40 Collier Bankr. Cas. 2d (MB) 1054, Bankr. L. Rep. (CCH) P 77779 (2d Cir. 1998); *Newbery Corp. v. Fireman's Fund Ins. Co.*, 95 F.3d 1392, 1398, 29 Bankr. Ct. Dec. (CRR) 956, 36 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 77075 (9th Cir. 1996).

12. *U.S. v. Dalm*, 494 U.S. 596, 611, 110 S. Ct. 1361, 108 L. Ed. 2d 548, 90-1 U.S. Tax Cas. (CCH) P 50154, 90-1 U.S. Tax Cas. (CCH) P 60012, 65 A.F.T.R.2d 90-1210 (1990); *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296, 299, 67 S. Ct. 271, 91 L. Ed. 296, 47-1 U.S. Tax Cas. (CCH) P 9106, 35 A.F.T.R. (P-H) P 297 (1946); *Bull v. U.S.*, 295 U.S. 247, 55 S. Ct. 695, 79 L. Ed. 1421, 35-1 U.S. Tax Cas. (CCH) P 9346, 15 A.F.T.R. (P-H) P 1069 (1935); *In re Malinowski*, 156 F.3d 131, 133, 33 Bankr. Ct. Dec. (CRR) 81, 40 Collier Bankr. Cas. 2d (MB) 1054, Bankr. L. Rep. (CCH) P 77779 (2d Cir. 1998); *In re University Medical Center*, 973 F.2d 1065, 1080, 38 Soc. Sec. Rep. Serv. 482, 23 Bankr. Ct. Dec. (CRR) 628, 27 Collier Bankr. Cas. 2d (MB) 800, Bankr. L. Rep. (CCH) P 74791 (3d Cir. 1992) (rejected on other grounds by, *In re St. Johns Home Health Agency, Inc.*, 173 B.R. 238, 46 Soc. Sec. Rep. Serv. 52 (Bankr. S.D. Fla. 1994)).

13. *U.S. v. Dalm*, 494 U.S. 596, 611, 110 S. Ct. 1361, 108 L. Ed. 2d 548, 90-1 U.S. Tax Cas. (CCH) P 50154, 90-1 U.S. Tax Cas. (CCH) P 60012, 65 A.F.T.R.2d 90-1210 (1990); *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296, 299, 67 S. Ct. 271, 91 L. Ed. 296, 47-1 U.S. Tax Cas. (CCH) P 9106, 35 A.F.T.R. (P-H) P 297 (1946); *Bull v. U.S.*, 295 U.S. 247, 55 S. Ct. 695, 79 L. Ed. 1421, 35-1 U.S. Tax Cas. (CCH) P 9346, 15 A.F.T.R. (P-H) P 1069 (1935); *In re Malinowski*, 156 F.3d 131, 133, 33 Bankr. Ct. Dec. (CRR) 81, 40 Collier Bankr. Cas. 2d (MB) 1054, Bankr. L. Rep. (CCH) P 77779 (2d Cir. 1998); *In re University Medical Center*, 973 F.2d 1065, 1080, 38 Soc. Sec. Rep. Serv. 482, 23 Bankr. Ct. Dec. (CRR) 628, 27 Collier Bankr. Cas. 2d

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(MB) 800, Bankr. L. Rep. (CCH) P 74791 (3d Cir. 1992) (rejected on other grounds by, *In re St. Johns Home Health Agency, Inc.*, 173 B.R. 238, 46 Soc. Sec. Rep. Serv. 52 (Bankr. S.D. Fla. 1994)).

14. *Matter of U.S. Abatement Corp.*, 79 F.3d 393, 398 (5th Cir. 1996); *In re B & L Oil Co.*, 782 F.2d 155, 157, 14 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 70964 (10th Cir. 1986); see *Lee v. Schweiker*, 739 F.2d 870, 6 Soc. Sec. Rep. Serv. 98, 11 Collier Bankr. Cas. 2d (MB) 834, Bankr. L. Rep. (CCH) P 69914, Unempl. Ins. Rep. (CCH) P 16982 (3d Cir. 1984).

15. Fed. R. Civ. P. 13(a) requires the assertion of a counterclaim “if it arises out of the same transaction or occurrence that is the subject matter of the opposing party’s claim.”

16. *Lee v. Schweiker*, 739 F.2d 870, 875, 6 Soc. Sec. Rep. Serv. 98, 11 Collier Bankr. Cas. 2d (MB) 834, Bankr. L. Rep. (CCH) P 69914, Unempl. Ins. Rep. (CCH) P 16982 (3d Cir. 1984).

17. Fed. R. Civ. P. 13(b); see 3 Moore’s Federal Practice 3d, § 13.31 (1998).

18. *In re Yonkers Hamilton Sanitarium Inc.*, 22 B.R. 427, 432, 9 Bankr. Ct. Dec. (CRR) 505 (Bankr. S.D. N.Y. 1982), judgment aff’d, 34 B.R. 385 (S.D. N.Y. 1983).

19. *In re Mirant Corp.*, 318 B.R. 377, 382, 43 Bankr. Ct. Dec. (CRR) 166 (Bankr. N.D. Tex. 2004), aff’d, 2005 WL 405304 (N.D. Tex. 2005).

20. *In re B & L Oil Co.*, 782 F.2d 155, 158-59, 14 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 70964 (10th Cir. 1986); *Waldschmidt v. CBS, Inc.*, 14 B.R. 309, 313-14 (M.D. Tenn. 1981); *In re Clowards, Inc.*, 42 B.R. 627, 628 (Bankr. D. Idaho 1984).

21. *In re McMahon*, 129 F.3d 93, 96, 31 Bankr. Ct. Dec. (CRR) 865, Bankr. L. Rep. (CCH) P 77538 (2d Cir. 1997).

22. *In re Anes*, 195 F.3d 177, 182, 42 Collier Bankr. Cas. 2d (MB) 1875, 23 Employee Benefits Cas. (BNA) 1953, Bankr. L. Rep. (CCH) P 78025 (3d Cir. 1999).

23. *In re Anes*, 195 F.3d 177, 182, 42 Collier Bankr. Cas. 2d (MB) 1875, 23 Employee Benefits Cas. (BNA) 1953, Bankr. L. Rep. (CCH) P 78025 (3d Cir. 1999); *Matter of Kosadnar*, 157 F.3d 1011, 1016, 33 Bankr. Ct. Dec. (CRR) 486, Bankr. L. Rep. (CCH) P 77838 (5th Cir. 1998); *In re McMahon*, 129 F.3d 93, 96, 31 Bankr. Ct. Dec. (CRR) 865, Bankr. L. Rep. (CCH) P 77538 (2d Cir. 1997).

24. In particular, the avoiding power contained in 11 U.S.C.A. § 553(b) is inapplicable, because it concerns setoffs. With regard to avoidable preferences, the Supreme Court has declared that recoupment “involves no element of preference.” *Reiter v. Cooper*, 507 U.S. 258, 265 n.2, 113 S. Ct. 1213, 122 L. Ed. 2d 604, Bankr. L. Rep. (CCH) P 75129A (1993).

25. *In re Anes*, 195 F.3d 177, 182, 42 Collier Bankr. Cas. 2d (MB) 1875, 23 Employee Benefits Cas. (BNA) 1953, Bankr. L. Rep. (CCH) P 78025 (3d Cir. 1999); *In re B & L Oil Co.*, 782 F.2d 155, 158, 14 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 70964 (10th Cir. 1986); *Lee v. Schweiker*, 739 F.2d 870, 875, 6 Soc. Sec. Rep. Serv. 98, 11 Collier Bankr. Cas. 2d (MB) 834, Bankr. L. Rep. (CCH) P 69914, Unempl. Ins. Rep. (CCH) P 16982 (3d Cir. 1984).

26. *Westinghouse Credit Corp. v. D’Urso*, 278 F.3d 138, 146 (2d Cir. 2002); see *In re B & L Oil Co.*, 782 F.2d 155, 158, 14 Bankr. Ct. Dec. (CRR) 133, Bankr. L. Rep. (CCH) P 70964 (10th Cir. 1986).

27. *In re Kmart Corp.*, 318 B.R. 409 (Bankr. N.D. Ill. 2004) leave to appeal denied, 2004 U.S. Dist. LEXIS 19829 (N.D. Ill. Sept. 30, 2004) (second decision referred to in text) (contains substantive discussion).

28. Fed. R. Civ. P. 12(f) provides: “Upon a motion made by a party before responding to a pleading or, if no responsive pleading is permitted by these rules, upon motion made by a party within 20 days after service of the pleading upon the party or upon the court’s own initiative at any time, the court may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent or scandalous matter.” This provision in applicable made applicable to bankruptcy adversary proceedings by Fed. R. Bankr. 7012.

29. The court held that the defense that a trustee may not recover when such recovery does not benefit the estate is a limitation grounded in section 550(a), and therefore, not implicated by its decision. *In re Kmart Corp.*, 318 B.R. 409, 415 n.1 (Bankr. N.D. Ill. 2004). Although the court does not call this defense a “threshold defense,” it would seem to meet that definition, since the defense does not go to the merits of whether a preferential transfer to the defendant had been made.

30. *In re Kmart Corp.*, 318 B.R. 409, 415 (Bankr. N.D. Ill. 2004).

31. *In re Kmart Corp.*, 318 B.R. 409, 417-18 (Bankr. N.D. Ill. 2004). The bankruptcy court relied on a prior decision from its own district that reached the same result. *Raleigh v. Mid Am. Nat'l Bank & Tr. Co.* (In re Stoecker), 131 BR 979, 983-84 (Bankr. N.D. Ill. 1991).

32. 28 U.S.C.A. § 158(a)(3) allows interlocutory appeals from decisions of bankruptcy judges with leave of the district court, or if applicable, the bankruptcy appellate panel. See 28 U.S.C.A. § 158(b) (discussing bankruptcy appellate panels).

33. 28 U.S.C.A. § 1292(b). Although the provision governing discretionary interlocutory appeals from the bankruptcy court, section 158(a), does not provide any criteria, many district courts employ, by analogy, the criteria set forth in section 1292(b). See, e.g., *In re OBT Partners*, 218 B.R. 418, 419 (N.D. Ill. 1998); *In re Dino's, Inc.*, 183 B.R. 779, 781 (S.D. Ohio 1995); *In re American Freight System, Inc.*, 153 B.R. 316, 321 (D. Kan. 1993).

34. *In re Kmart Corp.*, . 2004 U.S. Dist. LEXIS 19829, (N.D. Ill. Sept. 30, 2004). The court held that the non-enumerated defense of “earmarking” was not an affirmative defense, but a defense in the nature of negating one of the elements of a preference action, *In re Kmart Corp.*, 2004 U.S. Dist. LEXIS 19829, (N.D. Ill. Sept. 30, 2004); namely, “a transfer of an interest of the debtor in property.” 11 U.S.C.A. § 547(b).

35. See *Lee v. Schweiker*, 739 F.2d 870, 873 n.4, 6 Soc. Sec. Rep. Serv. 98, 11 Collier Bankr. Cas. 2d (MB) 834, Bankr. L. Rep. (CCH) P 69914, Unempl. Ins. Rep. (CCH) P 16982 (3d Cir. 1984). The converse of this statement is true as well: A setoff can be avoided as a preference, if it has not been validly preserved by section 553. See *Durham v. SMI Industries Corp.*, 882 F.2d 881, 882, Bankr. L. Rep. (CCH) P 73065 (4th Cir. 1989); *In re APF Co.*, 264 B.R. 344, 357 (Bankr. D. Del. 2001); *In re Keystone Foods, Inc.*, 145 B.R. 502, 508 (Bankr. W.D. Pa. 1992). The notion that a valid setoff is not a preference is hardly new. Under the Bankruptcy Act of 1898, courts distinguished between ordinary, valid setoffs, which were not avoidable as preferences, see *New York County Nat. Bank v. Massey*, 192 U.S. 138, 147, 24 S. Ct. 199, 48 L. Ed. 380 (1904); and unusual setoffs, especially those intended as payments of antecedent debt, which were avoidable as preferences, see *Katz v. First Nat. Bank of Glen Head*, 568 F.2d 964, 969-71, 14 C.B.C. 432 (2d Cir. 1977); *Goldstein v. Franklin Square Nat. Bank*, 107 F.2d 393, 394 (C.C.A. 2d Cir. 1939).

36. E.g., *In re Holyoke Nursing Home Inc.*, 273 B.R. 305, 309, 38 Bankr. Ct. Dec. (CRR) 250, Bankr. L. Rep. (CCH) P 78578 (Bankr. D. Mass. 2002), subsequently aff'd, 372 F.3d 1, 43 Bankr. Ct. Dec. (CRR) 34, Bankr. L. Rep. (CCH) P 80110 (1st Cir. 2004); *In re Balducci Oil Co., Inc.*, 33 B.R. 847, 852, 11 Bankr. Ct. Dec. (CRR) 237 (Bankr. D. Colo. 1983).

37. 11 U.S.C.A. § 101(54) defines “transfer” as “every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including the retention of title as a security interest and foreclosure of the debtor’s equity of redemption.”

38. In the version of the Bankruptcy Code originally passed by the House of Representatives, the definition of “transfer” had an explicit reference to “setoff.” H.R. 8200, sec. 101, § 101(39), 95th Cong. 1st Sess. (1977). The version initially passed by the Senate did not contain such a reference. S.2266, sec. 101, § 101(40), 95th Cong. 2d Sess. (1978). The statements of the legislative leaders in lieu of a conference committee report for the revised bill that was ultimately enacted identically provide that the Senate version of the definition was selected, and offer the following explanation: “The effect is that a ‘setoff’ is not subject to

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being set aside as a preferential 'transfer' but will be subject to special rules." 124 Cong. Rec. H11047, H11090 (daily ed. Sept. 28, 1978); 124 Cong. Rec. S17403, 17407 (daily ed. Oct. 6, 1978).

39. 11 U.S.C.A. § 553.

40. 11 U.S.C.A. § 101(54).

41. E.g., *Lamie v. U.S. Trustee*, 540 U.S. 526, 534, 124 S. Ct. 1023, 157 L. Ed. 2d 1024, 42 Bankr. Ct. Dec. (CRR) 122, 50 Collier Bankr. Cas. 2d (MB) 1299, Bankr. L. Rep. (CCH) P 80038 (2004); *Patterson v. Shumate*, 504 U.S. 753, 757-58, 112 S. Ct. 2242, 119 L. Ed. 2d 519, 23 Bankr. Ct. Dec. (CRR) 89, 26 Collier Bankr. Cas. 2d (MB) 1119, 15 Employee Benefits Cas. (BNA) 1481, Bankr. L. Rep. (CCH) P 74621A (1992); *Union Bank v. Wolas*, 502 U.S. 151, 155-56, 112 S. Ct. 527, 116 L. Ed. 2d 514, 22 Bankr. Ct. Dec. (CRR) 574, 25 Collier Bankr. Cas. 2d (MB) 1011, Bankr. L. Rep. (CCH) P 74296A (1991). As the Supreme Court has explained: "We have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there. When the words of a statute are unambiguous, the first canon is also the last; judicial inquiry is complete." *Barnhart v. Sigmon Coal Co., Inc.*, 534 U.S. 438, 462, 122 S. Ct. 941, 151 L. Ed. 2d 908, 27 Employee Benefits Cas. (BNA) 1545, 197 A.L.R. Fed. 689 (2002) (quoting *Connecticut Nat. Bank v. Germain*, 503 U.S. 249, 253-54, 112 S. Ct. 1146, 117 L. Ed. 2d 391, 22 Bankr. Ct. Dec. (CRR) 1130, 26 Collier Bankr. Cas. 2d (MB) 175, Bankr. L. Rep. (CCH) P 74457A (1992) (internal quotation omitted)).

42. *Shannon v. U.S.*, 512 U.S. 573, 583-84, 114 S. Ct. 2419, 129 L. Ed. 2d 459 (1994).

43. It is clear that the right to payment of a debt is "property" within the meaning of the definition of "transfer." The Code equates the concepts of being owed a debt with having a property right in section 542(b), which states in relevant part: "an entity that owes a debt that is property of the estate . . . shall pay such debt . . . to . . . the trustee, except to the extent that such debt may be offset under section 553 of this title against a claim against the debtor." 11 U.S.C.A. § 542(b).

44. *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 19, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995).

45. *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 19, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995). The automatic stay prohibits "the setoff of any debt owed to the debtor that arose before the commencement of the case." 11 U.S.C.A. § 362(a)(7).

46. The new provision reads as follows:

The term "transfer" means-

- (A) the creation of a lien;
- (B) the retention of title as a security interest;
- (C) the foreclosure of a debtor's equity of redemption; or
- (D) each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with
 - (i) property; or
 - (ii) an interest in property.

Pub. L. No. 109-8, sec. 1201(6) (amending 11 U.S.C.A. § 101(54)).

47. 11 U.S.C.A. § 547(b)(1) requires, as an element of a preference, that the transfer be "to or for the benefit of a creditor." A "creditor" includes an "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor." 11 U.S.C.A. § 101(10)(A). A "claim" is a:

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- (A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured; or
- (B) right to an equitable remedy for breach of performance if such breach gives rise to a right of payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.

Under this broad definition of “claim,” see *Pennsylvania Dept. of Public Welfare v. Davis*, 495 U.S. 552, 558, 110 S. Ct. 2126, 109 L. Ed. 2d 588, 20 Bankr. Ct. Dec. (CRR) 833, 22 Collier Bankr. Cas. 2d (MB) 1067, Bankr. L. Rep. (CCH) P 73382 (1990); it is clear that a recoupment is a “claim,” which makes the holder of recoupment right that exists perpetually into a “creditor.”

48. 11 U.S.C.A. § 547(b)(2) requires, as an element of a preference, that the transfer be “on account of antecedent debt.” This requirement has been held to be satisfied if the creditor has a “claim” against the debtor prior to the transfer. *Warsco v. Preferred Technical Group*, 258 F.3d 557, 569 (7th Cir. 2001); *In re First Jersey Securities, Inc.*, 180 F.3d 504, 511, 34 Bankr. Ct. Dec. (CRR) 638, Bankr. L. Rep. (CCH) P 77940 (3d Cir. 1999).

49. 11 U.S.C.A. § 547(b)(3) requires, as an element of a preference, that the transfer is “made while the debtor was insolvent.”

50. 11 U.S.C.A. § 547(b)(4) requires, as an element of a preference, that the transfer is made within 90 days of the petition date or within one year of the petition date if the creditor was an insider at the time of the transfer.

51. 11 U.S.C.A. § 547(b)(5) requires, as an element of a preference, that the transfer:

enables such creditor to receive more than such creditor would receive if -

- (A) the case were a case under chapter 7 of this title;
- (B) the transfer had not been made; and
- (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

52. Cf. *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 19, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995).

53. See *Reiter v. Cooper*, 507 U.S. 258, 265 n.2, 113 S. Ct. 1213, 122 L. Ed. 2d 604, Bankr. L. Rep. (CCH) P 75129A (1993) (“Recoupment permits a determination of the ‘just and proper liability on the main issue,’ and involves ‘no element of preference.’”) (quoting 4 Collier on Bankruptcy ¶ 553.03 (15th ed. 1991)). The statement concerning preference liability is dicta, because the case did not concern preference liability. The recoupment at issue was a claim by a shipper that the carrier’s so-called “filed rate” was unreasonable, when the trustee in bankruptcy for the carrier sued to recover the “filed rate.” *Reiter v. Cooper*, 507 U.S. 258, 260-63, 113 S. Ct. 1213, 122 L. Ed. 2d 604, Bankr. L. Rep. (CCH) P 75129A (1993).

54. 11 U.S.C.A. § 542(b) provides in relevant part that: “an entity that owes a debt that is property of the estate and that is matured, payable on demand, or payable on order, shall pay such debt to, or on the order of the trustee, except to the extent that such debt may be offset under section 553 of this title against a claim against the debtor.”

55. *Levit v. Ingersoll Rand Financial Corp.*, 874 F.2d 1186, 1197-1200, 19 Bankr. Ct. Dec. (CRR) 574, 22 Collier Bankr. Cas. 2d (MB) 36, 11 Employee Benefits Cas. (BNA) 1323, Bankr. L. Rep. (CCH) P 72910 (7th Cir. 1989) (disapproved of by, *In re Arundel Housing Components, Inc.*, 126 B.R. 216, 21 Bankr. Ct. Dec. (CRR) 959, Bankr. L. Rep. (CCH) P 73922 (Bankr. D. Md. 1991)) (rejecting an uncodified defense, based on “equity” or “policy,” to liability for a noninsider as the initial transferee of an avoided insider preference) *In re V.N. Deprizio Const. Co.*, 86 B.R. 545, 9 Employee Benefits Cas. (BNA) 2142, Bankr. L. Rep.

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(CCH) P 72390 (N.D. Ill. 1988), judgment aff'd in part, rev'd in part, 874 F.2d 1186, 19 Bankr. Ct. Dec. (CRR) 574, 22 Collier Bankr. Cas. 2d (MB) 36, 11 Employee Benefits Cas. (BNA) 1323, Bankr. L. Rep. (CCH) P 72910 (7th Cir. 1989) (disapproved of by, *In re Arundel Housing Components, Inc.*, 126 B.R. 216, 21 Bankr. Ct. Dec. (CRR) 959, Bankr. L. Rep. (CCH) P 73922 (Bankr. D. Md. 1991)) (N.D. Ill. 1988). A 1994 amendment adding a new 11 U.S.C.A. § 550(c) was intended as a legislative overruling of this result. Bankruptcy Reform Act of 1994, Pub. L. No. 103-393, § 202. See 140 Cong. Rec. H10,767 (daily ed. Oct. 4, 1994) (analysis of section 202); 140 Cong. Rec. S14,461 (daily ed. Oct. 4, 1994) (remarks of Sen. Grassley). Whether the provision fully accomplished its task was subject to question. The Bankruptcy Abuse and Consumer Protection Act of 2005 adds new 11 U.S.C.A. § 547(i) to complete the overruling of the *Deprizio* line of cases. That section provides:

If a trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider.

Pub. L. No. 109-8, sec. 1213(a)(2) (adding 11 U.S.C.A. § 547(i)). This section became effective upon enactment and is applicable to pending cases as well. Pub. L. No. 109-8 sec. 1213(b).

56. E.g., *In re Erin Food Services, Inc.*, 980 F.2d 792, 23 Bankr. Ct. Dec. (CRR) 1108, 27 Collier Bankr. Cas. 2d (MB) 1689, Bankr. L. Rep. (CCH) P 75013 (1st Cir. 1992); *In re C-L Cartage Co., Inc.*, 899 F.2d 1490, 20 Bankr. Ct. Dec. (CRR) 599, 22 Collier Bankr. Cas. 2d (MB) 901, Bankr. L. Rep. (CCH) P 73323 (6th Cir. 1990); *In re Robinson Bros. Drilling, Inc.*, 892 F.2d 850, 21 Collier Bankr. Cas. 2d (MB) 1405, Bankr. L. Rep. (CCH) P 73090 (10th Cir. 1989).

57. *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206, 108 S. Ct. 963, 99 L. Ed. 2d 169, 17 Bankr. Ct. Dec. (CRR) 201, 18 Collier Bankr. Cas. 2d (MB) 262, Bankr. L. Rep. (CCH) P 72186 (1988).

58. *In re Malinowski*, 156 F.3d 131, 133, 33 Bankr. Ct. Dec. (CRR) 81, 40 Collier Bankr. Cas. 2d (MB) 1054, Bankr. L. Rep. (CCH) P 77779 (2d Cir. 1998); *In re University Medical Center*, 973 F.2d 1065, 1080, 38 Soc. Sec. Rep. Serv. 482, 23 Bankr. Ct. Dec. (CRR) 628, 27 Collier Bankr. Cas. 2d (MB) 800, Bankr. L. Rep. (CCH) P 74791 (3d Cir. 1992) (rejected on other grounds by, *In re St. Johns Home Health Agency, Inc.*, 173 B.R. 238, 46 Soc. Sec. Rep. Serv. 52 (Bankr. S.D. Fla. 1994)); *Matter of Holford*, 896 F.2d 176, 178, 20 Bankr. Ct. Dec. (CRR) 416, 22 Collier Bankr. Cas. 2d (MB) 1097, Bankr. L. Rep. (CCH) P 73294 (5th Cir. 1990).

59. *In re Malinowski*, 156 F.3d 131, 133, 33 Bankr. Ct. Dec. (CRR) 81, 40 Collier Bankr. Cas. 2d (MB) 1054, Bankr. L. Rep. (CCH) P 77779 (2d Cir. 1998); see *In re Flagstaff Realty Associates*, 60 F.3d 1031, 1035, 27 Bankr. Ct. Dec. (CRR) 738, 34 Collier Bankr. Cas. 2d (MB) 152 (3d Cir. 1995); *United Structures of America, Inc. v. G.R.G. Engineering, S.E.*, 9 F.3d 996, 999, 39 Cont. Cas. Fed. (CCH) P 76598 (1st Cir. 1993).

60. 11 U.S.C.A. § 362(a)(7).

61. 11 U.S.C.A. § 362(a)(6).

62. 11 U.S.C.A. § 101(54). It is at least an “involuntary . . . parting with an interest in property,” namely the debtor’s right to collect payment of its just debt.

63. *The Random House Dictionary of the English Language, Unabridged Edition 4* (1971) (first definition).

64. *Black’s Law Dictionary, 6th Edition 25* (1990) (first definition) (citing Restatement, Second, Torts § 2).

65. 11 U.S.C.A. § 101(5).

66. 11 U.S.C.A. § 362(a)(6).

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67. 11 U.S.C.A. § 362(a)(3). Those cases holding that the debtor's estate has no interest in funds subject to recoupment would find no violation of this section.

68. *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16, 21, 116 S. Ct. 286, 133 L. Ed. 2d 258, 28 Bankr. Ct. Dec. (CRR) 97, 33 Collier Bankr. Cas. 2d (MB) 869, Bankr. L. Rep. (CCH) P 76666A (1995).

69. Here it must be observed that the notion in the "same right" cannot mean on the same side of the division created by the filing of the bankruptcy petition, as it is sometimes construed. See *In re County of Orange*, 183 B.R. 609, 616, 27 Bankr. Ct. Dec. (CRR) 435, 33 Collier Bankr. Cas. 2d (MB) 1604, 28 U.C.C. Rep. Serv. 2d 631 (Bankr. C.D. Cal. 1995); *In re Bay State York Co., Inc.*, 140 B.R. 608, 614, 23 Bankr. Ct. Dec. (CRR) 57, 26 Collier Bankr. Cas. 2d (MB) 1520 (Bankr. D. Mass. 1992). Rather, the operative notion should be the one applied outside of bankruptcy. Namely, that special purpose funds be used only for their designated purpose. See *Matter of Consolidated Indemnity & Ins. Co.*, 287 N.Y. 34, 38, 38 N.E.2d 119 (1941).

70. 11 U.S.C.A. § 362(a)(7) automatically stays "the setoff of any debt owing to the debtor that arose before the commencement of the case." There are several exceptions in section 362(b), and the new legislation adds several more.

71. 11 U.S.C.A. § 362(d)(1).

72. See *In re McMahon*, 129 F.3d 93, 98-99, 31 Bankr. Ct. Dec. (CRR) 865, Bankr. L. Rep. (CCH) P 77538 (2d Cir. 1997).

73. 11 U.S.C.A. § 366(c)(4), as added by section 417 of Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, 119 Stat. 23. (2005).

74. 28 U.S.C.A. § 1930(b) authorizes the Judicial Conference of the United States to prescribe additional fees in cases under the Bankruptcy Code. Under this authority it has prescribed fees for filing motions to lift the automatic stay. It has created an exception to the fee requirement for "a motion for relief from a co-debtor stay or for a stipulation for court approval of an agreement for relief from a stay." Judicial Conference Schedule of Fees, Bankruptcy Court Miscellaneous Fee Schedule ¶ (20).

75. See, e.g., *Westinghouse Credit Corp. v. D'Urso*, 278 F.3d 138, 148 (2d Cir. 2002).

76. 11 U.S.C.A. § 553.

77. 11 U.S.C.A. § 553(a).

78. 11 U.S.C.A. § 553(a)(1)-(3).

79. 11 U.S.C.A. § 362(a)(7).

80. 11 U.S.C.A. § 506(a) provides in relevant part: "An allowed claim of a creditor . . . that is subject to setoff under section 553 . . . is a secured claim . . . to the extent of the amount subject to setoff . . ."

81. 11 U.S.C.A. § 361; see *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 370, 108 S. Ct. 626, 98 L. Ed. 2d 740, 16 Bankr. Ct. Dec. (CRR) 1369, 17 Collier Bankr. Cas. 2d (MB) 1368, Bankr. L. Rep. (CCH) P 72113 (1988).

82. 11 U.S.C.A. § 362(d)(1).

83. See *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 370, 108 S. Ct. 626, 98 L. Ed. 2d 740, 16 Bankr. Ct. Dec. (CRR) 1369, 17 Collier Bankr. Cas. 2d (MB) 1368, Bankr. L. Rep. (CCH) P 72113 (1988).

84. 11 U.S.C.A. § 506(a).

85. See, e.g., *In re Dairy Mart Convenience Stores, Inc.*, 351 F.3d 86, 90, 51 Collier Bankr. Cas. 2d (MB) 223 (2d Cir. 2003); *In re Tultex Corp.*, 250 B.R. 560, 569 (Bankr. W.D. Va. 2000).

86. 11 U.S.C.A. § 549(a)(2)(B).

87. 11 U.S.C.A. § 553(b).

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88. 11 U.S.C.A. § 553(b)(1).

89. 11 U.S.C.A. § 553(b)(2).

90. 11 U.S.C.A. § 553(b)(1).

91. See also *Matter of P.A. Bergner & Co.*, 140 F.3d 1111, 1117, 32 Bankr. Ct. Dec. (CRR) 536, Bankr. L. Rep. (CCH) P 77688, 35 U.C.C. Rep. Serv. 2d 373 (7th Cir. 1998) (barring recovery in an avoidance action when there is no benefit to the estate).

92. 11 U.S.C.A. § 721 allows the court to authorize a chapter 7 trustee to operate the business of the debtor for a limited period.