

**UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa**

In Re	:	Case No. 95 - 2237 - CH
	:	
ADELLA MAY PAYTON,	:	Chapter 7
	:	
Debtor.	:	
-----	:	
ANITA L. SHODEEN,	:	Adv. No. 97 - 97031
TRUSTEE,	:	
	:	
Plaintiff,	:	
	:	
v.	:	
	:	
KEVIN R. KORTE,	:	
	:	
	:	
	:	
Defendant.	:	

ORDER -- MOTION FOR SUMMARY JUDGMENT

On August 14, 1997, a hearing was held on the Defendant's Motion for Summary Judgment and Plaintiff's Cross-Motion for Summary Judgment. Plaintiff, Anita L. Shodeen, Trustee, was represented by attorney Jerrold Wanek; Defendant, Kevin Korte, was represented by attorney John H. Terpstra. At the conclusion of the hearing, the Court took the matter under advisement. The Court now considers the matter fully submitted.

The Court has jurisdiction of this matter pursuant to 28 U.S.C. § 157(b)(1) and § 1334. This is a core proceeding. 28 U.S.C. §§ 157(b)(2)(E), (O). The Court, upon review of the briefs, pleadings, evidence, and arguments of counsel, now enters its findings and conclusions pursuant to Fed.R.Bankr.P. 7056.

FINDINGS OF FACT

1. On July 24, 1992, Adella M. Payton, f/k/a Adella Korte, and Kevin R. Korte were granted a dissolution of marriage in the Iowa District Court in and for Jasper County. The terms of the dissolution decree involved in this proceeding are:

a. "Debts. ADELLA shall pay the following indebtedness incurred by the parties:

DEBT	APPROXIMATE AMOUNT OWING
...	
Hawkeye Bank of Jasper County	\$ 86,000.00
For Promissory Note Inventory for Klassy Kids, Ltd.	
...	

ADELLA shall hold KEVIN harmless from any and all liability thereon ."

b. "Property Settlement. ADELLA is hereby awarded \$75,000.00 as and for an adjustment of the property rights of the parties. KEVIN shall satisfy this property award by paying to ADELLA \$15,000.00 within sixty days of this entry of this Decree and \$10,000.00 not later than thirty days after the anniversary of the date of this Decree and each and every year thereafter until paid in full. If KEVIN is late on any yearly payment, the entire remaining balance shall then bear interest at ten percent (10%) per annum. This property award constitutes a lien on KEVIN'S real estate and farm property until such time as the property award is satisfied. Judgment is hereby rendered against KEVIN in favor of ADELLA for such sums as they become due and payable."

2. Kevin timely made the initial payment of \$15,000 and the 1993 payment of \$10,000 on the property settlement.

3. In 1994, Kevin executed and delivered two checks totaling \$10,000 to Adella. The checks were made payable to Adella jointly with two separate creditors. The checks were refused and were not cashed.

4. On December 22, 1994, Kevin paid off the debt on the \$86,000 promissory note to Hawkeye Bank for which he and Adella were liable under the terms of the security agreement and for which Adella was responsible under the terms of the dissolution decree.

5. Adella Payton filed for protection under Chapter 7 of the Bankruptcy Code on July 27, 1995.

6. On February 27, 1997, the Trustee, Anita Shodeen, brought this Adversary Proceeding, seeking turnover of the remainder of the property settlement that Kevin was to pay to Adella.

7. Kevin filed a Motion for Summary Judgment, claiming he is entitled to judgment as a matter of law based on setoff under 11 U.S.C. § 553 for the amounts paid by him to Hawkeye Bank.

8. Trustee brought a Cross-Motion for Summary Judgment in her favor.

DISCUSSION

A motion for summary judgment is governed by Fed.R.Civ.P. 56, made applicable to bankruptcy proceedings pursuant to Fed.R.Bankr.P. 7056, which provides in pertinent part:

The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

Fed.R.Civ.P. 56(c).

The material facts of the case are not disputed and summary judgment is appropriate. The legal issue before the Court is whether Kevin is entitled to a setoff as a matter of law that is unaffected by bankruptcy. Except for specific situations, the Bankruptcy Code does not affect "any right of a creditor to offset a mutual debt" owing to the debtor that arose pre-petition against a claim against the debtor that also arose pre-petition. See 11 U.S.C. § 553 (a).

For Kevin to have a right of setoff unaffected by bankruptcy, the criteria of § 553 (a) must be satisfied by showing three elements:

- (1) the creditor has a right of setoff under nonbankruptcy law;
- (2) the debt owed to the debtor by the creditor and the claim against the debtor by the creditor both arose pre-petition; and
- (3) the debt and the claim are mutual obligations.

See 11 U.S.C. § 553 (a); 1 David G. Epstein et al., Bankruptcy, § 6-40 at 665 (Practitioner Treatise Series 1992); see also In re Allen, 135 B.R. 856, 860, 869 (Bankr. N.D.Iowa 1992).

These elements are established in the undisputed facts before the Court.

By its plain language, the Code does not create a creditor's right to a setoff where one did not exist outside of bankruptcy. After the parties' divorce, Adella and Kevin remained jointly liable under the terms of the Hawkeye Bank note. See Garton v. Garton, 533 N.W.2d 828, 833 (Iowa 1995). Under the hold harmless provision of the dissolution decree, Kevin has a claim against Adella for the debt on the \$86,000 promissory note to Hawkeye Bank that he paid in December 1994. See i.e. In re Marriage of Lenger, 336 N.W.2d 191 (Iowa 1983)(contempt cause of action available for enforcing property settlements). Under Iowa law, the equitable principle of setoff is well established. See i.e., Van Maanen v. Van Maanen, 360 N.W.2d 758, 762 (Iowa 1985)(citing Jorge Constr. Co. v. Weigel Excavating and Grading Co., 343 N.W.2d 439, 442 (Iowa 1984); Walters v. Iowa-Des Moines Nat'l Bank, 295 N.W.2d 430, 433-34 (Iowa 1980). In the dissolution context, however, Iowa courts generally do not allow a setoff against a debt owed for support; a modification of the dissolution decree is required. See In re Marriage of Mills, 441 N.W.2d 416 (Iowa Ct.App. 1989)(granting setoff of lien debt against child support arrears would require modification of dissolution decree); In re Marriage of Moffatt, 279 N.W.2d 15, 22 (Iowa 1979)(expenditures to or for to children could not be offset against child support obligation); but see Picht v. Henry, 107 N.W.2d 441 (1961)(narrow exception to general rule; setoff allowed where welfare of children not involved). Setoffs against non-support provisions have been recognized. See Smith v. Brown, 513 N.W.2d 732 (Iowa 1994)(assignee of lien arising

from dissolution decree would be subject to defense of setoff for pre-assignment obligations). In the case at bar, a setoff would affect the enforcement of the property settlement without modifying the dissolution decree. On this distinction, this Court finds that, as a matter of law, Kevin has a right of setoff outside of bankruptcy.

Under the terms of the 1992 dissolution decree, Kevin is obligated to pay a property settlement to Adella. Kevin has a claim against Adella for the amount he paid Hawkeye Bank in 1994. See 11 U.S.C. § 101 (5). Kevin's debt to Adella and Kevin's claim against Adella both arose before Adella filed bankruptcy on July 27, 1995.

Mutuality of obligation requires the parties be indebted to each other in the same capacity or right. Trustee argues that mutuality is lacking because the attempted post-petition setoff would be between Kevin and the Trustee representing the bankruptcy estate. This 'separate entity' doctrine was effectively invalidated by the Supreme Court for purposes of mutuality under § 553. See N.L.R.B. v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984); ASCS v. Gerth, 991 F.2d 1428, 1435-36 (8th Cir. 1993)(citing In re Allen, 135 B.R. at 868-69). In bankruptcy, the Trustee stands in the shoes of the debtor. Mutuality is not lost.

The debt owed by Kevin to Adella pursuant to the property settlement terms of the dissolution decree is property of the bankruptcy estate. See 11 U.S.C. § 541. Kevin's valid right of setoff under § 553 defeats the Trustee's cause of action for turnover of property of the estate. See 11 U.S.C. § 542 (b); David G. Epstein et al., Bankruptcy, §6-39 at 364 (Hornbook Series 1993).

ORDER

IT IS THEREFORE ORDERED that Defendant's Motion for Summary Judgment is GRANTED.

IT IS FURTHER ORDERED that Trustee's Cross-Motion for Summary Judgment in her favor is DENIED.

IT IS FURTHER ORDERED that Kevin Korte is entitled to a setoff against the property settlement owed Adella in the amount of his claim against Adella by virtue of his payment on the promissory note to Hawkeye Bank pursuant to 11 U.S.C. § 553.

Dated this _____ day of January, 1998.

RUSSELL J. HILL, CHIEF JUDGE
U.S. BANKRUPTCY COURT