

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

In the Matter of	:	Case No. 97 – 2228 - CH
	:	
MARK J. WINTER and	:	Chapter 7
PENELOPE WINTER,	:	
	:	
Debtors.	:	
	:	

ORDER – MOTION FOR RELIEF FROM STAY

On May 12, 1997, Debtors, Mark J. and Penelope Winter, filed a Voluntary Petition for Chapter 7 relief under the U.S. Bankruptcy Code. On October 23, 1997, hearing was held on the United States of America's Motion for Relief from Stay and Debtors' Objection thereto. Debtors were represented by attorney John P. Roehrick; Creditor, USA, was represented by Assistant U.S. Attorney William C. Purdy. At the conclusion of the hearing, the Court took the matter under advisement upon a briefing schedule. Post-trial briefs have been filed and 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)(G). 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. 7052.

FINDINGS OF FACT

1. Mark J. and Penelope Winter ("Debtors") filed for relief under Chapter 7 of the Bankruptcy Code on May 12, 1997.
2. Debtors listed Farm Service Agency ("FSA") in their bankruptcy schedules as the holder of a secured claim in the amount of \$80,300 secured by machinery and equipment valued at \$62,250.
3. FSA claims Debtors owe \$120,626.53 as of the date the bankruptcy case was filed.
4. The Notice of Commencement of Case in this matter, filed May 14, 1997, includes a Report of No Asset Case.
5. Debtors did not list any interests in any government program payments or government contracts on their schedules.
6. Debtors have utilized financing from the United States Farmers Home Administration and FSA for their farm operations since 1991.
7. In conjunction with the financing Debtors obtained for 1991, Debtors executed a security agreement on September 11, 1991, to the United States of America ("USA") covering crops, machinery and equipment, and, at Section II, Item 4:

All accounts, contract rights and general intangibles, as follows: All contract rights, chattel paper, documents, accounts and general intangibles, whether now or hereafter existing or acquired, any right to performance, entitlements to payment in cash or in kind, or other benefits under any current or future governmental program.
8. In conjunction with the financing for 1991, Debtors executed a financing statement filed with the Iowa Secretary of State's office on April 29, 1991, and identified as document number K239886.

9. On December 29, 1995, a continuation of the original financing statement was filed with the Iowa Secretary of State's office as document number K699679.

10. On August 23, 1996, Debtors executed a security agreement to the USA covering certain crops, machinery, equipment, accounts, contract rights and general intangibles. At Section II, Item 4, the security agreement covers:

All accounts, contract rights and general intangibles, as follows: All contract rights, chattel paper, documents, accounts and general intangibles, whether now or hereafter existing or acquired, any right to performance, entitlements to payment in cash or in kind, or other benefits under any current or future governmental programs.

11. On June 18, 1996, Debtors entered into a Production Flexibility Contract ("PFC") on CCC form 478 with the U.S. Department of Agriculture Commodity Credit Corporation ("CCC") for Hardin County farm number 1494 ("farm #1494") consisting of 107.6 contract acres.

12. In addition to executing the CCC 478 form, the contract on farm #1494 was supplemented by the terms and conditions contained in the form CCC-478 Appendix.

13. The June 18, 1996 PFC indicated that 100% of any 1996 PFC payments were to go to Mark Winter as Owner/Producer on farm #1494.

14. On December 13, 1996, the June 1996 PFC was supplemented by a certification of contract acres for the year 1997 which indicated 100% of all PFC payments on farm #1494 were to go to Mark Winter as Owner/Producer.

15. The total estimated payment range under the PFC for farm #1494 are found on form CCC-478B and are as follows:

a. 1997	\$5,093 - \$6,090
b. 1998	\$3,986 - \$4,761
c. 1999	\$3,875 - \$4,650
d. 2000	\$3,543 - \$4,318
e. 2001	\$2,879 - \$3,432

f. 2002	\$2,768 - \$3,321
Total:	\$22,144 - \$26,572

16. On June 18, 1996, Debtors entered into a PFC on CCC form 478 with the U.S. Department of Agriculture Commodity Credit Corporation for Hardin County farm #4495 ("farm #4495") consisting of 57.4 acres.

17. In addition to executing the CCC 478 form, the contract on farm #4495 was supplemented by the terms and conditions contained in the form CCC-478 Appendix.

18. The June 18, 1996 PFC indicated that 66.7% of any 1996 PFC payments were to go to Mark Winter as Owner/Producer on farm #4495.

19. On December 13, 996, the June 1996 PFC was supplemented by a certification of contract acres for the year 1997 which indicated 66.7% of all PFC payments on farm #4495 were go to Mark Winter as Owner/Producer.

20. The total estimated payment range under the PFC for farm #4495 are found on form CCC-478B and are as follows:

a. 1997	\$2,895 - \$3,462
b. 1998	\$2,266 - \$2,707
c. 1999	\$2,203 - \$2,644
d. 2000	\$2,014 - \$2,455
e. 2001	\$1,637 - \$1,952
f. 2002	\$1,574 - \$1,889
Total:	\$12,589 - \$15,109

21. On June 18, 1996, Debtors entered into a PFC on CCC form 478 with the U.S. Department of Agriculture Commodity Credit Corporation for Hardin County farm number 4690 ("farm #4690") consisting of 13.3 contract acres.

22. In addition to executing the CCC 478 form, the contract on farm #4690 was supplemented by the terms and conditions contained in the form CCC-478 Appendix.

23. The June 18, 1996 PFC indicated that 100% of any 1996 PFC payments were to go to Mark Winter as Owner/Producer on farm #4690.

24. On December 13, 1996, the June 1996 PFC was supplemented by a certification of contract acres for the year 1997 which indicated 100% of all PFC payments on farm #4690 were to go to Mark Winter as Owner/Producer.

25. The total estimated payment range under the PFC for farm #4690 are found on form CCC-478B and are as follows:

a. 1997	\$671 - \$802
b. 1998	\$525 - \$627
c. 1999	\$510 - \$612
d. 2000	\$466 - \$569
e. 2001	\$379 - \$452
f. 2002	\$364 - \$437
Total:	\$2,915 - \$3,499

26. On July 11, 1996, Debtors entered into a PFC on CCC form 478 with the U.S. Department of Agriculture Commodity Credit Corporation for Hardin County farm number 4796 ("farm #4796") consisting of 193.6 contract acres.

27. In addition to executing the CCC 489 form, the contract on farm #4796 was supplemented by the terms and conditions contained in the form CCC-478 Appendix.

28. The July 11, 1996 PFC indicated that 100% of any 1996 PFC payments were to go to Mark Winter as Owner/Producer on farm #4796.

29. On December 13, 1996, the July 1996 PFC was supplemented by a certification of contract acres for the 1997 year which indicated 100% of all PFC payments on farm #4796 were to go to Mark Winter as Owner/Producer.

30. The total estimated payment range under the PFC for farm #4796 are found on form CCC-478B and are as follows:

a. 1997	\$9,843 - \$11,769
b. 1998	\$7,703 - \$9,201
c. 1999	\$7,489 - \$8,987
d. 2000	\$6,847 - \$8,345
e. 2001	\$5,563 - \$6,633
f. 2002	\$5,350 - \$6,419
Total:	\$42,795 - \$51,354

31. On July 11, 1996, Debtors entered into a PFC on CCC form 478 with the U.S. Department of Agriculture Commodity Credit Corporation for Hamilton County farm number 3946 ("farm #3946") consisting of 42.5 contract acres.

32. In addition to executing the CCC 478 form, the contract on farm #3946 was supplemented by the terms and conditions contained in the form CCC-478 Appendix.

33. The July 11, 1996 PFC indicated that 100% of any 1996-2000 payments were to go to Mark Winter as Owner/Producer on farm #3946.

34. The total estimated payment range under the PFC for farm #3946 are found on form CCC-478B and are as follows:

a. 1996	\$1,170 - \$1,365
b. 1997	\$2,242 - \$2,680
c. 1998	\$1,754 - \$2,096
d. 1999	\$1,706 - \$2,047
e. 2000	\$1,560 - \$1,901
f. 2001	\$1,267 - \$1,511
g. 2002	\$1,218 - \$1,462
Total	\$10,917 - \$13,062

35. Debtors have received payments under the PFC for the first half of the 1997 PFC year.

36. Debtors were to receive their second part of their various 1997 PFC payments in the amount of \$7,219 in September 1997.

37. FSA filed a Motion to Lift Stay to pursue offset of the 1997 second-half PFC payments on September 30, 1997, and is currently holding said PFC payments.

38. The CCC and the FSA are both governmental agencies of the United States.

DISCUSSION

The USA seeks relief from the automatic stay provisions of 11 U.S.C. § 362 (a)(7) in order to enforce its alleged right of setoff under § 553 of Production Flexibility Contract payments by the CCC against the unpaid claims of the FSA. See In re Rinehart, 887 F.2d 165 (8th Cir. 1989). Debtors assert that the USA does not have a right of setoff and they, Debtors, are entitled to PFC payments that would be paid post-petition. Two matters before the Court are whether the USA has a right of setoff and whether grounds exist to grant relief from the automatic stay.

USA Right of Setoff

USA claims to have a right to setoff under § 553. Debtors argue that their agreement with the CCC contains conditions precedent by which CCC has no obligation to perform, that no CCC obligation to pay arose pre-petition, and that there is no present existing contract as to future payments with CCC.

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).

Three elements are required for the USA to establish a right of setoff:

- (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).

By its plain language, the Code does not create a creditor's right to a setoff where one did not exist outside of bankruptcy. The principle of setoff is expressly provided for in the Production Flexibility Contracts. Each of the PFCs entered into between the CCC and Mark Winter expressly states that the terms and condition of the contract are contained in the CCC-478 Appendix. By signing the contract, the producer, Mark Winter, agreed to abide by the terms of the contract and to comply with regulations governing the program, payment eligibility, and limitations. In the form CCC-478 Appendix, paragraph 5(F) states that "[o]ffsets for debts owed to agencies of the U.S. Government shall be made prior to making any payments to producers or their assignees." The Federal Regulations governing the PFC program contain the same provision and additionally incorporate the regulations governing offsets. See 7 CFR § 1412.406; see generally 7 CFR § 1403.7. Mark Winter, in executing the PFCs, agreed to the USA having a right of setoff outside of bankruptcy.

There is no argument that the USA's claim against Debtors, based on loans from FSA to Debtors, arose pre-petition. At issue is whether the debt from the USA to Debtor was "absolutely owed" and arose pre-petition. See Matter of Gerth, 991 F.2d 1528, 1433 (8th Cir. 1993).

Additionally, "[f]or setoff purposes, a debt arises when all transactions necessary for liability occur, regardless of whether the claim was contingent, unliquidated, or unmatured when the petition was filed" . . . and "a debt can be absolutely owing prepetition even though that debt would never have come into existence except for postpetition events." Id., at 1433-34.

After examining the written contracts, the regulations incorporated therein, and the enabling legislation, the Court concludes that the USA's debt to Debtor did arise pre-petition.

The contract terms themselves indicate that each contract was intended to be a seven-year contract. The contract terms contained in the Appendix specify that the contract became effective when signed by a CCC representative and set forth procedures for terminating the contract prior to September 30, 2002. This comports with the federal regulations, which state that the "CCC shall offer to enter into *a 7-year contract* with an eligible producer on a farm having eligible acreage." 7 CFR § 1412.201 (a) (emphasis added). The regulations set forth a window of opportunity, which closed August 1, 1996, during which a producer could enter into PFCs; an exception to the closing of the enrollment period is made for acreage enrolled in CRP contracts that terminate after August 1, 1996. See generally, 7 CFR §§ 1412.501. The regulations expressly state that all contracts terminate on September 30, 2002, absent mutual consent to an earlier termination date. See 7 CFR § 1412.501(c). In addition to the express contractual language, the enabling legislation provides for seven-year contracts as opposed to seven one-year contracts. The stated purpose of the Agricultural Market Transition Act is to "authorize the use of binding production flexibility contracts between the United States and agricultural producers . . ." 7 U.S.C. § 7201 (b) (1997). Under the statute, contracts had to be entered into on or before August 1, 1996 and the contract duration begins with the 1996 crop and extends through the

2002 crop, with limited exceptions not applicable under the facts of this case. See 7 U.S.C. § 7212 (b) (1997).

Debtors argue that the contract terms that impose obligations on Debtor are conditions precedent rather than binding mutual promises. This argument presents an issue of contract interpretation, which requires a determination of the parties' intent as gathered from the entirety of the instrument. See In re Allen, 135 B.R. 856, 864-65 (Bankr. N.D.Iowa 1992).

By signing the contract, Mark Winter agreed that he would timely file forms showing compliance with the federal regulations governing the program. The federal regulations expressly provide that full compliance with the terms of the PFC terms will result in PFC payments. See 7 CFR § 1412.101. Debtor agreed to comply with regulations that restrict land use, require compliance reporting, and that may require the producer to protect against weeds and erosion; the USA agreed to make payments. See generally 7 CFR §§ 1412.201, 1412.206, 1412.207, 1412.303, 1412.304, 1412.401 - 1412.405, 1412.407. The contracts provide for damages that may result from breach of the agreement and cause for termination of the contracts, lending support for the conclusion that the contracts are based on mutual promises as opposed to conditions precedent. The remedy for failing to perform mutual promises would be breach of contract, as provided for in these PFCs, whereas the remedy for failing to perform conditions precedent would be to vitiate the proposed contract. See In re Allen, 135 B.R. at 865. The only condition precedent found in the contracts is the express requirement that the contracts become effective when signed by the CCC's authorized representative. At the time the CCC representative signed the contracts, the parties were bound by their mutual promises.

Each of the contracts between Mark Winter and the CCC are seven-year contracts. Winter's obligations to comply with land use and to file compliance reports are promises under the

binding contracts; the USA promised to make contract payments so long as Winter kept his promises. Under the contract terms, payment eligibility is contingent on the producer obtaining crop insurance or providing a written waiver regarding crop loss assistance. Making payments under the contract contingent on Debtor's compliance with the federal regulations governing the program does not affect when the USA's contractual liability arose. See generally Gerth, 991 F.2d at 1434.

Separate departments and agencies of the federal government are a single entity for mutuality purposes under the setoff provisions of the Code. See Matter of Butz, 154 B.R. 541, 544 (S.D.Iowa 1989)("All federal agencies are an integral part of the federal government and entitled to settled statutory priority in collecting on loans made from government funds.")(cites omitted). The FSA and CCC are both governmental agencies of the United States and stand in the same capacity for purposes of setoff.

Relief from Automatic Stay

USA seeks relief from the automatic stay provisions of § 362 (a)(7) to allow it to proceed with collection and offset of PFC payments against the pre-petition claims of the Farm Service Agency. By establishing a right of setoff, the USA has made a prima facie showing of "cause" for relief from stay under § 362 (d)(1). See In re Warwick, 179 B.R. 582 (Bankr. W.D.Ark. 1995)(citing In re Orlinski, 140 B.R. 600, 603 (Bankr. S.D.Ga. 1991)). The burden then shifts to Debtors to show that adequate protection will be provided. Debtors in this case make no such showing.

ORDER

IT IS THEREFORE ORDERED that USA's motion for relief from the automatic stay in order to exercise a right of setoff under § 553 is GRANTED pursuant to 11 U.S.C. § 362 (d).

Dated this _____ day of March 1998.

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