

**SO ORDERED.**

**SIGNED this 6th day of October, 2014.**



*Dale L. Somers*

Dale L. Somers  
United States Bankruptcy Judge

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**Opinion Designated for Electronic Use, But Not for Print Publication  
IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF KANSAS**

**In re:**

**AMELIA LUE ROCK,**

**DEBTOR.**

**CASE NO. 13-22232-13  
CHAPTER 13**

**OPINION DENYING DEBTOR'S REQUEST FOR ATTORNEY FEES**

This matter is before the Court for a ruling following a hearing on August 28, 2014, on the Debtor's request for sanctions against UnitedHealthcare Specialty Benefits, LLC (UHCSB), for alleged violations of the automatic stay. The Debtor appears by counsel Sarah A. Sypher of Sypher Law Group, LLC. UHCSB appears by counsel Michael D. Fielding of Husch Blackwell LLP and Eric S. Goldstein of Shipman & Goodwin LLP. The Court has reviewed the relevant pleadings and heard the arguments of counsel, and is now ready to rule. At this point, the question is whether the doctrine of

recoupment provides UHCSB a defense to actions it took that would otherwise constitute violations of the automatic stay imposed by § 362(a) of the Bankruptcy Code. As explained below, the Court concludes UHCSB properly withheld money from postpetition disability benefits it owed the Debtor in order to recoup an overpayment of the benefits that had been made to the Debtor before she filed bankruptcy. Consequently, UHCSB did not violate the automatic stay, and is not liable to the Debtor for attorney fees she incurred in trying to get UHCSB to stop the withholding and refund the money it withheld postpetition.

## **Facts**

Before April 2010, the Debtor was working as a nurse for the State of Kansas in the psychiatric ward of a hospital. In 2010, she was injured by a patient in a way that led to back surgery. By April 2010, she was no longer able to work and began receiving long-term disability benefits under a plan sponsored by the Kansas Public Employees Retirement System. UHCSB administers the plan for KPERS. The plan called for the Debtor's benefits to be reduced to the extent she received income from certain other sources, including workers' compensation benefits. The plan gave the administrator the right to recover any overpayments, and to determine the method by which repayment would be made. In 2011, the Debtor received a workers' compensation award of \$7,300. Under the plan, that amount was treated as an overpayment of her disability benefits, and in accordance with the plan, UHCSB reduced the Debtor's future benefits by \$100 per month in order to recoup that overpayment from her.

Between 2011 and 2013, the Debtor developed additional health problems that she attributes to her work injury, including diabetes and a heart condition. She needs several medications in order to stay alive. The monthly withholding from her disability benefits has made it more difficult for her to pay her rent and purchase her necessary medicine. By August 2014, she was approximately 60 years old.

In August 2013, the Debtor filed a Chapter 13 bankruptcy petition. Her attorney assumed UHCSB would stop the \$100 per month withholding, and included that assumption in drafting the Debtor's Chapter 13 plan. The plan was confirmed in October 2013. Despite receiving actual notice of the Debtor's bankruptcy filing, UHCSB continued to withhold \$100 per month from her disability payments to continue recovering the overpayment from her.

The Debtor's attorney contacted UHCSB and at first was advised the withholding would stop, but later was told it would continue. Eventually, an attorney for UHCSB advised her that the company believed the monthly withholding was in the nature of recoupment and therefore not prohibited by the automatic stay, providing citations to a number of cases concerning recoupment. On June 11, 2014, the Debtor filed a motion asking the Court to compel UHCSB to turn over to the Debtor all the money it had withheld postpetition, to impose a sanction against UHCSB for violating the automatic stay by continuing to withhold \$100 per month from her benefits after she filed bankruptcy, and to require UHCSB to pay her \$1,500 in attorney fees as an additional sanction under § 362(k)(1). In a response filed on July 11, 2014, UHCSB continued to

assert the monthly withholding was a permissible recoupment that did not violate the stay. Nevertheless, it advised that KPERS had voluntarily agreed to stop withholding any money from the Debtor's future disability benefits, to waive the remaining balance owed on the prepetition overpayment (approximately \$4,120), and to refund the \$800 that had been withheld since the Debtor filed bankruptcy.

A hearing on the Debtor's motion was held on August 28, 2014. In light of KPERS's decision to waive the balance of the overpayment and to refund the money that had been withheld postpetition, the only outstanding relief the Debtor was seeking was for UHCSB to pay her attorney fees. The Court told the parties the only issue it had to decide was whether UHCSB had violated the automatic stay. There was no question that the company thought it had the absolute right to continue the monthly withholding without getting stay relief. If that was wrong, the Court stated that a reasonable attorney fee was the only sanction the Court would impose.

### **Discussion**

Ordinarily, any postpetition efforts a creditor takes to recover a prepetition obligation from a debtor are violations of the automatic stay imposed by § 362(a) unless the creditor first obtains relief from the stay. The Debtor sensibly suggests that even if UHCSB's actions were proper recoupment, the company should at least have asked this Court to confirm that fact by asking for stay relief, instead of relying solely on its own determination. A leading bankruptcy treatise says that courts are split on the question

whether the automatic stay applies to bar or restrain a legitimate right of recoupment.<sup>1</sup> However, assuming for the moment that UHCSB had a valid right to recoup the overpayment, binding Tenth Circuit precedent prohibits this Court from ruling that UHCSB was required to seek stay relief before it continued to withhold the \$100 from the Debtor's monthly benefit payment.<sup>2</sup>

At least within the Tenth Circuit, the doctrine of recoupment is a well-established exception to the automatic stay, as well as to the discharge injunction imposed by § 524(a).<sup>3</sup> Recoupment originated as an equitable rule of joinder, allowing adjudication in one suit of two claims that the common law had required to be brought separately.<sup>4</sup> “Under recoupment, a defendant could meet a plaintiff’s claim with a countervailing claim that arose ‘out of the same transaction.’”<sup>5</sup> In bankruptcy, “[r]ecoupment’ is an equitable doctrine . . . that allows one party to a transaction to withhold funds due another

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<sup>1</sup> *Collier on Bankruptcy*, ¶ 553.10 at 553-93 (Alan N. Resnick & Henry J. Sommer, eds.-in-chief, 16th ed. 2014).

<sup>2</sup> *Beaumont v. Dept. of Veteran Affairs (In re Beaumont)*, 586 F.3d 776, 781 (10th Cir. 2009) (“If the recoupment doctrine applies, then there is no ‘debt’ or ‘claim’ here as defined in the Bankruptcy Code, and [the party who exercised recoupment rights] has not violated the automatic stay nor the discharge injunction”).

<sup>3</sup> *See id.*, 586 F.3d at 781; *In re Lunt*, 477 B.R. 812, 818-19 (Bankr. D. Kan. 2012), *aff’d* 500 B.R. 9 (D. Kan. 2013); *see also Ashland Petroleum Co. v. Appel (In re B&L Oil Co.)*, 782 F.2d 155, 159 (10th Cir. 1986) (“The general principle is that a petition for bankruptcy operates as a ‘cleavage’ in time; but the recoupment doctrine has traditionally operated as an exception to the rule that applies to other debts.”).

<sup>4</sup> *Ashland Petroleum Co. v. Appel (In re B & L Oil Co.)*, 782 F.2d 155, 157 (10th Cir. 1986).

<sup>5</sup> *Id.* (citing J. Moore, 3 *Moore’s Federal Practice*, ¶ 13.02 at 13-13, n. 1 (2d ed. 1985) and 20 *Am. Jur. 2d Counterclaim, Recoupment, and Setoff*, §§ 16-18 (1965)).

party where the debts arise out of the same transaction. In other words, the doctrine ‘allows a creditor to recover a pre-petition debt out of payments owed to the debtor post-petition.’”<sup>6</sup>

Whether UHCSB’s postpetition withholding from the Debtor’s disability benefits was protected by the recoupment doctrine depends on whether the Debtor’s obligation to repay the benefits overpayment arose out of the “same transaction” as her right to receive continuing disability benefits.<sup>7</sup> This means that “both debts must arise out of a single integrated transaction so that it would be inequitable for the debtor to enjoy the benefits of that transaction without also meeting [the debtor’s] obligations.”<sup>8</sup> The Court must examine the equities of the case, and determine whether the Debtor’s claim for ongoing disability benefits and UHCSB’s claim to recover the prepetition overpayment of benefits “are so closely intertwined that allowing the debtor to escape [her] obligation would be inequitable notwithstanding the Bankruptcy Code’s tenet that all unsecured creditors share equally in the debtor’s estate.”<sup>9</sup>

After considering the equities here, the Court concludes it must agree with

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<sup>6</sup>*Beaumont*, 586 F.3d at 780 (quoting *Conoco, Inc., v. Styler (In re Peterson Distributing, Inc.)*, 82 F.3d 956, 959 (10th Cir. 1996), and *City of Fort Collins v. Gonzales (In re Gonzales)*, 298 B.R. 771 (Bankr. D. Colo. 2003)).

<sup>7</sup>See *Beaumont*, 586 F.3d at 781.

<sup>8</sup>*Peterson Distributing*, 82 F.3d at 960 (quoting *University Medical Ctr. v. Sullivan (In re University Medical Ctr.)*, 973 F.2d 1065, 1081 (3d Cir.1992)).

<sup>9</sup>*Peterson Distributing*, 82 F.3d at 960.

UHCSB that this case cannot be distinguished from *In re Beaumont*<sup>10</sup> on any relevant basis. In *Beaumont*, the Tenth Circuit held that the Department of Veteran Affairs (VA) did not violate either the automatic stay or the discharge injunction by reducing the debtor's ongoing benefits under a VA disability program in order to recover a prepetition overpayment of benefits, even though it continued with the reduction after the debtor filed bankruptcy and after he received a discharge. The debtor was a disabled veteran who had been receiving disability benefits for eight years when he was given a large probate distribution. Pursuant to federal statutes, the debtor's VA benefits were subject to being reduced if he received any payments from any other source, including an inheritance. After learning of the inheritance, the VA advised the debtor that it had determined the probate distribution had made him ineligible for his VA benefits for a period of time, which meant he had received an overpayment of \$18,448 in benefits, and that the VA intended to collect that amount by offsetting his future disability payments, as was expressly permitted by statute. The debtor responded by filing for bankruptcy relief, and the VA continued to offset his benefits during the bankruptcy proceeding and after he received a discharge. The debtor contended this conduct violated the automatic stay and the discharge injunction. The Tenth Circuit disagreed.

This Court finds that the obligations of both parties did arise from the "same transaction." [Plaintiff-debtor's] claim for and award of pension benefits generated the [Defendant VA's] obligation to pay those benefits. The Defendant's

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<sup>10</sup>586 F.3d 776.

obligation to pay benefits was and is contingent upon Plaintiff's financial situation, his annual income, and his responsibility to keep the Defendant informed of his financial situation. Plaintiff's inheritance had the effect of reducing the amount of benefits he could receive from the Defendant. Therefore, Plaintiff's inheritance was directly related to or intertwined with the amount of benefits Defendant was obligated to pay to him, and the resulting overpayment of benefits. It is unlawful for Plaintiff to keep any overpayments so long as the Defendant, through its own administrative procedures, has properly determined the amount of overpayment and properly considered Plaintiff's disagreement with that determination. The Court believes that it would be inequitable for the Plaintiff to receive his inheritance, continue to receive benefits as if his income was zero, then be able to discharge in bankruptcy the overpayments once it was determined that he had been overpaid.<sup>11</sup>

The same can be said in this case: It would be inequitable for the Debtor to receive her workers' compensation award, continue to receive disability benefits as if she had not received the award, then be able to discharge in bankruptcy the overpayment once it was determined she had been overpaid.

Pointing to the equitable nature of the recoupment doctrine, the Debtor argues her unfortunate ongoing health problems and financial condition should convince the Court not to condone UHCSB's efforts to recoup the overpayment of disability benefits she received. But the Court does not understand the 10th Circuit and other courts applying recoupment to mean the availability of the doctrine ever depends on its impact on the debtor based on anything about the debtor other than the direct relationship between the

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<sup>11</sup> *Id.* at 781.

prepetition obligation the creditor wants to recoup and the postpetition benefit the creditor will be providing to the debtor. Instead, the equities to be considered are whether the debtor's postpetition benefits are so intertwined with the overpayment or other obligation the debtor incurred that allowing the debtor to continue to receive those benefits without meeting the obligation would be inequitable, or whether it would be unfair for the party providing the postpetition benefits to recover on the related prepetition obligation when the debtor's other creditors are not being made whole.<sup>12</sup> The Debtor has cited no case where a court ruled that anything else about the debtor's circumstances precluded a party from exercising an otherwise proper right to recoup an obligation the debtor incurred before filing bankruptcy, and this Court has found none. While the Court feels sympathy for the Debtor's health and financial problems, the recoupment doctrine allows no room for such considerations to affect its application.

The Court did find one case relying on an equitable consideration that might be viewed as involving the debtor's unfortunate financial circumstances, the Third Circuit's decision in *Lee v. Schweiker*.<sup>13</sup> In that case, after the debtor filed bankruptcy, the Social Security Administration continued to reduce her monthly old-age benefits in order to recover a prepetition overpayment of those benefits. The Third Circuit ruled the SSA's

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<sup>12</sup>See, e.g., *Conoco v. Styler (In re Peterson Distributing, Inc.)*, 82 F.3d 956, 959-63 (10th Cir. 1996) (denying recoupment); *Davidovich v. Welton (In re Davidovich)*, 901 F.3d 1533, 1537 (10th Cir. 1990) (allowing recoupment of one obligation but not another); *B&L Oil*, 782 F.2d at 159 (allowing recoupment).

<sup>13</sup>739 F.2d 870 (1984).

action violated the automatic stay, saying,

Social welfare payments, such as social security, are statutory “entitlements” rather than contractual rights. The purpose of these payments is to provide income to qualifying individuals. Although the paying agency can ordinarily recover overpayments, just as creditors can ordinarily obtain payment from a debtor’s future income, the Bankruptcy Code protects a debtor’s future income from such claims once a petition has been filed, and the SSA violated the automatic stay in continuing to withhold part of [the debtor’s] benefits after she had filed her petition.<sup>14</sup>

Benefits paid to a debtor based on being unable to work could similarly be viewed as social welfare payments, which suggests the Third Circuit might apply a similar rule to disability payments like those the Debtor is receiving in this case. But the Tenth Circuit’s *Beaumont* decision, dealing with VA disability benefits, makes clear this Court cannot rely on the social welfare aspect of the benefits involved in this case to conclude that the recoupment doctrine did not protect UHCSB’s postpetition recovery of the prepetition overpayment the Debtor received.

Under the circumstances of this case, the Court concludes UHCSB was entitled to recoup the prepetition overpayment that resulted when the Debtor received her workers’ compensation award from the postpetition payments it owed the Debtor under the KPERS long-term disability plan. Consequently, UHCSB did not violate the automatic stay by deducting \$100 per month from the postpetition benefits it paid the Debtor, and is therefore cannot be liable to her for the attorney fees she incurred trying to get the deductions stopped.

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<sup>14</sup>*Id.* at 876.

## **Conclusion**

For the reasons stated, the Court denies the Debtor's request that UHCSB be ordered to pay her attorney fees.

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