

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF ILLINOIS**

IN RE:

JAMES H. COFFEY and SANDRA COFFEY,

No. 04-32287

Debtors.

**VANTAGE CREDIT UNION
FKA EDUCATIONAL EMPLOYEES CREDIT
UNION,**

Movant,

vs.

**JAMES H. COFFEY and SANDRA COFFEY,
Debtors, and DONALD M. SAMSON, Trustee,
Respondents.**

OPINION

The matter before the Court is the Motion For Relief From the Automatic Stay To Effectuate Post-Petition Setoff filed by the Vantage Credit Union [Vantage]. The pertinent stipulated facts are as follows. In February of 1999, the Debtors, James Coffey and Sandra Coffey (Debtors), entered into a credit card relationship with Vantage. The Debtors also maintained a checking account at Vantage. On June 7, 2004, the Debtors filed their Chapter 7 case in bankruptcy. At the time of the filing, the Debtors owed Vantage \$3,742.08 for charges made on the credit card and the Debtors had \$1,516.12 in their checking account. The notice of the filing of the bankruptcy was mailed to a lock box and resulted in some delay in Vantage actually learning of the bankruptcy. On June 22, 2004, Vantage placed an administrative hold on the funds in the checking account, and on June 23, 2004, filed the motion presently before the Court. Between June 7 and June 22, there were fifty-one (51) withdrawals from the checking account totaling \$1,968.82 and five (5) deposits totaling \$2,020.90.

Vantage seeks relief from the automatic stay to set off \$1,516.12 in the checking account against the debt owed it on the credit card. The Debtors oppose the motion, arguing Vantage cannot set off against funds deposited into the checking account postpetition against a prepetition debt. The Debtors are correct.

Section 553 of the Bankruptcy Code governs set-off and provides in part as follows:

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 owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor that arose before the commencement of the case....

11 U.S.C. § 553.

A creditor may not setoff postpetition deposits against a prepetition debt. *In re Czyzk*, 297 B.R. 406 (Bankr.D.N.J. 2003); *In re Harris*, 260 B.R. 753 (Bankr.D.Md. 2001). This Court, sitting in the Central District of Illinois, addressed this issue in *In Re Erickson*, 216 B.R. 938 (Bankr.C.D.Ill.1998), a case with similar facts and in holding the creditor did not have the right of set-off stated:

Section 553(a) of the Bankruptcy Code preserves a creditor's right of setoff, but only for a "mutual debt owing by such creditor to the debtor that arose before the commencement of the case," 11 U.S.C. § 553(a). The filing of a bankruptcy petition marks the time at which mutuality ceases; any funds thereafter deposited are considered property of the debtor or the bankruptcy estate. *In re Samuels*, 31 B.R. 120 (Bkrcty.M.D.Pa. 1983); *In re All-Brite Sign Service Co., Inc.*, 11 B.R. 409 (Bkrcty.W.D.Ky. 1981).

Furthermore, the right of setoff is not self-executing and a bank may fail to timely exercise its setoff rights. *First National Bank in Fort Lauderdale v. Davis*, 317 F.2d770(5thCir.1963). When a bank releases funds in the debtor's account the right to setoff is lost. *Matter of Litchfield Const. Management, Inc.*, 137 B.R. 98 (Bkrcty.D.Conn.1992); *In re Williams*, 422 F.Supp. 342 (N.D.Ga.1976).

[Defendant] suggests that it took appropriate steps as soon as it learned of the [Debtors'] bankruptcy filing and that the [Debtors] were wrong to continue to write checks on the account. As to the first point, a bank can monitor bankruptcy filings by its customers by a variety of methods. A bank can examine the court files daily. [FN2] It can read daily publications that publish bankruptcy filings, or it can check daily bulletins issued by credit bureaus. Finally, it can await actual notice from the bankruptcy system, with its attendant delay. *See In re Carpenter*, 14 B.R. 405 (Bkrcty. M.D.Tenn.1981). If it elects the latter, it cannot resurrect a right of setoff which has been lost in the interim.

FN2. This Court recognizes that is not an efficient method and that few, if any, banks utilize it.

Contrary to [Defendant's] assertion, the consequences of not allowing a bank to retroactively setoff against the balance in an account when it learns of the bankruptcy is not so great so as to justify deviating from the established holdings that the right of setoff can not reach post-petition deposits and the right can be lost if prompt action is not taken. In a broad sense banks have always had a problem when dealing with the deposit account of a bankrupt depositor during the period between the filing and notice of the bankruptcy, and the problem facing [Defendant] in this case is not a new or unique one for banks.

In re Bank of Marin, 385 U.S. 99, 87 S.Ct. 274, 17 L.Ed.2d 197 (1966) presented one

aspect of the problem and the United States Supreme Court held that a bank was not liable to a bankruptcy trustee for pre-petition checks honored post-petition when it had no notice of the bankruptcy filing. The effect of *Marin is* that until a bank receives notice of a depositor's bankruptcy, it can honor checks in a normal fashion as if bankruptcy had not occurred.

The case before this Court presents another aspect of the problem, one with a risk of loss for [Defendant]. Attendant to the right to honor a bankrupt depositor's checks in a normal fashion up until the time it receives notice of the bankruptcy, is the concurrent risk that its right of setoff will be diminished or lost during that period, just as it would be diminished or lost in a non-bankruptcy situation.[FN3]

FN3. In this case, contrary to [Defendant's] assertion, 6 or possibly 7 of the 15 checks honored by [Defendants] post-petition were written pre-petition.

The Stipulation of Facts merely provides the balance of the checking account at the time of filing and the total of the withdrawals and deposits. There is no specific itemization by date showing each withdrawal and each deposit and the balance after each activity.

In the typical checking account relationship, most courts follow a first-in, first-out rule. The Uniform Commercial Code also adopts a first-in, first-out rule. *See*, 1 BRADY ON BANK CHECKS: The Law of Bank Checks ¶16. 10 (Henry J. Bailey & Richard B. Hagedorn). As the withdrawals in the case before this Court exceeded the balance in the account on the date of the filing, all the funds on deposit on the date Vantage placed the administrative hold on the checking account are postpetition funds.

In *First Nat. Bank in Fort Lauderdale v. Davis*, 317 F.2d 770 (5th Cir. 1963), the court followed earlier bankruptcy cases applying the "first-in, first-out" rule to bank set-offs, and held the right to set-off is not self-executing, and where it is not exercised it was lost after funds on deposit at the time of the filing were paid out and the right did not run to funds deposited later.

Therefore the motion should be denied and Vantage should release the administrative hold on all the funds in the Debtors' checking account.

This Opinion constitutes this Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. A separate Order will be entered.

Dated: August 23, 2004

/s/ WILLIAM V. ALTENBERGER
UNITED STATES BANKRUJPTCY JUDGE

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