

## *The Law of Offset*

February 2010

Businesses build and exist on relationships. Unfortunately, sometimes those relationships become so strained that businesses and/or the partners start suing each other.

When this situation occurs the court may order an "offset." However, a litigant cannot wait until the day of trial to request one.

Two judgments from two lawsuits in one action are required before the court may order an "offset" of judgments.

The California Court of Appeals explained this legal option, "California has multiple statutory setoff provisions, including, and in addition to Government Code section 12419.5 and Code of Civil Procedure section 431.70 which authorizes the setoff of cross-demands for money and Code of Civil Procedure section 666, which *requires* a setoff where a cross-complainant's recovery exceeds that of the plaintiff." *Garg v. People ex rel. State Bd. of Equalization*, 53 Cal. App. 4th 199

As you can see, although offset sounds simple in theory, it can and is a very complicated matter. Not all of the different code sections are going to apply in every situation so each situation could require a different process.

CCP §431.70 allows an offset to be pled as an affirmative defense for a cross-demand for money only when it was not pled somewhere else before.

431.70. Where cross-demands for money have existed between persons at any point in time when neither demand was barred by the statute of limitations, and an action is thereafter commenced by one such person, the other person **may assert in the answer** the defense of payment in that the two demands are compensated so far as they equal each other, notwithstanding that an independent action asserting the person's claim would at the time of filing the answer be barred by the statute of limitations. If the cross-demand would otherwise be barred by the statute of limitations, the relief accorded under this section shall not exceed the value of the relief granted to the other party. **The defense provided by this section is not available if the cross-demand is barred for failure to assert it in a prior action under Section 426.30.** Neither person can be deprived of the benefits of this section by the assignment or death of the other. For the purposes of this section, a money judgment is a "demand for money" and, as applied to a money judgment, the demand is barred by the statute of limitations when enforcement of the judgment is barred under Chapter 3 (commencing with Section 683.010) of Division 1 of Title 9. CCP §431.70. [emphasis added]

In the usual case, an offset has the salutary effects of (1) eliminating a superfluous exchange of money between mutual debtors *Jess v Herrmann*, supra. 26 Cal. 3d at p. 137), and (2) protecting each party from the risk that the other may collect the debt owed to him or her, then default upon his or her own obligation. (*Ibid.*) However, the benefits of a setoff are sometimes outweighed by the risk of unfairness which may be created by

allowing a setoff in specific circumstances. When this is the case, in light of the equitable origin of setoff rights, such rights may be restricted by judicial limitations imposed to uphold independent state policy. *Kruger v Wells Fargo Bank*, supra 11 Cal. 3d at p. 367-368.) In *Jess v Herrmann*, supra. 26 Cal 3d 131, the mandatory setoff provided in Code of civil Procedure section 666 was found inapplicable and improper between insured parties in comparative fault cases, because in such cases, a setoff of liabilities would be in conflict with California's financial responsibility laws.

However, where one party's debt has been extinguished in bankruptcy, that debt can no longer be used to offset damages awarded to the other.

“It is well settled that once a debt has been extinguished, a creditor cannot effect a second recovery. *Adams v Southern Pacific Co.* (1928) 204 Cal. 63 [266 P. 541, 57 A.L.R. 1066].” ***Hughes Tool Co. v. Max Hinrichs Seed Co.*, (1980) 112 Cal. App. 3d 194.**

**This newsletter is provided as an example of a complex legal issue that the Law Offices of Lenore Albert can help you with in office. However, such complex legal issues are not dealt with through InteractiveCounsel.**

Copyright 2010 Law Offices of Lenore Albert