

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
ROOM 211
FEDERAL BUILDING AND U.S. POST OFFICE
225 SOUTH PIERRE STREET
PIERRE, SOUTH DAKOTA 57501-2463

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BANKRUPTCY JUDGE

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Subject: *In re Tri-State Ethanol L.L.C.*,
Chapter 7, Bankr. No. 03-10194

Dear Counsel:

The matter before the Court is the Motion to Approve Settlement with Murphy Brothers filed by Trustee John S. Lovald and the objection thereto filed by Tri-State Financial, L.L.C. This letter decision and accompanying order shall constitute the Court's findings and conclusions under Fed.Rs.Bankr.P. 7052 and 9014(c).

As set forth below, the trustee's motion will be granted.

Summary. Tri-State Ethanol L.L.C. ("Tri-State Ethanol") built and operated, for a short time, an ethanol plant. White Rock Pipeline, L.L.C. ("White Rock") constructed a pipeline to the ethanol plant. White Rock was owned by William F. Murphy Self-Declaration of Trust and Mike D. Murphy (collectively "the Murphys"), Walter Woods, Randy Kramer, and Tri-State Ethanol. On February 28, 2002, the Federal Energy and Regulatory Commission directed White Rock to transfer the pipeline to Tri-State Ethanol.¹

On October 15, 2002, Tri-State Ethanol, White Rock, and the Murphys entered into a LOAN AGREEMENT. The LOAN AGREEMENT provided, *inter alia*, that Tri-State Ethanol would borrow \$380,000.00 from the Murphys. As stated in the document, the loan's purpose was

[t]o purchase the interests of the members of White Rock as follows:

• Tri-State Ethanol Company, LLC	\$275,000.00
• William F. Murphy Self-Declaration of Trust	\$78,497.00
• Mike D. Murphy	\$78,504.00
• Walter Woods	\$78,616.00
• Randy Kramer	\$65,842.00

The interests of the William F. Murphy Self-Declaration of Trust, Mike D. Murphy, Walter Woods, and Randy Kramer, as set forth above, shall be paid for in cash. The interest of Tri-State Ethanol Company, L.L.C., in the amount of \$275,000.00, shall be paid by certain credits given to Tri-State Ethanol Company, L.L.C. pursuant to the terms of the Secured Promissory Note. By their signatures below, William F. Murphy, Trustee, Mike D. Murphy, Walter Woods and Randy Kramer hereby agree to accept the amounts set forth above respectively, for their interest in White Rock.

The document did not state when the Murphys were to pay the White Rock members. All parties involved, including the White Rock members, signed the document, though the members' signatures were on a separate page and were not attested to or notarized.

Under other terms of the October 15, 2002, LOAN AGREEMENT, Tri-State Ethanol was also borrowing \$2,100,000.00 from the Murphys to pay to Murphy Bros., Inc., and Alliance Pipeline, L.P., certain construction costs related to the pipeline's construction, which

¹ The Court was not provided with a copy of the Commission's directive and thus has no knowledge of why the directive was given and whether any time constraints were imposed.

totalled \$1,361,154.00, as well as other unknown accounts payable owed by White Rock. Any unused loan funds, which amount was also unknown, were to go to Tri-State Ethanol after the last White Rock accounts receivable were paid by the Murphys. Under this document, Tri-State Ethanol also agreed to give the Murphys a security interest in its real and personal property. It is unknown when, if ever, these secured interests were perfected.

In apparent conjunction with the October 15, 2002, LOAN AGREEMENT, Randy Kramer, as chairman of Tri-State Ethanol, signed a SECURED PROMISSORY NOTE dated October 15, 2002. Under this note, Tri-State Ethanol agreed to repay \$2,100,000.00 to the Murphys. The document acknowledged only \$1,825,000.00 would be advanced to Tri-State Ethanol and stated "[t]he \$275,000.00 difference represents the undersigned's interest in White Rock Pipeline, L.L.C., . . . , and the undersigned shall receive a credit for such amount in its monthly payments. . . ." The SECURED PROMISSORY NOTE provided "credit" only payments of \$31,500.00 for three months, a credit only payment of \$13,885.00 in the fourth month, payments of \$17,615.00 and "credit" payments of \$13,885.00 for the fifth through sixteenth months, and then full monthly payments of \$31,500.00 for the seventeenth month through the last monthly payment scheduled on October 15, 2012. The SECURED PROMISSORY NOTE also provided:

This Note may be paid in full at any time. Upon payment in full of the principal and accrued interest then due, the following amount shall then also be paid by the undersigned:

1. If the principal and accrued interest is paid in full on or before November 15, 2003, the undersigned shall also pay to the holder hereof the sum of \$100,000.00.
2. Thereafter, following each November 15th through the subsequent November 15th, an additional \$50,000.00 shall be added to the previous year's sum, not to exceed a total of \$500,00.00, as an additional amount due to the holder hereof at the time of payment in full of the principal and all accrued interest, more particularly set forth as follows . . .
3. In the event payment in full of the principal and all accrued interest prior to the end of the sixteenth (16th) month following the date hereof, any unused credits set forth in paragraphs A and B, above, shall be deducted from the amount then due from the undersigned to holder hereof.

Though somewhat difficult to decipher, these paragraphs appear to

create an accelerating penalty. The SECURED PROMISSORY NOTE also contained some provisions for interest terms and late charges the Court could not fully glean from the record provided.²

Randy Kramer also signed, on behalf of Tri-State Ethanol, a document dated October 15, 2002, entitled BALLOON SECURED PROMISSORY NOTE. This document provided the repayment terms for the \$380,000.00 Tri-State Ethanol borrowed from the Murphys. The first payment of principal and interest was to be made November 15, 2002, and a balloon payment was due March 15, 2004. The interest rate was 13.117%. The document provided the note could be paid in full at any time without penalty. The document also included certain default provisions and a default interest rate.

Randy Kramer, as secretary for White Rock, and Albert Braun, as secretary for Tri-State Ethanol, each signed a CERTIFICATE OF SECRETARY reciting each entity's resolution authorizing the notes and related agreements. The body of each certificate and the date line stated the documents were "effective October 15, 2002[.]" Thus, it is unknown when each entity's resolution was adopted and when the certificates were actually signed.

A fifth document dated October 15, 2002, was a SECURITY AGREEMENT signed by White Rock and the Murphys. The document gave the Murphys a secured interest in the natural gas pipeline as well as some personalty, accounts, and intangibles. The pledge was to secure all the debts owed by Tri-State Ethanol to the Murphys.

Three separate TRANSFER OF OWNERSHIP INTEREST documents were signed by Mike D. Murphy and William F. Murphy for his Self-Declaration of Trust (one document), Walter J. Woods (second document), and Randy

² The copy of the SECURED PROMISSORY NOTE dated October 15, 2002, provided to the Court as part of the Murphys' brief was not complete. The first page did not transition smoothly to the second page, and the second page did not transition smoothly to the third page. Trustee Lovald provided an apparent full page one as an attachment to his brief but the Court may still not have a full page two. It appears some lines at the bottom of page two may have been cut off during copying, as was the apparent problem with the page one provided by the Murphys.

Kramer (third document). Each was dated "as of October 15, 2002" and provided in full:

In consideration of Tri-State Ethanol Company, LLC, a South Dakota limited liability company, hereinafter called ("TEC"), signing the Loan Agreement dated as of October 15, 2002, with Whiterock Pipeline, L.L.C., a South Dakota Limited liability company, hereinafter called ("Whiterock"), Mike D. Murphy and the William F. Murphy Self-Declaration of Trust, and others along with all documents related to such Loan Agreement, the undersigned hereby transfers all of his ownership interest in Whiterock to TEC and hereby makes no further claim to any ownership interest in Whiterock.

The three transfer documents were nearly identical. In all three, the names of Randy Kramer and Walter J. Woods were never set forth in the body of the document.

The last document given to the Court was a DISBURSEMENT AGREEMENT, which said it was "made effective as of the 15th day of October, 2002" and was signed by Mike D. Murphy, William F. Murphy Self-Declaration of Trust, Walter Woods, and Randy Kramer. The DISBURSEMENT AGREEMENT acknowledged the LOAN AGREEMENT signed by the several parties and the BALLOON SECURED PROMISSORY NOTE for \$380,000.00 signed by Tri-State Ethanol. The DISBURSEMENT AGREEMENT stated "the parties desired to provide a mechanism to repay their membership interest in White Rock out of the loan payments to the William F. Murphy Self-Declaration of Trust and Mike D. Murphy required by the Balloon Secured Promissory Note." The DISBURSEMENT AGREEMENT then provided:

[I]n consideration of the premises and the promises contained herein, it is hereby agreed as follows:

A. 79.3% (\$301,459.00/\$380,000.00) of each monthly loan payment made to the William F. Murphy Self-Declaration of Trust and Mike D. Murphy pursuant to the terms of the Balloon Secured Promissory Note shall be disbursed to the parties hereto, *pari passu*, and the remaining amount of each monthly payment shall be retained by the William F. Murphy Self-Declaration of Trust and Mike D. Murphy, equally.

B. After the parties have been repaid their full membership interest in White Rock as follows:

- William F. Murphy Self-Declaration of Trust \$78,497.00
- Mike D. Murphy \$78,504.00
- Walter Woods \$78,616.00

• Randy Kramer	<u>\$65,842.00</u>
Total	\$301,459.00

all further monthly payments pursuant to the terms of the Balloon Secured Promissory Note shall be retained in total by the William F. Murphy Self-Declaration of Trust and Mike D. Murphy, equally.

The parties to this matter universally acknowledge the members of White Rock did not transfer their interests in White Rock to Tri-State Ethanol on or around October 15, 2002. There also appears to be no dispute that Tri-State Ethanol made only one payment on the BALLOON SECURED PROMISSORY NOTE on March 10, 2003.

On May 23, 2003, Tri-State Ethanol (hereinafter "Debtor") filed a Chapter 11 petition in bankruptcy. Debtor's Chapter 11 case was converted to a Chapter 7 case on July 29, 2004. John S. Lovald was appointed the case trustee. The ethanol plant owned by the bankruptcy estate was sold at auction on October 26, 2004. The high bidder was unable to timely close, and Tri-State Financial, L.L.C. ("Tri-State Financial"), the second highest bidder, closed the sale on February 5, 2005.

On January 28, 2005, between the auction and the closing with Tri-State Financial, Trustee Lovald filed a motion seeking authority to pay certain secured claims and some administrative expenses, including a portion of the claim held by the Murphys. In an attachment to the motion, Trustee Lovald stated William F. Murphy Self Declaration of Trust was to be paid \$1,986,000.00 and this claim

is under two promissory notes with principal and interest claimed of approximately \$3,000,000.00. The payment to be made pursuant to this Motion shall be applied as a reduction of the principal due upon the \$2,100,000.00 promissory note. Trustee continues to review the remaining elements of this claim.

One objection to the trustee's motion was filed by North Central Construction, Inc. ("North Central"). The objection was resolved by the trustee's creation of an escrow account from which to pay the claim held by North Central. An order authorizing the disbursements set forth in the trustee's motion was entered February 15, 2005.

On February 22, 2005, the William F. Murphy Trust³ and Mike D. Murphy filed a proof of secured claim for \$2,574,340.00. The proof of claim stated the creditors were secured by real estate and "UCC Financing Statement [sic]" and "Natural Gas Pipeline" valued at \$5,000,000.00 T."⁴ The proof of claim also set forth the amount sought included "\$99,390" for "[a]rrearage and other charges at the time the case was filed[.]" A box on the form to be checked "if claim includes interest or other charges" was not checked. On August 8, 2005, the William F. Murphy Trust and Mike D. Murphy filed another proof of claim that provided it was "intended to replace a previously filed claim" on February 17, 2005. The proof of claim stated they were owed \$2,526,324.75. The box on the form to be checked "if claim includes interest or other charges" was checked this time. The described collateral was the same (although "statement" was spelled correctly this time). The "[a]rrearage and other charges at the time the case was filed included in the secured claim" was stated to be \$97,857.72.

On August 25, 2005, Trustee Lovald filed a SETTLEMENT AGREEMENT BETWEEN CHAPTER 7 TRUSTEE AND MURPHY BROTHERS REGARDING MURPHY BROTHERS' PROOF OF CLAIM ("SETTLEMENT") and a motion to approve it. In the SETTLEMENT, Trustee Lovald said he and the Murphys disputed the amount owed by the bankruptcy estate under the \$2,100,000.00 note only and they had agreed to compromise the claim arising from both notes for \$675,886.80, which would be in addition to the \$1,986,000.00 already paid to the Murphys. The SETTLEMENT set forth the several significant corrections the parties had made to the Murphys' amended proof of claim based on the trustee's findings. The SETTLEMENT also provided the Murphys had agreed not to make a claim for post-petition attorneys' fees and post-petition late charges on either note.

Tri-State Financial objected to the proposed settlement in part because it had not been provided a satisfactory accounting of the sums due under both notes and because the Murphys had not paid at least one of the White Rock members, Randy Kramer, whom Tri-State Financial stated was owed \$82,996.00. Tri-State Financial argued there had been no consideration given to Debtor for the

³ The Court presumes the William F. Murphy Self-Declaration of Trust and the William F. Murphy Trust are the same entity.

⁴ What the "T" referenced, if anything, is unknown.

\$380,000.00 note because the condition precedent of the Murphys paying the White Rock members had not been met.

An evidentiary hearing on the matter was set for October 13, 2005. At the request of Trustee Lovald's attorney, a telephonic conference with counsel was held October 12, 2005. After a lengthy discussion of unresolved issues, the parties agreed to submit the settlement motion on exhibits, including the loan, note, and disbursement documents submitted to the Court earlier, and written arguments ("briefs"). Counsel for Tri-State Financial stated he had no objection to the admission of any exhibits the other parties had set forth on their previously filed witness and exhibits list. Counsel for Trustee Lovald reserved, with counsel for Tri-State Financial's consent, the right to object to the admission of a letter from him to counsel for Tri-State Financial dated, he thought, September 28, 2005 and one other exhibit he could not recall during the conference.⁵

After the October 12, 2005, telephonic conference, Tri-State Financial mailed a notebook of exhibits (1-27) to the Court. Tri-State Financial also filed a supplemental witness and exhibit list on November 9, 2005, which referenced the addition of exhibits 29 and 30 (each a letter) and 31 (Trustee Lovald's response to a request for production). The two letters were attached to the supplement.⁶

Trustee Lovald's exhibits 1-6 were attached to his earlier-filed witness and exhibit list. Trustee Lovald also attached to his November 10, 2005, brief a complete page 1 of the SECURED PROMISSORY NOTE and a "Revised Accounting" of the proposed settlement of the Murphys' claim, which modified the exhibit 4 he had submitted earlier.

With their brief, the Murphys attached the several October 15, 2002, documents and an Exhibit G, which was an explanatory accounting of the proposed settlement that was essentially

⁵ Trustee Lovald thereafter did not lodge a formal objection to any exhibit.

⁶ The letters each bore an exhibit sticker that did not match the number set forth on the supplemental exhibit list to which they were attached.

identical to page 1 of Trustee Lovald's revised accounting. In an earlier-filed witness and exhibit list, the Murphys indicated they intended to offer a "FERC Order Issuing Certificate" and a "Second Amendment to Application" of White Rock for "temporary and permanent certificates of public convenience and necessity." The Court was unable to find where these two documents were ever submitted.

Resolution of the matter was put on hold twice during the next year as major parties in the case attempted a more global settlement of several creditors' claims and related issues. Those efforts were unsuccessful.

In his brief, Trustee Lovald argued the Murphys' payment of the White Rock members was not a condition precedent to the \$380,000.00 note. He stated under the DISBURSEMENT AGREEMENT the Murphys were only obligated to pay the White Rock members as Debtor paid the Murphys. He also argued the consideration Debtor received was the additional 49% ownership interest in White Rock. He expressed no concern -- legally or otherwise -- that the interests in White Rock were not formally transferred to the bankruptcy estate until sometime in December 2004, at his request, by backdated documents. He characterized the TRANSFERS OF OWNERSHIP as "written ratification that it was the intent of the White Rock members to transfer their membership interest as of October 15, 2002."

In the revised accounting of the proposed settlement attached to his brief, Trustee Lovald's calculations on the \$380,000.00 note began with principal of \$301,459.00, which was the total to be paid to the White Rock members for their interests in the pipeline. In the revised accounting, Trustee Lovald also acknowledged one payment and then he added accrued interest and certain late charges, which resulted in a total owed of \$487,532.04.

Trustee Lovald's revised accounting regarding the \$2,100,000.00 note started with a principal balance of \$1,718,941.89,⁷ which the trustee stated reflected a credit of

⁷ A fourth page to Trustee Lovald's revised accounting set forth the calculations made to reach \$1,718,941.89. The Court presumes these are the accounts receivable owed by White Rock that the Murphys agreed to pay under the LOAN AGREEMENT.

\$275,000.00 to Debtor for its original 51% ownership interest in White Rock "less pre-petition attorney Fees plus credit for unused LOC." Trustee Lovald then added accrued interest, deducted one pre-petition payment by Debtor on March 26, 2003, and deducted the post-petition payment of \$1,986,000.00 he made on February 23, 2005. He calculated this resulted in a principal balance of \$301,914.07 on February 23, 2005. To that total he added subsequent interest and certain late charges for a total due of \$360,272.44.

When the trustee's calculations on both notes were added, a total of \$847,804.48 was reached. Trustee Lovald further stated in paragraph 3 on page three of the revised accounting:

On May 5, 2005, we agreed on \$850,000 with Murphy Bros. agreeing to make a claim for prepetition attorneys fees of \$122,588.28. Murphy Bros. also agreed not to make a claim for postpetition attorney fees and expenses as an oversecured creditor pursuant to 11 U.S.C. § 506. This settlement was subject to an accounting of the checkbook and approval of the Bankruptcy Court.

The SETTLEMENT, in the paragraph numbered 11, provided the Murphys were not entitled to any pre-petition attorneys' fees. The Court thus presumes paragraph 3 on page three of Trustee Lovald's revised accounting was missing a "not" before the word "agreeing" in the quoted text above. Also, while the SETTLEMENT, in paragraph 16, stated the Murphys had agreed not to make a claim for post-petition late charges, the accounting provided by Trustee Lovald with his subsequent brief seemingly did reflect them.

Following the agreed-to accounting of the Murphys' checking account, Trustee Lovald and the Murphys reduced the \$850,000.00 to \$675,886.80 to reflect a number of changes regarding the unused portion of a letter of credit and interest earned on a checking account. They also deducted \$108,631.38 for some "unauthorized" post-petition payments made by the Murphys. Few details about these deductions were provided. Also in the revised accounting attached to his brief, Trustee Lovald stated the Murphys had agreed not to make a claim for \$250,000.00 under paragraph 2 of the SECURED PROMISSORY NOTE.

In their original brief, the Murphys said the DISBURSEMENT AGREEMENT and the \$380,000.00 note provided for certain payments to them by Debtor to cover their fees and costs connected with the transaction. The Murphys acknowledged they were no longer pursuing those fees and costs and were only seeking principal of \$301,459.00

under the \$380,000.00 note. The Murphys also stated they and Trustee Lovald had compromised the \$301,459.00 in principal and the interest and late charges on that sum to \$487,532.04 as of November 30, 2005, the calculation which the Murphys set forth in the Exhibit G appended to their brief. The Murphys refuted Tri-State Financial's concerns regarding the lack of consideration, saying Debtor had received an additional 49% interest in White Rock in exchange for the loan. The Murphys also argued their payments to the White Rock members were not due until Debtor paid the Murphys, thus apparently acknowledging they would pay the White Rock members once the SETTLEMENT was approved.

In its brief, Tri-State Financial argued Debtor never timely received the White Rock membership interests or an advance of any sums under the \$380,000.00 note and deemed that a condition precedent to any obligation for Debtor to pay the Murphys. It challenged the Murphys' claim that the consideration for the \$380,000.00 note was the full ownership interest of White Rock, and it argued this note was unenforceable under Illinois law and 11 U.S.C. § 502(b).

In its brief, Tri-State Financial further stated Trustee Lovald acknowledged in some answers to interrogatories that he had requested the TRANSFERS OF OWNERSHIP INTEREST in December 2004 when the parties involved could not produce documents evidencing the transfer. Tri-State Financial also stated White Rock had been administratively dissolved on July 1, 2004, for a failure to file reports with the state for 2003 and 2004. It said Trustee Lovald obtained a certificate of reinstatement on December 13, 2004.

Tri-State Financial also pondered why the Murphys' unpaid proof of claim was not just \$540,324.75. It calculated that sum based on the amended proof of claim and the \$1,986,000 already paid by the bankruptcy estate. Tri-State Financial's calculations do not appear to have taken into account interest that accrued after the filing of the amended proof of claim.

In its reply brief, the Murphys argued the parties to the White Rock transfer of interests were free to select their own effective date. They argued there were no consequences under the law arising from the TRANSFERS OF OWNERSHIP INTEREST being back-dated from December 2004 to October 15, 2002. They also noted Debtor had thought it owned the pipeline when it filed its schedules. The Murphys further argued there would have been no legitimate reason

for Debtor to have borrowed \$2,100,000.00 from them to pay White Rock's debts if Debtor had not intended to become the sole owner of White Rock back in October 2002.

The Murphys further argued their payment of the other White Rock members was not a condition precedent to Debtor repaying the \$380,000.00 note. They referenced portions of the several October 15, 2002, documents in support of their conclusion.

Tri-State Financial also filed a reply brief that again delineated its several objections. They are addressed below.

Discussion - Tri-State Financial's objections related to the underlying October 15, 2002, transactions. Some of Tri-State Financial's objections to Trustee Lovald's proposed settlement of the Murphys' claim were actually objections to the several October 15, 2002, loan and transfer documents underlying the Murphys' claim. Though these objections would be more appropriate were the Murphys' actual claim being adjudicated, the Court will address them first for whatever relevancy they may hold in the context of the trustee's proposed settlement.

Foremost, contrary to Tri-State Financial's repeated assertions, the Court was unable to find, in the various loan and transfer documents described above, any provision that a transfer of the interests in White Rock to Debtor was a condition precedent to Debtor paying the Murphys on the \$380,000.00 note. Though a provision to that effect may have made better sense, for whatever reason or reasons, the parties chose not to include one. Likewise, it may have made better sense for the White Rock members to be able to look to the Murphys for payment if Debtor defaulted, but the Court was unable to find in any of the October 15, 2002, documents a provision addressing that contingency either. Thus, while none of the October 15, 2002, documents described above was a model of legal draftsmanship, what was clear was all the parties involved intended Debtor to purchase the other interests in White Rock and to pay substantial debts owed by White Rock on the credit provided by the Murphys. That intention was fulfilled. The transfer to Debtor of the other interests in White Rock provided the necessary consideration for the \$380,000.00 note. Moreover, but for obtaining sole ownership of White Rock, it would have made no sense for Debtor to borrow \$2,100,000.00 from the Murphys (the debt obligation that Tri-State Financial does not dispute) to pay White Rock's debts. While the \$380,000.00 note may have been an atypical

credit transaction, Tri-State Financial has failed to establish this note should be considered separate from the other October 15, 2002, agreements or that it was otherwise illegal or inequitable under Illinois law.

The Court shared Tri-State Financial's concern Debtor had not cleanly obtained full ownership of White Rock on or near October 15, 2002. However, the Court was unable to find in any of the subject documents a definitive date for the White Rock members to transfer their interests to Debtor. Further, none of the parties to those transfers has complained or argued the transfers were unenforceable. No party, including Tri-State Financial, identified any applicable state or federal governance that prohibited the backdated transfers. Most important, because problems with the Federal Energy Regulatory Commission were avoided, the costs arising from the pipeline construction were timely paid, and a successful sale of the ethanol plant took place, the record indicates Debtor benefitted from an effective full ownership of White Rock beginning on December 15, 2002, regardless of when the transfers were formalized. Accordingly, the Court could not, as Tri-State Financial urged, conclude the \$380,000.00 note was executory, unenforceable under applicable state law, or failed for a lack of consideration.

Tri-State Financial also challenged the default interest rate and the interest accruing date of October 15, 2002, Trustee Lovald and Murphy Brother's considered regarding the \$380,000.00 note. The first paragraph of the BALLOON SECURED PROMISSORY NOTE states the interest rate is 13.117%. The default paragraph at the second page states interest will increase by 7.0% so long as a default shall continue. Since Debtor's first payment was due November 15, 2002, and no payment was made until March 10, 2003, the Court is satisfied the default occurred November 15, 2002, and the default interest rate of 20.117% was applicable. Further, several provisions in the agreement indicate interest accrued from the date of the agreement, since both principal and accrued interest were components of each monthly payment, beginning with the first payment due November 15, 2002. Tri-State Financial has not established the legitimacy of any other interest rate or interest computation date. Accordingly, an objection on these grounds cannot be sustained.

Tri-State Financial also believed the Murphys were not entitled to interest on the late charges. Page two of the BALLOON SECURED PROMISSORY NOTE states interest upon a default shall be paid

"upon the total indebtedness." Tri-State Financial has not directed the Court to a contrary or other controlling provision.

Discussion - Tri-State Financial's objections related to the proposed settlement itself. Tri-State Financial's remaining objections are that the SETTLEMENT is not in the best interests of the estate and not fair and equitable.

A Chapter 7 trustee is permitted to compromise a claim so the estate may avoid the expense, burdens, and uncertainty associated with litigation. *ReGen Capital III, Inc. v Official Committee of Unsecured Creditors (In re Trism, Inc.)*, 282 B.R. 662, 668 (B.A.P. 8th Cir. 2002) (citing *In re Apex Oil Co.*, 92 B.R. 847, 866 (Bankr. E.D. Mo. 1988)); *Martin v. Cox (In re Martin)*, 212 B.R. 316, 319 (B.A.P. 8th Cir. 1997) (citing *Apex Oil Co.*, 92 B.R. at 866). Once the trustee is satisfied with the settlement, the trustee is required to obtain court approval of it after notice to all creditors and other parties in interest. Fed.Rs.Bankr.P. 2002(a)(3) and 9019(a). The purpose of the notice is to foster input from creditors and parties in interest in the court approval process. *Trism, Inc.*, 282 B.R. at 668.

Whether a settlement should be approved is within the discretion of the Bankruptcy Court. *Id.* at 166 (citing *inter alia Drexel Burnham Lambert, Inc. v. Flight Transportation Corp. (In re Flight Transportation Corp. Securities Litigation)*, 730 F.2d 1128, 1135-36 (8th Cir. 1984)). With a proposed settlement, the Court is presented with a question of fairness and equity, and it is required to determine whether the settlement is in the best interests of the bankruptcy estate. *Martin*, 212 B.R. at 319; *Trism, Inc.*, 282 B.R. at 668. The Court does not substitute its judgment for the trustee's. *Martin*, 212 B.R. at 319. Instead, the factors the Court considers include:

- (1) the probability of success in the litigation;
- (2) the difficulties, if any, to be encountered in the matter of collection;
- (3) the complexity of the litigation involved, and the expense, inconvenience, and delay necessarily attending it;
- (4) the paramount interest of creditors and a proper deference to their reasonable views in the premises.

PW Enterprises, Inc. v. Kaler (In re Racing Services, Inc.), 332 B.R. 581, 586 (B.A.P. 8th Cir. 2005) (quoting *Flight Transportation*

Corp., 730 F.2d at 1135 (citing *Drexel v. Loomis*, 35 F.2d 800, 806 (8th Cir. 1929))).⁸

[I]t is not necessary for a bankruptcy court to conclusively determine claims subject to a compromise, nor must the court have all of the information necessary to resolve the factual dispute, for by so doing, there would be no need of settlement. [Cite omitted.] Neither must the court find that the settlement constitutes the best result obtainable. Rather, the court need only canvass the issues to determine that the settlement does not fall "'below the lowest point of reasonableness.'"

Martin, 212 B.R. at 319 (quoting *Apex Oil Co.*, 92 B.R. at 867) (quoting *Cosoff v. Rodman (In re W.T. Grant Co.)*, 699 F.2d 599, 608 (2nd Cir. 1983)); *New Concept Housing, Inc. v. Poindexter (In re New Concept Housing, Inc.)*, 951 F.2d 932, 938 (8th Cir. 1991). "Compromise is an art, not a science." *Nangle v. Surratt-States (In re Nangle)*, 288 B.R. 213, 220 (B.A.P. 8th Cir. 2003). Though the Court must give deference to reasoned opinions of creditors when a proposed settlement is considered, *Trism, Inc.*, 282 B.R. at 667-68, as long as the settlement falls within a range of reasonable compromises, it may be approved. *Nangle*, 288 B.R. at 220. As long as the proposed settlement is reasonable, the debtor's approval of the agreement is not needed, and the settlement does not have to benefit the debtor. *Id.* at 219-20. This is so, in part, because a trustee represents the interests of the bankruptcy estate and the estate creditors, not the debtor or the debtor's principals; he owes no fiduciary obligation to the debtor. *Id.* (cites therein).

Finally,

regardless of the language used in the settlement agreement, the trustee is always bound by a duty to creditors and the estate to collect the assets of the debtor, reduce them to money, and close the estate as quickly as possible, as set forth in section 704 of the Bankruptcy Code.

⁸ The four factors are useful not only when analyzing the settlement of claims against the estate but also claims held by the estate against others. *Will v. Northwestern University (In re Nutraquest, Inc.)*, 434 F.3d 639, 644-45 (3rd Cir. 2006).

Id. at 219.

The Court is satisfied Trustee Lovald's proposed compromise of the Murphys' claim falls within the range of reasonableness and is in the best interests of the estate. On its face, it appears Trustee Lovald's and the Murphys' several compromises in reaching the settlement amount arose more from the unique documents and circumstances presented, including the intertwining business relationships among White Rock, the Murphys, Debtor, and their often-common principals, rather than from any legal or factual disputes arising from the October 15, 2002, documents and Debtor's subsequent bankruptcy. At most, if the claim was litigated, each party's accountant would testify as to his interpretation and application of the interest and late charge terms in the October 15, 2002, documents. Accordingly, litigation-related factors are largely not significant. Collection is not an issue at all. Moreover, no creditors but Tri-State Financial have objected to the SETTLEMENT, and Tri-State Financial has failed to demonstrate why its view of the Murphys' claim deserves greater deference, legally or equitably. The record also does not demonstrate, from whatever angle the SETTLEMENT may be viewed, that the SETTLEMENT falls below the lowest point in the range of reasonableness. Finally, the SETTLEMENT will foster a more timely payment of the bankruptcy estate's unsecured claims and should promote a good return on their claims.

Tri-State Financial objected on several grounds to the admissibility of Trustee Lovald's revised accounting and the Murphys' Exhibit G, which were appended to these parties' respective briefs. Most particularly, Tri-State Financial argued Trustee Lovald and the Murphys had disingenuously changed the premise of their settlement because Trustee Lovald's Exhibit 4 showed interest computed on a principal balance of \$380,000.00 while the revised accounting and Exhibit G stated a principal of only \$301,459.00 was used. An October 7, 2005, admission by Trustee Lovald indicates the difference in principal amounts may have been for bills owed by Debtor or White Rock that had been paid by the Murphys. The LOAN AGREEMENT and the BALLOON SECURED PROMISSORY NOTE are not particularly enlightening, though the LOAN AGREEMENT would support the Trustee's admission. If the consideration for the \$380,000.00 note, however, were just the remaining interests in White Rock, the principal more clearly was only \$301,459.00. The Murphys essentially have admitted they "funded" only \$301,459.00 of the \$380,000.00.

The Court shares Tri-State Financial's concern this principal figure apparently changed somewhere along the line. However, there is nothing in the record, other than mere argument by Tri-State Financial, that suggests the differences in the later-filed exhibits demonstrate bad faith by the settlement proponents. If that were true, one would assume these documents shone a more favorable light on the SETTLEMENT. They did not. Trustee Lovald's revised accounting and the Murphys' Exhibit G indicate about \$790,000.00 in principal, interest, and late charges were owed when the preliminary settlement amount of \$850,000.00 was reached on May 2, 2005, along with an understanding that several deductions would be subsequently made after additional account audits.

If the SETTLEMENT is considered on those less favorable numbers, however, it still falls within the range of reasonableness. Given potential disputes in the calculation of the interest and late charges, about which two CPAs would surely find plenty to disagree,⁹ the Court could not conclude the \$60,000 disparity between the estimated \$790,000.00 owed and the \$850,000.00 preliminary settlement on May 2, 2005, rendered the final SETTLEMENT unreasonable under the factors set forth above.

Most important, if the Court considers only Exhibit 4, an exhibit to which Tri-State Financial had no objection, the SETTLEMENT even more clearly passes muster. Exhibit 4 demonstrates Trustee Lovald compromised an estimated claim against the estate of \$964,793.13 on February 23, 2005, (the approximate date Trustee Lovald paid a portion of the Murphy's claim pursuant to the February 15, 2005, order) down to the initial settlement amount of \$850,000.00 as of May 2, 2005, a clearly reasonable deal.

Tri-State Financial also objected to the admissibility of the ownership interest transfer documents, Debtor's schedules, and a December 11, 2002, letter from Murphys' counsel to the Federal Energy Regulatory Commission. Neither the schedules nor the letter are material to the Court's decision today. While the ownership interest transfer documents were backdated, a fact no one

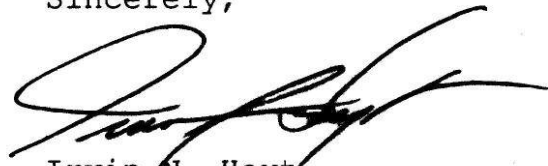
⁹ One of the exhibits offered by Tri-State Financial was the cover page only on a fax from the Murphys' counsel to Trustee Lovald's counsel dated April 11, 2005. In the cover page, the Murphys contended they would be owed \$1,267,467.19 on May 1, 2005. The other documents that were attached to the cover page were not included in the exhibit.

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disputes, Tri-State Financial has failed to establish any reason why the Court should not consider them.

An appropriate order approving the SETTLEMENT will be entered.

Sincerely,



Irvin N. Hoyt
Bankruptcy Judge

INH:sh

CC: case file (docket original; serve parties in interest)

On the above date, a copy of this document was mailed or faxed to the parties shown on the Notice of Electronic Filing as not having received electronic notice and Debtor(s), if Debtor(s) did not receive electronic notice.

Frederick M. Entwistle
Clerk, U.S. Bankruptcy Court
District of South Dakota

**NOTICE OF ENTRY
Under Fed.R.Bankr.P. 9022(a)**

**This order/judgment was entered
on the date shown above.**

**Frederick M. Entwistle
Clerk, U.S. Bankruptcy Court
District of South Dakota**