STATE OF MICHIGAN
IN THE 17th CIRCUIT COURT FOR KENT COUNTY

TROUT VALLEY ENTERPRISES, INC.,

Plaintiff,

vs.

EMERGING NATURAL GAS COMPANY; and CHARLES A. SMITH d/b/a EMERGING NATURAL GAS COMPANY,

Defendants.
_____/

Case No. 14-09799-CBB

HON. CHRISTOPHER P. YATES

FINDINGS OF FACT, CONCLUSIONS OF LAW, AND VERDICT

The Court finished the heavy lifting in this case when it resolved two motions for summary disposition on July 24, 2015, and March 18, 2016. Those decisions established that both defendants, Emerging Natural Gas Company ("ENG") and Charles Smith, must be held liable to Plaintiff Trout Valley Enterprises, Inc. ("Trout Valley") on one claim for breach of representations and warranties.[1] In the wake of those rulings, all that remains is the task of determining the appropriate damages to award Trout Valley. That task simply requires the Court to decide when Trout Valley obtained its right to a stream of working-interest payments from Dart Oil and Gas Corporation ("Dart") that the defendants surreptitiously redirected to themselves and then concealed from the bankruptcy trustee in the bankruptcy proceeding of Smith Petroleum Company ("Smith Petroleum"). The Court finds that the entirety of those payments, amounting to $121,568.32, must be awarded to Trout Valley as damages in this case. Consequently, the Court shall render a verdict in that amount in favor of Trout Valley and against both of the defendants.

[1] That single claim is set forth in Count Five of the plaintiff's First Amended Complaint.

I. Factual Background

Pursuant to MCR 2.517(A)(1), in an action tried without a jury, "the court shall find the facts specially, state separately its conclusions of law, and direct entry of the appropriate judgment." The Court must render "[b]rief, definite, and pertinent findings and conclusions on the contested matters" that may take the form of a written opinion. See MCR 2.517(A)(2) & (3). Therefore, the Court shall begin with findings of fact, followed by conclusions of law, and ultimately the verdict.

In 2000, Smith Petroleum filed for protection under Chapter 7 of the Bankruptcy Code. On May 29, 2001, John Byrne purchased some of Smith Petroleum's assets from the bankruptcy trustee. See First Amended Complaint, Exhibit 1. And on June 7, 2006, the United States Bankruptcy Court for the Western District of Michigan entered an order confirming the "sale of all remaining oil and gas and other mineral interests of the estate" to Plaintiff Trout Valley. Id., Exhibit 2. Because Trout Valley became the assignee of Byrne's interest in Smith Petroleum,[2] Trout Valley obtained the rights to every oil and gas interest of Smith Petroleum through the trustee in Smith Petroleum's bankruptcy proceeding. A bill of sale dated July 24, 2006, memorialized the transaction in which Trout Valley purchased from the bankruptcy trustee "all of the remaining oil and gas and other mineral interests that may be owned by Smith Petroleum Company and in which the estate may have an interest, and which the estate has not previously sold or otherwise liquidated." See Plaintiff's Brief on Damages, Exhibit 1. But that bill of sale went even further, conveying not only the "Property" described above, but also "any royalties or other payments that may be due and unpaid with respect to the Property as of the date of this Bill of Sale." Id. In other words, the bankruptcy trustee conveyed everything left in the Smith Petroleum bankruptcy estate to Trout Valley.

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[2] According to the complaint, Byrne "is the sole shareholder and principal" of Trout Valley.

Unbeknownst to Plaintiff Trout Valley and the bankruptcy trustee, however, Defendant Smith had concealed from the bankruptcy trustee a stream of payments from Dart to Smith Petroleum for working interests in wells owned and operated by Dart.[3] That is, Smith Petroleum sought bankruptcy protection on August 31, 2000, and then on October 17, 2000, Brenda Dickman sent a memorandum redirecting the working-interest payments to her personal residence.[4] See First Amended Complaint, Exhibit 3. As a result, for years, Dart sent periodic payments for Smith Petroleum to Dickman at her home address in Hopkins. See id., Exhibit 6. Those payments continued long after the United States Bankruptcy Court confirmed the sale of all of the remaining Smith Petroleum property and royalties to Trout Valley in 2006.

By filing this action, Plaintiff Trout Valley sought to recover all of the Dart working-interest payments that Defendant Smith redirected during the course of the bankruptcy proceeding, concealed from the bankruptcy trustee, and kept for himself through the use of Defendant ENG. The Court has already determined the defendants' liability, but the parties disagree about the date on which Trout Valley's right to those payments began, so the Court must consider the extent to which the working-interest payments can be treated as damages that the defendants must pay Trout Valley. To resolve that issue, the Court scheduled a bench trial to begin on July 12, 2016, but the parties informed the Court that they simply wished to have the case decided on trial briefs after each side had the chance to present oral arguments. Therefore, on July 12, 2016, the Court conducted an abbreviated trial at which counsel for both sides made arguments in support of their positions.

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[3] The working-interest payments are not oil and gas or mineral rights included in ownership of the real property. Instead, they are merely the fruits of a successful well operation.

[4] Plaintiff Trout Valley named Brenda Dickman as a defendant in this litigation, but she was dismissed from the case before the Court established any party's liability.

II. Conclusions of Law

The parties have offered the Court a wide menu of options in choosing the date on which the damages to Plaintiff Trout Valley began to run. Fundamentally, however, the two sides have staked out diametrically opposed positions. Trout Valley insists that the entire stream of working-interest payments from Dart must be awarded as damages because those payments belonged to the trustee in bankruptcy, who sold them to Trout Valley. In contrast, the defendants contend that Trout Valley has no right to any working-interest payments made prior to May 13, 2013 – the date on which Trout Valley recorded its interest in the stream of payments from Dart. The Court finds that Trout Valley has, by far, the better argument.

According to Plaintiff Trout Valley, the bill of sale transferring property from the bankruptcy trustee in the Smith Petroleum bankruptcy proceeding encompasses every working-interest payment from Dart. That bill of sale, dated July 24, 2006, conveyed to Trout Valley "all of the remaining oil and gas and other mineral interests . . . owned by Smith Petroleum" as well as "any royalties or other payments that may be due and unpaid with respect to the Property as of the date of this Bill of Sale."[5]

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[5] The defendants have objected to the Court's consideration of that bill of sale because it was not disclosed during discovery. During oral arguments on July 12, 2016, counsel for Plaintiff Trout Valley explained that the bill of sale dated July 24, 2006, did not surface until after the completion of discovery, and that counsel furnished the document to the defendants' attorney as soon as the bill of sale came to light. The Court finds that the bill of sale plainly must be considered as part of the record. The document was certainly not intentionally withheld by Trout Valley's counsel for some strategic or tactical reason. Indeed, the bill of sale is the strongest proof of the conveyance to Trout Valley by the bankruptcy trustee, the document clearly advances Trout Valley's claim, and there is no suggestion that the document was fabricated, so it stands to reason that Trout Valley did, in fact, turn over the document to the defendants as soon as possible. Under the circumstances, the Court finds no reason to exclude the bill of sale, which the defendants received well before the trial date. Although our Court of Appeals has noted that "MCR 2.313(B) . . . is broad enough to permit a trial court to exclude evidence if the court believes that such action is an appropriate remedy for violation of discovery practice[,]" Farrell v Auto Club of Michigan, 155 Mich App 378, 388 (1986), nothing in this case convinces the Court that exclusion of the 2006 bill of sale is an appropriate remedy.

See Plaintiff's Brief on Damages, Exhibit 1. That capacious conveyance swept within its ambit all of the Dart payments from the initiation of the Smith Petroleum bankruptcy proceeding in August 2000 through the final payment diverted to the defendants, which amounts to $121,568.32.

The defendants – seemingly relying upon the maxim that possession is nine-tenths of the law – contend that Plaintiff Trout Valley cannot recover any of the Dart payments. This truly audacious argument ignores the fact that, upon the commencement of the Smith Petroleum bankruptcy, all of the working-interest payments from Dart to Smith Petroleum belonged to the bankruptcy estate. As a result, neither Smith Petroleum, nor Defendant Smith, nor anyone else had the right to redirect the stream of payments from Smith Petroleum to Brenda Dickman, Defendant ENG, or any other entity. When the bankruptcy trustee entered into the sweep conveyance to Trout Valley, the trustee passed along every single remaining asset of Smith Petroleum. The fact that the defendants had managed to improperly conceal the diverted Dart working-interest payments from the bankruptcy trustee did not somehow result in the exclusion of those concealed payments from the trustee's conveyance to Trout Valley. In the Court's view, the sale of assets by the bankruptcy trustee to Trout Valley had nothing whatsoever to do with the defendants, who only became involved in the transaction when Trout Valley realized that the defendants had hidden the Dart working-interest payments from both the bankruptcy trustee and Trout Valley. Permitting the defendants to profit from their misconduct by allowing them to keep any of the Dart payments made during the Smith Petroleum bankruptcy would contravene the fundamental principles undergirding the bankruptcy system.[6]

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[6] Remarkably, the defendants have suggested that the Court should defer to the United States Bankruptcy Court for the Western District of Michigan by allowing that court to sort out this mess that the defendants created. The Court not only believes that the dispute can be resolved in the Kent County Circuit Court as a simple matter of contract law, but also that a return to the bankruptcy court could very well lead to the defendants' prosecution under 18 USC 152(1) for concealment of assets.

III. Verdict

For the reasons stated in the Court's findings of fact and conclusions of law, the Court hereby renders a verdict in favor of Plaintiff Trout Valley and against Defendants ENG and Charles Smith in the amount of $121,568.32, which constitutes the aggregate amount of working-interest payments from Dart that the defendants redirected to themselves through Brenda Dickman soon after the filing of the Smith Petroleum bankruptcy proceeding. The Court invites Trout Valley to submit a proposed judgment pursuant to MCR 2.602(B) that memorializes the Court's verdict.[7]

IT IS SO ORDERED.

Dated: July 14, 2016

HON. CHRISTOPHER P. YATES (P41017)
Kent County Circuit Court Judge

[7] Plaintiff Trout Valley may also present a proposed bill of costs with the judgment. Beyond that, if the Court has erred in determining the precise amount of diverted working-interest payments from Dart, Trout Valley may submit a proposed judgment reflecting the correct amount, rather than the amount of $121,568.32 set forth in the Court's verdict.