

1968

# John P. Jones v. Acme Building Products, Inc. and Gordon G. Lee : Appellant's Brief

Utah Supreme Court

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# IN THE SUPREME COURT OF THE STATE OF UTAH

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JOHN P. JONES,

*Plaintiff and Appellant,*

vs.

ACME BUILDING PRODUCTS, INC.  
and GORDON G. LEE,

*Defendants and Respondents.*

Case No.  
11171

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## APPELLANT'S BRIEF

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Appeal of plaintiff from the Third District Court of  
Salt Lake County, The Honorable Leonard W. Elton,  
Presiding.

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Clk. Supreme Court, Utah

## TABLE OF CONTENTS

	Page
Statement of the Case .....	1
Relief Sought on Appeal .....	1
Statement of the Facts .....	2
Argument	
POINT I: THE COURT COMMITTED ERROR IN RULING THE TERM "NET WORTH" AS USED IN EXHIBIT ONE WAS THE BOOK VALUE OF THE STOCK IN DEFENDANT CORPORATION AS OF JULY 1, 1966 .....	5
POINT II: THE COURT COMMITTED ERROR IN NOT RULING THAT THE TERM "NET WORTH" AS USED IN EX- HIBIT ONE MEANT THE ACTUAL NET VALUE OF THE CORPORATION .....	14
Conclusion .....	16

## INDEX OF CASES

Castelli v. Tolibia, 83 NYS 2d 554 .....	9
Continental Bank & Trust Co. v. R. W. Stewart, 4 Utah 2d 288, 291 P2d 980 (1955) .....	8
Cornwall v. Willow Creek Country Club, 13 Utah 2d 160, 369 P2d 928 (1962) .....	8

	Page
Eastern Capital Corp. v. Freeman, 168 NYS2d 834 (1957) .....	9
Ephraim Theater Company v. Hawk, 7 Utah 2d 163, 321 P2d 221 (1958) .....	6, 8, 12
Mathis v. Madsen, 1 Utah 2d 46, 261 P2d 952 (1953) .....	8, 14
Maw v. Noble, 19 Utah 2d 440, 354 P2d 121 (1960) .....	8
Miner Inc. v. Peerless Equipment, 115 F2d 650, 7th Cir. (1940) .....	9
Pacific States Cast Iron Pipe Co. v. Harsh Utah Corp., 5 Utah2d 244, 300 P2d 610 (1956) .....	14
Paclawski v. Bristol Laboratories, Inc., Okl., 425 P2d 452 (1967) .....	14
Plain City Irrigation Co. v. Hooper Irrigation Co., 11 Utah 2d 188, 356 P2d 625 (1960) .....	8, 13
Woodward v. Quigley, Iowa, 133 NW2d 38 (1965) .....	16

## INDEX OF TEXTS

America Jurisprudence 2d, Vol. 17, Contracts § 245 .....	6
American Law Institute, Restatement of Contracts	
Section 228 .....	5
Section 230 .....	7
Section 235 .....	8
Principals of Accounting by Finney and Miller ....	9
Williston on Contracts, Vol. 3	
Section 604 .....	5
Section 618 .....	8, 12

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Case No.  
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---

## APPELLANT'S BRIEF

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### STATEMENT OF THE CASE

This is an appeal from the Third District Court for Salt Lake County from a Declaratory Judgment entered and filed on the 2nd day of January, 1968, by the Honorable Leonard W. Elton.

### RELIEF SOUGHT ON APPEAL

The appellants seek reversal of the Declaratory Judgment entered herein holding that the words "net

worth'' in the Memorandum of Understanding and Agreement dated July 22, 1966, meant net worth based on book value of Acme Building Products, Inc. as of July 1, 1966.

## STATEMENT OF THE FACTS

Appellant commenced this action by filing a complaint under the Declaratory Judgment Act, Section 78-33-1 et. seq. Utah Code Annotated (1953) alleging a dispute between the parties with respect to various particulars of an agreement dated the 22nd day of July, 1966 (Exhibit 1) and specifically with respect to the value of the interest possessed by the plaintiff in the defendant corporation, the procedure for determining such value, and the subsequent payment thereof to the plaintiff. The defendants admitted the dispute, but alleged there was no basis therefor, thus framing the issue.

As a result of stipulation by the parties, a hearing was held on October 10, 1967, before Judge Elton for the limited purpose of interpreting the words "net worth" as used in paragraphs 2 and 3 of Exhibit 1 which provide:

"2. When the foregoing Releases are secured and/or the events take place, and it is determined the *net worth* value applicable to the interest in Acme Building Products, Inc., now owned by John P. Jones, then John P. Jones will quit-claim all right, title, and interest in said Acme Building Products, Inc., to the said corporation.

"3. As a condition to the aforesaid Release of all the interest in the business by John P. Jones,

it is understood and agreed that a financial statement will be first drawn as of July 1, 1966, and that Gordon Lee and John P. Jones, with the aid of Jerry Branagan and Allen E. Mecham, will negotiate and enter into an Agreement whereby Acme Building Products, Inc. will agree to pay John P. Jones upon terms as set forth by John P. Jones as a result of said negotiation, the balance due to him from an accounting which reflects the *net worth* of the said Acme Building Products, Inc.'" (emphasis added)

At the hearing before Judge Elton on October 10, 1967, the facts and circumstances surrounding the execution of Exhibit 1 were presented by the parties. Summarizing from the transcript of proceedings, they are as follows:

John P. Jones, plaintiff and appellant, and Gordon G. Lee, defendant and respondent, had been the owners of the defendant corporation, Acme Building Products, Inc. for a period of six and one-third years, each party owning one-half of the outstanding shares (TR 67, 84). During the latter part of this period, the parties had frequent disputes and as a result, they had discussed the possibility of one or the other parties disassociating from the business (TR 67-68). These discussions took place at least once a year, if not oftener (TR 67). In May of 1966, such a meeting took place with Jones, Lee, Jerry Branagan, and Allen Mecham present in Mr. Mecham's office. (TR 11, 33, 43, 106). At the time of that meeting, it had not been decided which party would disassociate from the corporation or how the disassociation was to be

accomplished (TR 46, 47, 48, 69). This meeting was the only time prior to the execution of Exhibit 1 that a method of placing a value on the corporate stock was discussed.

On the 23rd day of June, Mr. Mecham, attorney for the corporation and a member of the Board of Directors of Acme, wrote Mr. Lee in regard to his draws from the corporation. (Exhibit 6). Mr. Jones testified that within a few days after June 23, Mr. Lee drew another \$450.00 and Mr. Mecham wrote another letter suggesting that he (Mr. Lee) resign from the Board of Directors (TR 71 and 108).

Some time prior to July 22, (the agreement date) Lee came to Mecham and advised him that an obligation which both the parties had personally guaranteed to the Stewarts and Greens on a stock purchase contract could be assumed by Lee and Jones would be released from any liability (TR 97). Mr. Mecham testified that when he learned of that possibility he stopped at Mr. Jones' home one evening to discuss the matter and this was the first time Mecham thought it possible for Lee to be the survivor of the two (TR 97). That discussion between Mecham and Jones was the beginning of the negotiations which resulted in the drafting and execution of Memorandum of Understanding and Agreement (Exhibit 1). At Mecham's suggestion, Mr. Jones prepared a list of the things that he felt he had coming and gave it to Mecham so that the Memorandum could be drawn and presented to Lee (TR 72, 73, 97). The document was pre-



pared by Mecham and was later executed by the parties. Jones resigned as an officer and director of the corporation and terminated his employment with the company which paid him a salary of \$18,000.00 per year.

## ARGUMENT

### POINT I

THE COURT COMMITTED ERROR IN RULING THE TERM "NET WORTH" AS USED IN EXHIBIT ONE WAS THE BOOK VALUE OF THE STOCK IN DEFENDANT CORPORATION AS OF JULY 1, 1966.

The subject of the legal interpretation of contracts and agreements has been classified into numerous rules by the decisions, legal texts, and treatises through the years. It now is only a matter of defining nature of the problem to be resolved, selecting the correct rules to be applied to the problem, and then applying the rules to the evidence to resolve the issue between the litigants.

### THE NATURE OF THE PROBLEM

In order to define the nature of the problem, it must be determined what kind of a contract or agreement was entered into between the parties. 3 Williston on Contracts §604. Here we have a fully integrated written memorandum of understanding and agreement (Restatement of Contracts §228) between three different parties, to wit: John P. Jones, Gordon Lee, and Acme Building Products,

Inc., a corporation, (Exhibit 1). The expressed intention of the parties in the writing is found in the three "Whereas" clauses at the beginning of the document which are as follows:

"Whereas both Messrs. Jones and Lee desire to disassociate themselves in the conduct of the business known as Acme Building Products, Inc. and "Whereas, Gordon Lee has indicated a willingness to continue the operations of Acme Building Products, Inc., and John P. Jones has indicated a willingness to disassociate himself from said business; and,

"Whereas, it is agreed by both John P. Jones and Gordon Lee that the income from Acme Building Products, Inc. can be used to purchase the net worth value of the business accrued to the account of John P. Jones."

This expressed intent of parties to the contract is controlling upon the court unless same is insufficient in describing the intention of the parties. 17 Am Jr 2d 633, Contracts §245. *Ephraim Theater Company v. Hawk* 7 Utah 2d 163, 321 P2d 221 (1958).

The district court was requested to interpret the phrase "net worth" as used in the body of the agreement in paragraphs two and three which is quoted above. The parties agreed that the words "net worth" were ambiguous, in that they were susceptible to more than one interpretation, and the court hearing was held to determine the meaning of said words by the use of parol evidence, if necessary.

Therefore, the problem is one of interpreting the words "net worth" as used in paragraphs two and three of the fully integrated written agreement wherein the parties have expressly stated their intentions and where it was agreed that the words were susceptible to more than one interpretation.

## THE RULES TO BE APPLIED

Restatement of Contracts §230 states the rule to be applied, or the standard of interpretation, where there is an integration.

"The standard of interpretation of an integration, except where it produces an ambiguous result, or is excluded by a rule establishing a definite meaning, is the meaning that would be attached to the integration by a reasonably intelligent person acquainted with all operative usages and knowing all the circumstances prior to and contemporaneous with the making of the integration, other than oral statements by the parties of what they intended it to mean."

This standard of interpretation is the primary source when there is an integration as in the case at hand. The objective viewpoint of a third person is taken who has knowledge of all operative usages as well as of other accompanying circumstances. Oral statements by the parties of what they intended the written language to mean are excluded even though such statements might show the parties gave their words a meaning that would not otherwise be apparent. Restatement of Contracts §230, Comment (a).

Additional rules can be used to aid in the application of the foregoing standard if necessary. These are found in Restatement of Contracts §235 and 3 Williston §618. Those applicable to the problem at hand are:

(a) Technical terms and words of art are given their technical meaning unless the context or usage which is applicable indicates a different meaning. Williston states that this rule will yield if the application of other primary rules show a contrary meaning. 3 Williston §618.

(b) The writing will be read as a whole, and every part will be interpreted with reference to the whole; and if possible, it will be so interpreted as to give effect to its general purpose. In general, a word used by the parties in one sense is to be interpreted as employed in the same sense through out the writing in the absence of countervailing reasons. 3 Williston §618, Restatement of Contracts §235.

This Court has on numerous occasions adopted all the foregoing rules of contract interpretation. See: *Cornwall v. Willow Creek Country Club*; 13 Utah 2d 160; 369 P2d 928 (1962), *Ephraim Theater Company v. Hawk*, 7 Utah 2d 163, 321 P2d 221 (1958); *Maw v. Noble*, 19 Utah 2d 440, 354 P2d 121 (1960); *Vitagraph, Inc. v. American Theatre Co.* 77 Utah 76, 291 P2d 303 (1930); *Mathis v. Madsen*, 1 Utah 2d 46, 261 P2d 952 (1953); *Continental Bank and Trust Co. v. R. W. Stewart*, 4 Utah 2d 288, 291 P2d 890 (1955), *Plain City Irrigation Co. v. Hooper Irrigation Co.*, 11 Utah 2d 188, 356 P2d 625 (1960).

## APPLICATION OF THE RULES

The net worth of a business has been defined as the remainder after deduction of liabilities from assets. *Miner Inc. v. Peerless Equipment*, 115 F2d 650, 7th Cir. (1940), *Castelli v. Tolibia*, 83 NYS2d 554, *Eastern Capital Corp. v. Freeman*, 168 NYS2d 834 (1957). Both certified public accountants who testified agreed that in an accounting sense net worth meant assets less liabilities, or stated another way, it is the capital account plus the surplus account. However, the term net worth is not a precise term, in that the use of the term itself does not enable one to determine how the assets or what assets would be valued (TR 38, 39, 59, 63, & 83). Therefore, net worth is to some extent a technical term meaning assets less liabilities, but without defining the term further, and depending on the context and surrounding circumstances, it can either mean the actual value of all assets of a company or the value of merely those assets carried by the company on its books at the depreciated value or at some other means of valuation. *Principles of Accounting* by Finney and Miller, page 47.

Knowing foregoing accounting definition of "net worth", our reasonably intelligent third person in **Re**-statement of Contracts §230 must also keep in mind the surrounding circumstances prior to and contemporaneous with the making of the agreement. All of the circumstances cannot be cited here, but those of greatest importance are as follows:

- (1) The parties, Jones and Lee, each owned one-half

of the outstanding stock in the corporation and by this writing they were attempting to sever their six and one-third year relationship.

(2) The withdrawing party, Jones, was giving up not only his stock ownership in the corporation, but also his \$18,000.00 per year position as president.

(3) The remaining party, Lee, would become the sole stockholder in the corporation after the corporation had purchased the stock owned by Jones.

(4) The corporation's capital assets were carried on the corporation books at their depreciated value and the method of depreciation used was a double-declining balance or accelerated method which depreciates the assets faster in the first five years (TR 58).

(5) The only discussion between the parties about the term book value in attempting to set a buyout price took place sometime in May of 1966, and at that time the negotiations had not yet been commenced which resulted in the drafting of the agreement here in question. This meeting with Jones, Lee, the C.P.A. Branagan, and Allen Mecham was one of a long series of meetings and not in any way related to the contents of said agreement (TR 43, 44, 46, 68 & 69).

(6) The withdrawing party, John P. Jones, was told by the author of the agreement, prior to its execution, to make a list of the items he would want in consideration for his withdrawing from the business. No discussions ever took place prior to the execution of the

agreement as to what the words "net worth" as used in paragraph three were intended to mean.

With knowledge of the definition of "net worth" and of the foregoing circumstances, our reasonably intelligent third person should now be able to interpret the words "net worth" as used in paragraph three of the agreement. To conclude that the parties intended them to mean the book value of the stock in the corporation produces a totally unrealistic and unreasonable result.

It is interesting to note that the author of Exhibit 1 used the term net worth three different times. First, in the third introductory paragraph:

"WHEREAS, it is agreed by both John P. Jones and Gordon Lee that the income from Acme Building Products, Inc. can be used to purchase the NET WORTH value of the business accrued to the account of John P. Jones." (emphasis added).

Second, in paragraph number two:

"When the foregoing releases are secured and/or the events take place, and it is determined the NET WORTH value applicable to the interest in Acme Building Products, Inc. now owned by John P. Jones, then John P. Jones will quit-claim all right, title, and interest in any stock or interest in said Acme Building Products, Inc. to the said corporation." (emphasis added).

Third, in paragraph number three:

"As a condition to the aforesaid Release of all the interest in the business by John P. Jones,

it is understood and agreed that a financial statement will be first drawn as of July 1, 1966, and that Gordon Lee and John P. Jones, with the aid of Jerry Branagan and Allen E. Mecham, will negotiate and enter into an Agreement whereby Acme Building Products, Inc. will agree to pay John P. Jones upon terms as set forth by John P. Jones as a result of said negotiation, the balance due to him from an accounting which reflects the *NET WORTH of the said Acme Building Products, Inc.*" (emphasis added)

One of Williston's rules of interpretation states:

"... In general, a word used by the parties in one sense is to be interpreted as employed in the same sense throughout the writing in the absence of countervailing reasons." 3 Williston §618.

If the words net worth in paragraph three mean net worth based upon the book value of the stock of the corporation, then they should also mean the same thing in the third introductory paragraph and in paragraph two. Such an interpretation cannot in any way be made without destroying the whole context of both usages of the words.

The expressed intent of the parties is found within the four corners of the instrument and that intent must govern. *Ephraim Theatre Company v. Hawk*, 7 Utah 2d 163, 321 P2d 221 (1958). The parties were attempting to sever their joint ownership of a going business and in doing so the surviving party was to pay to the departing party, through the corporate facade, all of his interest in the business, not merely the book value of his corporate stock.



This court stated in *Plain City Irrigation Company v. Hooper Irrigation Company*, 11 Utah 2d 188, 356 P2d 625, 628 (1960):

“Generally, where there is doubt about the interpretation of a contract, a fair and equitable result will be preferred over a harsh or unreasonable one. And an interpretation that will produce an inequitable result will be adopted only where the contract so expressly and unequivocally so provides that there is no other reasonable interpretation to be given to it.”

If net worth in Paragraph 3 of Exhibit 1 is interpreted to mean net worth based upon book value of the corporation as of July 1, 1966, the resulting consequences to the withdrawing party is unreasonable. The assets of the corporation were being depreciated at an accelerated rate and the actual or real value may exceed the depreciated value (TR 58). Therefore, Gordon Lee, as the sole stockholder of the corporation after the purchase of John Jones' stock, could liquidate all the assets at their market value, pay off the liabilities, and have a handsome win-all. Such a result was certainly not contemplated by the parties to the agreement. Whereas, such an unreasonable result would not be possible if the withdrawing party were paid all of his interest based upon the actual or real value of the corporate assets as contemplated by the agreement as a whole and specifically paragraphs two and three which refer to “. . . all right, title, and interest in any stock or interest in said Acme . . .” and “As a condition of the aforesaid Release of all the interest in the business . . .”

## POINT II

THE COURT COMMITTED ERROR IN NOT RULING THAT THE TERM "NET WORTH" AS USED IN EXHIBIT ONE MEANT THE ACTUAL NET VALUE OF THE CORPORATION.

The fact that the instrument here in question was poorly drawn does not relieve the court of its responsibility to ascertain its meaning if at all possible. *Mathis v. Madsen*, 1 Utah 2d 46, 261 P2d 952 (1953). When the meaning of ambiguous words in a contract can be clarified by reference to other parts of the contract, or where ambiguity arises by reason of the language used and not because of extrinsic facts, the court must interpret the words as a matter of law. *Paclawski v. Bristol Laboratories, Inc.* Okl, 425 P2d 452, 456 (1967).

An intergrated contract cannot be varied, modified, or contradicted by parol evidence and its interpretation is a question of law for the court. *Pacific States Cast Iron Pipe Co. v. Harsh Utah Corp.* 5 Utah 2d 244, 300 P2d 610, 616 (1956).

Chief Justice Wolfe in *Mathis v. Madsen*, supra, at page 956, adopting the trial court's memorandum decision stated:

"In searching for the meaning the court must first examine the language used in the instrument itself and accord to it the weight and effect which the instrument itself may show that the parties intended the words to have. If then its meaning is still ambiguous or uncertain, the court may con-

sider other contemporaneous writings concerning the same subject matter, and may, if still uncertain, consider parole evidence of the parties' intention."

Applying the foregoing principals and those rules stated in Point One herein, the trial court should have concluded that "net worth" as used in the agreement meant the actual net value of the corporation as opposed to its ruling that it meant mere book value of the corporation's stock. The plaintiff was not merely selling stock back to a corporation; he was giving up all those things that the stock he owned represented including an \$18,000.00 per year salary, one-half ownership in a going business which was making a profit at the time the transaction was entered into, one-half interest in the assets owned by the corporation, and the attendant power to determine the use to which those assets would be put to bring him a return on his investment. None of these items are taken into consideration in determining book value of corporate stock. However, if the actual net value of the corporation is used in determining what the plaintiff would receive for all his interest in the corporation, the basis of the bargain between the parties is more realistically arrived at. Depreciated value of assets have no relationship to the actual value of a corporation.

The Supreme Court of Iowa has been often confronted with an analogous situation in cases commenced under a statute providing for the payment of the real value of the stock owned by a stockholder voting against renewal of a corporate existence. In *Woodward v. Quig-*

ley, Iowa, 133 N.W. 2d 38 (1965) the court uses various formulae and calculations to arrive at a figure which would represent the real value of descending stockholder's stock. The "net asset value" of the corporation was used in this determination. Such a method of evaluation takes into consideration all those factors which must necessarily be considered in arriving at an equitable price for the stock. Such a method of evaluation could be used in the case at hand to arrive at the real value of the plaintiff's interest in Acme Building Products, Inc.

## CONCLUSION

The trial court's finding that words "net worth" as used in the Memorandum of Understanding and Agreement meant the net worth of the corporation based upon book value of the corporation is unreasonable when the correct principals of contract interpretation are applied.

This court is respectfully requested to reverse the trial court's holding and hold as a matter of law that the words "net worth" as used in the agreement meant the actual net value of the corporation.

Respectfully submitted,  
BROWNING & YOCOM  
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