

1979

# Rio Algom Corporation v. Jimco Ltd et al : Brief of Appellant

Utah Supreme Court

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Clinton D. Vernon; Clifford L. Ashton; Attorneys for Defendants-Respondents;  
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CASE NO. 16032

Appeal from an Order of the 3rd  
District Court for Salt Lake County  
Hon. Dean E. Conder, Judge

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JUN 2 1979

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IN THE SUPREME COURT OF THE STATE OF UTAH

\* \* \* \* \*

RIO ALGOM CORPORATION,	)	BRIEF OF APPELLANT
	)	
Plaintiff-Appellant,	)	
	)	
v.	)	
	)	
JIMCO LTD., HUMECA EXPLORATION	)	
COMPANY, JIM L. HUDSON, JUANITA	)	CASE NO. 16032
J. MEYER AS EXECUTRIX OF THE	)	
ESTATE OF DANIEL H. MEYER,	)	
ELDON J. CARD, NORMA HUDSON,	)	
JEAN L. CARD, JUANITA J. MEYER,	)	
N. J. WHITE, AUDREY WHITE,	)	
WILMA WHITE, OTIS DIBLER,	)	
DOROTHY MAE DIBLER, GRACE DAVIS,	)	
and MARLOWE C. SMITH,	)	
	)	
Defendants-Respondents.	)	

\* \* \* \* \*

STATEMENT OF THE CASE

This is a declaratory judgment action brought by plaintiff-appellant, Rio Algom Corporation (hereinafter referred to as "Rio") against two groups of respondent-defendants, the Jimcos<sup>1</sup> and the Audreys.<sup>2</sup> Rio's complaint seeks a declaration of the method it should employ in calculating and paying royalty obligations owed to both groups of Defendants under two agreements relating to the lease of certain unpatented uranium mining claims.

---

<sup>1</sup> This group consists of Jimco Ltd., Humecca Exploration Company, Jim L. Hudson, Juanita J. Meyer (both individually and as Executrix of the Estate of Daniel H. Meyer), Eldon J. Card, Norma Hudson and Jean L. Card.

<sup>2</sup> This group consists of Audrey White, N. Y. White, Wilma White, Otis Dibler, Dorothy Mae Dibler, Grace Davis and Marlowe C. Smith.

The Jimco defendants counterclaimed against Rio, seeking rescission or reformation and damages based on theories of mutual mistake, unilateral mistake, breach of an implied covenant, fraud and negligent misrepresentation. The Jimcos also crossclaimed against the Audrey defendants on theories of mutual mistake, unilateral mistake, fraud and negligent misrepresentation.

The Audrey defendants crossclaimed against the Jimco defendants and counterclaimed against Rio asserting breach of an agreement with the Jimco defendants, of which Rio is the assignee.

#### DISPOSITION IN LOWER COURT

This appeal is from an Order entered by Judge Dean E. Conder of the Third Judicial District Court of Salt Lake County which dismissed all claims by Rio and the Jimcos against the Audreys, all claims by the Audreys against Rio and the Jimcos, and certain claims by Rio against the Jimcos. The Order here appealed from was entered by Judge Conder based upon an agreement purportedly binding all parties, including Rio, although only the Jimcos and the Audreys were parties to that agreement, and Rio timely objected to its provisions.

#### RELIEF SOUGHT ON APPEAL

Rio seeks reversal of Judge Conder's Order, which dismissed the Audreys from this lawsuit and determined that Rio

has no cause of action based on the agreement entered into between the Audreys and the Jimcos.

### STATEMENT OF FACTS

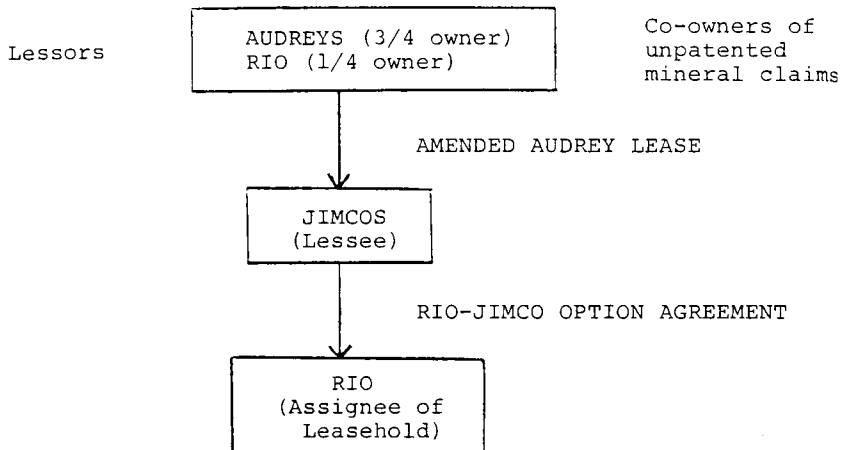
#### 1. Relationship of the Parties.

Rio and the Audreys are tenants in common of certain unpatented mining claims in San Juan County, Utah, containing valuable uranium ore. Rio owns a one-fourth and the Audreys a three-fourth undivided interest in these properties. In June 1968, Rio and the Audreys entered into an agreement leasing these claims to the Jimcos. That agreement has been styled the "Amended Audrey Lease" in this lawsuit (R. 74-125).

In July 1968, the Jimcos in turn granted Rio an option to take an assignment of their leasehold interest in those uranium claims under an agreement entitled the "Rio-Jimco Option Agreement" (R. 7-72). Rio exercised this option, took possession of the claims, developed a uranium mine, and built a mill to refine the ore extracted from these claims and others. Since taking possession in 1968 Rio has been mining, refining and marketing the uranium ore extracted from the claims (R. 2101).

The following schematic summarizes the relationships between the parties:





## 2. Pertinent Royalty Provisions.

(a) Royalties under the Amended Audrey Lease. In the Amended Audrey Lease the Jimcos agreed to pay a royalty of four percent of the price received for yellowcake ( $U_3O_8$ ) to the Audrey defendants and Rio, the owners-lessors, (R. 80-83). In addition, the Audreys and Rio reserved the right in the Amended Audrey Lease to have those royalties based on eight percent of the fair market value of crude ore produced from the claims, in lieu of the four percent royalty just described (R. 80). In other words, the owners were entitled to royalties based on either four percent of the price received for the refined product ( $U_3O_8$ ) or on eight percent of the value of unprocessed, raw ore, at their election. The decision to elect either the eight percent ore or four percent yellowcake royalty is vested

exclusively in the Audreys under the Amended Audrey Lease, and Rio is not entitled to participate in that decision (R. 80, 118).

Rio gave up the right to participate in making the royalty election decision after negotiations between all three parties. The other parties were concerned that Rio would have a conflict of interest in making the election because it was both a lessor (under the Lease) and a lessee (under the Rio-Jimco Option Agreement). As the Audrey lease explains:

21.3 Rio . . . shall, by reason of its interest in this Lease as described in Section II hereof, be excluded from any vote or decision of the lessors relating to royalties. . . . [R.120]

2.3 The parties hereto recognize and acknowledge that Rio Algom Corporation, in a capacity distinct from its capacity as one of the Lessors herein, on June 18, 1968 held a valid and subsisting option to acquire an assignment of the leasehold interest of the Lessee. . . . The parties hereto recognize the validity of the exercise of said option by Rio. . . . [Section II, R.79-80].

While Rio delegated the election decision to the Audreys in the foregoing provisions, however, it certainly expected that the Audreys would make the election from time to time so as to choose the election which would pay them the most money. That decision would of course also benefit Rio since it was entitled to one-fourth of the total royalties under either election. As one permissible royalty formula became more lucrative than the other because of changing market conditions for ore and yellowcake, all the parties doubtless anticipated that the Audreys would choose the more profitable of the two elections.

(b) Royalties under the Rio-Jimco Option Agreement.

After Rio exercised the option granted to it by the Jimcos in the Rio-Jimco Option Agreement, it assumed the lessees' obligation to pay royalties under the Amended Audrey Lease (R. 25). After Rio exercised that option it also became obligated to pay royalties to the Jimco defendants. In summary, Rio became obligated by virtue of the two agreements to pay royalties to itself, the Jimcos, and the Audreys (R. 33-43).

Like one of the two royalties payable to itself and the Audreys, the royalties which Rio was obligated to pay to the Jimcos are based on the price received for yellowcake. Those royalties may vary from eight percent to a ceiling of fifteen percent of that price (R. 33-35). The royalties due to the Jimcos are to be paid only after satisfaction of the full royalties due to the lessors (the Audreys and Rio) under the Amended Audrey Lease. It is this order of priority in making royalty payments which led to this lawsuit, since the Jimcos might conceivably collect no royalties at all under certain circumstances which are explained next.

(c) Interrelationship of Royalties. As noted above, one of the elections available under the Amended Audrey Lease is based on yellowcake sales price, like the sole royalty basis for payments to the Jimcos under the Rio-Jimco Option Agreement. So long as the Audreys chose to elect royalties based on yellowcake price, then, the Jimcos would always be

assured of receiving the royalties allowable to them under the Rio-Jimco Option Agreement, up to the fifteen percent ceiling provided in that agreement.

If market conditions changed, however, and the Audreys elected the second royalty option based on the value of crude ore, the Jimcos could conceivably be caught in a royalty "squeeze" and receive little or no royalties. The following hypotheticals illustrate this potential "squeezing effect."

#### EXAMPLE I

Assume:      Total price for yellowcake = \$100.00  
                 Total value of ore                        = \$ 75.00

Ceiling on total royalties payable    = \$ 15.00

I.A. If Audreys choose 4% yellowcake election, the parties receive:

Audreys:    3% yellowcake  
                 = \$3.00

Rio:            1% yellowcake  
                 = \$1.00

Jimco:        \$15 ceiling less royalties to Lessors:

15 - [3+1] = 15-4  
= \$11.00

I.B. If Audreys choose 8% ore election, the parties receive:

Audreys:    6% ore = 6% (75)  
                 = \$4.50

Rio:            2% ore = 2% (75)  
                 = \$1.50

Jimcos:        \$15 less royalties to lessors:

\$15 - [4.50+1.50]  
= \$9.00

## EXAMPLE II

Assume:    Total price for yellowcake = \$100.00  
            Total value of ore                = \$187.50

Ceiling still same because  
yellowcake price same                                = \$ 15.00

II.A If Audreys choose 4%  
yellowcake election,  
the parties receive the  
same royalties as I.A.

II.B. If Audreys elect 8%  
ore, the parties receive:

Audreys:    6% ore = 6% (187.50)  
                             = \$11.25

Rio:                2% ore = 2% (187.50)  
                             = \$3.75

Jimcos:        \$15 - [11.25+3.75]  
                             = \$15-15 = \$0.

The foregoing examples are of course hypothetical and are not intended to reflect actual current or projected values of ore and yellowcake. Nonetheless, they are useful to illustrate the general principle that the Jimcos' earned royalties will suffer, perhaps dramatically, if (1) the Audreys choose the eight percent ore royalty, and (2) the value of ore approaches or exceeds the price received for yellowcake. Even under the first example, in which ore has a lower total value than yellowcake, the Jimcos would receive \$2.00 less under the ore election than they would under the yellowcake election -- an eighteen percent decrease in income.

Nor are these examples completely hypothetical. Counsel for the Jimcos is in fact deeply concerned about this "squeeze," as illustrated by the following argument he made to the court:

If Audrey and Rio were to prevail on their original theory of fair market value of ore and get this Court to impose a fair market value figure that is in effect the present spot prices for small size, that would eliminate Jimco . . . if the price goes up another couple of bucks. . . .  
[Remarks of Mr. Savage, R.2206].

### 3. Genesis of this Lawsuit.

In August 1975, the Audrey defendants elected to exercise the option in the Amended Audrey Lease to change the royalty payment basis from the four percent yellowcake to the eight percent ore option (R. 3). It must logically be assumed that they believed this election would increase the income they would receive as lessors. It was that election which gave rise to Rio's institution of this declaratory judgment action, after unsuccessful attempts by the parties to determine the basis for computing that royalty obligation.

The Audreys asserted that the basis for calculating this royalty was to be arrived at by reference to an "external" uranium ore market, i.e., that the royalties should not be computed on the basis of what Rio itself received for sales of materials from the subject claims (R. 4). The Jimcos, on the other hand, asserted that the basis for calculating the royalty should be arrived at by reference to the "internal" market, i.e., Rio's actual selling price for yellowcake produced from the subject properties (R. 4). The Jimcos doubtless believed that this "internal" reference would be lower than the Audreys' preferred "external" reference, so that the Jimcos' total

share of the royalties would not be reduced as much. Since the Jimcos and the Audreys could not compromise on these materially different positions, Rio instituted this action so that the court could resolve that issue (R. 6).

4. The Purported "Settlement" Between the Audreys and Jimcos.

In July 1978, shortly before the matter was scheduled to go to trial, the Audreys and the Jimcos entered into an agreement to which Rio was not a party, and which they cosmetically entitled "Settlement Stipulation and Motion." In that agreement, the Audreys and the Jimcos attempted to permanently determine the basis to be used by Rio in calculating its royalty obligations under the Amended Audrey Lease (R. 2241-2247). Not only was Rio not a party to this stipulation, Rio also objected to its terms.

The purported settlement contains two provisions which Rio contends fundamentally violate its rights flowing from the Amended Audrey Lease. As noted above, the Amended Audrey Lease provided that the Audreys could annually elect whether to take their royalty on the basis of four percent yellowcake or eight percent ore. In the purported settlement agreement the Audreys forever forfeit this option, as more fully explained in the following contract language from the purported settlement:

2. For the calendar year 1979, and all years thereafter, the Audrey defendants hereby waive their right to the election of royalty payments based upon market value of crude ore as provided in paragraph 3.2 of the Audrey Lease, and

agree to timely revoke their previous election under paragraph 3.2. Timely notice of the revocation of said election will be provided by the Audrey defendants to Rio. [R.2243].

Rio contends that the waiver of this election directly affects its rights and expectancy interests under the Amended Audrey Lease. Rio contends that it could originally have expected (when the contract was executed) that the Audreys would perpetually make elections in their own selfish interests (and thereby benefit Rio which receives twenty-five percent of the royalties paid under the Audrey Lease). Under the purported settlement, however, the Audreys have forfeited this election and have agreed to perpetually elect four percent yellowcake, leaving Rio with twenty-five percent of that royalty (or one percent yellowcake), even though the ore election may produce greater returns to Rio in the future.

In exchange for the waiver of the election, the Jimcos agreed in paragraph 1.c of the purported settlement to transfer certain of their royalties to the Audreys. The purported settlement provides that the Jimcos assign to the Audreys "that amount which, when added to that amount which the Audrey defendants would otherwise receive directly from Rio, equals 5.5 percent of the proceeds received by Rio from Duke Power Company, or any other purchaser, for the sale of yellowcake" (R. 2243).

Rio contends that this too directly violates its rights under the Audrey Lease because under that lease Rio always



received twenty-five percent of the "Audrey royalty pie," whereas under the new arrangement Rio will receive one percent of yellowcake while Audrey will receive 5.5 percent of yellowcake -- effectively reducing Rio's percentage of the so-called royalty pie from twenty-five percent to 15.3 percent.

The purported settlement agreement was presented to the court for approval in the form of a "Settlement Stipulation and Motion." The motion for approval was much more than a mere request of the court to approve a settlement as between the two parties to that settlement; in addition, it requested the court to make a substantive ruling determining Rio's rights. The motion which accompanied the request for approval read as follows:

The Audrey defendants and the Jimco defendants hereby move the court for a ruling that Rio has no standing under either the Audrey lease or the Jimco agreement, or any other theory of law or equity, to challenge or otherwise bar the effectuation and implementation of the foregoing Settlement Stipulation, that such Settlement Stipulation is not in violation of any duty owed to Rio by any of the defendants, that upon effectuation and implementation of said Settlement Stipulation the Audrey defendants are effectively and totally dismissed from this litigation, and that those funds presently on deposit with the court equal to 5.5% of the proceeds from the sale of yellowcake by Rio since January 1, 1976, together with accrued interest thereon, less any amounts previously withdrawn by Audrey defendants therefrom, be promptly paid to the Audrey defendants. [R.2246].

What was presented to Judge Conder, therefore, was a procedurally unique request whereby he was directly asked to rule that the purported settlement had no impact whatsoever on any rights of Rio either in law or in equity.

Rio filed objections to the proposed Settlement Stipulation and also filed an amended complaint wherein it asserted that the Stipulation constituted, among other things, tortious interference with its contract rights, a breach of fiduciary duties owed to it, and a violation of its contract rights.

After argument and the submission of memoranda (but without the benefit of discovery, jury trial, or other procedural niceties), the trial court summarily approved the Settlement Stipulation, ruled that Rio had no rights in the matter, allowed Rio to amend its complaint, and then dismissed the complaint for failure to state a cause of action. It is from this Order that the appeal is brought.

The following chart briefly summarizes the various ownership, tenancy and royalty relationships among the parties.

NAME	PARTIES TO AGREEMENT	OWNERSHIP/TENANCY STATUS	ROYALTY RIGHTS	OTHER PERTINENT PROVISIONS	OBLIGATIONS TO PAY ROYALTIES
I. THE AMENDED AUDREY LEASE					
RIO	YES	CO-OWNER (1/4)	OPTION 1: 1% YELLOWCAKE SALES OPTION 2: 2% FMV ORE	A. JIMCOS AGREE TO PAY ONE OF FOLLOWING TO CO-OWNERS: 4% YELLOWCAKE SALES; OR 8% FMV CRUDE OPE B. ONLY AUDREYS CAN ELECT WHICH OF THE ABOVE ROYALTIES WILL BE PAID TO BOTH CO-OWNERS	JIMCOS TO PAY NOTED ROYALTIES TO: 1. RIO 2. AUDREYS
AUDREYS	YES	CO-OWNER (3/4)	OPTION 1: 3% YELLOWCAKE SALES OPTION 2: 6% FMV ORE		
JIMCOS	YES	LESSEE	NONE		
II. THE RIO-JIMCO OPTION AGREEMENT					
RIO	YES	ASSIGNED OF TENANCY	BASIS NOT AFFECTED	A. RIO ASSUMES ALL THE JIMCOS' TENANCY OBLIGATIONS WHICH WERE CREATLD IN THE AMENDED AUDREY LEASE B. NO AMENDMENTS TO AGREEMENT CAN BE MADE WITHOUT WRITTEN CONSENT OF ALL PARTIES (CLAUSE XXV, R. 64)	RIO IS TO PAY ROYALTIES TO: 1. RIO 2. AUDREYS 3. JIMCOS
AUDREYS	NO	NOT AFFECTED	BASIS NOT AFFECTED		
JIMCOS	YES	ASSIGNOR OF TENANCY	8% to 15% GROSS SALES VALUE OF YELLOWCAKE, TO BE PAID AFTER FIRST DEDUCTING AUDREY LEASE ROYALTIES		
III. THE SETTLEMENT STIPULATION AND MOTION					
		THOSE INTERRELATIONSHIPS WERE NOT AFFECTED BY THE STIPULATION. BY VIRTUE OF THE COMBINED EFFECT OF THE TWO PRECEDING AGREEMENTS, THOUGH, THOSE INTERRELATIONSHIPS ARE:			
RIO	NO	1/4 OWNER AND TENANT OF CO-OWNERS	1% YELLOWCAKE SALES (I.E., FIRST OPTION ONLY)	A. AUDREYS PERMANENTLY RESCIND SECOND ROYALTY ELECTION UNDER AMENDED AUDREY LEASE B. AUDREYS GET ADDITIONAL 2.5% ROYALTY IN CONSIDERATION FOR PERMANENT WAIVER OF ROYALTY ELECTION	
AUDREYS	YES	3/4 OWNER AND LESSOR TO RIO	3% YELLOWCAKE SALES PLUS NEW 2.5% YELLOWCAKE SALES (I.E., FIRST OPTION PLUS 2.5%). TOTAL: 5.5%		
JIMCOS	YES	FORMER TENANT; PRESENT ROYALTY HOLDERS	FORMULA NOT AFFECTED		

## STATEMENT OF POINTS

- I. The trial court erred in approving the Stipulation because that agreement varies the Amended Audrey Lease and the Rio-Jimco Option Agreement without the concurrence of all parties to both agreements.
- II. The trial court erred in allowing the Audreys and Jimcos to alter the Amended Audrey Lease without Rio's consent, since Rio is an intended beneficiary of that lease.
- III. The trial court erred in approving the Stipulation because waiver of the royalty election in exchange for an additional 2.5 percent yellowcake proceeds royalty is a breach by the Audreys of fiduciary duties owed to Rio.
- IV. The trial court erred in approving the Stipulation because that agreement breaches an implied covenant by the Audreys in favor of Rio.
- V. The trial court erred in dismissing Rio's Amended Complaint.

## PREFACE TO ARGUMENT

It should be understood by the Court, in reviewing the arguments which follow, that the unique and summary procedure employed below in approving the purported settlement, a procedure violative of fundamental concepts of due process, colors the entire appellate consideration of the substantive issues. The closest analogy that we can suggest is that the trial court has, in effect, granted a motion against Rio finding that Rio cannot state a claim upon which relief can be granted. (We suggest this analogy because there has been no trial of the matter, there was no evidentiary hearing, and there were not even the limited procedural safeguards normally attending a motion for summary judgment under Rule 56). Therefore, we contend that the normal appellate presumptions and standards applicable to a ruling under Rule 12(b)(6) of the Utah Rules of Civil Procedure should apply in the Court's analysis of the substantive issues set forth hereinafter. The legal standard in this state in such matters was set forth by this Court in Liquor Control Commission v. Athas, 121 Utah 457, 460, 243 P.2d 441, 443 (1952), wherein the Court held:

A motion to dismiss should not be granted unless it appears to a certainly that plaintiff would be entitled to no relief under any state of facts which could be proved in support of its claim. [Emphasis added].

See also Christensen v. Lelis Automatic Transmission Service, Inc. 24 Utah 2d 165, 467 P.2d 605 (1970).

Merely because this matter has been presented in the form of a purported "Settlement Agreement" (which automatically evokes the traditional judicial sympathy in favor of settling matters), the Court should not lose sight of the fact that in addition to merely settling disputes as between themselves, the Audreys and Jimcos have purported definitively to determine the rights of Rio as well.

We suggest, therefore, that in reviewing the arguments to follow herein, the Court review them as it would the granting of a motion to dismiss under Rule 12(b)(6). The questions thus presented, for example, are not whether Audrey and Jimco have violated duties to Rio but whether, under the Athas holding, it has been demonstrated to a certainty that Rio could not prove a violation of duties under the pleadings as set forth in its Amended Complaint.

#### ARGUMENT

##### POINT I

THE TRIAL COURT ERRED  
IN APPROVING THE STIPULATION  
BECAUSE THAT AGREEMENT VARIES  
THE AMENDED AUDREY LEASE  
AND THE RIO-JIMCO OPTION AGREEMENT  
WITHOUT THE CONCURRENCE OF ALL PARTIES  
TO BOTH AGREEMENTS.

By virtue of the Stipulation and the trial court's Order entered in accordance therewith, the Audrey defendants agreed to permanently waive the eight percent ore royalty election in

exchange for an additional yellowcake proceeds royalty of two and one-half percent. In so acting, the Audreys have permanently rescinded an election in whose proceeds Rio formerly would have shared, in exchange for an additional yellowcake royalty in which Rio will not share. Because of that agreement, Rio's participation in royalty proceeds from the subject claims will be permanently reduced from twenty-five percent of the whole to 15.3 percent.

The effect of the Stipulation is to work two material and permanent changes to the Amended Audrey Lease and the Rio-Jimco Option Agreement. Those modifications are: (1) permanent waiver of the ore election in the Amended Audrey Lease, and (2) a permanent reduction in Rio's pro rata share of royalties from the subject claims. The trial court erred in approving the Stipulation which implements those material changes to the agreements between the parties without Rio's consent to either change.

The second change (reduction of Rio's share of the royalties) is by itself sufficient to constitute significant damage to Rio. But the first change (waiver of the election) could conceivably have an even more damaging impact. Reference to the hypotheticals in Section 2(c) of the preceding Statement of Facts is perhaps the best summary of the impact of this waiver on Rio. Had the Audreys maintained their insistence on an eight percent ore royalty, Rio might well have received considerably more money than it will under the four percent yellowcake election. By

abandoning the ore royalty the Audreys have of course also permanently precluded Rio from sharing in the consequences of that potentially more lucrative formula.

The trial court approved this outcome and dismissed Rio's amended complaint without taking any evidence whatsoever on the potential consequences of the Audreys' waiver. Rather, the trial court was apparently persuaded by Jimco counsel's assertion in oral argument that, "You can't presume that Audrey would prevail on its theory of fair market value [at trial] and assume from that that Audrey and Rio together would have made a lot more money on the royalties. It can't be presumed that they are going to succeed" (Remarks of Mr. Savage, R.2304]. Certainly it cannot be "presumed" that the Audreys would have prevailed on their asserted basis for computing ore royalties. But it likewise cannot be "presumed," as the trial court apparently did, that the Audreys would certainly have lost at trial either. If, as Jimco counsel hinted, the Audreys had prevailed, Rio had paid the Lessors that ore royalty, and as a result "Audrey and Rio together. . . made a lot more money on the royalties," then Rio is clearly damaged by the "settlement." It will never be entitled to that more lucrative income because the Audreys have abdicated the ore royalty election and the trial court failed to allow any discovery or trial on these potential damages.

The trial court approved the "settlement" between the Audreys and Jimcos in complete disregard not only of Rio's claims of damage but also of the fundamental principle that a contract



cannot be modified without the consent of all contracting parties. In this case, both the Audrey Lease and the Rio-Jimco Agreement have been materially modified without Rio's consent. The Stipulation materially alters the terms of the Amended Audrey Lease, to which Rio was a party and a lessor, because both Rio's ownership rights and the former ore royalty election are set forth in that agreement.

The Stipulation also materially amends the Rio-Jimco Option Agreement because that agreement expressly provided that Rio was assigned the Jimcos' tenancy rights under the Amended Audrey Lease subject to "all . . . provisions, terms, covenants and conditions" contained in that lease (Rio-Jimco Option Agreement, Clause V(a), R. 24, and Amended Audrey Lease, ¶19.1, R. 116-17). Because Rio was assigned the Jimcos' tenancy rights subject to all the terms and conditions of the Amended Audrey Lease, and because the terms of that lease have been materially modified in two respects by virtue of the Stipulation, the effect of the Stipulation is also to alter materially the obligations which Rio assumed under the Rio-Jimco Option Agreement.

It is fundamental law that the terms of a written lease cannot be varied without the prior written consent of all lessors. The same rule of course applies to all contracts: prior consent of all parties is a prerequisite to any material modification of the contract. E.g., 17 Am. Jur. 2d, Contracts, §465 at 935 ("A modification of a contract requires the assent of . . . all parties to the contract"). Accord: Malstrom v. Consolidated

Theaters, 4 Utah 2d 181, 184, 290 P.2d 689, 691 (1955). "A meeting of the minds of contracting parties is required not only to make a contract, but also to abrogate or modify it after it is made." Western Airlines v. Hollenbeck, 124 Colo. 130, 235 P.2d 792, 796 (1951). For that matter, "[the] terms of a contract cannot be changed even for the benefit of a party without his knowledge and approval. . . ." Columbian Nat'l Life Ins. Co. v. McClain, 115 Colo. 458, 174 P.2d 348, 351 (1946) [emphasis supplied].

Since Rio is a named lessor in the Amended Audrey Lease, the foregoing law clearly precludes any amendments to the terms of that lease without Rio's prior written consent. Similarly, the Rio-Jimco Option Agreement expressly precludes any amendments to that agreement without the prior written consent of all parties (Clause XXX, R. 64). Because the amendments effected by the Stipulation do materially alter both those agreements, the trial court clearly erred in entering the Order appealed from, an Order approving a modification which violates fundamental contract law. Furthermore, given the express prohibition to amendments of the Rio-Jimco Option Agreement without the prior consent of all parties, the lower court's approval of the Stipulation also violates the fundamental rule that where "the intent of the parties can be ascertained with reasonable certainty it must be given effect." Maw v. Noble, 10 Utah 2d 440, 443, 354 P.2d 121, 123 (1960).

Because the Stipulation violates the express intentions of the parties to both agreements, and because it materially alters

the terms of both agreements, the Order approving that Stipulation must be reversed.

## POINT II

THE TRIAL COURT ERRED IN  
ALLOWING THE AUDREYS AND JIMCOS  
TO ALTER THE AMENDED AUDREY LEASE  
WITHOUT RIO'S CONSENT, SINCE RIO  
IS AN INTENDED BENEFICIARY OF THAT LEASE.

Rio is not only a party to but also an intended beneficiary of the Amended Audrey Lease. Rio is an intended beneficiary by virtue of the lease provisions governing the royalty election. That is, although Rio is not allowed to exercise the royalty election, a decision vested solely in the Audreys, it is still entitled to participate in the outcome of whichever election is made since it is a one-fourth owner and therefore has a one-fourth interest in any royalty payments made under the lease.

Rio is an intended beneficiary of the lease because the original contracting parties, including Rio, intended that it would be benefited (i.e., that it would receive one-fourth of the royalty payments) under the election option. See Hammill v. Maryland Cas. Co., 209 F.2d 338 (10th Cir. 1954); Montgomery v. Rief, 15 Utah 495, 50 P. 623 (1897).

Once a beneficiary has accepted or acted on the terms of an agreement made for his benefit, the original parties to that agreement cannot alter its provisions without the consent of that beneficiary. See Manning v. Wiscombe, 498 F.2d 1311 (10th Cir. 1974) (applying Utah law).

When the Audrey defendants signed the Stipulation, they agreed permanently to waive their right to exercise the eight percent ore royalty election. The effect of this decision was to abdicate forever the rights of both Rio and the Audreys to choose to have royalties paid based upon eight percent of the fair market value of crude ore. The permanent waiver of that election constitutes a material modification to the Amended Audrey Lease, a modification made without Rio's consent and accomplished by virtue of an agreement to which it was not a party.

Therefore, because the effect of the Stipulation is to vary the Amended Audrey Lease without Rio's consent, even though Rio is an intended beneficiary, the trial court erred in approving the Stipulation and its Order must be reversed.

### POINT III

THE TRIAL COURT ERRED IN APPROVING  
THE STIPULATION BECAUSE WAIVER  
OF THE ROYALTY ELECTION IN EXCHANGE  
FOR AN ADDITIONAL 2.5 PERCENT YELLOWCAKE PROCEEDS  
ROYALTY IS A BREACH BY THE AUDREYS  
OF FIDUCIARY DUTIES OWED TO RIO.

When the trial court approved the Audrey defendants' permanent waiver of the royalty election, it also approved a deliberate breach of fiduciary duties owed by the Audreys to Rio. As a one-fourth owner of the properties, Rio was entitled to the benefits of whichever election was made by the Audrey defendants, even though it had no right to exercise that election option itself. When the Audrey defendants agreed permanently to waive that option, in whose benefits Rio was formerly

entitled to participate, and the Audreys received in exchange an additional 2.5 percent royalty, they clearly engaged in self-dealing to Rio's detriment.

In Britton v. Green, 325 F.2d 377 (10th Cir. 1963), co-owners of oil and gas leases sued another co-owner whom they had designated as the operating agent and lessee of those properties. The co-tenant/operating agent agreed in the leases to operate the subject properties to the mutual interests of all parties to the leases. The co-tenant/lessors alleged that the operating agent had failed to protect and market the minerals discovered in his drilling activities.

The Tenth Circuit noted that when one or more co-tenants vest another co-tenant with the rights and responsibilities of operating their common property, all the co-tenants "become co-adventurers in the enterprise, and stand in a fiducial relationship to each other." The court further noted that the operating agent/co-tenant assumed the responsibility under the leases of acting "for and on behalf of his co-tenants and he is thus the trustee for his co-tenants and co-adventurers." 325 F.2d at 383. The court also explained that, given this interrelationship between the parties, the operating agent assumed the following responsibilities:

. . . [A]n undivided owner who is to manage and operate the lease stands in a fiduciary relationship to his coadventurers and is bound to exercise the utmost good faith in managing and operating such lease and reporting and accounting to his co-owners with respect to such management and operation.

-- Id. at 387-88.

Rio and the Audreys stand in a position similar to that among the co-owners in Britton. Both parties are tenants in common of the subject claims, and Rio delegated to the Audreys an important right under the Amended Audrey Lease, i.e., the decision to elect between either permissible basis for royalty payments under that lease. Therefore, the Audreys owe Rio a fiduciary duty in exercising that royalty election, and they must make election decisions in a manner which evidences the "utmost good faith" and which benefits not only themselves but Rio as well. When the Audreys took an additional 2.5 percent yellowcake royalty by virtue of the Stipulation, increasing their own royalty interest and decreasing Rio's pro rata share in those royalties, they made a decision which clearly evidences self-dealing and abrogates their fiduciary responsibilities to Rio, the other co-owner of the Audrey claims.

For that matter, even where one co-tenant does not delegate important operating rights to other co-tenants, tenants in common still owe each other fiduciary responsibilities in dealing with the property subject to their co-tenancy. E.g., Hendrickson v. California Talc Co., 55 Cal. App. 2d 279, 130 P.2d 806 (1943) (also involving mining claims). As the Hendrickson court explained:

The usual rules that a fiduciary relationship exists between tenants in common and that one cotenant may not gain a present advantage by acting adversely to his fellow tenants should be applied to [this] case.

The general rule is that parties engaged in a common enterprise owe a duty to each other with respect to all matters in connection therewith, that a trust relationship is inherent in such an association for a common purpose, and that one of the parties will not be allowed to deal with the subject matter of the association for his own advantage.

-- 103 P.2d at 810.

By the logic of the Hendrickson decision, then, the Audrey defendants have breached a fiduciary duty owed to Rio independent of the responsibilities which they owed Rio by virtue of their exclusive right to exercise the royalty election. That is, the mere fact that Rio and the Audreys are both tenants in common of the subject claims is in itself independently sufficient to create a fiduciary relationship between them, and when the Audreys permanently waived the election decision and engaged in self-dealing in agreeing to that waiver, they violated a basic fiduciary responsibility to Rio.

For each of the foregoing independent reasons, the trial court erred in approving the Stipulation, as the conduct approved in the court's Order constituted a breach of fiduciary obligations to Rio. The Order must therefore be reversed.

#### POINT IV

THE TRIAL COURT ERRED IN APPROVING  
THE STIPULATION BECAUSE THAT AGREEMENT  
BREACHES AN IMPLIED COVENANT BY THE AUDREYS  
IN FAVOR OF RIO.

Not only does the Settlement Stipulation entail breaches of fiduciary duty owed by the Audreys to Rio, it also constitutes a breach of an implied covenant of good faith owed by the Audreys to Rio. Many jurisdictions recognize implied covenants in mineral leases which impose a duty on the operator of such leases to conduct the business to the mutual profit of both the lessee and the non-participating landowner-lessor.

In Shaw v. Henry, 216 Kan. 96, 531 P.2d 128 (1975), for example, the Kansas Supreme Court recognized that all lessees under oil and gas leases are required by an implied covenant to exercise "reasonable diligence in doing what would be expected of an operator of ordinary prudence, in the furtherance of the interests of both lessor and lessee." 531 P.2d at 131. Accord: Weymouth v. Colorado Interstate Gas Co., 367 F.2d 84, (5th Cir. 1966); Harding v. Cameron, 220 F. Supp. 466, 470 (W.D.Okla. 1963).

In this case, the Amended Audrey Lease contains an implied covenant that the Audreys will make the election determination in "furtherance of the interests of" all lessors, including Rio. The Audreys' waiver of their right to exercise the election in exchange for an additional yellowcake proceeds royalty in which Rio does not participate breaches that implied covenant.

The implied covenant principles above stated with respect to oil and gas leases have been broadly applied to other situa-



tions involving tenants in common, and clearly derive from the beneficiary duties owed by co-tenants to each other. As one commentary has succinctly explained those principles:

In certain situations, fiduciary duties between co-tenants will rest upon a bailiff arrangement. Where one co-owner surrenders management functions to another for the development of joint interests, the manager is called the bailiff and by the great weight of authority has a fiduciary status very similar to that of a trustee. Although he lacks title to a common trust corpus, he tacitly agrees to serve the property of all. When he obtains an advantage over his co-tenant by contract, he assumes the duty to exercise that advantage fairly and responsibly. His fiduciary obligations, accordingly, are very broad.

-- Martz & Hames, "Implied Rights of Royalty Owners," 3 Rocky Mtn. Mineral Law Inst. 195, 222 (1957).

The same writers stress that implied duties have provided equitable protection to one party against overreaching by another. Equity will intervene where the following conditions are present:

First, where the parties have a relationship to each other arising out of a common interest in the property or enterprise. Second, where they stand to gain or lose as a direct consequence of failure of the enterprise. Third, where one party by contract or conveyance has obtained the executive control over the interest of another. And finally, where the non-executive has no adequate way to protect himself against unfair or inequitable decisions of the executive. All of these elements characterize the mineral royalty relationship and give a sound basis for the implication of fiduciary duties to the mineral owner.

-- Id. at 228-29.

In summary, whenever one co-owner surrenders some "executive control" to another, the executive co-owner occupies a

fiduciary position. The Audreys' exclusive right to exercise the royalty election therefore imposes on them such responsibilities to Rio.

Furthermore, the Audreys owe Rio a duty to act in good faith simply by virtue of their status as co-owners. Examination of the Amended Audrey Lease (R. 74-125) reveals that Rio surrendered no rights in that document as an owner-lessor co-tenant to its other tenants in common, except the right to participate in any decision as to whether or not to exercise the royalty election. Rio did not surrender any rights to participate fully in the proceeds arising out of its status as owner-lessor of an undivided one-fourth interest, or to demand and receive from its other co-tenants an accounting with respect to the use of, and proceeds derived from, the property.

Tenants in common owe each other fiduciary duties with respect to their dealings with commonly held property. Consequently, one or a number of co-tenants may not gain an advantage by acting adversely to his or their fellow co-tenants. See Webster v. Knop, 6 Utah 2d 273, 312 P.2d 557 (1957). If one or a number of co-tenants deal with commonly held property to the detriment of a fellow co-tenant, that fiduciary duty is breached. See Webster v. Knop, supra; Hendrickson v. California Talc Co., supra.

In Webster v. Knop this Court considered facts analogous to the instant case and discussed the scope of a co-tenant's fiduciary duty. In that case, two plaintiffs and a defendant

executed a mining grubstake contract whereby plaintiffs supplied labor and the defendant furnished supplies. They agreed that each would receive a one-third undivided interest in any claim staked pursuant to the contract, which expired July 31, 1954. Various claims were filed in the names of the three parties. The parties were later informed that the claims were void because of an existing oil and gas lease. Congress then enacted legislation allowing valid claims to be filed over existing oil and gas leases. Thereafter, on August 14, 1954, the defendant refiled the claims in his own name.

In holding that the scope of the fiduciary duty survived the expiration of the grubstake agreement, this Court emphasized equitable considerations. Defendant knew of the mining claims only out of his fiduciary relationship with plaintiffs. Defendant's self-dealing attempt to use knowledge of the legislation and of the claims to gain title to an entire claim, when he had specifically agreed to a one-third interest, was deemed unfair.

The foregoing discussion related to this case because the Webster court extended the fiduciary duty beyond the strict confines of the contract to prevent inequity. The contract had expired when the defendant refiled the claims. Nevertheless this Court held that the defendant's fiduciary duty required him to refile the claims in the name of all three parties.

In this case, the Audrey defendants owe a fiduciary duty to their co-tenant, Rio. That duty is consistent with the lease and with the principles enumerated by this Court in Webster. By self-dealing with the Jimco defendants, the Audreys have

attempted to sever the link between themselves and Rio. Webster indicates that the Audreys' duty to their co-tenant to choose the more profitable royalty formula extends beyond the provisions of the lease and precludes them from self-dealing with the election.

The foregoing authorities clearly support a finding that the Audreys are bound by an implied covenant of good faith which runs in favor of Rio in making the royalty election determination. This duty arises independently by virtue of (1) the parties' status as co-tenants and (2) the Audreys' responsibilities to Rio as managers of the royalty election. Their overreaching in this case was approved by the trial court's Order implementing the Stipulation, and that Order must be reversed.

#### POINT V

#### THE TRIAL COURT ERRED IN DISMISSING RIO'S AMENDED COMPLAINT.

Two weeks after the Audreys and the Jimcos submitted their Settlement Stipulation to the trial court for its approval, Rio submitted a motion to amend its complaint and a proposed amended complaint (R. 2023-24, 2099-110). Rio moved to amend its complaint on the grounds that the Stipulation gave rise to additional causes of action in its favor against both the Jimcos and the Audreys.

Rio alleged in its Amended Complaint that the Audreys had breached fiduciary duties owed to it arising out of the election

option waiver and their common status as co-owners of the subject claims (R. 2104-07). Rio further alleged that the Jimcos had induced the Audreys to breach the fiduciary duties which the Audreys owed to Rio (R. 2107-09). Rio prayed for the imposition of a continuing constructive trust on the proceeds received by the Audreys arising out of the Stipulation and also sought damages from the Jimcos.

The merits of Rio's claims for breach of fiduciary duty against the Audrey defendants are discussed at some length in the foregoing arguments and will not be reiterated here. Rio simply respectfully submits that the trial court erred in ruling that those claims failed to state a cause of action against the Audreys.

As to Rio's claims that the Jimcos induced the Audreys to breach fiduciary duties they owed Rio, absolutely no evidence was taken by the trial court which would either support or negate that cause of action. Obviously, if the court below erred, as Rio asserts that it did, in dismissing the causes of action in Rio's Amended Complaint against the Audreys, it also erred in dismissing those causes asserted against the Jimcos, as it should have been entitled to conduct discovery and present facts to the trial court in support of its claims that the Jimcos induced the Audreys to breach those fiduciary duties.

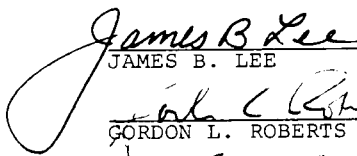
Rio submits that the trial court erred in refusing Rio the opportunity to conduct discovery and attempt to prove those claims, which involve material issues of fact as to the intent

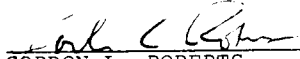
of the parties and the detriment which would be suffered by Rio as a result of the Stipulation. Under those circumstances, either summary judgment or dismissal under Rule 12(b)(6) of the Utah Rules of Civil Procedure is precluded. E.g., Livingston Ind., Inc. v. Walker Bank & Trust Co., 565 P.2d 1117, 1118 (Utah 1977); See also, Bill Brown Realty, Inc. v. Abbott, 562 P.2d 238, 239 (Utah 1977); Liquor Control Commission v. Athas, supra. Consequently, the trial court also erred in dismissing Rio's Amended Complaint and that portion of its Order must also be reversed.


#### CONCLUSION

As the foregoing arguments and authorities demonstrate, the trial court erred both in approving the Stipulation and in dismissing Rio's Amended Complaint. For those reasons, the entire Order of the court below should be reversed.

RESPECTFULLY SUBMITTED this 2<sup>nd</sup> day of January, 1979.

  
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JAMES B. LEE

  
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GORDON L. ROBERTS

  
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MAILING CERTIFICATE

I hereby certify that on this 2<sup>nd</sup> day of January, 1978, I personally mailed one (1) true and accurate copy of the foregoing BRIEF OF APPELLANT, postage prepaid, to Clifford Ashton, of VanCott, Bagley, Cornwall & McCarthy, 141 East First South, Salt Lake City, Utah, 84111, and to William G. Waldeck, Post Office Box 2188, Grand Junction, Colorado, 81501.

Kent W. Winterhake

CERTIFICATE OF SERVICE

I hereby certify that on this 2<sup>nd</sup> day of January, 1978, I personally delivered two (2) true and accurate copies of the foregoing BRIEF OF APPELLANT to Albert J. Colton, Fabian & Clendennin, 800 Continental Bank Building, Salt Lake City, Utah, 84101 and to Clinton D. Vernon, 415 Kearns Building, Salt Lake City, Utah, 84101.

Kent W. Winterhake