1966

Rocket Mining Corporation, A Utah Corporation, and Pioneer Carissa Gold Mines, Inc., A Wyoming Corporation v. Bulan J. Gill and Angelo M. Billis : Brief of Appellants

IN THE SUPREME COURT OF THE STATE OF UTAH

ROCKET MINING CORPORATION, a Utah corporation, and PIONEER CARISSA GOLD MINES, INC., a Wyoming corporation,

Plaintiffs and Respondents,

vs.

RULAN J. GILL and ANGELO M. BILLIS,

Defendants and Appellants.

Case No. 10467

BRIEF OF APPELLANTS

Appeal from Summary Judgments of the Third District Court for Salt Lake County Honorable Aldon J. Anderson, Judge

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STATEMENT OF THE KIND OF CASE

Rocket Mining Corporation brought suit September 21, 1961 on a Complaint against six defendants who had been officers and directors of that company, alleging they unlawfully conspired together to sell the corporate assets and divide the money realized from such sale, which resulted in damage to the corporation in the sum of $250,000 and that they unlawfully with-

drew from the corporate treasury $28,000. The plaintiff further asked for an accounting from defendants for all funds expended by them and for exemplary damages of $50,000 for their fraudulent acts. Defendants filed a timely motion to dismiss and the court thereupon ordered the plaintiff to file an Amended Complaint alleging with particularity the acts of fraud complained of. On July 28, 1962 an Amended Complaint was filed joining another plaintiff, Pioneer Carissa Gold Mines, Inc., which company was subsequently alleged to be the successor of Rocket Mining Company's assets. This Amended Complaint expanded the original fraud cause of action set forth in the first complaint, into eight counts generously larded with accusations and innuendoes, seeking damages of $1,330,584.69 plus such additional sums as an accounting may develop.

DISPOSITION IN LOWER COURT

After several minor amendments to the Amended Complaint and following the taking of the defendant's depositions for the second time, a single issue was identified and summarily adjudged against two of the defendants, A. M. Billis and R. J. Gill, the appellants in this proceeding. This Summary Judgment entered April 21, 1965, held that these two defendants were individually liable for the return of salaries received by them for employment services they rendered the corporation during the year 1957, as general manager and president of Rocket Mining Corporation, respec-

tively. Billis received a total of $8,400.00 representing $700.00 per month and Gill received a total of $9,000.00 representing $750.00 per month. Interest from January 14, 1958, the time of the lump sum payment of these salaries, made the Judgment summarily rendered against Billis $12,050.00 and against Gill $12,915.00. The lower court further ruled that these summary judgments were final and ripe for appeal.

The summary judgments were based solely upon the court's interpretation of the following phrase contained in Rocket Mining Company's offering circular:

> "No salaries or other compensation shall be paid directly or indirectly to officers, directors, or promoters of issuer, other than Secretary-Treasurer, who will receive $75.00 per month, until issuers' mining operations are on a paying basis."

RELIEF SOUGHT ON APPEAL

Each of these two defendant appellants seek reversal of the judgments against them and judgments in their favor as a matter of law with respect to the adjudicated issue or, that failing, a new trial thereon.

STATEMENT OF FACTS

This case is representative of the lingering aftermath of a rather strange interlude in Utah history—the great uranium boom of the early fifties, when many

Utahns with limited knowledge of geology, mining and corporate law and finance attempted to develop another Mi Vada mine to make them financially independent. Most such attempts were soon thwarted by the limited nature of production and market and the harsh reality that successful mining ventures require substantial financial resources.

Rocket Mining Corporation, a Utah corporation, was incorporated in 1955 for the purpose of conducting exploration for and development of uranium and other valuable minerals. It was given under its Articles of Incorporation, all the usual powers of a mining company, including the power to deal with respect to mining property in the leasing, buying and selling of lands. (Exh. P-7).

Defendant Gill began obtaining mining properties and organizing this mining corporation in July of 1955, at which time he was employed by the U.S. Rubber Company. He was an incorporator of Rocket Mining Corporation and was the president and director of the company from the time of its incorporation until March of 1959, when he sold his interests in the corporation to one Roy Cram. Defendant Billis, although not an incorporator, was active in the promotion and development of the company and during the year 1957, the period of time in question, was general manager of the company.

A public offering was authorized for the sale of Rocket Mining Company's corporate stock at 5c per

share, but because the stock would not sell, the price was subsequently reduced to 1c per share. The corporation obtained only $30,000 as a result of this public offering, approximately $15,000 of which was subscribed and paid for by certain of the organizers of the company. The offering circular used for this public offering (Exh. P-3), contained the following phrase, which phrase was apparently used during the latter days of the uranium boom to allay investors' fears that officers might use the moneys received by the company as a result of the public stock sale for corporate salaries rather than a development of the company interests:

> "No salaries or other compensation shall be paid directly or indirectly to officers, directors, or promoters of issuer other than Secretary-Treasurer, who will receive $75.00 per month, until issuers' mining operations are on a paying basis."

The public offering was terminated because of the difficulty in selling the registered stock and also because the company had obtained an apparently valuable mining lease in the Temple Mountain area of Utah and it appeared that mining operations commenced by the company on this lease would produce adequate capital for the company's operations. The promising operations in the Temple Mountain area were ultimately discontinued because Rocket Mining Company's lessor became involved in a dispute as to the ownership of the property.

The company, however, continued to operate and acquire numerous claims and mining interests, which

acquisitions were made, in part, from the limited capi realized from the public offering but, mainly fro moneys loaned to the corporation by its officers. Som of the properties and interests acquired included a interest in a producing oil well in Wyoming, a Mercur mine in Nevada, valuable uranium claims in Ne Mexico, stock in the Empress Oil and Uranium Co poration, and in the Mobile Oil and Uranium Cor poration, and a leasehold interest in a group of claim in the Gas Hills Mining District of Wyoming, known as the Rim Group. Although development of some of these properties was begun by the company and some production was obtained from them, it is conceded that the financial return from actual production was insufficient to produce a net profit to the company.

In March of 1956 Defendant Gill resigned from his employment with the U.S. Rubber Company and thereafter until sometime in the year 1958, he devoted his full time to the affairs of Rocket Mining Company. Defendant Billis began devoting his full time to the interests of Rocket Mining Company in the late summer of 1955 and also continued such endeavors until sometime in 1958. No compensation was authorized or paid to either of these defendants until December 14, 1956, when the Board of Directors of Rocket Mining Company finally authorized salaries of $750.00 per month for Gill and $700.00 per month for Billis.

On November 2, 1956, Pioneer Carissa Gold Mines, Inc., entered an Agreement to sell to Rocket Mining Corporation a gold ore processing mill located near

Lander, Wyoming for the sum of $60,000 and 2,000,000 shares of Rocket Mining Company stock. This stock under the agreement was required to be provided by Defendant Gill. Rocket intended to convert this mill into a uranium processing mill and use it in an integrated operation to process the ore that had been blocked out on its Rim Group claims. These Rim Group claims had been initially acquired by defendants Gill and Billis in their own names and transferred by them to Rocket at no cost to the company. The drilling program which had blocked out a substantial amount of valuable ore on the Rim Group claims had been performed by the Uranium Research and Development Company for a percentage interest in the claims. This drilling had been arranged for by defendants Gill and Billis and again Rocket was not required to provide any funds therefor.

In order for Rocket to develop and mine these valuable Rim Group claims and make the necessary conversion of the processing mill, it needed to obtain substantial funds. Defendant Gill, as President of the company, negotiated an underwriting agreement with an Eastern concern to provide the required capital. The terms of the underwriting agreement required that all large stockholders escrow their stock. Pioneer Carissa Gold Mines, Inc., was the only large stockholder to refuse to comply with this escrow requirement and this refusal caused the loss of this necessary financing

Under Rocket's drilling agreement with the Ura-

nium Research and Development Company, Rock was required to contribute its proportionate share all future costs of development and mining operation or sell its interests to Uranium Research. Because the required financing had been thwarted by Pioneer Carissa Gold Mines, Inc., and there were no other sources available for the required funds, Rocket Mining sold its interest in the Rim Group claims to Uranium Research and Development Company for $130,000. This sale was consummated in January of 1957 and from the profits thus realized by Rocket, it paid to defendants Gill and Billis the 1957 salaries that had been authorized them by the Board of Directors of the company, in December of 1956. Most of the remainder of the sales price of the claims was used to pay incurred corporate debts.

Because of the continuing disagreement with Pioneer Carissa representatives regarding Rocket Mining Corporation, defendants Gill and Billis sold out their interest in Rocket to one Roy Cram in 1959 and have not been connected with the corporation since that date. At the time of such sale, the corporation still had extensive assets, including all the mining properties enumerated hereinabove except the Rim Group claims, plus the processing mill near Lander, Wyoming and cash in excess of $4,000 remaining from the proceeds of the Rim Group sale after payment of the corporate debts.

The facts as here stated are taken from the Affidavit of R. J. Gill and are deemed admitted for purposes of Summary Judgment. *Reliable Furniture Co.*

v. *Fidelity and Guaranty Insurance Underwriters, Inc.*, 16 Utah (2d) 211, 398 Pac. (2) 685.

ARGUMENT

POINT I. THE PAYMENT OF OFFICERS' SALARIES WAS A PROPER CORPORATE FUNCTION AND WAS PROPERLY PAID FROM THE PROCEEDS OF THE SALE OF THE CORPORATE PROPERTY.

(a) THE INTERDICTION OF THE OFFERING CIRCULAR WAS LIMITED TO THE PROCEEDS FROM THE PUBLIC OFFERING.

An offering circular is required under the Securities Acts for the information and protection of an investor. Its purpose is to fully and fairly advise any prospective investor of the true facts regarding the company. The offering circular constitutes an offer by the company to sell stock to those persons to whom the circular is delivered. A contractual relationship based upon such circular is entered into by investors who accept such offer through their purchase of stock in the company. There is nothing about an offering circular that constitutes a contract between the company and anyone except such purchasing shareholders.

The court will note that the limitation on the payment of salaries relied on by plaintiff is included under the heading in the offering circular title "Use

of Proceeds" and is set forth within the item outlining the proposed use of the anticipated proceeds from the public offering. Clearly this restriction was recited to eliminate a prospective buyer's concern that paid-in capital might be dissipated in officers' salaries. The record discloses that only $30,000 worth of stock was sold of the $300,000 authorized in the public offering and that none of these funds were used in payment of officers' salaries, having all been properly invested in company properties and assets long before such payment. Thus, no one in the class of persons to whom the offering circular was directed and who may have invested in reliance thereon could complain, nor have any such persons complained.

The language used in the restrictive phrase regarding officers' salaries was perhaps unfortunately chosen to express the obvious purpose and intent of its framers, for it appears similar to the words often used within the habendum clause of a mining lease or deed which permits the reversion of the property unless production in paying quantities is achieved within a stated time. With respect to such habendum clauses, the courts have often strictly construed the forfeiture provisions thus conditioned for the obvious reasons of preventing speculation and waste of the owner's property. *Waring v. Lockett,* (Texas), 118 S.W. 2d 1000. A similar result was reached in the case of *Nelson vs. Steele*, 165 Cal. 15 130 P. 886, upon a contract providing for cancellation if the business was not on a paying basis within one year. It is respectfully submitted that these

cases where a condition subsequent terminated a contract cannot be applied as authority to the present case where the failure of a condition precedent might prevent the payment of an obligation already incurred, for such a determination would result in a distortion of the concept of recision, since equity requires the return of value received.

(b) THE PROCEEDS OF THE SALE OF MINING PROPERTIES USED IN PAYMENT OF APPELLANTS' SALARIES WERE IN FACT PROFITS FROM MINING OPERATIONS.

The mining property sold by Rocket which provided the funds used in payment of salaries to defendants Gill and Billis was property acquired for the corporation through the efforts of these two defendants and had been proven through mining operations directly resulting from their efforts. When the property was first acquired it had not been drilled and its mineral value was then speculative. The drilling program developed by these two defendants on the land revealed a substantial ore body. Rocket attempted to mine and ship the ore discovered on the Rim Group of claims, but was unable to obtain the necessary financing required for this endeavor because of Pioneer Carissa Gold Mines, Inc.,'s refusal to escrow its stock.

Not only was the power to sell property contemplated in the Articles of Incorporation of Rocket Mining Corporation and granted to it by statute, U.C.A.

1953, 16-10-4 (d) (e), but it has been held that a power creates a duty on a corporation to make a sale where financial stress can only thus be avoid *Biggs vs. Myton Canal and Irrigation Co.*, 54 U 120, 179 Pac. 984. Unable to continue the develop of the mining operations on the Rim Group beca of the action of the respondent in its capacity a large shareholder of Rocket Mining Corporation corporate officers thus had a duty to sell the prope and thereby achieve a substantial profit for the c poration. This profit was equal to the sales price, sin the corporation had paid defendants Gill and Bil nothing for the property and the drilling operati thereon had been financed by Uranium Research a Development Company.

The sale of these mining claims by Rocket w clearly a sale of an ore body which had been blocke out through a drilling program that was a "minin operation." The resulting net profit to the compa from the sale of the product of such "mining operation produced total proceeds in excess of all obligation incurred by the company from its inception. This surel then, put the company's "mining operations" on paying basis so that the salaries paid Gill and Bill were proper and not in violation of the restrictiv clause found in the offering circular.

(c) THE BUSINESS OF MINING INCLUDE THE SALE OF REAL ESTATE AND TH LANGUAGE OF THE OFFERING CI

CULAR SHOULD BE INTERPRETED BROADLY TO INCLUDE THIS CONCEPT.

Even under the common law, it was recognized that a mining corporation had the necessary power to sell property within its operations even though it could not dispose of all of its property without the consent of all shareholders, *Geedes v. Anaconda Copper Min. Co.*, 245 F.225. Under former Utah law, a *non*-mining corporation could dispose of property without the consent of shareholders only if its articles of incorporation authorized such transactions, but the dealing in property was deemed to be in the usual course of business of a mining corporation and the property could be disposed of without the consent of the shareholders. Thus, although the articles of incorporation in *Miller v. Peruvian Consolidated Min.* Co., 79 Utah 401, 11 P. 2d 291, did not recite that the corporation had the power to transfer real property and spoke generally with relation to products of mines, the court interpreted the purposes of the company to include the power to engage in the general business of mining, carrying with it the right to dispose of property within that framework.

> " . . . But as we read the articles of incorporation in this case we were impressed with the fact that the company was not organized merely to deal in the products of mines, but to engage in the general mining business. The introduction to the articles reads as follows: "Witnesseth:

Whereas the undersigned are desirous of asso ating themselves for the purpose of establishi and conducting a general mining business a holding property therein and of incorporati for the purpose under and in pursuance of t laws of said territory of Utah." Again the la two lines of Article 4 speak of 'doing all suc things as are customarily incident to the carry ing on of a general mining business.' In t clause of Article 4 referring to products, t incorporators use the terms working and de veloping which ordinarily have application t the mines or claims for the purpose of gettin the ores. Still further: What has been the prac tical application of these articles by the incor porators and their successors? Under Article they immediately purchase certain mines c claims; they purchase the additional one-hal interest in the Fritz claim; they lease the claim to the plaintiff in 1914; they enter into othe leases of their claims. *Did they not have in min that they were dealing in mines and minin claims and not merely the products, and did the not intend by the words 'purchasing, working developing, selling and otherwise disposing o to include mines and mining claims as well a the products?"* (Emphasis added).

(d) EQUITY AND PUBLIC POLICY RE-QUIRE PAYMENT OF SALARIES TO EMPLOYEES SOLELY RESPONSIBL FOR PROFITS TO THE CORPORATION

The property here sold was originally obtained i the names of defendants, Gill and Billis, and the transferred the property to the corporation, under th

belief that the contract of employment and consequent fiduciary duty required them so to do. If, in fact, the contract was unenforceable because of lack of consideration, the defendants should be entitled to a return of this valuable property given Rocket under a mistake of law.

Under respondent's view of the language of the offering circular, no payment could ever be made to full-time officers of the corporation if the corporation found that developing mining properties for profitable sale obtained more income than producing ore. The Board of Directors here voted a reasonable salary for defendants Gill and Billis, but even had they failed to do so, an officer who renders beneficial service to a corporation, under circumstances negativing an intent that they were to be gratuitous, may recover the reasonable value of his services. *Caminetti v. Prudence Mut. Life Ins. Ass'n.*, 62 C.A. 2d 945, 146 P 2d 15.

It would be in opposition to the best interests of Rocket Mining Corporation to interpret this provision as contended by the respondent. There was no binding obligation on any of the officers to continue to expend their time and efforts in behalf of the company. If such officers could not look forward to a reasonable expectation of compensation for their best efforts on behalf of the company in the event the company developed funds through its operation to pay a reasonable salary, there is every likelihood that the corporation would become totally inactive for no one would be interested

in pursuing its affairs. Such a situation would cl
be against public policy and adverse to the inter
of all stockholders.

POINT II. THE PLAINTIFF HAS N RIGHT OF ACTION UPON A STATEME MADE BY THE ROCKET MINING CORP RATION AS AN INDUCEMENT TO TH SALE OF STOCK.

The original complaint was filed by Rocket Min Corporation on September 21, 1961. In an amend complaint, July 27, 1962, Pioneer Carissa Gold Min Inc., was added as a party plaintiff without notice defendant and without leave of court. Upon defen ant's challenge to the parties plaintiff, the court pe mitted plaintiff to file an amendment to the amend complaint, February 28, 1964, in which it was alleg that "plaintiff, Pioneer Carissa Gold Mines, Inc., ha merged with Rocket Mining Corporation and is th surviving corporation as a result of said merger." N proof was offered as to the merger and although it wa denied, the court accepted the allegation as true.

Assuming for purposes of determining this Sum mary Judgment issue that Pioneer Carissa Gold Mine Inc., is a proper party for bringing rights of actio owned by Rocket Mining Corporation, Pioneer Carissa Gold Mines, Inc., still has no right of action upon a statement made by Rocket in an offering circular.

This is not a derivative action—it is not alleged

that stock was purchased in reliance upon the representation that the officers would be paid no salary until "issuer's mining operations are on a paying basis." In fact, the statement made, was the statement of the corporation itself, the corporation paid the salaries, and rather than having been damaged by reason of the statement, and the payment it appears that the corporation was benefited thereby.

Additionally the payment of salaries was not made out of capital obtained through the offering circular nor capital in the corporation at the time the statement was made.

One who purchases stock in reliance upon a fraudulent misrepresentation has a right of action upon such a statement in a public offering, if he was damaged by the statement. Here there was no misstatement of fact, no reliance, and no damage shown.

> "Plaintiff is not entitled to recover where there is no evidence to show that he suffered pecuniary loss by reason of the alleged fraudulent misrepresentation. The measure of damages is the difference between the real value of the stock at the time of the purchase and what the purchaser was induced to pay by reason of misrepresentation." 19 C.J.S. *Corporations*, Sec. 851 (5).

POINT III. ROCKET MINING CORPORATION, HAVING RECEIVED THE BENEFITS OF THE EMPLOYMENT CONTRACTS AND HAVING RETAINED THE FRUITS THEREOF, IS ESTOPPED FROM URGING

THAT SUCH CONTRACTS WERE ULTRA VIRES OR THAT THE CORPORATE OFFICERS WERE WITHOUT AUTHORITY WITH RESPECT THERETO.

The employment contracts here involved are illegal, violating neither statute nor public policy, have been fully performed by both parties to the contract, the officers and the corporation. If the disputed phrase of the offering circular is interpreted as a restriction on the contract between the officers and the corporation, the corporation's act in paying and the officers' act of receiving salaries is merely ultra vires and cannot constitute a basis for suit. Utah cases have been consistent in quoting and following the doctrine set forth in 3 Fletcher, Cyc. Corp., Sec. 1559, p. 2631:

> "When an ultra vires contract with a corporation has been fully performed on both sides neither party can maintain an action to set aside the transaction or to recover what has been parted with. In other words, neither a court of law nor a court of equity will interfere in such a case to deprive either the corporation or the other party of money or property acquired under the contract."

In the case of *Millard County School District v. State Bank of Millard Co.*, 80 Utah 170, 14 P.2d 967, the Utah Supreme Court recognized the distinction between an illegal or void contract and one merely ultra vires. The holding of this case committed Utah to the well-recognized rule that if a corporation has received

the benefits of a contract and retains the fruits thereof, it will be estopped from urging that the contract was ultra vires or the corporate officers were without authority with respect thereto.

In order to rescind, a showing must be made that the contract involved fraud and illegality or the corporation must restore the value it has received before a rescission or recoupment can be made. In this particular case the elements necessary to an action for rescission are impossible to achieve. Rocket Mining Company received not only the benefits of the defendants' full time and labor for the year 1957, but also applied the results of that labor, the substantial funds produced for the corporation, to the payment of the company's existing obligations.

Zion's Savings Bank & Trust Co. v. Tropic & East Fork Irr. Co., 102 Utah 101, 126 P.2d 1053, held that an ultra vires contract not otherwise illegal, is not void, but under certain circumstances and conditions may be enforced and that where a party has received benefits under the contract, it is estopped to set up the defense of ultra vires the corporation or that the corporate officers were without authority with respect thereto.

POINT IV. THE ACTION IS BARRED BY THE STATUTE OF LIMITATIONS.

U.C.A. 1953, 78-12-27, provides that the time within which action must be brought against corporation

officers for misfeasance in the performance of u
is "3 years, after discovery by the aggrieved pa
the facts upon which . . . the liability accrued."

Although defendants pleaded the bar of the st
plaintiff proffered no evidence to show that the
of discovery was a time later than January 14,
the date of payment of the salaries. This actio
instituted September 21, 1961.

Minutes of the directors' meeting of Decem
26, 1957, record the proposed distribution of proc
from the sale of the Rim claims, and it has been h
that both the corporation and the shareholders
charged with notice of the books of record, *Jones M*
Co. v. Cardiff Min. & Mill. Co., 56 Utah 449, 191
426. Respondent, Pioneer Carissa, was a shareho
at this time.

Likewise, Utah has followed the general rule
A.L.R. 1217, that in non-derivative suits, the St
of Limitations may be pleaded in bar of action u
wrongs of corporate officers or directors inasmuc
the trust of office is regarded as implied or construc
rather than express, which required a repudiatio
the trust to start the statute running. See *Jones M*
Co. v. Cardiff Min. & Mill. Co., supra; *Gibson v. Jens*
48 Utah 244, 158 P. 426; *S.L.C. v. S.L. Investm*
Co., 43 Utah 181, 134 P. 603.

Under code pleading, there was some dispute a
whether a pleaded conclusion that plaintiff had

knowledge of the cause of action prior to three years before bringing the action was sufficient to prevent judgment on demurrer. ***S.L.C. v. S.L. Investment Co.,*** supra, held that lack of knowledge must be alleged with particularity and that alleging a conclusion was insufficient. Insofar as this holding might be interpreted as requiring a plaintiff to anticipate a limitations defense, this holding was overruled in ***Nunnelly v. First Federal Building & Loan Association,*** 107 Utah 347, 154 P.2d 620. However, there is no question that the burden of alleging and proving a reason why the three-year limitation should not apply remains with the plaintiff upon the assertion of that defense. See Justice Wade's dissent in ***Nunnelly v. First Federal,*** *supra;* ***Bay City Lumber Co. v. Anderson,*** .... Wash. ..., 111 P. 2d 771.

The time for bringing action in this case expired on January 14, 1961, and the trial court erred in failing so to rule.

CONCLUSION

It is respectfully submitted that the Summ Judgments that have been entered against each of t two appellants, defendants Rulan J. Gill and A. Billis, should be reversed and Judgments entered their favor as a matter of law as to this adjudic issue, or, that failing, a new trial ordered thereon.

Respectfully submitted,

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