

OFFICE OF THE ATTORNEY GENERAL
State Capitol
Salt Lake City, Utah

February 22, 1949

Mr. Lawrence Taylor
Department of Business Regulation
B U I L D I N G

Dear Mr. Taylor:

We have received your letter of February 17, 1949 in which you inquire whether or not the following described transaction involves the sale of securities within the meaning of Section 82-1-4, Utah Code Annotated 1943.

You state that William I. Gomm of Vernal, Utah, is the owner of 160 acres of land in Ashley Valley, Utah. He has given an oil lease on the entire tract to the Equity Oil Company. Under the terms of this lease, the oil company is retaining a 7/8 interest in all oil produced on the tract and paying to Gomm, the lessor, a 1/8 interest of the oil produced thereon. Mr. Gomm has made an arrangement with a Mr. Pendleton, a securities dealer, whereby Mr. Pendleton is offering to the public a 1/160 interest in the 1/8 interest retained by the owner, lessor, Mr. Gomm. This is actually an undivided 1/1280 interest of the whole 160 acre tract. This interest is represented by a mineral deed which purports to convey an undivided interest in the real estate itself. The narrow question which you present is whether or not the interest represented by this mineral deed is an interest in real estate or is a security within the meaning of Utah law.

Under date of February 8, 1949, this office, in an opinion addressed to you, stated that a mineral deed as such, conveys an interest in real estate and a duly licensed real estate broker would be authorized to handle such transactions. Additional information which you have furnished us, puts an entirely different light on the matter. It is true that a mineral deed, without more, is a conveyance of real estate. However, under the facts stated above, it appears that the mineral deed is used as a subterfuge in an effort to circumvent the Utah Securities law. Section 82-1-4, Utah Code Annotated 1943, states in part:

"Security' shall include ...certificate of interest or participation or certificate of interest in a profit-sharing agreement; certificate of, contract for, or any conveyance or other instrument conveying, representing, or purporting to convey or represent, an interest or any right in, to or under any oil, gas or mining lease or permit;" (underscoring added)

Although there is no hard and fast rule by which it may be determined whether a transaction falls within this definition, the provisions should be liberally construed with a view to its remedial purposes. In determining whether or not a transaction involves the issuance of securities within the meaning of the statute, we must look to the substance and not to the form of the transaction. Securities and Exchange Commission v. Wickham 12 F. Supp. 245. In the case of State v. Pullen, 192 Atl. 473, the Texas Supreme Court passed on a fact situation which is nearly identical with the one you present in light of a statute very similar to our Utah statute. The court held that a transaction by a mineral deed was a security within the meaning of the statute. The court held in the following language:

"We cannot agree with the contention of the respondent that the sale of these 'Mineral Deeds' constitutes merely the sale of an interest in land in Texas. It is difficult to read these documents and not come to the conclusion that, notwithstanding the legal verbiage in which the transaction is clothed by such documents, they are nevertheless, securities evidencing an investment by the purchaser in a share of oil produced and brought to the surface by the lessee of the land described therein. Technically they may also evidence an interest in realty in Texas, but such interest, it seems to us, is an unsubstantial interest, because, by the very term of these documents, the purchaser thereof is actually precluded from the enjoyment of that interest in any other effective way than by receiving his proportionate share of the value of the oil produced and brought to the surface by the lessee. In other words, these documents are primarily evidence of a share in oil produced under an oil lease and only incidentally evidence of a transfer of an interest in realty. While they may be instruments conveying realty interests, according to the law of the state of Texas, that is not a good reason for holding they are not also securities, according to the law of this State regulating the sale of securities.

"These documents, upon close examination, clearly present a situation which demands that the realities prevail over the merely technical effect of the legalistic form of the documents themselves. Really and actually behind the form of a conveyance of an interest in land set out in these documents is an investment contract, and it is peculiarly the kind of an investment contract which lends itself readily to the perpetuation of the evil which the Securities Act is designed to eradicate.

"we are unwilling our construction of our statu' to make the mere form of such a contract a barrier to the carrying out of the will of the Legislature to protect the public welfare, as we have found it expressed in chapter 273. It would be a grave misfortune if, by slavish adherence to form and blind disregard of substance, the declared public policy of the State in the regulation of the sale of securities was thus nullified by this court."

In the case of People v. McCalla 220 P. 436 the court had the following to say in a similar situation:

"Where a corporation conveyed a small parcel constituting a 1/4000 part of a large tract subject to an oil lease, and the right on the part of the corporation to receive and disburse all income received from such land to the proper parties and to make any new agreements necessary for increasing or protecting such income, and contemporaneously with the execution of the deed issued to the grantee a certificate entitling the grantee to a 1/4000 part of the net income received from the land, held a 'security', within Corporate Securities Act, 2, subd. 6, as amended by St. 1921, p. 1116, 1, defining a 'security' as any instrument issued or offered to the public by any company evidencing or representing any right to participate or share in the profits or earnings, or distribution of assets of any business to carried on for profit, since the grantee's relation to the corporation was similar to that of a stockholder, the contract between them being not merely one of agency."

The case of People v. Daniels, 76 P (2nd) 556 is to the same effect.

Upon examining the transaction which you present, it appears to us that even though the transfer was made by means of a mineral deed which normally is used to convey an interest in real estate, in reality the deeds are nothing more than certificates of an interest in the oil lease. We do not feel that the form of the conveyance is controlling and we are of the opinion that the transaction to which you refer involves a "security" within the meaning of Section 82-1-4, Utah Code Annotated, 1943.

Yours very truly,

CLINTON D. VERNON
Attorney General

MCB:MLC
Ev