SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1939

No. 1010

A. C. FROST & COMPANY,

Petitioner,

vs.

COEUR D'ALENE MINES CORPORATION.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF IDAHO.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

A. C. Frost & Company, by its attorneys, prays that a writ of certiorari issue to review the judgment of the Supreme Court of the State of Idaho entered in the above cause on December 15, 1939.

Opinions Below.

The trial court rendered no written opinion, but adopted findings of fact and conclusions of law which appear at R. 205-218.

The opinion of the Supreme Court of the State of Idaho (R. 226), as modified following a petition for rehearing

(R. 235), appears in 98 P. (2d) 965, and is not yet officially reported.

Jurisdiction.

The judgment of the Supreme Court of the State of Idaho was entered December 15, 1939 (R. 226). A petition for rehearing was entertained; and the opinion originally announced was modified February 15, 1940 (R. 235), at which time the petition for rehearing was denied.

The statutory provision believed to sustain the jurisdiction of this Court is Section 237(b) of the Judicial Code, as amended. The statute of the United States which is involved is the Securities Act of 1933 (Act of May 27, 1933, c. 38, Title I, 48 Stat. 74, 77 §§ 4 and 5, Title 15 U. S. C. §§ 77 d, e). The judgment of the Supreme Court of the State of Idaho directs entry of a final judgment against petitioner. It is, therefore, final for purposes of this Court's jurisdiction. *Mower* v. *Fletcher,* 114 U. S. 127. The Supreme Court of the State of Idaho founded its decision on its interpretation of the Securities Act of 1933, holding that a contract for the sale of stock not registered under the Securities Act of 1933 is void as violative of the spirit or intent of that act. The question involved has not heretofore been passed upon by this Court. No provision of the Securities Act of 1933 purports to declare such a contract void; and counsel have found no opinion except that here sought to be reviewed which supports the decision below. The Federal question is, therefore, substantial. *Levering & Garrigues Co.* v. *Morrin,* 289 U. S. 103, 105; *Milheim* v. *Moffat Tunnel Dist.,* 262 U. S. 710, 716.

Questions Presented.

1. Whether an option under which shares of mining stock may be purchased from time to time is invalid as to the vendee where the vendor has failed to register the stock

with the Securities and Exchange Commission under the provisions of the Securities Act of 1933.

2. Whether one who takes an option to purchase all the shares of stock of a corporation remaining in its treasury (1,300,000 shares out of 3,000,000 authorized) and who subsequently waives the right to take some of the shares so the issuer can sell them to others is engaged in a transaction "involving any public offering" (Sec. 4 [1], clause 2, of the act).

Statutes Involved.

Section 5 of the Securities Act of 1933 (15 U. S. C. §77e), c. 38, 48 Stat. 74, 77 provides:

> "SEC. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
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> "(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or
>
> "(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.
>
> "(b) It shall be unlawful for any person, directly or indirectly—
>
> "(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security registered under this title, unless such prospectus meets the requirements of section 10 [15 U. S. C. § 77j].
>
> "(2) to carry or to cause to be carried through the mails or in interstate commerce any such security for

the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 10 [15 U. S. C. § 77j]."

Section 4 of the Securities Act of 1933 (15 U. S. C. § 77d) provides as follows:

"The provisions of section 5 [15 U. S. C. § 77e] shall not apply to any of the following transactions:

"(1) Transactions by any person other than an issuer, underwriter, or dealer; transactions by an issuer not involving any public offering; or transactions by a dealer (including an underwriter no longer acting as an underwriter in respect of the security involved in such transaction), except transactions within one year after the first date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter (excluding in the computation of such year any time during which a stop order issued under section 8 [15 U. S. C. § 77h] is in effect as to the security), and except transactions as to securities constituting the whole or a part of an unsold allotment to or subscription by such dealer as a participant in the distribution of such securities by the issuer or by or through an underwriter.

"(2) Brokers' transactions, executed upon customers' orders on any exchange or in the open or counter market, but not the solicitation of such orders."

Other provisions of the Securities Act of 1933 are copied in the appendix.

Statement.

Petitioner commenced this action against respondent in an Idaho state court to recover for breach of a contract (entered into with one Boland on September 10, 1934 and assigned by him the same day to petitioner). The contract (R. 175; 210) provided that, upon the monthly payment of certain sums, petitioner might acquire lots of stock at 10

cents a share up to the total of 1,300,000 shares held in the treasury of respondent company (R. 176). The stock of respondent was not registered with the Securities and Exchange Commission (Finding 10, R. 215). During the month of June, 1935, respondent refused further to deliver stock to petitioner, giving as the excuse for its refusal the want of registration of the stock with the Securities and Exchange Commission under the Securities Act of 1933 (R. 215). However, the contract (as modified, R. 212-213) was substantially complied with so far as petitioner's obligations were concerned until the payment due October 10, 1935 (Finding 8, R. 214). On March 13, 1936, respondent notified petitioner of the termination of the agreement on the ground that petitioner had failed to comply with the option agreement (R. 215).

Petitioner's president made every effort to have respondent register the stock with the Securities and Exchange Commission (R. 47), even securing registration forms and filling them up as far as he could (R. 61). There is no evidence that petitioner violated the Securities Act of 1933 by selling any of the shares which it acquired from time to time (R. 64). However, respondent (or its president, Nuzum) did make some sales of its treasury stock to certain brokers and, perhaps, others (R. 214). Since these sales were out of treasury stock to which petitioner was entitled, it was necessary to secure a waiver by petitioner of its right to take the shares; and this was done under an agreement whereby the petitioner was to be credited with the difference between the price received by respondent and the 10 cents which petitioner would have had to pay for the shares under the option agreement (R. 213).

The trial court entered findings of fact and conclusions of law (R. 205-218), denying petitioner any relief on the unexecuted portion of its contract (involving some 805,150

shares of stock (R. 215)), but allowing petitioner judgment for $16,306, with interest, as to the shares which had been sold by respondent itself (or Mr. Nuzum) to others than petitioner (R. 218). Both sides appealed; and the Supreme Court of Idaho, by a divided bench, affirmed as to that part of the judgment which denied petitioner recovery for damages arising out of the unexecuted part of the contract, and reversed the judgment so far as it was in favor of petitioner, it being its view that the contract was void for failure to register the shares under the Securities Act of 1933, so that the parties would be left where they were found (R. 226-235, 235).

Specification of Errors to be Urged.

1. The court erred in holding that the contract of September 10, 1934, as modified, violates the Securities Act of 1933.

2. The court erred in holding that the contract of September 10, 1934, as modified, is void.

3. The court erred in holding that the contract of sale and purchase of the shares of stock involved is not exempt from the provisions of Section 5 of the Securities Act of 1933 by reason of Section 4 of said Act.

4. The court erred in failing and refusing to enter judgment for petitioner.

5. The court erred in entering judgment for respondent.

6. The court erred in finding and holding that petitioner sanctioned the sale of treasury stock to all and sundry.

Reasons for Granting the Writ.

The decision below involves the determination of an important question of Federal law which has not heretofore been determined by this Court. The questions involved are

of public importance. This Court has taken no opportunity to pass on the Securities Act of 1933 except in the case of *Jones* v. *Securities & Exchange Commission,* 298 U. S. 1. The present case broadly involves the spirit and purpose of the act—for unless found in such spirit and purpose there is nothing in the act which declares contracts for the purchase of unregistered securities to be void. A proper exposition of the intent of the act is of great public importance, since practically all financing enterprises come face to face with that act.[1]

1. We are to remember that the Securities Act of 1933 is the so-called "truth in securities" law. The public purposes of the act are not served by permitting one who has failed to register its securities in accordance with the provisions of that act to profit from its violation by avoiding the consequences of its contract. See *Logan County Bank* v. *Townsend,* 139 U. S. 67, 75-76, and cases cited. Certainly the duty to register the stock, if one was present here, was on respondent. An examination of Section 6(a) (15 U. S. C. §77f), which covers "registration of securities and signing of registration statement," as well as of the act as a whole, will disclose that it was contemplated that the duty of registering was on the issuer (respondent). Section 12(2) (15 U. S. C. §77*l*) of the act gives to the purchaser (petitioner) alone, and not to the issuer (respondent), the right of rescission in the event of non-registration, provided certain facts are shown; but the contract is not declared void. It therefore appears that the decision below is in conflict with the statute itself, and sets at naught the purposes of

[1] When the question is presented as to whether a contract is void by reason of its execution in violation of a statute, the court must consider the entire statute generally, and its aims specifically, to determine whether the legislature intended to make such a contract void. *Harris* v. *Runnels,* 12 How. 79, 84; *National Bank* v. *Matthews,* 98 U. S. 621, 627; *Thompson* v. *St. Nicholas National Bank,* 146 U. S. 240, 251.

Congress expressly set forth. To allow respondent to hide behind the statute by repudiating the contract permits the statute to be used as a cloak for fraudulent operations.

The notion of the court below that the contract is invalid apparently was inspired by the provisions of an entirely different act (R. 229). It quoted provisions of the Securities Exchange Act of 1934, Section 29 (15 U. S. C. §78cc) which provides that every contract made in violation of that act and every contract which involves a violation of any provisions of the Act shall be void as regards the rights of any person, who, in violation of any such provision shall have made or engaged in the performance of any such contract. But the Securities Exchange Act of 1934 concerns entirely different subject matter, and the provisions relied on by the court below were inserted in the act by amendment (Act of May 27, 1936, c. 462, 49 Stat. 1375, 1377, §3), to be effective 90 days after its enactment (§13), subsequent in time to all the transactions herein involved. This ground of the decision was struck out following the petition for rehearing (R. 235). The court below thus removed the basis of its original decision without changing its erroneous conclusion. The court below ought to have realized that since the Securities Act of 1933, which is alone applicable, contains no remotely similar provision, a like effect was not intended with respect to contracts involving application of the provisions of the Securities Act of 1933 —even assuming that the contract involved did contemplate violation of that act. A different purpose is to be understood with respect to the Securities Act of 1933 in its entire structure and theory. The central purpose of that act is to ensure publicity of the factors involving value of stocks—not to prohibit dealings in stock. H. R. Rep. No. 85, 73d Cong. 1st Sess., *passim*. What the act strikes

against by civil liability is false statements of fact to the investing public. *Ibid,* p. 9.

The Securities Act of 1933 establishes its own penalties for failure to comply with its provisions. The penalty of making contracts void is not among those stated by the act. It is well settled that where a statute provides penalties for its violation the judiciary may not add a further penalty of its own making by declaring a contract to be void. *Fritts* v. *Palmer,* 132 U. S. 282, 289; *National Bank* v. *Matthews,* 98 U. S. 621, 627; *Dunlop* v. *Mercer* (C. C. A. 8th, 1907), 156 Fed. 545; cf. *Thompson* v. *St. Nicholas National Bank,* 146 U. S. 240, 251; *Logan County Bank* v. *Townsend,* 139 U. S. 67, 75-76. As was said in *Hobbs* v. *McLean,* 117 U. S. 567, 579, "When a provision is left out of a statute, either by design or mistake of the legislature, the courts have no power to supply it. To do so would be to legislate and not to construe."

The cases cited by the court below to sustain its holding that the contract is void because in contravention of positive law, were decided on the ground that there had been a violation in which the parties were in *pari delicto,* and so the law would leave them where it found them. Here the violation of the statute (failure to register), assuming there were a violation (see *infra*), is the unilateral fault of the issuer (respondent). The transaction involves a public offering or else it does not. If it does not, then the provisions of Section 5 are inapplicable [2]—in which event the failure to register is immaterial. If, on the other hand, it did involve a public offering, then the purchaser (petitioner) is of the class for the protection of which the act was adopted, so that the failure of respondent to register cannot be pleaded against petitioner.

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[2] Sect. 4(1) exempts transactions not involving any public offering.

Furthermore, the contract did not involve or contemplate any violation of the Securities Act of 1933. The mere contract for the sale of stock which is not already registered with the Securities and Exchange Commission does not give rise to a violation of the act. That act prohibits the use of the mails or instruments of interstate commerce to sell or offer to buy, or to carry, an unregistered security which involves a public offering. This contract did not contemplate, certainly so far as petitioner is concerned, any public offering of the stock. It was a sale by which petitioner was to take a large block of shares. It did not contemplate using the mails or instruments of interstate commerce in connection with any public offering as to stock which was not registered. It did not contemplate the non-registration of the stock;[3] and there is no showing whatever that respondent might not, for aught the contract provided, have registered the stock, or that petitioner did anything which might embarrass such registration. The evidence affirmatively shows just the reverse. Petitioner did all it could to aid and induce respondent to register the stock. R. 47, 61; Plaintiff's Exhibits 35, 37-42, inclusive; Defendant's Exhibits 44, 63 (all exhibits are on file with the Clerk of this Court). If there is any inference possible from the contract (R. 175; Plaintiff's Exhibit No. 9) it is only that respondent acted fraudulently in representing that it was authorized to sell and deliver the stock. The contract is "instinct with the obligation" on the part of respondent to register.

2. The contract involved in this case is exempt from any taint of illegality under Section 5 by virtue of the express provision of Section 4(a). Clause 2 of Section 4(a) pro-

[3] Any provision of a contract calling for non-registration of a security (but not, *semble*, the contract apart from such provision) would be void by the express declaration of Section 14 of the act.

vides that Section 5 shall not apply to "transactions by an issuer not involving any public offering." The court below held that this transaction constituted a "public offering," relying on *Securities & Exchg. Comm.* v. *Sunbeam Gold Min. Co.* (C. C. A. 9th, 1938), 95 F. (2d) 699. That case was a suit by the Securities and Exchange Commission itself to restrain issuance of unregistered securities. The issuer defended on the theory that, since the securities were to be sent only to certain shareholders of the issuer and of another company, the issue was not a "public offering." The Ninth Circuit Court of Appeals held, however, that Congress specifically intended to include within the term "public offering" sales of stock to shareholders unless they were so few that the sale to them would not constitute a "public offering" (citing and quoting the conference report of the House of Representatives at the time the act was passed). In that case, however, there were proposed sales to 530 individuals, shareholders in the two companies. In the present case, so far as petitioner's intent was concerned, there was a sale to but one person (petitioner), and petitioner, as was testified below (R. 64, 87), did not wish to and did not sell any of the shares which it received. It is true that, because petitioner was in some financial difficulties, it waived its right to take certain of the treasury shares so that respondent (or its President, Mr. Nuzum) might sell them. These sales were primarily to two brokerage firms; but respondent itself is guilty of any violation of the act in this respect, and it is impossible to see how the Federal law can permit a defendant to plead its own violation of that law in avoidance of its obligations.

But even if petitioner itself had resold some of the shares which it purchased from respondent, no violation of the act would be involved. For petitioner is not an "issuer, underwriter, or dealer" within the meaning of clause 1 of

Section 4(a) of the act; and, unless it is one or the other, its sales would have been expressly exempt from Section 5. It has never been suggested that petitioner is a dealer (§ 2[12] of the act), since it has not conducted the business of offering, etc. or otherwise dealing or trading in securities issued by another person. Nor is it an underwriter, since it did not purchase securities from respondent with a view to their distribution (§ 2[11] of the act). If it were held that petitioner is an issuer within Section 2(4) of the act, the holding would conflict with the rationale of the decision in *Landay* v. *United States* (C. C. A. 6th, 1939), 108 F. (2d) 698, 704, wherein the Sixth Circuit Court of Appeals is apparently of the opinion that the only persons, beyond the person actually obligated by the terms of the security, who can be considered "issuers" are those persons who completely dominate the corporation so that the acts of the corporation were their individual acts. As is apparent from the course of the proceedings in this case, including the repudiation of petitioner's contract, certainly petitioner far from dominated respondent.

Conclusion.

It is respectfully submitted that the writ should be granted.

ERNEST L. WILKINSON,
CHARLES J. KAPPLER,
JOHN W. CRAGUN,
Counsel for Petitioner.

APPENDIX.

Miscellaneous provisions of the Securities Act of 1933, c. 38, 48 Stat. 74, as amended (15 U. S. C. § 77a *et seq.*)

SEC. 2 (15 U. S. C. § 77b):

"(4) The term 'issuer' means every person who issues or proposes to issue any security; * * *"

"(11) The term 'underwriter' means any person who has purchased from an issuer with a view to, or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commission. * * *"

"(12) The term 'dealer' means any person who engages either for all or part of his time, directly or indirectly, as agent, broker, or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person."

SEC. 6 (15 U. S. C. § 77f):

"(a) Any security may be registered with the Commission under the terms and conditions hereinafter provided, by filing a registration statement in triplicate, at least one of which shall be signed by each issuer, its principal executive officer or officers, its principal financial officer, its comptroller or principal accounting officer, and the majority of its board of directors or persons performing similar functions (or, if there is no board of directors or persons performing similar functions, by the majority of the persons or board having the power of management of the issuer), and in case the issuer is a foreign or Territorial person by its duly authorized representative in the United States; except that when such registration statement relates to a security issued by a foreign government, or political subdivision thereof, it need be signed only by the under-

writer of such security. Signatures of all such persons when written on the said registration statements shall be presumed to have been so written by authority of the person whose signature is so affixed and the burden of proof, in the event such authority shall be denied, shall be upon the party denying the same. The affixing of any signature without the authority of the purported signer shall constitute a violation of this subchapter. A registration statement shall be deemed effective only as to the securities specified therein as proposed to be offered."

SEC. 12 (15 U. S. C. § 77l):

"Any person who— * * *

(2) sells a security (whether or not exempted by the provisions of section 77c, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security."

SEC. 14 (15 U. S. C. § 77n):

"Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void."