

1953

# Summit Range and Livestock Co. v. Ray Rees : Brief of Appellant

Utah Supreme Court

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**IN THE SUPREME COURT**  
**of the**  
**STATE OF UTAH**

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SUMMIT RANGE AND LIVESTOCK  
COMPANY, a corporation,

*Plaintiff and Respondent,*

vs.

RAY REES,

*Defendant and Appellant.*

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**APPELLANT'S BRIEF**

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Appeal From The District Court Of The Third Judicial  
District, In And For Summit County, State of Utah  
Honorable Clarence E. Baker, Judge

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GUSTIN, RICHARDS & MATTSSON,  
JAMES W. BELESS, Jr.,  
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# INDEX

	Page
STATEMENT OF FACTS .....	1
STATEMENT OF POINTS .....	6
ARGUMENT .....	7
1. The by-laws are illegal because they change the purpose of the corporation .....	7
2. The specific provisions of the by-laws are illegal by authorizing stockholders a free use of corporation assets....	12
3. The by-laws are illegal in authorizing the corporation to purchase its own stock .....	13
CONCLUSION .....	16

## TABLE OF CASES

Attorney General v. Lorman, 59 Mich. 157, 26 N. W. 311, 60 Am. Rep. 287 .....	7
Canyon Creek Irr. Dist. v. Martin (Mont.), 159 P. 418.....	11
Fower v. Provo Bench Canal & Irrigation Company, 99 Utah 267, 101 P. 2d 375.....	8
Miller v. Peruvian Consolidated Mining Co., 79 Utah 401, 11 P. 2d 291 .....	9
Pace v. Pace Bros. Co., 91 Utah 132, 59 P. 2d 1.....	14, 15
Tracy Loan & Trust Co. v. Merchants' Bank, 50 Utah 196, 167 P. 353 .....	8
Zion's Sav. Bank & Trust Co. v. Tropic & East Fork Irr. Co., 102 Utah 101, 126 P. 2d 1053.....	7

## STATUTES

Compiled Laws of Utah, 1888, Chapter I, part 4.....	2
Constitution of Utah, Section 10, Article 12.....	7, 12
Utah Code Annotated 1953, Section 16-2-14.....	11
Utah Code Annotated 1953, Section 16-2-16.....	15
Utah Code Annotated 1953, Section 16-2-45.....	8, 9
Utah Code Annotated 1953, Section 76-13-4.....	13, 14, 15
(Formerly Utah Code Annotated 1943, Section 103-12-4)	

IN THE SUPREME COURT  
of the  
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SUMMIT RANGE AND LIVESTOCK  
COMPANY, a corporation,

*Plaintiff and Respondent,*

vs.

RAY REES,

*Defendant and Appellant.*

Case No.  
8063

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APPELLANT'S BRIEF

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The basic question involved in this appeal is whether the ordinary business or trading corporation can be changed into a cooperative merely by adoption of by-laws to that effect. The judgment appealed from and which appellant seeks to have reversed would countenance such procedure.

STATEMENT OF FACTS

The Summit Range and Livestock Company was organized October 2, 1900 under the provisions of Chap-

ter I, part 4 of the *Compiled Laws of Utah, 1888* as a general business corporation (R. 40-47). The articles of incorporation originally provided:

“The object, business and pursuits of this Corporation shall be to buy, hold, own, occupy and sell Real Estate, and lease for range or grazing purposes, real estate, and to raise and deal in live stock, to sell wood, timber and stone, and personal property that may be necessary to carry into effect the purposes of this Corporation, provided, however, that no land shall be leased from the company upon which to graze sheep, whether of the lands now owned by the company, described as follows, to-wit: \* \* \* (describing lands) \* \* \* or any lands to which title may hereafter be acquired.” (R. 40).

The articles of incorporation were amended on April 25, 1925, to provide:

““The business and pursuits of this corporation shall be to own, purchase, hold, sell, mortgage and lease real estate, and to acquire or dispose of range or grazing land in any lawful manner, and to lease any of said land for grazing or other lawful purposes, and to sell wood, timber, stone or other material therefrom, and to purchase, lease, sell, raise or graze livestock, and to do all and everything necessary or incidental to carrying into effect the purposes and objects of this corporation.’”

thereby deleting the restriction as to the grazing of sheep on company lands (R. 48-49). The articles of incorporation were amended again on September 2, 1950, as follows:

“ ‘This corporation shall continue in existence for a period of one hundred years, unless sooner dissolved and disincorporated according to law.’ ” (R. 50-51).

The purpose of the corporation since 1900 has remained that of a general business corporation for profit.

The principal assets of the corporation over the years have been certain tracts of range lands located in Summit County, Utah. The trial court found that as time passed the company assumed a mutual, non-profit character and the range lands were held by the corporation “for the use and benefit of the stockholders of plaintiff corporation as range land upon which the said stockholders are authorized to place their livestock for grazing purposes” (R. 18).

On March 4, 1952 by-laws were adopted by the board of directors of plaintiff corporation (R. 18). The by-laws in their entirety were introduced as exhibits at the hearing before the trial court (R. 30-39). The gist of the by-laws was a spelling out and an attempted ratification of the then current practices of the corporation in allowing its stockholders to use, rent free, the grazing lands of the company, and the total effect was to give a mutual, non-profit, cooperative character to the corporation.

Appellant, Ray Rees, is a stockholder of the corporation, owning 910½ shares of stock out of the authorized 6000 shares of a par value of \$1.00 per share. During 1952 Rees was the only stockholder grazing cattle upon

the corporation's range (R. 28). There is no contention made that appellant ever joined in the adoption of the by-laws.

By its complaint filed June 2, 1952 the plaintiff corporation alleged the cooperative nature of the use of the company's lands as provided by its by-laws and set forth therein that the said by-laws provided for a designation by the company of separate areas for the grazing of sheep and cattle. The complaint further alleged that in accordance with the by-laws the board of directors of the plaintiff corporation designated certain areas for the use of defendant's cattle, and that in disregard of the by-laws the defendant placed his cattle on the range prior to the date set by the directors for the first use thereof and allowed his cattle to stray from the areas designated to defendant, and that the acts of defendant in defiance to the by-laws of the company would result in irreparable damage to the range, the plaintiff corporation and the other stockholders. Plaintiff's prayer is for an injunction against defendant's use of the range in disregard of the company's by-laws (R. 1-4).

Defendant Rees answered alleging affirmatively that the by-laws of the company were unlawful and contrary to the objects of the articles of incorporation (R. 7-13).

At the trial the parties stipulated for the admission in evidence of the articles of incorporation of the corporation and the amendments thereto (R. 40-51) and the

by-laws (R. 30-39). The stipulation then filed (R. 28-29) limited the issue to be tried by the trial court to the legality of the by-laws, and particularly as to the legality of three sections of said by-laws, namely: paragraph 8 of Article V, paragraph 11 of Article V, and paragraph 5 of Article I.

Paragraph 8 of Article V of the by-laws (R. 36-37) provides that areas of the range shall be designated for the feeding of cattle or horses and that this area shall be determined on the basis of the number of shares held by the stockholders desiring to place cattle or horses thereon.

Paragraph 11 of Article V of the by-laws provides that cattle and horse men shall be responsible for keeping their cattle and horses within the designated areas on the range (R. 37).

Paragraph 5 of Article I provides a first refusal option in favor of the company or its other stockholders in the event any stockholder shall desire to sell and shall receive a bona fide offer for his stock, and it restricts the sale of stock to outsiders without "first offering to sell the same to the company or other stockholders." (R. 30-31.)

The trial court found that the range was held by plaintiff corporation "for the use and benefit of the stockholders of the corporation as range land upon which the said stockholders are authorized to place their livestock



for grazing purposes" (R. 18), and gave judgment for the plaintiff corporation, thereby adjudging that the by-laws, and particularly the three sections thereof referred to by stipulation, were legal and binding upon the stockholders of the corporation (R. 20-21).

This appeal challenges the conclusions of law and the judgment of the trial court in adjudging that the by-laws of the plaintiff corporation are valid and binding upon defendant, and in support of our contention that the judgment is contrary to law we assert the following:

## STATEMENT OF POINTS

I. THE BY-LAWS OF PLAINTIFF CORPORATION ARE INVALID AND ILLEGAL IN THAT THEY CHANGE THE PURPOSE AND CHARACTER OF THE COMPANY FROM THAT OF A GENERAL BUSINESS CORPORATION TO A NON-PROFIT COOPERATIVE ASSOCIATION WITHOUT PROPER AMENDMENT OF ARTICLES OF INCORPORATION.

II. PARAGRAPHS 8 AND 11, ARTICLE V OF THE BY-LAWS ARE ILLEGAL BY GIVING THE CORPORATION A NON-PROFIT MUTUAL CHARACTER BY AUTHORIZING STOCKHOLDERS TO USE THE COMPANY'S RANGE ON THE BASIS OF SHARES HELD.

III. PARAGRAPH 5, ARTICLE I OF THE BY-LAWS IS ILLEGAL BY AUTHORIZING THE COMPANY TO PURCHASE ITS OWN STOCK IN CONTRAVENTION OF LAW.

## ARGUMENT

## POINT I.

THE BY-LAWS ARE ILLEGAL BECAUSE THEY CHANGE THE PURPOSE OF THE CORPORATION.

It is a basic concept of corporation law that the powers of a corporation are only such as are given it by its articles of incorporation and that its object and purpose is firmly set and determined by its contract with the State. *Fletcher Cyclopedia Corporations*, Vol. 1, Sec. 100, page 360 states:

“In either case the articles themselves are the sole criterion to ascertain the purpose for which it was formed, and the intent must be gathered alone from the written instrument, and cannot be aided or varied or contradicted by testimony or averments aliunde the instrument itself.”,

citing *Attorney General v. Lorman*, 59 Mich. 157, 26 N.W. 311, 60 Am. Rep. 287. The *Constitution of the State of Utah* expressly provides in Article 12, Sec. 10, as follows:

“No corporation shall engage in any business other than that expressly authorized in its charter, or articles of incorporation.”

In *Zion's Sav. Bank & Trust Co. v. Tropic & East Fork Irr. Co.*, 102 Utah 101, 126 P. 2d 1053, this Court held that a strict interpretation must be given the company's articles of incorporation in regard to the express purpose of the corporation and that the implied powers

of a corporation are those only incidental to and connected with the carrying into effect of the general purposes of a corporation as expressed in its articles. This same rule was previously set forth by the Court in *Tracy Loan & Trust Co. v. Merchants' Bank*, 50 Utah 196, 167 P. 353.

The general rule is stated at 13 *Am. Jur.* 224 as follows:

"Thus, there is a contractual obligation on the corporation with respect to its stockholders and on the stockholders with respect to each other that no fundamental, radical, or material change in the purposes of the corporation shall be made, and the corporation, even with the consent of a majority of its stockholders, has no right to accept an amendment of its charter so changing the purposes of the corporation as against nonconsenting stockholders."

Section 16-2-45, *Utah Code Annotated 1953*, specifically provides that

"\* \* \* the original purpose of the corporation shall not be altered or changed without the approval and consent of all the outstanding stock, but the adding to the purposes or object or extending the power and business of the corporation shall not be deemed a change of the original purpose of the corporation; \* \* \*".

This section was construed in *Fower v. Provo Bench Canal & Irrigation Company*, 99 Utah 267, 101 P. 2d 375,

where it was held that whether an amendment of the articles altered the original purpose of the corporation was a question of fact.

In *Miller v. Peruvian Consolidated Mining Co.*, 79 Utah 401, 11 P. 2d 291, it was held that the object and nature of its business as stated in the articles of incorporation are the criteria to determine the true character of a corporation, there quoting from 7 *R. C. L.* 55, Sec. 33, as follows:

“To determine the actual character of a corporation regard must be had to the objects of its formation and the nature of its business as stated in the articles themselves.”

The articles of incorporation of the plaintiff corporation clearly gave the plaintiff company a general purpose to engage in business for profit. The two amendments to the articles continued this business purpose and there has been no amendment as necessary under Section 16-2-45, *Utah Code Annotated 1953*, to change the character and purpose of the corporation. The plaintiff corporation has admitted in its complaint in this action (R. 1) that “said range land has been and is now held by the plaintiff for the use and benefit of the stockholders of plaintiff Corporation as range land upon which the said stockholders are authorized to place their livestock for grazing purposes in accordance with the provision of the Articles of Incorporation and By Laws of the plaintiff.” The complaint further alleges that “The By Laws so

adopted authorize the stockholders of the Corporation to use the Company range for the purposes of grazing their individually owned livestock thereon in accordance with their respective shares of stock in the Corporation, \* \* \* (R. 2).

The effect of the corporation's by-laws clearly was to ratify the current acts of the company in allowing its stockholders to use, rent free, the company's range land, to change the character of the corporation from a general business purpose and to simulate the object and nature of a cooperative non-profit association. No greater change in the object and purpose of this corporation could have been made than was attempted to be accomplished in completely abandoning its stated business purpose and becoming, without proper amendment to its articles, a mutual association.

The law of corporations is clear that the company's by-laws are only the rules governing its operations; that the by-laws must be consistent with and not contrary to the charter and the nature, purpose and objects of the corporation and that the corporation cannot, by adopting by-laws, change the character fixed upon it by its charter in any fundamental respect. *Fletcher Cyclopaedia Corporations*, Vol. 6, Sec. 2494, and Vol. 8, Section 4190.

This general rule is set forth at 13 *Am. Jur.* 286 as follows:

"As a general rule the bylaws of a corporation are valid if they are reasonable and calculated to carry into effect the objects of the corporation, and are not contradictory to the general policy of the laws of the land. On the other hand, it is equally well settled that bylaws must be reasonable and for a corporate purpose, and always within charter limits. They must always be strictly subordinate to the Constitution and the general law of the land, and may not infringe the policy of the state or be hostile to public welfare. It is a well-settled principle that all bylaws which are inconsistent with the charter of a corporation or with the governing law are void".

*Canyon Creek Irr. Dist. v. Martin* (Mont.), 159 P. 418, involved a situation where an irrigation company's articles of incorporation declared its purpose as being to supply water to the public, and where subsequently the corporation, by by-laws, attempted to limit the use of its waters to persons holding stock in the company, and to such stockholders only in proportion to the lands owned by each of them. The Montana court held that the essential nature of the corporation was set forth in its articles of incorporation and that by-laws of the company could not change that character, purpose and object from those of a general profit seeking corporation to a mutual company.

Section 16-2-14, *Utah Code Annotated 1953*, defines a corporation's powers and provides:

"(5) To make all such by-laws, rules and regulations, not inconsistent with law or with other corporate rights and vested privileges, as may be

necessary to carry into effect the object of the corporation; and such by-laws, rules and regulations may be made in a general meeting of the stockholders or by the board of directors."

It is our contention that the by-laws of the plaintiff corporation are entirely contrary to Section 10, Article 12 of the *Constitution of Utah*, in that they authorize and direct a change in the entire nature and purpose of the corporation from that provided in its articles of incorporation. The by-laws are entirely inconsistent with the stated purpose of the company as set forth in its articles and amendments thereto.

## POINT II.

THE SPECIFIC PROVISIONS OF THE BY-LAWS ARE ILLEGAL BY AUTHORIZING STOCKHOLDERS A FREE USE OF CORPORATION ASSETS.

By their stipulation (R. 28-29), filed at the time of hearing before the trial court, the parties raised the question of the legality of three particular sections of the by-laws. Two of these sections, namely: paragraphs 8 and 11 of Article V provided that areas of the range should be designated by the company for the feeding of cattle or horses and that this area should be determined upon the basis of the number of shares held by the stockholders desiring to place cattle or horses thereon, and that the stockholders so using the range should be responsible for keeping their cattle or horses within the designated areas.

It is our contention that these particular sections of the by-laws have the effect, by allowing the stockholders to use the range, rent free, in proportion to their shares held, of attempting to create a non-profit mutual corporation. Such a change of the character and purpose of the corporation may have been desirable as a practical matter to some stockholders, but we believe from an examination of the statutory law and the interpretations thereof, as set forth under our previous point, that any change in the nature, purpose and object of the corporation must, by legal necessity, have been accomplished by proper amendment to the articles of incorporation and not through the adoption of by-laws.

### POINT III.

#### THE BY-LAWS ARE ILLEGAL IN AUTHORIZING THE CORPORATION TO PURCHASE ITS OWN STOCK.

The issue as to the legality of paragraph 5, Section I of the by-laws was raised specifically by the stipulation of the parties (R. 28-29). The by-law provides a first refusal option in favor of the company or its other stockholders in the event any stockholder should desire to sell and should receive a bona fide offer for his stock, and it further restricts the sale of stock to persons outside of the corporation without "first offering to sell the same to the company or other stockholders" (R. 30-31).

Section 76-13-4, *Utah Code Annotated 1953*, subsection (2), provides that it shall be illegal for a corporation



“To divide, withdraw or in any manner, except as provided by law, pay to the stockholders, or any of them, any part of the capital of the corporation; \* \* \*”, and this section has been construed to prohibit the purchase by a corporation of its own stock. In *Pace v. Pace Bros. Co.*, 91 Utah 132, 59 P. 2d 1, Chief Justice Wolfe held that Section 76-13-4, *Utah Code Annotated 1953* (then 103-12-4, *Utah Code Annotated 1943*), specifically prohibited the purchase by a Utah corporation of its own capital stock. Similar statutes of other states were examined and our Court found that it is a very general rule that the Courts of the states having a statute similar to ours have interpreted such actions unequivocally to prohibit a corporation from buying its own stock. In *Morawetz on Private Corporations*, Section 112, the reasoning behind this rule is set forth. It is there stated:

“A purchase by a corporation of shares of its own stock in effect amounts to a withdrawal of the shareholder whose shares are purchased, from membership in the company, and a repayment of his proportionate share of the company’s assets. There is no substitution of membership under these circumstances, as in case of a purchase and transfer of shares to a third person, but the members of the company and the amount of its capital are actually diminished. \* \* \* every continuing shareholder is injured by the reduction of the fund contributed for the common venture; and the creditors who have trusted the company upon the security of the capital originally subscribed, or who are entitled to expect that amount of security are entitled to complain.”

Section 16-2-16, *Utah Code Annotated 1953*, was added by the 1951 Legislature. The section provides five specific instances wherein a corporation may purchase or redeem its capital stock. No provision is made in Section 16-2-16 for a general purchase by the corporation of its own stock which would change in any way the restriction of Section 76-13-4 or the strict interpretation placed upon that latter section by the *Pace* case.

The provision of the by-laws for a first refusal option in favor of the corporation to purchase its own stock necessarily assumes and thereby authorizes the corporation to make such a purchase of its own stock. It is our contention that this is another instance of an attempt by the corporation to enlarge the powers as given to the corporation by its charter through the adoption of by-laws. There should be no question but that the corporation cannot by its by-laws authorize an illegal act and that any attempt by the company through its by-laws to authorize the purchase by the company of its own stock is an illegal act in direct contravention of Section 76-13-4, subsection 2, and that the by-laws so authorizing are illegal and void.

*Fletcher Cyclopedia Corporations*, Vol. 8, Section 4205, states:

“Thus, a corporation will not be permitted to restrict the alienation of its stock, by a by-law, merely because it has the power under the statute or its charter to ‘regulate’ the transfer thereof,

the legislature being regarded as having intended no more than that the corporation might prescribe the formalities which as to it, itself, are to be observed in the making of transfers."

Paragraph 5, Article I of the by-laws is but a part of the whole whereby the entire character and purpose of the plaintiff corporation was intended to be changed to a non-profit mutual association. The first refusal option in favor of the corporation was but one phase of the plan of the directors to limit the activities of the corporation to a small group of stockholders who were mutually interested in using solely for their own benefit, and without realizing any pecuniary profit for the corporation as a unit, the range lands.

## CONCLUSION

The practical effect of the by-laws of plaintiff corporation is to entirely and radically change the purpose of the corporation by altering its character and object from that of a general business corporation organized for profit to that of a mutual, non-profit cooperative.

By-laws of the plaintiff corporation cannot effect any change in the purpose of the company, and any and all of the by-laws authorizing a mutual use of the company's assets and restricting such use to the company's stockholders are void and illegal. By-laws specifically restricting transfer of the company's stock except in ac-

cordance with a first refusal option in favor of the company itself are illegal in authorizing a purchase by the company of its own stock.

Strict compliance with the Constitution of Utah and statutes regarding corporate existance and franchise rights is mandatory, and the will of individual stockholders cannot prevail over the basic contract with the state.

The judgment of the District Court in adjudging the by-laws of plaintiff corporation valid and legal should be reversed.

Respectfully submitted,

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