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NO PAR VALUE STOCK

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In reviewing the history of legislation authorizing the issue of no par value stock New York stands out prominently as the pioneer in the movement. The passage of a no par value law was discussed at several of the Meetings of the New York Bar Association. As early as 1896 a committee made a report favoring such legislation and later in 1907 a committee of the same association drafted a bill which was passed by the legislature but was vetoed by Governor Hughes. This bill was opposed by Governor Hughes not because of the principle involved but on account of certain technical objections advanced by the State Comptroller in regard to the levying and collecting of stock transfer taxes and annual franchise assessments. He said that while it represented "an important departure with regard to the capitalization of a corporation, it had received the approval of public spirited students of corporate problems." Again a similar bill in 1910 with some modifications: namely, meeting the requirements of the State Comptroller, was introduced into the legislature but failed to pass due to one vote. The bill was finally passed April 15, 1912.

PRESENT STATUS OF THE LAW

The popularity of the law is evidenced by the large number of states that have authorized or approved of corporations issuing no par value stock, either as domestic corporations or foreign corporations. Since the passage of the New York Law some twenty-three states passed such legislation. The following states have passed legislation authorizing the issue of no par value stock: Alabama, California, Colorado, Delaware, Idaho, Illinois, Kansas, Maine, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New Hampshire, New Jersey, North Carolina, Ohio, Oklahoma, Pennsylvania, Rhode Island, Utah, Virginia, West Virginia, Wisconsin.

In states where no par value laws exist such laws apply to domestic and foreign corporations alike. However, in some states where no provision has been made for stock with no par value, foreign corporations are not allowed to do business; but if the trend of judicial opinion is indicative of a general attitude

of the states it would seem that nearly every state in the Union will soon allow foreign corporations, using this device, to transact business within their respective confines. Judicial approval has been given notably in two states, Kansas and Missouri. The Kansas case¹ arose out of a Delaware corporation which sought by mandamus to force the state charter board to admit it to do business within it confines. The court rendered a decision that upheld the corporation in its action permitting it to do business in the state of Kansas.

The Missouri case² is similar to that of Kansas. Again a Delaware corporation sought admission to engage in business in the state of Missouri and was refused. Immediately proceedings in mandamus were brought. The court handed down a decision allowing the corporation to transact business as a foreign corporation. The court found "nothing inherently fraudulent or *contra bonos mores* in that species of stock or in corporations organized with it." The major objection advanced by the state charter board in the case of Kansas and the secretary of state in the case of Missouri against no par value corporations doing business within such states was the difficulty involved in the computation of franchise taxes. In answer to the objection raised by the state charter board of Kansas, the court replied, "Any prudent charter board in determining whether a foreign corporation is worthy of admission to do business in Kansas, would attach little importance to the nominal value of its shares of stock, even if they have a nominal value. As in all other cases, the charter board should concern itself earnestly to ascertain the genuine capital—those assets permanently devoted to the corporate business as a fair basis for its business credit and upon which its hope of profits is rationally founded."

Both Kansas and Missouri courts held that the computation of taxes in the case of foreign corporations using no par value stock should be determined by the act relating to foreign corporations in Kansas and Missouri. In the cases of Illinois,³ Michigan,⁴ and Massachusetts,⁵ no par value shall be determined on the basis of \$100 par value for taxation purposes.

The unusual importance attached to this new device of corporate finance is due not only to the official sanction given it by the large number of states but also due to the increasing number of corporations that are making use of it.

Professor Albert S. Keister, made a survey⁶ in 1922 of the

capitalization changes during the period, 1916-21, covering 269 issues of stock by representative corporations. Of the 269 issues 136 were common and 133 preferred and of the 136 common sixty-two were issued on a no par value basis. This survey shows a distinct tendency toward the issue of no par value stock by small and large corporations alike. Some of the important corporations issuing such stock within recent years are: Kennecott Copper, Columbia Graphophone, Cuba Cane Sugar, General Motors Corporation, Radio Corporation of America, Sinclair Consolidated Oil Corporation, United Retail, Wilson & Company, Goodyear Tire and Rubber, International Cement. Vanadium Corporation, and more recently Consolidated Gas. There are also a few corporations such as Montgomery & Ward, Disco Milling, and Lucey Manufacturing that have ventured to issue preferred no par value stock.

ADVANTAGES

Professor Arthur Stone Dewing of Harvard succinctly states the advantages of no par value. "The essential character of capital stock that remains permanent whatsoever the fortunes of the actual capital is that which stands for a definite proportion of the corporate property and earnings. This involves no par value. The purpose of stock is therefore fully accomplished if the shares were merely proportionate parts of the total, in other words, shares without par value."

The use of no par value stock makes for truthfulness insofar as it does away with a dollar-stamped certificate. In the case of par value, there is a certain fixed monetary value attached to each share, usually \$100.

But, as we know from experience, this fixed value is very often fictitious and does not represent market or book values in money or property. Frequently, only a part of the capital stock is paid in at the organization of the corporation, so the par value is no par value, but a fictitious value based upon the assumption that, allowing for the part paid in, the remaining part will be paid in at some time in the future. This future time often proves to be indefinite. And even assuming that the total subscribed would be paid in at the time of organization (which is very seldom done) such capital will begin fluctuating. There may be appreciation or depreciation and therefore the dollar marked certificate no longer represents true and actual values. The cogency of the

whole argument rests on the well-founded and patent fact that the value of corporate securities is essentially based on corporate earnings.

Again from the point of view of investors the abolition of the dollar marked certificate invites investigation on the part of prospective purchasers of securities. It makes them look beyond the so-called par value and ascertain whether the value represented on the certificate is real or imaginary. It helps to do away with "bargain counter" investing where the seller can offer a \$100 par value security for a few dollars which is plainly worthless.

Stock without par value can be sold at any price determined by a board of directors making corporate financing highly adjustable. The corporation may sell its stock at different prices and eliminate the discomfiting feature of selling par value at a discount. The objection is often advanced that with the issue of no par value, accuracy of financial statement and accounts is sacrificed. The difficulty seems to be over-emphasized as such stock may be carried at book value, market price, original price, or at an arbitrarily fixed price. The famous Players-Lasky Corporation in 1921 carried its no par value stock at a market price for accounting purposes while General Motors carried its no par stock at a fixed price, ten shares of no par value issued in exchange for one share of old common at \$100 par.

MAJOR CHARACTERISTICS OF THE LAW

1. Issues of no par value may be authorized upon organization by charter provision or by an amendment of the existing charter.
2. Such issue is confined to so-called business corporations engaged in manufacturing, mining, merchantile, enterprises. Public utility corporations have not generally used no par value although there is no valid objection to their employment of such a device. Approval was made of the application of no par value to public utilities as early as 1910 by a commission appointed by President Taft, and such report was sent to Congress with his sanction. "All of these considerations seem to apply with equal force to the securities of Railroads under state incorporations and we believe that the laws of the several states could with advantage be modified so as to provide for the issuance of stock without par value." (*House Documents*, vol. 139, 62nd Congress, 2nd Session, 1911-12.)

3. Each share is equal to every other share. This being the common law it is re-affirmed by all statute laws.

4. The certificates of stock must indicate the number of shares to which each holder is entitled and further the number of shares authorized to be issued. In New York each shareholder must be informed as to the fractional part of the whole issue which he is entitled to such as one-hundredth or one-five-hundredth of the total.

5. Methods of price fixation varies with the number of statutes. The price may be fixed,

(a) by charter provision,

(b) by directors' action, or in some states by two-thirds of the stockholders.

6. Its use is no longer limited to common stock as there are now some fifteen states that provide for preferred no par value stock. The issue of no par value stock is by no means a cure-all for the manifold evils of over-capitalization, stock watering and other unethical corporate conduct. It is certainly a move in the right direction and will prepare the way for further legislation that should be helpful in placing corporate finance on a sounder basis and higher plane. Its one fundamental and pre-eminent characteristic is to show and prove to an investing public which is not always intelligent in its choice of securities that the real and only true basis of security values is earning power.

¹*North America Petroleum Co. vs. State Charter Board* (1919), 105 Kan., 161; 181 Pac. 625.

²*State ex rel. Standard Tank Car Co. vs. Sullivan* (1920), 282 Mo., 261; 221 S. W. 728.

³*Mich., Detroit Mortgage Corporation vs. Vaughn* (1920), 221 Mich., 320; 178 N. W. 697.

⁴*Illinois General Corporation Acts* (1919), Sec. 101.

⁵*Massachusetts Corporation Acts* (1918), Ch. 235.

⁶"Recent Tendencies in Corporation Finance," *Journal of Political Economy*, April, 1922.

⁷*Financial Policy of Corporations*, Vol. I, pp. 13-14.