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Treatment of No-par-value Stock

IN NEW YORK, NEW JERSEY, AND MASSACHUSETTS

By PERCIVAL F. BRUNDAGE

The subject of no-par-value stock has been prominent in the minds of accountants, bankers and lawyers during the last few years. The question is becoming increasingly important as more and more corporations are adopting this form of capital issue. Of the common-stock issues advertised or referred to in advertisements in the four numbers of the *Commercial and Financial Chronicle* published during January, 1926, over 85 per cent. were without par value. These issues covered the field of industrial corporations and public utilities.

The opinions of speakers and writers on this subject have differed widely. This difference is due partly to the fact that the statutory provisions of the different states authorizing the issue of no-par-value stock are so dissimilar. Any attempt to summarize them is difficult, and to draw conclusions that will apply equally to all the states is impossible. It seems, therefore, that something may be gained by restricting our attention for a short time to two or three of the states, and in this article the writer will attempt to summarize the statutory requirements of three eastern states, New York, New Jersey and Massachusetts. It may then be seen whether or not it is possible to formulate any definite rules of accounting procedure that will be applicable to no-par-value stock, at least under the laws of the states examined.

For this purpose it is unnecessary to discuss the reasons leading up to the enactment of provisions legalizing the issue of no-par-value shares, other than the desire for greater flexibility in the corporate capital structure which would permit the issue of capital stock at market value without the restrictions of a par value and would remove the necessity for meaningless balancing of figures with intangible values. No one can deny that greater

NEW YORK

Original issue................	A corporation may issue its authorized shares without par value (a) for such consideration as may be prescribed in certificate of incorporation (b) in the absence of fraud for such consideration as may be fixed by board of directors, or vote of majority of stockholders, but no shares shall be issued except for money, labor done or property received.
Stated value of shares	(See below)
Stated amount of capital......	Certificate of incorporation must include one of the following statements: "The capital of the corporation shall be at least equal to the sum of the aggregate par value of all issued shares having par value" plus (A) "\$....(\$1.00 or more) in respect to every issued share without par value", or (B) "the aggregate amount of consideration received by the corporation for the issuance of shares without par value"; plus (in both cases) such amounts as from time to time, by resolution of the board of directors, may be transferred thereto.
Increase or reduction in number of shares and change from par value shares to no par value...	Authorized in all three states upon proper
Restrictions on reduction......	No corporation shall reduce capital or capital stock if effect of such reduction or distribution of assets pursuant thereto will be to reduce actual value of assets below total amount of debts and liabilities plus reduced amount of capital or capital stock. (See also under dividends)
Purchase of treasury stock	There is no statutory authority for the acquisition by a corporation of shares of its own stock, but it has been held that a corporation may acquire its own shares provided it acts in good faith and without prejudice to the rights of the creditors (*City Bank of Columbus* v. *Bruce*, 17 N. Y. 507).
Dividends..................	No stock corporation shall declare or pay any dividend which shall impair its capital or capital stock, nor while its capital or capital stock is impaired, nor shall any corporation declare or pay any dividend or make any distribution of assets to any stockholder, whether upon a reduction of the number of its shares or of its capital or capital stock, unless the value of its assets remaining shall be at least equal to the aggregate amount of its debts and liabilities including capital or capital stock as the case may be.

ON NO-PAR-VALUE STOCK

New Jersey	Massachusetts
A corporation may issue its authorized shares without par value (a) for such consideration as may be prescribed in certificate of incorporation (b) as may be fixed by board of directors if so provided in certificate of incorporation or (c) by two-thirds vote of stockholders, but nothing but money shall be considered as payment for shares except property, real and personal, and amounts actually paid for labor performed at a fair bona-fide valuation.	A corporation may issue its authorized shares without par value for such cash, property, tangible or intangible services or expenses as may be determined from time to time by the board of directors, subject to the provisions of the agreement of association, articles of organization or amendments thereof.
No requirement	No requirement
No requirement	No requirement

action by stockholders and filing of amendment to certificate of incorporation.

New Jersey	Massachusetts
Certificate decreasing capital stock shall be published for three weeks successively, at least once in each week, in a newspaper published in the county in which the principal office of the corporation is located. (See also under dividends)	No reduction of capital stock shall be lawful which renders corporation bankrupt or insolvent but all shares may be surrendered and reduced number of shares issued if assets are not reduced thereby without creating any liability of the stockholders in case of subsequent bankruptcy of corporation.
Decrease of capital stock may be effected by retiring or reducing any class of the stock, ... or by the purchase at not above par of certain shares for retirement, or by retiring shares owned by the corporation. A company may purchase its own stock, and may even purchase on credit (*Berger* v. *United States Steel Corporation*, 63 N. J. Eq. 809).	No statutory provisions, in absence of which corporation which is solvent may purchase in good faith or hold or sell its own stock, and may receive it in pledge or in payment in the lawful exercise of its corporate powers (*Tappen* v. *Boston Chamber of Commerce*, 126 N. E. 464).
The directors of a corporation "shall not make dividends except from its surplus, or from the net profits arising from the business of such corporation", nor divide, withdraw, or in any way pay to the stockholders any part of the capital stock or reduce its capital stock except by law.	No dividend shall be declared when a corporation is or if it will thereby be rendered bankrupt or insolvent.

flexibility has been obtained; but other difficulties at least as great have resulted.*

During the development of the corporate form of organization many years ago, with the granting of limited liability to stockholders, the trust-fund doctrine arose as a protection for creditors. Although this doctrine is now rejected by many legal authorities,† the ideas underlying it have been sustained by the courts, and have the sanction of sound economic principles. Whether the capital contributed by shareholders is actually deemed to be held in trust for creditors or not, before corporate credit can be established there must be some security, real or apparent, represented by such capital contributions. This, for the sake of simplicity, will be called "capital fund".

With par-value stock it is comparatively easy to determine the amount of the capital fund. In most of the states par-value stock either can not legally be issued for less than its par value, or the stockholders are held to be liable (on part-paid stock) up to the par value of the shares held by them. No part of the amounts paid in as capital can be distributed as dividends to the stockholders; nor can the capital fund be reduced, except by the purchase of treasury stock, without taking proper legal steps which would act as advice to creditors of the contemplated reduction.

In the case of no-par-value stock the amount of the capital fund is of no less importance than in the case of par-value stock, but its determination is more difficult, particularly under the present state laws. Let us, therefore, review (see pages 242 and 243) the salient provisions of the statutes of the three states chosen for study with respect to no-par-value shares (summarized from *Corporation Manual*, 1925 edition).

Original Issue

The requirements as to consideration for the issue of no-par-value shares of capital stock are the same as for par-value shares. The statutes of the three states differ in phraseology but not in substance. New Jersey is apparently the most rigid, and Massachusetts the most liberal.

As to the amount of the consideration to be received there is a greater divergence. In New Jersey and Massachusetts there are at present no statutory requirements as to the unit value per share or the total value to be assigned to the no-par-value stock.

* J. C. Bonbright, "The Dangers of Shares without Par Value", *Columbia Law Review*, May, 1924.
† Cook, *Corporations*, 8th edition, 1923.

Under the laws of New York state a corporation must either affix a stated value to each share ($1.00 or more), or set up as the capital value the aggregate amount of consideration received therefor (1923 laws).

There is no requirement in any of the states that contemporaneous issues must be for equal consideration per share. This affords great latitude to the directors of a corporation if, as is often the case, the certificate of incorporation or articles of organization give them the power to determine the amount of consideration for the issue of no-par-value shares. In the absence of fraud their decision is final and it is necessary for the accountant, in verifying the original book figures, to go back only to the original papers and the board authorizations.

A few of the troublesome points that sometimes arise with the original issue of no-par stock are as follows:

1. Mixed issue of par-value and no-par-value shares for an aggregate consideration of cash, property and/or services.

    Par-value stock can not legally be issued in New York and Massachusetts for less than par, so the par-value stock is considered first and the capital value of the no-par stock is usually the excess of the consideration received over the amount of par-value stock issued. If there is no excess whatsoever, i. e. if one share of $100 par value and one share of no-par-value stock are sold together in blocks for $100 a block, the transaction would appear to be illegal in those states where par-value stock can not be issued at less than par, as either the par-value stock would be issued at a discount or the no-par stock would be issued for no consideration. This is sometimes covered by a previous transaction.

    The New Jersey statutes hold the stockholders liable to creditors up to the full par value of their share holdings so that the allocation as between par-value shares and no-par-value shares should be the same as in New York and Massachusetts.

    If a value is assigned to each share of no-par stock or to the total no-par stock (in New Jersey or Massachusetts) less than the excess of the consideration received over the amount of par-value stock, the difference may be carried to a reserve or capital surplus. Although this is apparently legal, it is doubtful whether it is in accordance with the best accounting practice, and it will be considered more fully hereafter.

2. Issue of several classes of no-par-value stock for an aggregate consideration of cash, property and/or services.

The separation should be indicated in the articles of organization or should be covered by a vote of the stockholders or board of directors. If one or more of the classes of no-par stock have preferences as to assets in case of liquidation or definite redemption values greater than the issue price, the further question arises as to whether the amounts of such preferences or redemption values should be reflected in the books and published accounts. This would not appear to be necessary for a going concern, although an opposite opinion is held by F. H. Hurdman in his article which appeared in THE JOURNAL OF ACCOUNTANCY, January, 1925. The questions of preferences and redemption values are only of contingent interest to an operating company. In the case of par-value stock it has never been considered necessary to take up these values in the books when differing from the par value except in case of immediate importance, such as after a vote calling for redemption of the stock in question. The points are certainly of interest to stockholders but they can be covered adequately in journal comments and balance-sheet notes.

3. Issue of no-par-value stock for intangible values.

One of the principal reasons for the creation of no-par stock has been the elimination of fictitious intangible values recorded in the books and approved by the directors in the case of par-value stock in order that the amount of the assets might be made to equal the amount of the liabilities and capital stock. It is, therefore, to be desired that the initial intangible values be sound and conservative. The trend of public opinion seems to be in this direction, and it is becoming more and more common to eliminate intangible values altogether or to carry them at a nominal value only.

4. Creation of initial reserve for dividends or capital surplus.

In dealing with this question it is necessary to consider the common-law rule and the statutory provisions of the states with respect to the payment of dividends.

The common-law rule is to the effect that dividends can be paid only out of profits, but the courts in several of the states have held that dividends can be paid as long as the capital is not impaired. A New York decision (*Equitable, etc.*

Society v. *Union Pacific Railroad*, 212 N. Y. 360, 1914) approved the payment of a dividend out of premium surplus. A similar decision is recorded in Massachusetts (*Smith* v. *Cotting*, 120 N. E. 177 Mass., 1918).*

Under the present New York statutes it would appear that if a fixed value per share is assigned to no-par stock under option (A) there is no legal obstacle to setting aside at once the balance of the consideration received as a reserve for dividends or as capital surplus, or to the subsequent payment of dividends therefrom so long as the assets exceed the liabilities plus the stated capital.†

It might also be argued that the rights of creditors are not infringed, as they are advised of the amount of capital set aside for their protection.

Under the Massachusetts law likewise there would appear to be no legal obstacle in the way of providing a reserve or capital surplus available for dividends over and above the established capital value per share or in toto.

The New Jersey statutes, however, provide that dividends shall not be declared except from "surplus, or from the net profits arising from the business. . . ." The word "surplus" is vague, and it is not clear that the courts would uphold the payment of dividends out of an initial reserve for dividends or capital surplus.

From a sound accounting standpoint it is difficult to see the justification of the initial reserve for dividends except in extraordinary circumstances. Whether or not so stated dividends paid therefrom are in effect payments out of initial capital—a return to stockholders of a portion of the capital originally contributed when the no-par-value stock was issued—without the justification of a distribution from capital which may exist in the case of a mine or other wasting asset.

Where the question arises, however, in the case of a consolidation of two or more corporations, one or both of which have accumulated a substantial earned surplus, there would appear to be no sound objection, if the law offers none, to the withholding from the capital fund of the new

* There is a contrary decision under the California statutes, *Merchants', etc. Co.* v. *Youtz*, 178 Pac. 540 (Cal., 1918).

† This was not the case prior to the 1923 amendment of the New York stock corporation law which previously forbade the payment of dividends except from "the surplus profits arising from the business." The penalty attaching to payments other than from surplus profits (penal law sec. 664) was not removed (C. W. Wickersham, "The Progress of the Law on No Par Value Stock," *Harvard Law Review*, February, 1924)

corporation of a reasonable amount as a reserve for dividends or contingencies. To the new corporate entity, it is true, the amount of the total assets acquired over and above the amount of the liabilities assumed would constitute the theoretical capital fund, and in the case of the issue of par-value stock therefore would necessarily establish the amount of the capital fund. The justification for a different segregation would be the continuing of business operations and the equities of the situation. If, as said before, the predecessor companies had accumulated substantial earned surpluses, and if by the consolidation the capital fund of the new corporation is increased over and above the amounts of the combined capital funds of the predecessor companies, no injustice is done to either creditors or stockholders. In such circumstances the directors would be exercising only reasonable business foresight in establishing a contingency reserve as provision against a possible business depression and a consequent impairment of the capital fund. Furthermore, there are several other ways by which the same result could be obtained, such as by the intervention of a holding company or the original issue of par-value shares.

In cases where the capital fund is separated, however, it is important that the separation be clearly indicated in the organization papers or that definite action be taken in this regard by the board of directors and stockholders before the accountant can lend his sanction thereto.

An initial capital surplus does not appear to the writer to be logical in a balance-sheet in which the capital-stock issues are of no par value. With par-value stock this is the only way to show a paid-in surplus. But one of the advantages of no-par stock is that it does not have a par-value label to disguise the fact that a stock certificate represents a share of ownership in a business. The simplest method of statement in the opening balance-sheet is, therefore, to be desired, i. e., to give under the heading of capital stock as nearly as possible its value at the date of the inception of the company. This is modified to the extent that surplus reserves have been provided.

Furthermore, it seems important to separate the earned surplus of a corporation whether the capital stock has a par value or not. If, therefore, there is a capital surplus in addition to earned surplus and surplus reserves, the stockholders' equity is not simply stated in the balance-sheet. The capital-stock account, it would seem, should represent the original capital contributions by the shareholders or, if issued upon the acquisition of a going concern, the excess of the assets over the liabilities and reserves, plus such amounts as are subsequently transferred to capital account out of accumulated profits as representing amounts permanently invested in the business.

It is recognized that this is not a generally accepted rule and that it is not required by the statutes of the states examined. Indeed statements frequently appear with no-par-value stock and an initial capital surplus. Taking one example, that of the recent issue of preferred and common stocks of no par value by Dodge Brothers, Inc., the balance-sheet of that company "giving effect to the acquisition of assets and proposed issue of securities" contains the following:

Capital stock and surplus:	
Preference stock, no par value,	
\$7.00 per annum cumulative:	
Issued 850,000 shares	\$850,000.00
Common stock, class A—no par value:	
Issued 1,500,000 shares	150,000.00
Additional 1,035,000 shares authorized for conversion of 6% sinking fund gold debentures.	
Common stock, class B—no par value:	
Issued 500,000 shares	50,000.00
Capital surplus	4,608,681.78

The preference stock is shown at a value of one dollar a share, the common stocks at ten cents a share and there is a capital surplus of over four million dollars. The assets as shown in the same balance-sheet include fixed property at appraised values and goodwill at the nominal value of one dollar. There are also reserves for contingencies of \$4,575,796.35. The statement is much the same as would appear if the preferred and common stocks had a par value of one dollar and ten cents respectively.

The company in question is not incorporated under the laws of any of the states now under consideration but it provides an illustration of the difference of opinion that exists on the subject, and of the fact that no definite and inflexible rule can be laid down, at least in the present stage of development of accounting procedure with respect to no-par-value stock.

Increase or Reduction in No-par Stock

An increase or reduction in the number of shares of no-par stock and a change from par-value to no-par-value shares are authorized by the statutes of the three states under consideration if proper action is taken by the stockholders and due notice is filed with the state authorities.

The conditions with respect to the issue of additional shares of no-par stock are the same as for the original issue. The value to be assigned to the new stock is established by the amount of cash and other consideration received (unless otherwise determined by the directors) regardless of the value at which the original stock was issued. In the case of the acquisition by a going concern of the capital stock or assets of another corporation, or other corporations, the net value of the property acquired would fix the value of the no-par stock issued therefor.

If a reduction is made in the number of shares of no-par capital stock outstanding, as for example, by surrender without redemption, there is no essential change in the capital structure; but if a reduction is made in the capital value, the rights of creditors are affected. It is, therefore, most important that proper action be taken in advance by stockholders and notice be given to all interested parties.

There is also a restriction in the statutes of each of the three states that no distribution of assets shall be made if by such distribution the amount of the assets is reduced below the total amount of the liabilities and the reduced amount of capital stock.

If a corporation has suffered losses, and a deficit appears upon the books, the deficit can be eliminated only by proper legal action definitely reducing the capital value of the no-par stock. It is improper, therefore, to deduct the deficit from the capital value in the published statements unless the facts are clearly presented therein.

It is also a generally recognized rule in this country (although contrary to the precedents established by decisions in the British courts) that a deficit, whether resulting from operations or capital losses, must be made good before dividends can be paid unless the capital has been previously reduced by proper legal steps.*

Treasury Stock

The purchase of treasury stock by a corporation is only another form of a reduction of capital even if it be acquired only as a temporary investment. There is no statutory authority for the acquisition of treasury stock in the states under consideration, but, in the absence of restrictions in the charter, the purchase of treasury stock has been approved by many court decisions as long as the creditors do not suffer. It also appears to be unnecessary to comply with the legal formalities required for a formal reduction in the capital stock.

In England a long line of decisions has established the rule that, at common law, a corporation can not purchase shares of its own capital stock (*Trevor* v. *Whitworth*, L. R. 12 App. Cas. 409, H. L. 1887).

The object of the rule is to preserve the rights of the corporate creditors, and also to confine the corporation within the express powers given it, and the implied powers necessary to its transaction of business.†

"In the United States the courts of some of the states have followed the English rule, but the clear weight of authority upholds the right of a corporation to buy its own stock if the purchase is made in good faith and does not prejudice the rights of creditors." (*Re Rechheimer-Fishel Co.*, 212 Fed. 357, 1914.)‡

When treasury stock is purchased for immediate resale, as, for example, to employees, it may perhaps be carried temporarily as an asset and valued at the cost of purchase. Otherwise, it should be deducted from the liability side of the balance-sheet.

A considerable difference of opinion exists as to the proper method of recording the purchase and resale of no-par treasury stock. The point seems of sufficient importance to warrant a careful study. In reaching a decision it is helpful to consider the different methods of treatment that might be adopted.

* C. F. Schlatter, *Payment of Dividends Before Restoring Impaired Capital*, The Journal of Accountancy, March, 1923.

† Cook, *Corporations*, volume 2, paragraph 309.

‡ Cook, *Corporations*, volume 2, paragraph 311.
So far as dissenting minority stockholders are concerned "a corporation, in the absence of constitutional or statutory provision has in general an inherent right, for a bona-fide purpose, to retire by purchase its capital stock," and may issue its mortgage bonds in exchange for its own capital stock so purchased (*Allen* v. *Francisco, etc. Co.*, 193 Fed. 825, 831, 1912).

1. The whole cost of the purchase might be charged to surplus in order to keep the capital fund intact, until official permission is received from the state to reduce it.
2. The original capital amount contributed on the shares in question might be charged to capital account and the difference charged or credited to surplus as the case may be.
3. In the case of the issue of a number of blocks of stock at different prices, the average issue price might be charged to capital account and the difference absorbed in surplus.

Although the second and third alternatives have had their proponents,* the first method appears to the writer to be correct for the reason that the purchase of treasury stock is a reduction of the outstanding capital stock without the official sanction of the state or the approval of the creditors. There have been a number of court decisions to the effect that the purchase of treasury stock by a corporation is invalid and will be set aside if the corporation is insolvent or if the creditors are injured thereby.

"A corporation having no surplus profits can not purchase shares of its own stock," was stated as a principle in *Hale* v. *Henderson* (126 Ala. 449, 1900). In *Fraser* v. *Ritchie* (18 Ill. App. 554, 1881) it was held that the right of the corporation to purchase its own stock is subject to certain restrictions, one of which is that it shall not be done at such time and in such manner as to take away the security upon which the creditors of the corporation have the right to rely for the payment of their claims, or, in other words, so as not to diminish the fund created for their benefit.†

It is quite evident from these rulings that the purchase of treasury stock is recognized to be a return of capital to the stockholders surrendering their shares and that the rights of creditors must be protected. It follows that the capital or trust fund should not be reduced and that the purchase should not be made unless the surplus is sufficient to absorb the whole cost thereof.

* C. B. Couchman, *Principles Governing the Amounts Available for Distribution of Dividends*, THE JOURNAL OF ACCOUNTANCY, August, 1924.

† Cook, *Corporations*, volume 2, paragraph 311.
Other quotations are as follows: "A purchase by a corporation of its own stock is not good as against existing corporation creditors (*Hall & Farley* v. *Alabama, etc. Co.* 173 Ala. 398, 1911). If a corporation, by a purchase of shares of its own capital stock, thereby reduces its actual assets below its capital stock and debts, or if the actual assets at that time are less than the capital stock and debts, such purchase may be set aside (*Buck* v. *Ross*, 68 Conn. 29, 1896).

If it be granted that the first of the suggested methods of treatment is correct, the question may arise as to why it has not been followed in the case of par-value stock. This may be due partly to the difficulty of correctly stating the capital account if the cost of par-value stock is charged to surplus and partly, perhaps, to a failure to appreciate the actual effect of the transaction. The desire to reverse the original entry has also been important. When the stock is first issued, cash is charged and capital stock credited. When the stock is re-acquired, the obvious entry is to credit cash and charge capital stock. It has been overlooked that this does not necessarily follow until the retirement of the stock.

In the case of no-par-value stock the difficulty of clearly stating the capital account is removed. The capital account is established by the amount of the original contributions and will remain unchanged by the purchase of treasury stock until a formal reduction is approved by the state authorities. The amount of the treasury stock should, of course, be kept in a separate ledger account, but the total ledger balance should be deducted from surplus for statement purposes, until the resale of the stock or its formal cancellation. The reduced number of shares outstanding should also be indicated.

If the treasury stock is resold, the amount received will be credited to the ledger account for the treasury stock, and the balance will be transferred to surplus on the statement. The capital account will remain the same and the net result will be a charge or credit to surplus by the amount that the assets of the company have been reduced or increased by the two transactions. If the treasury stock is distributed as additional compensation to officers or employees, the ledger account will be credited and surplus charged, but the surplus on the company's statement will not be affected.

If the treasury stock is formally retired and cancelled, a reduction of the capital-stock account is, of course, entirely proper. The amount of the reduction will depend upon the vote of the directors or stockholders and statements filed with the state authorities, but it normally would be based either on the original issue price or average issue price of capital stock of the same class as that retired.

When no-par stock is donated to a corporation, no entry would appear to be necessary other than a reduction in the number of shares outstanding. As such stock is resold the total proceeds of the sale can be credited to surplus. The question as to whether or not such surplus and surplus arising from the purchase and sale of the company's own shares is available for dividends is another matter. Under the present laws of New York and Massachusetts they would seem to be so available, but the wiser course would be to segregate such items and to refer the question to a competent lawyer.

The treasury department in its regulations promulgated under the revenue acts of 1918, 1921 and 1924, has taken the position that "a corporation realizes no gain or loss from the purchase of its own stock". (Art. 542. Reg. 45). This rule is laid down, however, for the purpose of the determination of taxable income and it does not follow that the same applies in ordinary accounting.

Where a corporation with par-value capital stock changes its stock to no-par-value shares, the amount of the capital account would ordinarily remain unchanged.

Stock Dividends

Stock dividends paid in no-par-value shares merely increase the total number of shares outstanding without necessarily increasing the amount of the capital fund. An amount may or may not be transferred from surplus to capital account as determined by the board of directors.

If no amount is transferred to capital account, the question might be raised as to what is the consideration for the issue of the additional shares. The consideration for the issue of the original shares would appear to be the consideration for the issue of the dividend shares. The increase in the number of shares results merely in a dilution of the value per share. It is quite similar to a reduction of par value in the case of par-value shares as, for example, a reduction from $100 to $50 per share, and an exchange of two shares for one.

If any other theory should be adopted, we are met by the problem of determining the capital value of the new shares. Take for example, a company with a capital stock of $550,000 made up of 30,000 shares of no par value issued in blocks of 10,000 shares each at $10.00, $20.00, and $25.00 a share, respectively. Assume that there is an earned surplus of $170,000, making the book value of the outstanding stock $24.00 a share. Assume further that, owing to the demonstrated earning power of the business, the market value is $30.00 a share. Additional 10,000 shares are authorized by the stockholders and a stock dividend of that number of shares is declared. The directors vote to transfer an amount of $100,000 from surplus to capital-stock account. Proper authorization for the stock dividend has been obtained and the necessary papers have been filed with the state authorities.

It is quite evident that the surplus in this case is inadequate to permit the transfer to capital account of an amount equal to the average consideration received for the 30,000 shares outstanding, the average book value of the shares, the consideration received for the last block of shares issued, or the market value per share. Yet the writer believes that the action of the directors is both legal and proper and that if it had been voted to transfer from surplus to capital account an amount of only $50,000, or no amount whatever, the procedure would have been equally correct.

In cases where a stated value has been assigned to each no-par share a modification of the above rule is required. The stated value is a label that closely resembles a par value, and the amount of the capital account after the stock dividend must at least equal the aggregate stated values of all the then outstanding shares.

Conclusion

From this discussion of these questions certain conclusions may be reached: First, the statutes of the three states examined do not afford adequate protection to creditors of corporations with capital stock of no-par-value shares. Under the present laws of New York and Massachusetts, the greater part of the capital contributions by share-holders in all probability may be set aside as reserves or surplus and subsequently distributed as dividends. Indeed the writer has been informed by good authority that under the Massachusetts law it is possible that even the original amount set up as the capital value of the no-par shares may be subsequently transferred to surplus and distributed in full as dividends. It is also possible that dividends on both no-par and par-value shares may legally be declared in some states out of surplus created by unrealized appreciation of physical properties. The dangers of this situation are very real.

Second, the statutes of the different states differ widely in their provisions with respect to no-par-value shares, which makes it difficult, if not impossible, to approach the subject from a common angle.

Third, the opinions of individual accountants, lawyers and bankers are far apart on the subject. The actual treatment adopted in many cases is largely influenced by the technicalities of the law and the results desired.

The remedy for this situation would seem to be, first, to obtain more definiteness in the statutes, particularly as to safeguards for the creditors of a corporation. This, it seems to the writer, should include the enactment of a provision that the capital value of no-par shares issued for property should be the fair value of that property; and if issued for a mixed aggregate of different kinds of property, the value of the assets in excess of the liabilities, if any, and such reserves as are set aside by vote of the incorporators, stockholders or directors. There should also be a provision that no dividends can be paid out of the capital fund thus determined or out of any profits or surplus not actually realized. Second, we should work for more uniformity between the laws of the different states so that the enactment of restrictive provisions in one state will not result in the flight of its corporations to other states. Uniformity between the essential provisions of the different state laws is also necessary before agreement upon any uniform accounting procedure. Third, we should discuss the problems involved more frequently with other accountants and with lawyers and bankers in order that divergent opinion may be reconciled, and that public opinion may be educated on this subject. This is the first step to be taken. Improvement in the statutes will follow in time. Our legislators have a wholesome respect for public opinion—once it is aroused.

For the education of the public on this subject the accountant is particularly well fitted, and he should feel a very real and personal responsibility. Our professional societies are already working on the problem, and it is probably through their committees, and by their influence, that the most effective work can be done. The prize competition for the submission of essays on the subject of no-par-value stock and the general principles governing the determination of capital and amounts available for distribution of dividends has been helpful. But much remains to be done towards reaching an agreement on what is the best and soundest accounting procedure, and to obtain for that procedure public recognition.