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Non-Par Stock in Texas

F. Morris Mason

NON-PAR STOCK IN TEXAS

ORIGINALLY stock corporations were required to divide capital shares having a par value stated in the corporate charter or amendments. Theoretically this was a representation that par value for each share of outstanding stock had been received into the capital account, which in turn was to act as a "cushion for creditors,"[1] *i.e.*, as the fixed amount of the legally limited liability of the corporation. Then in 1912 New York passed a statute authorizing the issue of shares having no nominal or par value[2] which became a pattern for legislation in the other states, precipitating bitter controversy over its benefits and detriments.[3]

The objective of no-par legislation was to provide a means of ready finance when the market value of par stock was less than par, since sale at less than par by the corporation was prohibited.[4]

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[1] "Capital stock of a corporation is a fund set apart in case of necessity for payment of debts and creditors have a right to look to it for payment of their claims." Cunningham v. Com'r of Banks, 249 Mass. 401, 144 N. E. 447 (1924).

[2] N. Y. Laws 1912, c. 351.

[3] See, *e.g.*, the controversy in (1921) 7 A. B. A. J. At p. 534 appears an article attacking the idea of such stock by William W. Cook of New York City, and at p. 579 is a reply to Cook's article by two members of the Chicago Bar, Hollen and Tuthill. At p. 671 is a discussion of both preceding articles by Henry Colton, a member of the Nashville Bar.

Apparently the controversy arises because there are three separate interestes involved: (1) the creditor of the corporation wants security; (2) the shareholder is primarily interested in the real value of his shares; and (3) the corporate entity is seeking efficient and convenient avenues of finance. It is almost impossible to expect incorporation laws fully to protect both investors and creditors and at the same time allow business enterprise complete freedom of finance. As a matter of fact, however, the state Blue Sky Laws and the Federal Securities Act have afforded practical protection to both creditors and stockholders in most cases and the biggest gap has been in the question of adequacy of consideration for non par shares issued in exchange for property. 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) § 5259. See Masterson, *Consideration for Non Par Shares* (1939) 17 TEX. L. REV. 247.

Donald Kehl of the New York Bar, in CORPORATE DIVIDENDS (1941) § 9.1, says, "The past quarter of a century has seen a change" in the dominant note of creditor protection of the nineteenth century. "The wildcat mining corporation had largely passed from existence before the adoption of the Securities Act. By and large the twentieth century corporation was not viewed as constantly in danger of dissolution; economic responsibility was more certain."

[4] "In view of the fact that it has not been definitely established in this state that a corporation, finding its capital depleted by losses, may issue par stock at its market value to secure assets and to prevent bankruptcy, it would seem that the safe and sane method

Formerly corporate bonds represented the common devices for this purpose, but they had proved unsatisfactory because they weakened the corporate credit as direct obligations, carried too high a rate of interest and made imminent the danger of foreclosure of the corporate assets in case of any default. One other alternative was the issuance of preferred stock, and in the majority of cases preferences were already great.[5] This situation became a stimulus to the watering of stock by reputable companies.[6]

With the advent of no-par stock, however, problems as to capital arose as apprehension was felt over this destruction of the creditors' protection resulting from the combination of non-par stock and the concept of limited liability. What part of such stock sales was capital stock, and what part surplus?[7] How was it to be carried on the books?[8] How was it to be taxed?[9]

... would be legally to reduce the capital stock to the actual value of the company's assets.... The corporation can then authorize an additional issue of stock ... after the water has been squeezed out of its nominal capital stock." 2 HILDEBRAND, TEXAS CORPORATIONS (1942) 108. But see note 38 *infra*.

The Texas statutes have never had a provision specifically requiring par stock to be sold at its par value. The present tendency is to get away from such provisions. CAL. CIV. CODE (Deering, 1941) § 299 authorizes sale of par shares at less than par "if the board of directors determine that such shares cannot be sold at par" and Sec. 300a provides that "In the absence of fraud in the making of such determination of value, such determination shall be conclusive."

[5] See Bonbright, *Shares Without Par Value* (1924) 24 COL. L. REV. 449, 457, n. 9: "The handicap under which a company may labor when its stock is selling below par is well brought out by the recent action of the American Telephone and Telegraph Company in raising its dividend rate from 8 per cent to 9 per cent ... in order to maintain the value of the stock well above par so as to make possible further financing by stock issues."

[6] See Hurdman, *No Par Stock and Asset Valuation* (1929) 47 J. OF ACCOUNTANCY 81, 83: "It is held by some that overvaluation of assets still exists and that it is caused by a desire to show large capitalization. This is unquestionably true, but I feel sure that in cases where it does exist in companies with no par value stock it is due to a definite intention to mislead the public, whereas in the case of par value it arose in addition from the practical necessity of evasion caused by law."

Cook argued that no-par merely legalizes stock watering and says: "(1) The exemption of stockholders from personal liability on corporate debts should be withdrawn. This for creditors. (2) A public registry should be required of all contracts ... for the purchasers of the stock." Cook, *Stock Without Par Value* (1921) 7 A. B. A. J. 534, 537.

[7] The question of what is the capital stock obscures the more important question of what is the nature of the surplus. "Whether profits exist is in no way dependent on capitalization regardless of whether" the shares are par value or no-par shares. Weiner, *Amount Available for Dividends Where No-Par Shares Have Been Issued* (1929) 29 COL. L. REV. 906.

[8] "In most jurisdictions no-par stock will be represented on the balance sheet by a

Confusion resulted from stop-gap types of legislation not accompanied by a revision of existing statutes, which not only proved ineffective in many instances but added problems of construing apparent inconsistencies between the state constitution and incorporation laws.

Out of this situation rose a further anomaly—stated value non-par stock.[10] Real no-par stock has no ascertainable value save by reference to the corporate books. Each share actually represents an aliquot part of the corporate assets,[11] and the statutes require only that the number of such shares authorized shall be stated in the incorporation papers. On the other hand any statement in the incorporation papers fixing value per share such as a statement

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capital entry of some amount. Some portion of the consideration ... must under many statutes, be allocated to stated capital. This item of stated capital occupies the same position on the balance sheet ... as the entry for capital where the corporation's stock has a par value." But see note 34 *infra*.

"Stock without par value complicates the declaration of dividends in balance sheet surplus jurisdictions because of the new item of paid-in surplus.... Where ... the test is a plain and simple excess of assets over liabilities including capital, paid-in surplus falls within the excess and is available. In other jurisdictions ... permitting dividends from a balance sheet surplus, the premium paid on par stock has been considered available for dividends and presumably the same result would follow as to paid-in surplus on no-par stock. Many states in the adoption of recent statutes have, however, limited the use of paid-in surplus for dividends." KEHL, CORPORATE DIVIDENDS (1941) § 24. The problem involves the availability of types of unearned surplus.

TEX. REV. CIV. STAT. (Vernon, 1925) art. 1329 says, "profits from the business." and TEX. PEN. CODE (Vernon, 1925) art. 1083a says "actual earnings." Whether a premium on par stock comes within those definitions has never been litigated. 2 HILDEBRAND, TEXAS CORPORATIONS (1942) §§ 473, 475.

[9] Franchise tax and filing fee are much the same as in the case of par stock capitalization. Though article 1538-f provides that a corporation authorizing issuance of no-par shares shall pay "The fees now or hereafter provided by the laws of this state as to any shares of its stock having a par or face value; *and*" also the fees set out for no-par shares, where companies have both par and no-par stock. The filing fee for the no-par shares is computed on the basis of the actual consideration received for them, and the franchise tax of a no-par company is based on its gross assets. (1926-1928) REPORT AND OPINIONS OF THE ATTORNEY GENERAL OF TEXAS 101.

[10] KEHL, CORPORATE DIVIDENDS (1941) § 45.1 avoids the ambiguity of the phrase "stated value non par" and states that "When any portion of the consideration is treated as capital, what is created is not true stock without par value, but rather par value stock of lower denomination."

See Berle, *Problems of Non Par Stock* (1925) 25 COL. L. REV. 43, 44: "The name may be a contradiction in terms but so is the idea."

[11] "For example 'not more than one hundred shares of stock having a par of one hundred dollars can be issued for ten thousand dollars' worth of consideration. But for the same amount of consideration any number of no-par shares may be issued." 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) § 5260.

that a certain number of no-par shares is represented by a definite sum is said to make the shares *stated value non-par* shares. The present New York statute embraces both the true and the stated value no-par alternatively,[12] and one or the other has been copied in substance by practically all the states. Alternative A puts a minimum stated value of one dollar a share on the non-par while B,[13] representing the true non-par, requires all the consideration *received* for those shares to be carried as capital.

Much of the no-par mist is dissipated by understanding at the outset that the applicable rules of law are much the same as those applied to par value stock and that accounting entries do not alter the fundamental legal principles. The basic idea of a capital stock held in reserve was accomplished by division into "capital account" and "surplus" and the entry of capital stock on the liability side of the ledger under "capital account." The elimination of capital stock or legal capital through the device of no-par stock does not remove the necessity of carrying some item of liability in its stead. Nor would an accounting entry as "paid-in surplus" or "earned surplus" or "capital surplus" or under any other name be more effective to change the legal aspects of the fund in the case of non-par stock than in the case of par. Though a no-par stock corporation is said to be one without capital stock (legal capital) as such, it does have capital and good accounting practice guards against misapplication of the value of the capital assets as originally entered on the books.[14]

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[12] N. Y. CONS. LAWS (Cahill, 1930) c. 60, § 12 requires statement of the total number of authorized shares, the par value of the par shares, the number of the shares without par value and either:

"(A) The capital ... shall be at least equal to the sum of the aggregate par value ... plus.....dollars (the blank space to be filled in with some number representing one dollar or more) in respect to every issued share without par value, plus such amount as ... may be transferred thereto," or

"(B) The capital of the corporation shall be at least equal to the sum of the aggregate par ... plus such amounts as from time to time, by resolution of the board of directors, may be transferred thereto."

[13] Alternative B of the New York Statute has been adopted in substance by the UNIFORM BUSINESS CORPORATION ACT § 17.

[14] "The theory of stated capital ... seems to be that a statement of amount as capital affords reliance to creditors and other persons dealing with a corporation that such

"A party who buys no-par shares in a corporate enterprise, giving $100,000 in exchange therefor, has contributed $100,000 of capital. Whether he receives 10,000 or 20,000 shares is immaterial.... But if as a matter of fact, he receives 10,000 shares, by no stretch of the imagination, or interpretation of the law, can he be considered to have contributed $50,000 to the capital and $50,000 to the surplus of the enterprise. The plain fact is that the amount of capital contributed is equal to the value placed on that which was contributed.... If this first principle is accepted, much of the confusion incident to shares without par value will be avoided."[15]

The Texas Securities Act could prevent sale of the same issue of no-par at a lesser figure if the difference were material, and doubtless equity would enjoin such sale at the instance of a prior shareholder. It might also be considered a "fictitious increase" within the prohibition of Article XII, § 6 of the Texas Constitution.[16] Any serious impairment of the capital of such a company would also impair the value of outstanding shares and probably give the stockholder a remedy in equity. As stated by the Delaware court of Chancery in *Bodell v. General Gas & Electric Corp.*,[17]

"While an arbitrary sale of the same issue of stock at different prices to different persons would not be sanctioned, such differential sales will be sustained if based on business and commercial facts which, in the exercise of fair business judgment, lead directors to follow such a course.

"It may be impossible to lay down a general rule on this subject but we think the discretion of a board of directors in the sale of its no par value stock should not be interfered with, except for fraud, actual or constructive, such as improper motive or personal gain or arbitrary

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amount will be maintained in the business. By the same token it would appear consistent to expect that a corporation having stock with par value would maintain its capital stock intact. Yet everyone... knows that a corporation may have an impairment of capital resulting from a series of operating deficits and go on exhausting its capital. It is prevented by statute of most states from declaring dividends while in such condition, but nothing happens beyond possible damage to its credit.... Capital once set up, whether in accordance with the consideration received or on an arbitrary basis per share, should be made to reflect any encroachment through losses by the deduction on the balance sheet of the operating deficit from the capital." WILDMAN AND POWELL, CAPITAL STOCK WITHOUT PAR VALUE (1928) 144.

[15] *Id.* at 62.

[16] TEX. CONST. (1876) Art. XII, § 6.

[17] 15 Del. Ch. 420, 140 Atl. 264 (1927).

> action or conscious disregard of the interests of the corporation and the rights of its stockholders."

Reduced to practical truth this means only that non-par shares have some slight flexibility in the determination of consideration whereas the par shares have none. Time and the absence of case law are evidence that the creditor is at no serious disadvantage in having to rely on the assets of such corporations for his claim in the event of liquidation.

Stated value and stated capital requirements were designed as checks on the unrestricted use of no-par,[18] but such value may be required for some particular purpose only. Some states require a minimum capital with which business is to be begun;[19] some require a minimum sales price for non-par shares by the corporation. Also, where stated value is required, it may be for purposes of taxation, or as a minimum with which business is to be begun or as a minimum sales price for the shares or for some combination of purposes. The purpose and requirements of the particular statute authorizing no-par stock should be carefully noted.[20]

Non-par stock is authorized in Texas by articles 1538a-1538m. Provision may be made for issuance of such shares by one of two

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[18] Though "stated value" and "stated capital requirements are often criticized as being unsound and misleading. See note 14 *supra*. For a theoretical discussion of these fallacies see WILDMAN AND POWELL, CAPITAL STOCK WITHOUT PAR VALUE (1928) c. XI.

[19] Arkansas requires the amount of capital with which the corporation will begin business to be stated in the charter as not less than $300. ARK. STAT. (Pope, 1937) c. 37, § 2129(9). The New Mex. statute is similar but the minimum figure is $2000. N. MEX. STAT. ANN. (1941) c. 54, 1101. The Kansas statute requires statement of the amount of capital with which the corporation will begin business and that no indebtedness shall be incurred until that amount is fully paid in. KAN. GEN. STAT. (Corrick, 1935) Corp. Code § 17-3209.

TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538-d, sub-sec. d., requires the stockholders "in good faith, to subscribe and pay for at least ten per cent" of the authorized no-par "before said corporation shall be chartered or have its charter amended so as to authorize the issuance" of such shares and "provided further that in no event the amount so paid shall be less than $25,000.

[20] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538-g says "The certificate required by this Act to be filed setting forth the value received by a corporation for the shares of its stock without nominal or par value which it may issue shall not be construed as fixing any value upon such shares, but said certificate shall be for the sole and only purpose of furnishing the Secretary of State a basis upon which to compute the filing fees and franchise tax ..." In other words, the statute requires value statement only for the purposes of taxation and as a minmum with which business is to be begun, *i.e.*, $25,00.

methods: (1) on organization, or (2) by amendment of the charter of any corporation for profit, other than banking or insurance corporations.

The no-par shares may be issued and disposed of for the consideration prescribed in the original charter or any amendment thereof; or if no consideration is so prescribed, then for such consideration as may be fixed by the stockholders at a meeting called and held for that purpose, or by the board of directors acting under authority granted either by the stockholders or by the original charter or an amendment thereto.[21]

The Texas Constitution requires that the consideration must be either "money paid, labor done or property actually received."[22] This provision prevents use of non-par shares as bonus stock. Some consideration must be paid, and the Constitution goes further to declare that all "fictitious increase of stock or indebtedness shall be void."[23] Any attempt to use no-par shares as stock dividends would have to hurdle a further obstacle that dividends be paid only from "net profits."[24]

Where consideration for shares is involved in the law of corporations, it is particularly true that "equity cuts across all transactions;" and the "fair value" test plus the constitutional limitation that stock be issued only for money paid, labor done or property received tend to make inappropriate the criticism that one "may even receive ten thousand shares of stock for a yellow dog and a dead cat without being subject to further assessment." More-

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[21] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538-c.

[22] TEX. CONST. (1876) Art. XII, § 6.

[23] *Ibid.*

[24] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1329, with reference to directors, provides: "They shall... declare and make such dividends of the profits from the business of the corporation as they shall deem expedient, or as the by-laws may prescribe." Only in Texas are dividends limited merely to profits, but there are other restrictions. See note 8 *supra.*

"Both in states which have a special clause for dividends on no-par stock and in states which have no statute or one applicable equally to par and no-par shares, the solvency test, the impairment of capital test, the profits tests or a combination of them is employed. Weiner, *Amount Available for Dividends* (1929) 29 COL. L. REV. 906, discussing dividend payments under the respective theories.

over, it is extremely unlikely that no-par shares could be issued for insufficient consideration in Texas due to the discretionary power of the Secretary of State.[25]

However where non-par shares have been issued for insufficient consideration, it would be of little benefit to the creditor to discover that the stock is void. Doubt as to the creditor's practical remedy is raised by article 1538-c providing that no-par shares "issued for the consideration prescribed . . . shall be fully paid stock and not liable to any further call or assessment thereon." But the statute does not say what the result will be if the prescribed consideration has not been exacted.[26] The better view is that the creditor would recover to the extent of the fair market value.[27]

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[25] See REPORT AND OPINIONS OF THE ATTORNEY GENERAL OF TEXAS (1926-1928) 117, Op. 2713. See also the varied restrictions and requirements in the discretion of the Secretary of State under the Texas Securities Act, TEX. REV. CIV. STAT. (Vernon, 1925) art. 600a; also art. 1353 ("No corporation shall issue any stock whatever, except for money paid, labor done which is reasonably worth at least the sum at which it was taken by the corporation, or property actually received reasonably worth at least the sum at which it was taken by the company"). All come within the ministerial functions of the Secretary of State.

[26] WASH. COMP. STAT. (Remington, 1922) § 3805, as amended by Laws 1925, c. 87, § 1, provides that an "Initial Non Par Capital" must be stated and the subscriber is liable to the extent of the "Initial Non Par Capital."

For a discussion of this problem and other questions involving the requirements and sufficiency of consideration in Texas, see Masterson, *Consideration for Non Par Shares and Liability of Subscribers and Stockholders* (1939) 17 TEX. L. REV. 247.

[27] *Id.* at 266 *et seq.* The constitutional provision that such stock shall be void "does not change the rule long established in Equity that the shareholders are liable to the creditors for the par value of the capital stock." Mathis v. Pridham, 1 Tex. Civ. App. 58, 20 S. W. 1015 (1892); Park v. Rich, 216 S. W. 146 (Com. App. 1919). There is no reason why the fair value of no-par capital should not be treated the same. Even in Delaware such a rule was applied in a stockholders suit, Cohen v. Loan Corp., 69 F. Supp. 297, (District Court D. New Jersey 1946).

A contrary view is expressed in THE CORPORATION TRUST CO. OF N. Y., SHARES WITHOUT PAR VALUE (1926) 3: "Counsel's reliance is placed upon the statutory provision common in many states to the effect that the judgment of the board of directors as to the valuation . . . is conclusive in the absence of actual fraud in the transaction. The decisions of various courts on the question, however, have impressed counsel with the importance of requiring directors to act within reasonable limits . . . Where . . . property . . . is arbitrarily valued by directors in order to dispose of the question of stock liability, there are still grave legal doubts that their appraisal will stand the test of judicial scrutiny. Considerations of this kind led naturally to the authorization of stock without par value, which provides a safe and effective means of making shares full paid."

Masterson is probably correct. There is no more reason to believe that the statute declaring that such stock issued for the consideration prescribed is "fully paid and non-

Whether non-par shares may be used in payment for preincorporation service rendered by promoters involves the same questions of consideration[28] and is also a problem in itself in Texas.

Despite the authorization of non-par shares in Texas, the no-par share is somewhat a curiosity in common parlance. Few attorneys outside large corporation legal staffs have ever prepared charters or amendments providing for no-par shares. Probably the most obvious reason is the provision of article 1538-d that at least ten per cent of such shares must be subscribed and paid "provided further that in no event the amount so paid shall be less than $25,000." Literal compliance would mean that no-par shares are authorized only in the case of companies with at least $250,000 non-par capital exclusive of the par capital stock.

Since the statute stipulates "at least ten per cent," it has been argued that if the $25,000 represents 100 per cent or more than 10 per cent, then $250,000 capital might not be required. As to the argument that 100 per cent of capital might be represented by $25,000, the point is purely academic since the issue of no-par would serve little if any purpose to the corporation where the issue is out of its hands at the outset. Where less than 100 per cent but more than 10 per cent is thereby represented, it is necessary to determine the meaning of article 1538-d.[29] Is its requirement a minimum with which business is to be begun or does it require a

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assessable" would preclude inquiry as to the actual consideration than would the old corporate practice in par stocks of stamping on their faces "full-paid and non-assessable" so preclude inquiry. See Smith v. General Motors Corp., 289 Fed. 205 (C. C. A. 6th, 1923) (a subscription for stock of par value and one for no-par at a fixed and definite price on the same principles); also Loewus & Co. v. Highland Queen Packing Co., 125 N. J. Eq. 534, 6 Atl. 2d 545 (Court of Chancery, 1939).

[28] Masterson, *Consideration for Non Par Shares and Liability of Subscribers and Stockholders* (1939) 17 TEX. L. REV. 247.

[29] If Texas articles 1538a-1538m are read in their entirety, the only logical construction would seem to be that a minimum for beginning business of $25,000 is required. Since no-par corporations are exempt from the requirement that capital stock be 100 per cent subscribed and half paid-in, it is provided that "at least ten per cent" must be subscribed. The fact that the statute says "at least" and also declares that the statement of value is for fees and taxes *only* when included in the certificate and requires only a statement of the number of shares of no-par authorized seems to rebut the idea of a stated value or stated capital.

stated value on no-par shares through a representation that 10 per cent represents $25,000? Was it meant to make 10 per cent (not less than $25,000) a stated capital? If the latter, then the shares assume stated value by mathematical calculation.

It was the opinion of Dean Hildebrand[30] that the statutes require stated value and that there is no such thing as true no-par stock in Texas. Stayton's Form Book advises statement of value not only in the certificate, as required by article 1538-d, but also in the corporate charter or amendments.[31] If the value is included in the charter or amendments, the shares do have a fixed value without reference to the corporate books; though it is debatable whether the inclusion of value according to Stayton's form would be regarded as fixing value since it refers to past consideration and negatives future representation by the statement "The remaining shares shall be disposed of by the corporation when it sees fit at $..... per share, or for such consideration as may be fixed by the board of directors." However such a statement of value is not required in the charter or amendments. While the certificate is filed with the charter and amendments and is of public record, the statute specifically provides that it is notice

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[30] No authority is cited for the statement. 2 HILDEBRAND, TEXAS CORPORATIONS (1942) 473: "If the corporation issues non-par stock the consideration to be paid therefor must be prescribed in the charter 'or if no consideration is so prescribed, then for such consideration as may be fixed by the stockholders . . . or by the board of directors.' For this reason Texas corporations are not authorized to issue 'true non-par stock' but what is known as 'stated value non-par stock'." The result does not necessarily follow. "It is immaterial how much or how little consideration is received for no-par shares at the outset." Bodell v. Gen. Gas and Elec. Corp., 15 Del. Ch. 119, 132 Atl. 442, 447 (Ch., 1926), *aff'd*, 15 Del. Ch. 420, 140 Atl. 264 (Court of Chancery, 1927). But even though there is no requirement of the amount of consideration that must be received in respect to an original issue of no-par stock, yet the quality of consideration must meet the same requirements as stock having a par value, Cohen v. Beneficial Industries Loan Corp., 69 F. Supp. 297, 300 (District Ct. D., N. J. 1946), citing the *Bodell* case. This is not the same thing as stated value: it pertains to the quality of consideration.

[31] STAYTON'S TEXAS FORM BOOK (3rd ed. 1938) §§ 885-887. It has been argued that art. 1538-e (see note 40 infra) requires such statement in the charter or amendment by implication and art. 1538-g providing that "The certificate required by this act . . . for" no-par shares "which it *may issue*" strengthens the argument. However 1538-a says statement of value may be made by stating the number of shares and that they are without par value. Furthermore 1538-d requires statement of the *value received in the certificate*. It would seem a stronger implication that the charter or amendments need not specify the consideration, and there is danger of imposing stated value in such statements.

of value only for the purpose of taxation by the state, and one opinion of the Attorney General is seemingly in accord.[32] There is no basis for the argument that article 1538-d fixes any value for any other purpose, and it is doubtful that the certificate would be admissible in evidence to establish value except for the purposes enumerated by articles 1538a-1538m.

The capital of a no-par corporation has been repeatedly defined as the value of all its assets, and the consideration received for the shares should be as rigidly guarded as the capital stock of a par value corporation.[33] If the stock is later sold at a premium, it is evident from the entry under "capital account" at the time of the original issue. Stated value and stated capital statutes merely furnish legal excuses for improper accounting and should not be superimposed on our Texas statute if the question ever arises.[34] Stated capital forces the corporation to make a representation of capital for creditors though it may not turn its assets back to the stockholders in the first place. Stated value was designed to prevent gross inadequacy of consideration and is unnecessary with our constitutional provision. Both are theoretically unsound. So long as there has been subscribed and paid in $25,000 representing 10 per cent or more of the authorized shares of no-par, the corporation should be authorized to issue

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[32] (1926-1928) REPORT AND OPINIONS OF THE ATTORNEY GENERAL OF TEXAS, 101, Op. 2674.

[33] Capital stock is but another name for assets contributed.

[34] "Doubt may well be expressed that the statutes permitting an assignment of value to shares having no par value would stand the test of litigation were dividends to be declared and paid on the strength of surplus derived from a segregation of paid-in capital." Assuming a case under a $5 minimum value statute, "The opinion has often been expressed that a corporation might legally credit $5.00 to capital stock, place $15.00 per share in the surplus account and proceed to declare a cash dividend out of such surplus. . . . It is difficult to see how a corporation successfully could defend a legal contest over action such as the foregoing. . . . Any corporation wishing to avoid legal difficulties would do well to credit all amounts received for capital shares to a capital stock account regardless of what the law may permit by way of minimum requirements. . . . The same advice applies to stated capital. The amount of stated capital when shown on the balance sheet or in the financial books may be valuable information but it should not be permitted to interfere with well-established principles of accounting. . . . The chief concern of the law is whether or not the profit is in the assets." WILDMAN & POWELL, CAPITAL STOCK WITHOUT PAR VALUE (1928) 101.

such stock, though it must set forth the actual number of shares sold and the actual consideration therefor in the certificate.

Where an issue of no-par has been authorized, except for the 10 per cent "the Secretary of State does not require the payment of any unpaid shares at *any* time after . . . even to the extent of the life of the charter"[35] and thus "there is, of course no forfeiture of the charter."[36] Also, if a certificate is filed "showing the payment of any additional shares of no-par at a figure less than that for which the original shares were sold, the actual consideration received is used as the basis for computing the franchise tax."[37] Nor is there any reason why later shares of the same issue could not be sold for less than the original consideration if the stockholders consent and creditors are not prejudiced thereby.[38]

If a corporation authorized to issue non-par shares shall fail or refuse to file a certificate within 90 days after the issuance of additional shares, setting forth the consideration received, it is subject to penalty of not less than five nor more than one hundred dollars for each day in default, to be recovered by suit by the Attorney General; and on proof in such suit that it has not yet filed, the corporation shall forfeit its charter.[39] The requirement of such certificate is dispensed with where the shares are given stated value at the outset.[40]

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[35] The office of the Secretary of State of Texas considerately supplied this information.

[36] *Ibid.*

[37] *Ibid.*

[38] "It has been said that when the amount of the capital stock of a corporation, and the par value of its shares are fixed by its charter or the general law, . . . the corporation has no power to issue the stock upon payment of less than its par value. This statement, however, is entirely too broad and is not supported by authority" . . . where "there is no charter, statutory or constitutional provision requiring that stock shall be paid for at its par value, and where no rights of other stockholders are violated, and there is no fraud against creditors, there is nothing whatever to render it either illegal or ultra vires for a corporation to issue its stocks as full paid upon payment of less than its par value." 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) § 5200. Texas has no such limitation as to either par or no-par stock.

[39] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538.

[40] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538-e ("In the event the original charter or any amendment . . . authorizing the issuance of shares of stock without nominal or par value does not prescribe the consideration for which such shares, other than those subscribed and paid for at the time of the filing of the charter or any amendment to a

It should be pointed out that all rights and privileges to be accorded the holders of non-par shares should be specified in the corporate charter or amendments. Due to what has been termed an unfortunate opinion, non-par shareholders have no rights not so specified—not even those of the common law.[41] But no non-par share certificate "shall express . . . any rate of dividend, preference as to assets in liquidation, or price at which such shares may be redeemed except in dollars and cents per share."[42]

In addition to the authorization of an issue of non-par shares either by original charter or amendment, article 1538-h authorizes amendment by majority of the outstanding voting stock, at an annual meeting or a special meeting for that purpose, to change the par stock "or any class or classes thereof into the same number or into a larger or smaller number of shares without" par value, or to change the no-par "or any class or classes thereof into a larger or smaller number of shares without" par value. There is no provision for a change of non-par shares into par shares and corporations being the creature of statute it may well be questioned whether such a conversion could be made. If the authority were granted by an approved charter or amendment, since the conversion is a ministerial function,[43] it would probably not be questioned. In the final analysis it becomes a question whether the Secretary of State would approve it.

What is contemplated by the statute authorizing the conversion of shares is an alteration in stock structure without any change in the capital stock or capital account,[44] and when it is done no

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charter, shall be issued, then within ninety (90) days after the issuance of any such shares, the corporation shall file, . . . a certificate . . . setting forth the number of shares so issued and the actual consideration received. . . ."

[41] 1 HILDEBRAND, TEXAS CORPORATIONS (1942) 287, commenting on West Tex. Utilities Co. v. Ellis, 133 Tex. 104, 126 S. W. (2d) 13 (1939) which stated that "The rights and privileges running with a share of stock are those and only those which the charter or some amendment thereof may attach."

[42] TEX. REV. CIV. STAT. (Vernon, 1925) art. 1538-b.

[43] 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) §§ 5152-53.

[44] TEX. REV. CIV. STAT. (Vernon, 1925) arts. 1330, 1332, for provisions as to increase or decrease of capital stock.

further fee is required[45] except the fee charged for amendment.[46] Article 1538-h further provides that "preferences, rights, limitations, privileges and restrictions" as to outstanding stock "shall not be impaired, diminished or changed without the consent of the owner," but his consent may be derived from charter provisions.[47]

In *A. B. Frank Co. v. Latham*,[48] it was decided by the Texas Supreme Court that only by strict compliance with the statute could there be a reduction in capital stock; that "stock once issued is 'outstanding' though returned to and owned by the corporation issuing it, until retired and canceled as provided by statute for the reduction of capital stock." Though the opinion purported only to determine the meaning of a tax statute, the tax was being imposed on the value of the corporation's stock and the opinion is in harmony with the true theory of non-par. Regardless of the number of no-par shares after the conversion from par shares, they still represent the same amount of capital.

It could hardly be contended that a stated capital minimum (less than the former capital stock) is now to represent the share capital without a reduction in capital stock. If such book juggling can be found acceptable from the accountant's viewpoint, even though a conversion is ministerial[49] and beyond the court's power, it is not likely that a court would sanction disposition of the so-called surplus on complaint by either stockholders or creditors.

F. Morris Mason.

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[45] 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) § 5152, n. 107. For a case relating to the Federal stamp tax, see Cleveland Provision Co. v. Weiss, 4 Fed. (2d) 408 (N. D. Ohio, 1925).

[46] As per TEX. REV. CIV. STAT. (Vernon, 1925) art. 3914.

[47] Ainsworth v. Southwestern Drug Corp., 95 Fed. (2d) 172 (C. C. A. 5th, 1938). A majority vote authorized by charter altered the stock structure to plaintiff's prejudice, and he was denied an injunction.

[48] ... Tex. ...., 193 S. W. (2d) 671 (1946).

[49] 11 FLETCHER, CYCLOPEDIA OF CORPORATIONS (perm. ed. 1932) § 5152, n.