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Book Review

Capital Stock Without Par Value*

By JOHN R. WILDMAN and WELDON POWELL

Reviewed by P. L. Wilton

A GLANCE at the financial section of any daily newspaper will show one that many advertisements for new offerings of stocks are for capital stocks without par value. Of recent issues appearing, out of 125 advertisements, 90% of the common stock was without par value and 35% of the preferred stock was without par value. Many established corporations are changing to a no-par basis.

This change has been so rapid that comparatively little has been written on the subject of capital stock without par value, and there has been much misunderstanding of the real nature of such stock. *Capital Stock Without Par Value* should help greatly to clear up misunderstandings. It covers the subject in a concise, comprehensive manner, and the complete story of no-par shares is interestingly told with a wealth of detail.

The advantages and disadvantages of capital stock without par value are convincingly presented. When used rationally and in accordance with sound economic principles, no-par stock generally has advantages which outweigh those of capital stock with a par value. A distinct advantage is that working capital can be obtained without inflating the book value of assets. There is no occasion for placing assets on the books at a figure equal to the par value of stocks issued, as is often done with par value stock. No-par shares are flexible, adaptable to the market and to the purchasing class. They dispense with the necessity of having to account for discount and other deferred charges in connection with the issue of par stock, since such expenses can be deducted from the proceeds, the net proceeds being capitalized. It is not to be thought that no-par shares are without any disadvantages. One in particular is that they may be used to conceal deficits from operations, since this is possible under some statutes.

The book should be of help to accountants in advising clients, to bankers and business men in corporate financing, mergers, and reorganizations, and to investors in judging security offerings, inasmuch as all must frequently understand the principles relating to no-par stock. The legal, accounting, and economic aspects of the subject are fully presented.

After discussing the significance and historical background of capital stock without par value, the authors describe specifically the points to be considered in originally issuing no-par stock, determining capital value, acquiring own stock and the relation of such stock to surplus, the effect on surplus of changing the form of shares, and the use of no-par stock in flotations; to mention but a few of the topics.

The accounting treatment is fully outlined. In general, the principles are the same as in accounting for par value shares, and in connection with this discussion comparison is made between accounting for no-par and par value stock. The accounting procedure must, of course, take cognizance of the statute provisions on no-par stock. Excellent illustrations are used and many court decisions are introduced to aid in explanation.

The next to the last chapter reviews the principal provisions of the various state laws relating to capital stock without par value. Wisconsin has an admirable no-par stock law. It adheres to the sound and conservative economic principles governing

*A. W. Shaw Company, Chicago, 1928.

no-par stock. The Delaware law seems to allow extreme latitude in respect to no-par stock.

The final chapter gives conclusions on the subject, and is a concise summary of the most important principles elucidated in detail in the body of the treatise. The book is supplemented with excerpts from the statutes of various states, which affords excellent reference to their provisions.

"Don'ts" for Finance Companies

By E. E. Bergmann, New York Thirty-ninth Street Office

WITH the undertaking of each new engagement, the accountant starts out in the hope that the assignment will be one in which his technical and practical knowledge may prove to be of material aid to the client. But too often the engagement seems to be lacking in subject-matter which may be explored and developed with advantage to the client, and without too great an expense of time.

An engagement covering an examination of the accounts of a finance company, to which the writer was assigned, proved to be Utopian with respect to such opportunity, inasmuch as it disclosed practices and policies which almost precluded the company from the possibility of being able to operate profitably, even though the accounting methods were practically ideal.

Among these practices were a number which are summarized briefly herein, and which truly can be called a list of "don'ts" for finance companies.

The company, first of all, agreed to finance the distributors of certain manufacturing companies without recourse to the distributors, or to the companies. This practice led to the acquisition, through repossessions, of used equipment for which the finance company could find no ready market.

Second, the company advanced large sums to certain distributors on their notes which were to be liquidated in equal monthly payments. These notes were secured only by collateral purchase agreements. This plan of financing gave the distributor a great leeway in making sales without regard to the credit risk of the purchaser. It is only reasonable to suppose that in some instances a dealer, seeing the impossibility of meeting coming installments on his notes, would be tempted to make sufficient sales, without due regard for the credit risk, to enable him to obtain funds through down payments with which to satisfy his current indebtedness, and then to gamble more or less on the future, knowing that if he could pay his current debts he could secure further financing.

Third, the company allowed dealers to make collections from the purchasers, instead of having the purchasers remit direct to the finance company. This opened up several dangerous possibilities, chief among which was the withholding of collections by dealers.

Fourth, the finance company, in accepting new business, financed many dealers at remote points far from the control of the field force. Such dealers could withhold collections at will and could otherwise transact their business in such manner as to cause large monetary losses to the finance company.

A finance company generally works on a slender margin of profit and must use every safeguard against possible losses. In making audits of finance companies, the accountant would do well to analyze thoroughly, and consider carefully, the fundamental policies and practices employed by the company in making loans, bearing in mind the points brought forth in this article as dangers to be guarded against in warding off huge potential losses.