2876.

APPROVAL, AGREEMENT RELATING TO RECONSTRUCTION OF CROSSING OVER TRACKS OF BALTIMORE AND OHIO RAILROAD COMPANY NEAR RAVENNA, PORTAGE COUNTY, OHIO.

COLUMBUS, OHIO, January 27, 1931.

HON. O. W. MERRELL, *Director of Highways, Columbus, Ohio.*

2877.

APPROVAL, BONDS OF VILLAGE OF CEDARVILLE, GREENE COUNTY, OHIO—$7,500.00.

COLUMBUS, OHIO, January 27, 1931.

Retirement Board, State Teachers Retirement System, Columbus, Ohio.

2878.

SALE OF STOCK—SAME CLASS OF SHARES SOLD AT SAME TIME—DIFFERENT AMOUNTS OF CONSIDERATION JUSTIFIED WHEN FAIRNESS SHOWN — LESSER CONSIDERATION NOT NECESSARILY INDICATIVE OF DISCOUNT.

SYLLABUS:

1. *Although the arbitrary sale of the shares of stock of the same class for different amounts of consideration at the same time is not authorized by the General Corporation Act of Ohio, if more than one price is justified by a showing of fairness, and in the light of all the circumstances is made for adequate business and administrative reasons, such sale is lawful.*

2. *When a corporation has authority to issue and sell shares of the same issue for different amounts of consideration, such shares which are sold for a lesser consideration are not under all circumstances necessarily sold at a discount within the meaning of the word as used in Section* 8624-6, *General Code.*

COLUMBUS, OHIO, January 28, 1931.

HON. THEODORE H. TANGEMAN, *Director of Commerce, Columbus, Ohio.*

DEAR SIR:—Your predecessor recently requested my opinion as follows:

"Under the General Corporation Act of 1929 provision is made for the issuance of shares without par value. There are six provisions for such issuance. The sixth provision is as follows:

'At any time or from time to time, in all other cases for such amount of consideration as may be fixed by the affirmative vote of the holders of a majority of the outstanding shares of the class to be issued, and by a like vote of the holders of shares of each class junior thereto (regardless of limitations or restrictions on the voting power of any such classes) or by the Board of Directors when authorized by a like vote of the shareholders or by the articles, or if no shares of the class to be issued are outstanding and there are no shares junior thereto then for such amount of consideration as may be fixed by the board of directors.'

Under the Ohio Securities Act (Sec. 8624–6, General Code of Ohio), registration is authorized for a transaction as follows:

'The sale of its securities by a corporation organized under the laws of this state when no part of the securities to be sold is issued directly or indirectly in payment or exchange for intangible property or for property not located in this state, and when the total commission, remuneration, expense or discount in connection with the sale of such securities does not exceed two per centum (2%) of the total sale price thereof plus five hundred dollars ($500).'

The questions upon which I request your opinion are:

1. Can a corporation acting under the above provisions of the General Corporation Act authorize the issuance of no par shares of the same class at the same time at three separate and distinct valuations, that is, may a corporation authorize in one action the issuance of 50,000 shares of Class A stock, to be sold as follows:

A—22,500 shares to be exchanged for stock of another corporation on the basis of $24.50 per share.
B—22,500 shares to be sold to a dealer, for cash at $20.00 per share.
C—5,000 shares to be sold to employes and to other dealers at $30.00 per share?

2. If the above question is answered in the affirmative, may the entire 50,000 shares be qualified under Section 8624–6 of the General Code of Ohio, and if so how can it be determined that 'the total commission, remuneration, expense or discount in connection with the sale of such securities, does not exceed 2% of the total sale price thereof, plus $500.00'?"

Attached to the foregoing communication there was submitted a supplemental letter of explanation as to the circumstances surrounding the proposed issuance of shares and the considerations to be received therefor, which is in part as follows:

"The question arises out of a filing under Section 6–1 of the Securities Act attempting to exempt 50,000 shares of the Class A stock of a certain corporation.

22,500 of the shares are exchanged for stock of another corporation, the book value of such other shares being $24.50 per share. The action of the issuing corporation provides for the exchange on the basis of share for share, the book value being fixed at $24.50 per share for the purpose of the exchange.

A dealer takes an option of 22,500 shares of Class A stock of the issuing company, the Board of Directors agreeing to sell them to the dealer at $20.00 per share, the first year at $22.50 per share, the second year, the price depending upon the time in which the option is exercised. This option is really given in connection with the purchase by the dealer from the issuer, of the issuer's notes aggregating $225,000.

At the same time that the above prices are fixed, they provide that the remaining 5,000 shares shall be sold to the employes and to other dealers at $30.00 per share.

The question really is as to the fairness of the action in designating three separate prices for the same stock at the same time, when of course the book value of all shares should be the same, but under this arrangement the book value will be somewhere below $24.50 and above $20.00."

The provisions of Section 8623–17, General Code, as amended by the 88th General Assembly, a portion of which is quoted, are primarily controlling as to the first question. This section provides as follows:

"Shares without par value may be issued:

(a) Pursuant to subscriptions taken by the incorporators, for such amount of consideration as may be specified in the articles, or, if none is specified, for such amount of consideration as may be specified by the incorporators;

(b) At any time or from time to time, if offered to the shareholders having preemptive rights with respect thereto, or if issued as a share dividend, for such amount of consideration as may be fixed by the board of directors;

(c) At any time or from time to time, in the case of shares so offered to the shareholders having preemptive rights and not subscribed for by them, for such amount of consideration not less than that at which the same shall have been so offered to the shareholders, less such reasonable compensation, allowance or discount for the sale, underwriting or purchase of such shares as may be fixed by the board of directors, unless and until by the vote, consent or written order of the holders of two-thirds of the shares of the class entitled to preemptive rights in respect to such shares a different amount of consideration shall be fixed;

(d) Upon consolidation, merger, reorganization, or change of shares, as may be provided in the agreement of consolidation, plan of reorganization or in the amendment authorizing a change of shares;

(e) Unless otherwise provided in the articles, when it is proposed to issue shares without par value for considerations other than money only, and the fair value to the corporation of the considerations other than money cannot be immediately or readily determined, for such considerations as may be approved by the affirmative vote of the holders of a majority of the outstanding shares of the class to be issued and by a like vote of the holders of shares of each class junior thereto (regardless of limitations or restrictions on the voting power of any such classes) or by the board of directors when authorized by a like vote of the shareholders or by the articles, but in such case, if the amount of considerations for such shares when determined is to be allotted partly to stated capital and partly to surplus, the amount or proportion to be allotted to stated capital shall be fixed at the time the issuance of such shares is authorized, and as soon as practicable after the authorization of the issuance of such shares the amount of the fair value of the considerations other than money shall be determined and entered on the books of the corporation;

(f) At any time or from time to time, in all cases for such amount of consideration as may be fixed by the affirmative vote of the holders of a majority of the outstanding shares of the class to be issued, and by a like vote of the holders of shares of each class junior thereto (regardless of limitations or restrictions on the voting power of any such classes) or by the board

of directors when authorized by a like vote of the shareholders or by the articles, or if no shares of the class to be issued are outstanding and there are no shares junior thereto, then for such amount of consideration as may be fixed by the board of directors."

It will be seen that the legislature has in the foregoing section comprehensively provided for the numerous circumstances under which no par shares may be issued and the considerations which may be received therefor. Nowhere in this section is there any provision to the effect that shares of the same class which may be issued at the same time must be issued for the same amount of consideration.

Prior to amendment, the foregoing section provided as follows:

"Shares without par value may be issued:

(a) Pursuant to subscriptions taken by the incorporators, for such amount of consideration as may be specified in the articles, or if none is specified, for such amount of consideration as may be specified by the incorporators;

(b) At any time or from time to time after organization, for such amount of consideration for each share (which amount shall be equal in respect of all the shares of the same class authorized to be issued at the same time) as may be fixed by the affirmative vote of the holders of a majority of the outstanding shares of the class to be issued, and by a like vote of the holders of shares of each class junior thereto (regardless of limitations or restrictions on the voting power of any such classes) or by the board of directors when authorized by a like vote of the shareholders or by the articles, or if no shares of the class to be issued are outstanding and there are no shares junior thereto then for such amount of consideration for each share as may be fixed by the board of directors."

It is pertinent to note that the clause "which amount shall be equal in respect of all the shares of the same class authorized to be issued at the same time", appearing in the original enactment of this section of the General Corporation Act, adopted in 1927, has been omitted in the amendment thereof by the 88th General Assembly. This fact is, of course, indicative of a legislative intent that the inhibition against issuing no par shares of the same class for different considerations at the same time shall no longer prevail. It is not, however, necessary that an answer to your first question depend entirely upon the application of this principle of statutory construction.

The General Corporation Law of the State of Delaware has for some time contained a provision for the consideration to be received for no par shares which, insofar as the question here under consideration is concerned, is substantially identical with the Ohio law. I refer to the provision now appearing in Section 14 of the General Corporation Law of the State of Delaware, which same language was heretofore contained in Section 4a thereof, it being there provided that capital stock without nominal or par value "may be issued by the corporation from time to time for such consideration as may be fixed from time to time by the board of directors." This provision was adjudicated in the case of *Bodell* v. *General Gas and Electric Corp.*, decided by the Court of Chancery of Delaware, March 2, 1926, reported in 132 Atl. 442, the court holding that Delaware corporations are authorized to sell stock of the same issue at different prices to different persons at the same time. After quoting the foregoing clause of the Delaware Corporation Law, the court said:

"I do not recall that any special emphasis was laid by the complainants at the argument on the phrase 'from time to time' as of significance in the

instant case. Here of course the two offerings were concurrent. In substance there was no interval of time between them. But this is of no moment. Prices at which no par stock is issued cannot be made to depend for their fairness upon the immaterial circumstance of the length of time intervening between the moments of their issuance. The phrase 'from time to time' gives to the section this meaning —that no par stock may be issued at any time for such consideration as may be fixed by the directors at the time the issue is authorized."

The facts in the foregoing case were as follows: Class A no par common stock was authorized to be sold to the public at $45.00 per share. It paid a dividend of $1.50 per share. At the same time Class A stockholders were authorized to accept dividends at such rate payable in Class A common stock at a price of $25.00 per share. Injunction was brought by the Class B common stockholders, complaining of injury, first, that if a sales price for Class A common stock is established for sales at $45.00 such price is the sum which the directors must demand for all stock concurrently offered,—this for the reason that less capital is brought in than would otherwise be possible, and so the junior Class B common would suffer in that less earnings would accrue from which Class B might hope for its junior dividend rates to be taken care of, and on liquidation less capital would be on hand for distribution and the amounts distributable to it thereby diminished. Upon this point the court said:

"Now when it was desired to sell 48,000 more shares of Class A common, it was announced that the right to use dividends in subscribing for further shares of the same kind at twenty-five dollars would continue as a policy. This policy it is claimed made the sale of the additional stock an easy matter, for in addition to the regular dividend of $1.50 a year which the stock was paying, the announced policy held out to purchasers the prospect, just referred to, of making a profit on the stock they might take at twenty-five dollars for their regular dividends. Thus, to use an old expression, the stock lifted itself by its own boot-straps. If the value of forty-five dollars per share is thus created by the combined action of the announced policy and the creation of market prices by the sustaining operations of the bankers on the exchange, it is manifest that forty-five dollars, the price which was concurrently obtained by the corporation when it was announced that Class A dividends would be allowed to buy it at twenty-five dollars per share, does not represent a sales price which the directors can in fairness be held to. It would be highly unreasonable to point to sales at forty-five dollars as showing the inadequacy of sales at twenty-five dollars if the latter was what in fact made the former possible."

The court further held that:

"The mere showing of the two prices would without satisfactory explanation undoubtedly entitle the complainants to relief. But if these two prices are justified by a showing of fairness in the light of all the circumstances so that what appears to be an injury turns out to be a benefit to those complaining, there can be no ground for interference. If the directors, in the course they are pursuing are acting in the genuine and beneficial interest of the corporation and are thereby promoting the interests of all stockholders in a very tangible way and especially the interests of the class of stockholders who are complaining, why should not the general principles applicable to persons standing in trust relationships come to their supporting aid?"

In your supplemental communication you state that the book value of the shares upon which your question is predicated is somewhere below $24.50 and above $20.00. I do not believe that the directors in fixing the amount of consideration at which no par shares are to be sold are bound by the book value thereof. The ninth headnote in the case of *Bodell* v. *General Gas and Elec. Corp.*, supra, is as follows:

> "Neither price for which no par stock was originally sold, nor current value quoted on stock exchange, nor book value, is necessarily proper criterion for price at which directors ought subsequently to issue similar stock."

Upon this point the court held in its exhaustive opinion:

> "A study of the quoted market values of stocks and their book values will disclose strange and striking inconsistencies in their relations to each other when the issues of various corporations are comparatively examined. We may accept the general proposition that managers of corporations ought to be required to market new issues of no par stock at prices that are fair to the corporation and existing stockholders and best calculated to yield the largest possible capital. These prices should be fixed in the light of all legitimate considerations such as appraised and sale value of assets, book values, market values of outstanding shares, present and probable earning power, market conditions, size of the issue, reputation of the corporation, and such exceptional considerations as honest and fair minded men might properly take into account. It would be hazardous to venture an examination of all the possible considerations which directors might take into account in fixing a price which will be fair to the corporation and its existing stockholders and best calculated to yield the largest possible capital. Whether in a given case they have fixed such price is a question which must be determined in the light of the particular conditions surrounding the transaction."

The next controlling case as to the question of issuing no par common stock of the same class for different amounts of consideration at the same time, is the case of *Atlantic Refining Co.* v. *Hodgman, et al., Superior Oil Corp.* v. *Same*, decided by the United State Circuit Court of Appeals, 3d. Circuit, July 9, 1926, reported in 13 Fed., 2d Series, 781. This case involved certain transactions whereby the Superior Oil Corporation settled an indebtedness to the Atlantic Refining Company by issuing to the Atlantic Company its common stock on a basis of $8.54 per share under an agreement whereby such stock was to be kept off of the market for two years, at the same time entering into an agreement with bankers to sell its common stock of the same class at $16.00 per share. The headnotes are in part as follows:

> "Defendant, by purchase of corporation stock at less than price paid for same stock by bankers' syndicate underwriting it, *held* not guilty of unfair dealing toward syndicate, which had knowledge thereof and required defendant to tie up its stock for 2 years and to enter into 10-year contract to purchase oil output of corporation.
>
> Stockholders of corporation cannot complain of alleged fraud on third party exchanging property to corporation for stock because of purchase of stock by defendant at lower price; such third party not complaining thereof.
>
> Though under Delaware law arbitrary sale of same issue of stock at different prices to different persons will not be sanctioned, such sales will be sustained, if based on business and commercial facts, justifying it in exercise of fair business judgment.

Corporation *held* to have acted within its authority in selling stock to creditor at lower price than to others in payment of loan, and in consideration of 10-year contract for sale of oil output, in view of fact that corporation could not increase its stock until loan was paid, and requirement of bankers' syndicate underwriting stock relative to oil contract.

Sales of corporate stock at different prices are lawful under Delaware law, if made for adequate business and administrative reasons."

The facts surrounding the issuance of the 50,000 shares of Class A no par common stock about which you inquire are not sufficient for me to say whether or not the variations in the price at which these shares are proposed to be issued, are occasioned by adequate business and administrative reasons such as to be authorized by the Ohio General Corporation Act. The sale of 22,500 shares for cash at $20.00 per share appears to be in connection with the sale of notes of the corporation in the amount of $225,000. Undoubtedly the financing of notes in this amount is a matter to be given consideration in passing upon the sale of stock at $20.00 per share. I have no information relative to any matters which may be pertinent surrounding the circumstances bearing upon the proposed sale of 5,000 shares to employes and other dealers at $30.00 per share.

In answer to your first question, it is my opinion that although the arbitrary sale of the shares of stock of the same class for different amounts of consideration at the same time is not authorized by the General Corporation Act of Ohio, if more than one price is justified by a showing of fairness, and in the light of all the circumstances is made for adequate business and administrative reasons, such sale is lawful. It is believed that a more specific answer to your first question may not be given in view of the limited facts submitted.

Coming now to your second question as to the qualification of such shares by registration under Section 8624-6, General Code, the pertinent portion of which you have quoted, I am advised that this question is occasioned by some doubt as to the meaning of the word "discount" appearing in this section. It is therein provided that "the total commission, remuneration, expense or discount in connection with the sale of such securities does not exceed two per centum of the total sale price thereof plus five hundred dollars." When, for instance, part of an issue may be sold at $20.00 and another part of the same issue may be sold at the same time at $25.00, the question becomes one of whether or not shares sold at $20.00 may be said to be sold at a "discount" within the meaning of this section of the Ohio Securities Law. If the answer is in the affirmative, then of course such shares may not be qualified under this section, since the amount of "discount" would be in excess of two per cent, viz. twenty per cent.

The word "discount" is defined by Webster's New International Dictionary as follows:

> "A counting off or deduction made from a gross sum on any account whatever; an allowance upon an account, debt, demand, price asked, and the like, usually made in consideration of prompt or cash payment; something taken off or deducted."

If it were sought to deduct from the fixed selling price of a block of shares any amount, for whatsoever reason and depending upon considerations of whatsoever nature, such deduction would undoubtedly amount to a discount. For instance, if it should be provided that stockholders may exercise their preemptive rights as to an issue and purchase any amount of the shares they desire at a price five per cent less than the price at which the shares are to be offered to the public, the sale of such shares to the stockholders would probably amount to selling them at a discount. In the event,

however, the board of directors should, for valid reasons, authorize the sale of a certain block of shares of a given issue for a certain consideration and at the same time authorize the issuance and sale of another block of shares of the same issue for a different consideration, it does not necessarily follow that the block which is sold for a lesser consideration is sold at a discount. Notwithstanding the fact that the two blocks of shares may be of the same issue, the action of the board in fixing the consideration for one block may not be so dependent upon the action of the board in fixing the consideration for the other as to result in a portion of the shares being sold at a discount. A consideration of the amount to be credited to capital account might be pertinent in determining this matter. Under such circumstances, there is no reason why such shares may not be qualified by registration under the provisions of the portion of Section 8624-6, which you quote in your communication.

Specifically answering your second question, it is my opinion that when a corporation has authority to issue and sell shares of the same issue for different amounts of consideration, such shares which are sold for a lesser consideration are not under all circumstances necessarily sold at a discount within the meaning of the word as used in Section 8624-6, General Code. It is believed that a more specific answer to your inquiry may not be given.

Respectfully,
GILBERT BETTMAN,
Attorney General.

2879.

WATERWORKS FUND—MUNICIPALLY OWNED WATERWORKS—REIMBURSEMENT OF GENERAL SINKING FUND FROM SURPLUS ARISING FROM OPERATION OF WATERWORKS PROHIBITED.

SYLLABUS:

No part of the surplus in the waterworks fund of a municipally owned waterworks may be used to reimburse the general sinking fund of the municipality, notwithstanding the fact that waterworks bonds may have been paid from such fund prior to the time the waterworks became self-sustaining.

COLUMBUS, OHIO, January 28, 1931.

Bureau of Inspection and Supervision of Public Offices, Columbus, Ohio.

GENTLEMEN:—Your letter of recent date is as follows:

"Section 3959 G. C., provides for the disposition of any surplus water works funds and authorizes the use thereof for the payment of interest on any loan, and for a sinking fund for the liquidation of the debt.

"The water works of the village of————was contructed and paid for by the issuance of bonds, and for several years the earnings were insufficient to provide a surplus for the payment of the interest and bonds in full. The difference was paid out of the general sinking fund of the village. The surplus in the water works fund at this date is in excess of the amount necessary to provide for the payment of the outstanding bonds and interest, and the village council desires to reimburse the general sinking fund out of such water