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Larry Forest

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CORPORATIONS — CONSIDERATION FOR CAPITAL STOCK — UNSECURED PROMISSORY NOTES

The constitutional and statutory provisions of North Dakota relevant to consideration for shares of stock are similar to those of a number of other states. North Dakota has a constitutional provision which is as follows: "No corporation shall issue stock or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void. The stock and indebtedness of corporations shall not be increased except in pursuance of general law, nor without the consent of the persons holding the larger amount in value of the stock first obtained at a meeting to be held after sixty days notice given in pursuance of law."

This constitutional provision is repeated and enlarged upon by statute which provides that, "No corporation shall issue stock or bonds except for money, labor done, or property, estimated at its true money value, actually received by it, and all the officials of a corporation who consent to the issuance of stock or bonds for labor or property in excess of its actual cash value, or who have knowledge thereof and do not at the time dissent therefrom in writing shall be jointly and severally liable to the creditors of such corporation for the difference between the actual cash value of such labor or property at the time such stock or bonds were issued and the par value of the stock or bonds issued therefor." Another section provides; "No note or obligation given by a stockholder, whether secured by pledge or otherwise, shall be considered as payment of any part of the capital stock; but the capital stock shall be paid in, either in cash, or in the manner provided in this article."

Another section which is also relevant because it provides for the issuance of shares not fully paid reads, "All corporation for profit must issue certificates of stock when fully paid up, signed by the president and secretary, and may provide in their by-laws for the issuance of certificates prior to the full payment under such restrictions and for such purposes as their by-laws provide"

In *German Mercantile Co. v. Wanner*, the controlling case, the North Dakota court ruled that an unsecured promissory note was good consideration for shares and that a corporation could legally issue the certificates. The Court said that a note was "property received" under the provisions of the law. In construing the provision in the North Dakota law that "no note shall be considered . . . as payment", the court held that this was not a prohibition against taking a note for shares but only against taking a note in payment. It seems that such a ruling has thwarted the purpose to be served by the provisions which undoubtedly were meant to protect stockholders and creditors from dummy

¹N. D. Const. § 138.

²Comp. Laws of N. D. (1913) § 4528.

³Comp. Laws of N. D. (1913) § 4529.

⁴Comp. Laws of N. D. (1913) § 4527.

corporations and watered stock, where stock issued would not be backed by solid assets. An unsecured note is valueless until paid; and it is not a property which is capable of being used in the business, while it may well be at a great discount.⁵

The majority rule is well stated in an annotation in the American Law Reports which reads, "It appears to be the majority rule that under a statute forbidding issuance of stock except for money, labor done, etc. . . , a note given in payment for corporate stock does not constitute 'money paid, nor property received' and is not a good consideration for the issuance of the stock . . ." The bulk of the states follow this rule, which is favored by most authorities."⁶

States following the minority and North Dakota rule that a note is property and therefore good consideration are California, Idaho, South Dakota.⁷ The California statute is similar to ours but has an additional distinguishing provision which defines property received as including intangibles such as notes.⁸

There has not been a square decision in point in North Dakota since the controlling case of German Mercantile Co. v. Warner was decided, but several cases have cited it, and it seems likely that any decision today would follow the same rule. In Baird vs. Kilene⁹ the Court ruled that a note given by a prospective stockholder could not be considered as payment for any part of capital stock of a corporation. The Court says in brief that under the statute in regard to a note as payment for shares," a corporation cannot enter the shares as paid on its books, but this does not prohibit the corporation from issuing shares for a promissory note, as it was the intention of the Legislature under another statute, that a corporation should be able to issue shares before being fully paid."¹⁰

It is to be noticed that in one case the Court as dictum made a statement to this effect, ". . . and the note or obligation of a stockholder may not be accepted in payment of stock in the corporation, unless it is stock which the corporation has purchased from its surplus profits, under provisions of sec. 4531, N. D. Compiled Laws of 1913, and holds among its assets the same as other property."¹¹ Section 4531 provides; "Unless otherwise provided, a corporation may purchase, hold and transfer shares of its own stock from its surplus profits, or as provided in the article on assessments of stock, or by the unanimous consent in writing of all its stockholders, in such manner and for such price or consideration as the said stockholders may unanimously decide upon."¹²

⁵25 N. D. 479, 142 N. W. 463 (1913), 52 L. R. A. (N. S.) 453.

⁶Ballatine on Corporations, § 208.

⁷Followed by Ala., Ark., Del., Ky., Mass., N. Y.

⁸Also includes N. D. - 58 A. L. R. 708.

⁹52 L. R. A. (N. S.) 453.

¹⁰53 N. D. 244, 205 N. W. 681 (1925).

¹¹Comp. Laws of N. D. (1913) § 4529.

¹²Comp. Laws of N. D. (1913) § 4527.

¹³Jackson v. Sabie, 36 N. D. 49, 161 N. W. 722 (1917).

It follows, then, that a note may be taken as payment for treasury shares, an exception to the rule as laid down in sec. 4529."

In the case of *Nybakken v Baird* the syllabus states misleadingly that stock cannot legally be issued before payment of a note given "in settlement when paid." But the actual holding is not contra to the *Wanner* case as again the court really decides only that a note cannot be considered as payment for stock under the statute."

The North Dakota Courts hold, then, that an unsecured note is property and is good consideration for capital stock, but is not payment, except for treasury shares. The Court's interpretation is logical and literal but eviscerates the constitutional and statutory provisions designed to protect stockholders and creditors. The surest remedy lies in changing the statute. The limiting definition of "property" excluding the unsecured promissory note would give to the law the effect which the Legislature undoubtedly intended it to have.

LARRY FOREST,
Law Student,
University of North Dakota.

¹⁴56 N. D. 786, 219 N. W. 472 (1923).

¹⁵Comp. Laws of N. D. (1913) § 4529.

EVIDENCE — ADMISSIONS — PRELIMINARY HEARING ON VOLUNTARY CHARACTER OF ADMISSION NOT REQUIRED IN CRIMINAL CASES

From a judgment of conviction for murder in the second degree the defendant appealed, alleging as error the admission in evidence of a written statement that she had killed her husband to protect her daughter. The defendant contended that the statement constituted a confession and had been involuntarily given, and requested a preliminary hearing as to the voluntary character of the alleged confession. The court refused the request, but charged the jury to disregard it if they had found it to have been made under compulsion. Held: That since the statement was an admission and not a confession, no preliminary hearing was necessary. *State v. Gibson*, 284 N. W. 209 (N. D. 1938).

A confession is an acknowledgement in express terms, by a party in a criminal case, of his guilt of the crime charged, while an admission is a statement by the accused, direct or indirect, of facts pertinent to the issue and tending, in connection with proof of other facts, to prove his guilt. *People v. Crowl*, 82 P. (2d) 507 (Cal. 1938); *State v. Gibson*, supra; *Moore v. State*, 220 Wis. 404, 265 N. W. 101 (1936).

An admission in criminal matters relates to matters of fact not involving a criminal intent; a confession is an acknowledgement of guilt. It is only with respect to confessions that preliminary proof that they were voluntary must be made before they are admissible in evidence. *People v. Fowkes*, 178 Cal. 657,