The Theory Of Capital In Virginia: An Historical Comma And A Disjunctive Conjunction

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For some years Virginia lawyers have discussed, in an academic sort of way, problems concerning the true meaning of the dividend section of the Virginia Corporation Statute. One of the moot questions has been: Does the statute permit a corporation, operating under a continuing capital deficit, to pay dividends out of net earnings for the current fiscal year without either restoring net assets to the level of capital, or reducing capital stock in the manner prescribed by the statute? The question has frequently taken some such form as this: Suppose a Virginia corporation was launched in 1930 with a stated capital of $100,000 and with $100,000 worth of net assets; that it has had five lean years, losing on the average $10,000 of its net assets each year for five consecutive years, thereby winding up the fifth year with a 50% capital impairment, or a $50,000 capital deficit; but that during its sixth year, its business has taken a turn for the better, and the books show $10,000 net earnings for 1935; does the Virginia statute permit the $10,000 to be distributed to shareholders as dividends, without restoration of capital or reduction of capital stock? Some have contended that the statute clearly permits a solvent corporation to make a distribution upon the basis of “net earnings” for the sixth year, regardless of the shortage of net assets to measure up to stated capital. Others have refused to believe that the dividend section of the Virginia Corporation Statute was intended to abolish, so far as it ever existed, the whole requirement of maintaining a fixed capital as a condition to the right to pay dividends.

The dividend section of the statute reads as follows:

“Directors are empowered to declare and pay dividends out of net earnings, or out of net assets in excess of capital....”

The Supreme Court of Appeals of Virginia has never passed upon the problem of whether dividends can be paid out of such “net earnings” as only go to decrease a capital deficit. The United States Circuit Court of Appeals has held that the statute permits dividends to be paid out of such net earnings, provided that such dividends do not exceed the amount of net earnings for the year in which they are declared. However, the Virginia courts have held that the statute does not permit dividends to be paid out of such net earnings, unless the corporation has restored its net assets to the level of stated capital or reduced its capital stock in accordance with the statute.

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Court of Appeals, however, in United States v. Riely, has recently held that the Virginia statute does permit a Virginia corporation with impaired capital to pay dividends out of net earnings for the current year.

The occasion for the federal court making an interpretation of the Virginia Corporation Statute was a tax refund case. The taxpayer, Pierce Oil Corporation, had paid an undistributed profits tax under protest. The ground of the protest was that the taxpayer did not owe the amount of the undistributed profits tax unless it could have made a legal distribution for the year the tax was assessed, 1937, and that the taxpayer could not have legally made a distribution for 1937 because it began and ended the year with a heavy capital deficit. The plaintiff, receiver for the Pierce Oil Corporation, recovered a judgment for the amount paid, in the Federal District Court, that court expressing the view that whether the plaintiff owed the amount of the tax depended upon whether it could legally have made a distribution, which in turn depended upon whether the Virginia statute permitted a corporation with impaired capital to make a distribution. The District Court held that the statute did not permit a capital-deficit company to pay dividends. The Circuit Court of Appeals accepted the theory that the duty to pay the tax depended upon the legality of the corporation making a distribution for 1937, but reversed the District Court upon the ground that the Virginia statute expressly permits a capital-deficit corporation to pay dividends out of net earnings for the current year.

Although the Riely case may arouse little interest among tax counsel because the undistributed profits tax is no longer effective as such, it is nevertheless a significant case in the corporations field, since it goes to the heart of the problem of what constitutes the capital of a corporation incorporated under Virginia law. The case is especially significant for the reason that the judge who happened to write the opinion is a distinguished expert on Virginia law. In the absence of a decision of the

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4 Net earnings computed under Revenue Act of 1936 were $86,412.46. The corporation's capital was impaired on Dec. 31, 1936 by at least $1,149,642.76, and on Dec. 31, 1947 by at least $1,000,000. See Pierce Oil Co. v. United States, 77 F. Supp. 273 (E. D. Va. 1947).
5 The Pierce Oil Corporation was dissolved by decree of the Circuit Court of the City of Richmond, entered Dec. 27, 1940, and in April, 1940, Henry C. Riely and Robert T. Barton were appointed Receivers. See United States v. Riely, 169 F. (2d) 542 (C. C. A. 4th, 1948).
7 For current tax relief under undistributed profits tax see: Revenue Act of 1936, Sec. 26 (c), as amended by Revenue Act of 1942, Sec. 501 (a) (c).
8 Armistead M. Dobie, formerly Dean of the Department of Law of the University of Virginia.
Virginia Supreme Court of Appeals, the opinion in the Riely case will perhaps be accepted as an authoritative interpretation of the dividend section of the Virginia statute, so long as the law remains unamended.

The far-reaching result of the decision is that there is no such thing as a fixed capital requirement for Virginia corporations. All Virginia corporations are practically reduced to the status of wasting assets corporations. When it comes to paying dividends, the only thing left which a solvent Virginia corporation cannot do is to pay a liquidating dividend out of a bare remnant of its impaired capital while operating as a going concern.

Under general rules of corporation law, as found in textbooks, treatises, cases, and articles, a corporation is not permitted to pay dividends out of current net earnings while its capital is impaired without restoring capital or reducing capital stock. "Net earnings" accruing while capital is impaired are looked upon as mere decreases of capital deficit and not as "net earnings" for dividend purposes. Under current theories of corporate finance and accepted accounting practice, the only source of legal dividends is found in the excess of net assets over capital. A corporation capitalized at $100,000 is required to keep $100,000 more than barely solvent as a condition to paying dividends. Typical statutes, including the Virginia statute, impose drastic penalties upon directors for paying dividends out of capital—meaning paying dividends out of "net assets" which do not measure up to their fixed capital margin—and the same statutes require innocent recipients of such dividends to return the illegal payments to the corporation, or else impose liability on the shareholder to the creditor, in case of insolvency, to the extent illegal dividends have been received.

Such statutory provisions do not concern themselves with insolvent corporations paying dividends or with corporations paying dividends which render them insolvent, but concern themselves with infringe-
ment of the capital margin over and above solvency. A corporation capitalized at one million dollars, which has net assets of five cents is still 100% solvent. So, too, is a naked Indian with no assets and no liabilities (because he has no credit). Unless no liability is to take the place of limited liability in America, continuing solvency seems a poor test for the propriety of paying dividends.

Under prevailing corporation law and by accepted accounting practice, "capital is a quantum and not a res." In practical application it becomes a mere numerical figure which is to be subtracted from the numerical figure standing for the money value of "net assets," in order to ascertain the numerical figure representing the money value of "legal surplus" available for legal dividend payments. The capital figure is a constant and not a variable. The figure representing net assets varies, but capital remains a constant unless the charter is amended. In terms of the inevitable graph, expressing dollar values in terms of inches, $10,000 to the inch, when capital is $100,000, the capital line is ten inches above the solvency line. When net assets drop to $50,000, the net assets stand half-way between the capital line and the solvency line and the graph shows a 50% capital deficit. If net assets rise to $110,000, the net assets stand one inch above the capital line and the graph shows $10,000 "surplus." Net assets rise and fall, but capital remains a constant until reduced by amendment of the charter. Capital does not fold up like an accordion, under general rules of corporation law; but under the Virginia statute, as interpreted by the Riely case, capital is not a constant. It is something that shrivels and shrinks as the net assets diminish. Presumably a corporation could be launched with a capital of $100,000 and net assets of $100,000, lose all of its net assets the first year (ending the year nakedly solvent) and yet, if it had net earnings of $100,000 the second year, it could distribute the whole amount of net earnings for the year as dividends, and begin the third year nakedly solvent.

In the Riely case, the court begins with the proposition that the case must be decided solely upon the provisions of the Virginia statute and not upon general corporation law. Certainly no one will take issue with the proposition that the Virginia statute controls. In the second place, no one can deny that the Commonwealth of Virginia has the power to pass a law which abolishes the fixed capital requirement. Nor can any living man deny that the framers of the Virginia statute may possibly have intended to do just that. Some Virginia lawyers may dis-

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16 Fletcher, Cyclopedia Corporations (Rev. ed. 1931) § 5334.
sent, however, from the method by which the Federal Circuit Court of Appeals arrived at its interpretation of the Virginia statute, and may remain unconvinced that the law has been correctly interpreted, no matter what degree of respect the high court which decided the Riely case deservedly commands.

Some Virginia lawyers had assumed that the dividend section of the Virginia Corporation Statute, when read in connection with other provisions thereof, made "excess of net assets over capital" the only legal source of a dividend. Though the statute reads "...out of net earnings or net assets in excess of capital," they had assumed that the statute meant "...out of such net earnings as should constitute an excess of net assets over fixed stated capital or, to put it another way, out of any excess of net assets over and above capital whether carried as surplus or not." They were familiar with the fact that "net earnings" is an ambiguous expression, which may vary in meaning with the context. To them, "net earnings" for a given fiscal year in the broadest sense included two types: (1) net earnings which only decrease a capital deficit, (2) net earnings which create or augment a surplus. They had assumed that "net earnings" as used in the dividend section of the Virginia statute excluded the former and included the latter. They were not entirely presumptuous in this assumption, because other jurisdictions had interpreted similar statutory forms of expression in that manner. It seemed to be an accepted interpretation of the type of expression found in the Virginia statute.\(^{17}\) Other Virginia lawyers have pointed out that "net earnings" has been frequently used to mean net earnings for the whole period of a corporation's life, as distinguished from net earnings for a particular year (or particular accounting period). If a corporation has never paid a dividend, "over-all period net earnings" and "surplus" are the same thing. For example, suppose a corporation launched in 1931, fairly capitalized at $100,000, lost $10,000 in 1931 and another $10,000 in 1932. In 1933 it earned $30,000. At the end of 1933, assuming there have been no dividend payments, the company's "surplus" is $10,000; its over-all net earnings are also $10,000 and its excess of net assets over capital is $10,000. They point out that the Virginia statute does not say that dividends may be paid out of "net earnings for the current year," but that the statute reads "...out of net earnings, or net assets in excess of capital."

There are, therefore, two theories of the meaning of "net earnings" in the Virginia dividend section which are consistent with the maintenance of the integrity of a fixed capital margin: (1) that the refer-

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\(^{17}\)Ballantine, Corporations (Rev. ed. 1946) 583.
ence is to over-all net earnings for the whole period of the corporation's life, thereby making "net earnings" synonymous with "surplus;" (2) that "net earnings," though actually referring to net earnings for the particular fiscal year, is used in the narrow sense of net earnings which create or augment a surplus, and not in the broad sense including annual "net earnings" which only go to reduce a capital deficit.

The only theory of the meaning of "net earnings," as employed in the Virginia dividend section, which is destructive of the whole fixed capital requirement is the theory that the words "net earnings" are used in the sense of net earnings for the fiscal year rather than for the over-all period, and also that the term is used in the broadest sense to include capital deficit decreases, as well as net earnings which create or augment surplus. It seems not only undesirable to destroy the fixed capital requirement in Virginia, when it is so nearly universally maintained in most of the great industrial states, but the achievement of such a destructive result requires the violation of accepted rules of interpretation of statutes of the Virginia type, a statute which we largely borrowed from New Jersey. Courts of other states, when obliged to interpret similar statutes, had not so interpreted their statutes as to produce such a radical result as destroying the fixed capital requirement. Why, may we ask, did a high federal court feel obliged to secede the Commonwealth of Virginia from the Union of conventional corporation law? The answer seems to be found in the punctuation, an historical comma, producing a disjunctive conjunction.

The Federal Circuit Court of Appeals tells us that the Virginia statute makes an express grant of power to the Board of Directors of a Virginia corporation to pay dividends out of either of two entirely separate and independent sources: (1) out of "net assets" in excess of capital, or in the alternative (2) out of the "net earnings" for the current fiscal year (regardless of whether the corporation has a capital deficit or not).

The language of the court, concerning the meaning of net earnings, is as follows:

"The words 'net earnings' are followed by a comma, then before the words 'out of its net assets in excess of capital' comes the disjunctive conjunction 'or.' As the English language is rationally used, this would seem to imply two separate sources of dividends (1) net earnings and (2) excess of assets over capital, each with no relation to, no connection with the other. To arrive at the interpretation reached by the Federal District Court, it is necessary to insert in the Statute, right after the words net earnings some such non-existing negative proviso as 'provided there is an excess of corporate assets over capital.' "
Thus we observe the whole law of a fixed capital requirement in the Commonwealth of Virginia demolished by a “disjunctive conjunction” which derives its powerful disjoining effect from the position of a comma. The whole battle for the integrity of the capital margin is lost “all because of a horse-shoe nail” of punctuation. Certainly such a comma is worth looking into very carefully. We may approach the study of such commas by the case method, in order to test their effect in similar English sentences having nothing to do with law. Suppose we pick up a high school student’s mathematics manual and read the following words: “The area of a circle is $\pi R^2$, or 3.1416 multiplied by the square of the radius.” Do we assume that the comma before the word “or” makes the word “or” a disjunctive conjunction and that it compels us to decide that two separate and independent methods of arriving at the area of a circle are intended? On the other hand, do we not assume that the “or” is an ordinary signal of an explanatory appositive? Is it incorrect to use the comma? If so, it must be under some new Federal Rule of Punctuation.

Suppose we turn the problem around in order to see whether the word “or” may be a disjunctive conjunction in a similar sentence, without the aid of the comma. We read a note from our hostess: “You can find sugar in the breakfast room in the sugarbowl or in the tin box in the pantry.” Do we assume that only one source of sugar is intended because the comma is omitted after the word bowl? Is it wrong to omit the comma?

Suppose a section of a given statute defines “surplus” in the broad sense “all excess of ‘net assets over capital,’ whether carried as ‘surplus’ on the books or not.” Following the definition appears the following statement as to dividend payments: “Dividends may be paid out of surplus, or excess of net assets over capital.” In such case, would we assume two separate and independent sources of a dividend? Would the “or” be disjunctive? Would it be incorrect to put the comma after the word surplus? Would not the comma simply indicate that a parenthetical explanatory clause is to follow? It is submitted that the comma in the dividend section of the Virginia statute is a neutral element in our problem of interpretation.

But the comma in the Rieby case is an historical comma. The fixed capital requirement in New Jersey was temporarily sent to the junk heap in 1904 because a similar comma was held to have created a disjunctive conjunction in the dividend section of the New Jersey corporation statute. In Goodnow v. The American Writing Paper Com-
pany the New Jersey court permitted a corporation, launched with a capital deficit, to pay a dividend without either restoring capital or reducing capital stock, upon the theory that the comma in the following dividend section indicated alternative sources of dividends: "... from its surplus [comma] or from its 'net profits.'" The New Jersey court said: "Under the Act of 1896 there was room to contend that the words net profits were intended to be synonymous with the word surplus; the language used was—from surplus or net profits. Under the Act of 1904 this contention is no longer possible; the language used is: 'from its surplus, (comma) or from its net profits.' The evident intention of the change is to point out two funds from which dividends may be paid." Joseph L. Weiner, in commenting on the Goodnow case in the Columbia Law Review,\(^1\) says: "... the court said that the Amendment, by adding the comma, between surplus and net profits, made clear that these two measures of the propriety of a dividend were not synonymous but alternative. Whatever we may think of the New Jersey court's theory of the effect of the comma, the opinion shows clearly that such expressions as net earnings and net profits were sometimes used in the early statutes synonymously with surplus, and the court admits that, absent the atomic comma, there was room to contend that net profits meant overall-period net profits and was therefore synonymous with surplus." The language of the court, in the Riely case, is strangely reminiscent of the language of the court in the Goodnow case but the Goodnow case has been discredited in New Jersey, the jurisdiction from which we borrowed our basic statute.

In a recent New Jersey case, National Newark & Essex Banking Co. v. Durant Motor Co.,\(^2\) the court denied that dividends could be earned while the corporation was operating under a capital deficit. Under the charter contract, the holders of so-called non-cumulative preferred stock were entitled to no dividend credits for passed-over years "unless earned" but were entitled to dividend credits for passed-over years "if earned." "Net earnings" of the type which decrease a capital deficit did accrue during the period in question but there were no "net earnings" of the type which create or augment a surplus. No dividend credits were allowed for years in which the net earnings went only to decrease a capital deficit. The court said: "From the beginning of operations Dec. 1, 1931 to Dec. 31, 1937, there was a loss of $232,000; assume that

\(^{18}\)73 N. J. Eq. L. 692, 69 Atl. 1014 (1908).
\(^{19}\)Weiner, Theory of Anglo-American Dividend Law, American Statutes and Cases (1929) 29 Col. L. Rev. 461, 469.
\(^{20}\)124 N. J. Eq. 213, 1 A. (2d) 316 (1938).
there will be a profit of $50,000 for 1938, reducing the deficit that much. Would the preferred stock earn a dividend in 1938? Our statute forbids payment of dividends except from surplus or from net profits of the business of the corporations—Though the company be $50,000 better off at the close of 1938 than at the beginning yet there will be no net profits at the end of the year but only a smaller deficit.” In terms of law-student slang, where “earnings” below the solvency line are earnings in the red, and earnings above the capital line are earnings in the black, and earnings in the capital-deficit zone are earnings in the pink, we may say that this case holds that earnings in the pink are not earnings for dividend purposes. The mercury in the thermometer was rising toward the melting point but hadn’t risen to 32 degrees.

Mr. Henry W. Ballantine, one of the most highly respected authorities on corporation law, in the 1946 edition of his textbook, in commenting on the Goodnow case, says: “It may be doubted whether the New Jersey Legislature really intended to create alternative sources of dividends by referring to net profits without specifying any particular period for their determination. In most of the statutes in which the terms surplus or net profits are employed without specifying some particular accounting period for net profits, particularly where impairment of capital is prohibited, it is believed that no alternative sources of dividends are intended. The purpose of using the terms in the alternative seems to be to include all excess of net assets over the amount of legal capital, whether carried on the books in a surplus account or otherwise.”21 It should be recalled at this point that the Virginia statute does prohibit payment of dividends out of capital and does prescribe severe penalties on Board members for paying dividends out of capital.22 It should also be kept in mind that the Virginia statute includes a very elaborate procedure for reducing capital stock.23 It is difficult to imagine why anyone should take the trouble to comply with this section of the statute if capital, instead of being a constant, shrivels or shrinks or reduces itself automatically as net assets dwindle away. If a corporation is launched with $100,000 stated capital and $100,000 net assets, why bother to reduce capital stock, in the manner prescribed by statute, when capital automatically reduces itself to $50,000 as soon as $50,000 of the net assets are lost.

There are three different provisions of the Virginia corporation statute which seem to be utterly inconsistent with the interpretation of

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21 Ballantine, Corporations (Rev. ed. 1946) 583, 584.
the Riely case: (1) the provision against paying dividends out of capital; (2) the penalties imposed upon directors for paying dividends out of capital; (3) the provisions for making a reduction of capital stock. While it is possible to argue that paying dividends out of capital means "paying dividends out of the remnant of capital, as impaired, when there are no current net earnings," the writer can imagine no useful purpose for the section in the Virginia statute providing an exact procedure for reducing capital stock, when capital reduces itself as net assets dwindle away.

Lawyers who experience some degree of shock as well as surprise at the decision in the Riely case will perhaps read the opinion carefully, feeling between the lines to try to learn whether the court rejected the fixed capital requirement for Virginia reluctantly or not. They will want to know whether the court felt driven to an admittedly unfortunate result by a bad statute, or whether, on the other hand, the Federal Circuit Court of Appeals felt that it did not make much difference whether Virginia corporations or any other corporations were governed by a fixed capital requirement. Such lawyers will not have to feel between the lines. They will be told in unambiguous, forthright English in black and white that the court does not think the fixed capital requirement amounts to much one way or another. This may be of some interest to lawyers outside Virginia. The words of the court on the matter are as follows: "Let us suppose, however, that (absent any statute) a corporation starts with a capital of $100,000. After several difficult years, the corporation's assets are reduced to $90,000. There are no creditors and there is ample cash to carry on the corporation's business. Now comes a good year in which the corporation's net earnings are $5,000. We believe that if the directors in their sound discretion so determine, there is no compelling reason in corporate finance or economic practice, which would prevent the directors from declaring a $5,000 dividend for the stockholders. Surely this would not be a very unusual performance. For the rule in England, see 55 A. L. R. 20." The court's illustration presents such a mild case of paying dividends out of capital that one is made to feel guilty of petty-mindedness to object. One wonders if the court is announcing a policy of temperance, as distinguished from total abstinence, in dipping into capital's bowl for a little Virginia Gentleman's drink of dividends. Under the actual decision of the case, however, a corporation could lose all its net assets and be reduced to naked solvency and yet pay dividends the first year its books showed any net earnings of the type which go to reduce a deficit.
Now certainly no one has any right to feel shocked on moral
grounds on learning that one of the highest courts in the United States
has flouted the fixed capital requirement or because it has expressed
the view that the strict maintenance of a fixed capital is of little or no
importance. Certainly no question of morals or basic propriety is in-
volved. America would continue to run and even prosper, perhaps,
with or without its corporations being required to maintain a fixed
capital. We have had corporations in England, without limited lia-

tibility;24 we have had American corporations whose stockholders were
subject to ratable liability;25 and we have had corporations with a
capital that shrank as net assets diminished. We have survived an era
when stock-watering was the fashionable thing to do, even for gentle-
men. We have survived the era of true no-par stock. We could survive
an era when American corporations generally were permitted to
operate without any requirement of maintaining a fixed capital. Per-
haps most good citizens would never be conscious of any change. In
this sense, there is no compelling reason for maintaining the require-
ment of a fixed capital margin. But to say that there is no compelling
reason in corporate finance or in economic practice for maintaining
the capital margin, as the law exists today, is quite another thing. It
had seemed, to some lawyers that the capital margin requirement was
the most all-pervading principle in the law of corporate finance, as
omnipresent as the rule requiring consideration in the law of contracts.

The following illustrations indicate that much of the law of cor-
porate finance rotates around the axis of fixed capital rather than the
solvent line. 1. When may a corporation purchase its own stock, we
ask the student of corporate finance. The answer is, when the purchase
can be made out of surplus.26 The answer is not when the purchase
will not render the corporation insolvent. 2. May holders of preferred
stock which is convertible into bonds exercise their conversation privi-
lege (thereby transforming themselves into creditors of the corpora-
tion rather than shareholders in the debtor company) whenever the
conversion will not render the corporation insolvent? The taught-law
answer is no.27 There must be a surplus. Capital must not be impaired.
3. To what extent may cumulative preferred stock be "guaranteed?"
Answer: Only to the extent that there be a surplus at the time of pay-

25See discussion in Gray Construction Co. v. Fantile, 62 S. D. 345, 253 N. W.
464 (1934).
26Levy, Purchase by a Corporation of Its Own Stock (1930) 15 Minn. L. Rev. 1.
27"Conversion into bonds is a decrease of capital." See In Re Phoenix Hotel Co.
ment. 4. Suppose the charter contract insures to holders of so-called non-cumulative preferred shares, dividend credits for passed-over years if earned. Do the holders of these securities get dividend credits for earnings which only go to decrease a capital deficit? The answer is no. 28

5. May dividends be paid out of reduction-surplus? The answer is yes, if the net assets exceed capital as reduced.

In the law of bankruptcy and fraudulent conveyances, we concern ourselves continually with the problem of solvency, but in the law of corporate finance we more frequently are concerned with whether an excess of net assets over capital exists. In view of the foregoing, it seems to the writer that the dividend section of the Virginia corporation statute should be amended in such manner as to prohibit payment of dividends except out of net assets in excess of capital.

This brings us to the second problem: what constitutes capital under Virginia law. There is no use talking about maintaining a fixed capital unless the ascertainment of the exact amount of it can be precisely determined. How do we calculate its money value? How do we arrive at the numerical figure to be subtracted from the figure standing for net assets in order to get the surplus figure? The statute (omitting problems concerned with legal increases and legal reductions pursuant to Section 3781) defines capital, in Section 3840, in terms of "the sum of the consideration received in payment for the shares (whether with or without par value)." Section 3840 does not, in so many words, define capital as the sum of the money values of the considerations received in payment for the shares. The words are "the sum of the consideration." Since a verbal property description cannot be subtracted from a numerical figure standing for net assets, we must look beyond Section 3840 for the method of finding the exact amount of money value which constitutes capital. Virginia's definition of capital is of a vague, out-moded type.

Mr. George S. Hills, of New York, writing in the Harvard Law Review, in discussing definition of capital under the early statutes, says: "Capital has been variously defined in terms of property and consideration received for the shares . . . . The more modern laws contain a clear definition of capital. In composite, modern laws fix the amount of legal or stated capital of a corporation at any particular time as follows: 'the sum of the aggregate par value of all shares having par value plus

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30Hills, Model Corporation Act (1935) 48 Harv. L. Rev. 1334.
the aggregate amount of consideration received for all issued shares without par value, except such part thereof as may have been allocated to paid-in surplus'... (plus legal increases and minus legal reductions) ... [Having] been established, legal capital crystallizes into an amount, a quantum and not a res, which remains constant unless or until it is increased or reduced in a manner expressly required or permitted by statute." Thus under modern statutes, a corporation which has issued 1000 shares of $100 par value plus 10,000 shares of no par value, for which it has received $10 a share, is capitalized at $200,000. In Virginia the multiple of the so-called par value of the par shares times the number of par shares has nothing to do with the fixing of capital, nor does the actual value of the consideration received for the no-par shares have any bearing. Virginia has her own unique system of fixing the quantum or amount which constitutes capital. For lack of an established term, we may describe the Virginia rule as a recorded valuation rule. Making allowance for the inaccuracy inherent in all over-simplification, we may say that the Virginia statute apparently requires that a corporation's capital must be centrally recorded in terms of dollars and cents with the State Corporation Commission. If a corporation has issued 1000 shares of so-called 100 par stock and takes from the subscribers property, services and money estimated by the board of directors to be worth only $50,000 and the officers have recorded the $50,000 valuation with the S.C.C. in the form and manner required by statute, then the corporation's capital apparently becomes $50,000 and not $100,000. If the expression "$100 par" has any useful meaning in Virginia law, it does not have the usual effect in fixing capital. In Monk v. Barnett the court said: "All persons contracting with corporations chartered in this state must look to the records of the State Corporation Commission as to the character, location and value of the assets of the corporation." In Monk v. Barnett the subscribers issued to themselves stock of the aggregate par value of $40,000 for properties upon which they themselves placed a value of $4,000. In subsequent insolvency, the court held that the subscribers were not liable to creditors for so much of the difference between the $40,000 and the $4,000 as should be necessary to pay unsatisfied creditors. The subscribers had complied with the statutes of Virginia by filing their valuation with the S.C.C., together with the description of the property in the manner prescribed. Although Section 3840 of the statute is rather vague in defining capital in terms of the "sum of the considera-

\[\text{Monk v. Barnett, 113 Va. 635, 75 S. E. 185 (1911).}\]

\[\text{Va. Code Ann. (Michie, 1942) § 3840.}\]
tion," Section 3788, in pursuance of a mandate of Section 167 of the Constitution, prescribes that an estimated valuation of the aggregate value of the consideration be filed with the S.C.C. in the form and manner required by the S.C.C., and the S.C.C. requires a precise valuation in terms of amount of money values of the considerations in dollars and cents.

It has been argued by persons who find it difficult to understand how radically the Virginia capital theory differs from the conventional theory, that a Virginia corporation is launched with a capital deficit whenever the recorded valuation is less than the aggregate par value of the par stock. "Suppose," they argue, "that a Virginia corporation is launched with 1000 shares of $100 par value stock and that the recorded valuation of the consideration for the stock is only $50,000; doesn't the corporation begin life with a capital deficit? Will it not be necessary for the corporation to earn more than $50,000 before showing a surplus available for dividends?" The answer seems to be no, because the corporation's capital is really $50,000 and not $100,000 under Virginia statute law. A Virginia corporation could be launched with a capital deficit if the actual value of the property received for the stock was less than the recorded value thereof.

It should also be noted at this point that the organizers are required to record a valuation of the considerations received for the so-called no-par stock as well as the so-called par stock, and that this becomes a part of the capital under the definition of Section 3840. If a Virginia corporation issues 1000 shares of so-called no-par stock for a recorded consideration value of $10,000 or $10 per share, assuming there are no other shares, then the capital becomes $10,000. Though erroneously called "no-par" stock, the shares upon analysis appear to be in reality a stated value stock, or to use the self-disputing form of expression frequently encountered, the stock is "stated value no-par stock." We may also observe that a $10 stated-value share is the equivalent of a $10 low par share. It thus appears that there is no such thing as true par stock under Virginia corporation law; nor is there any such thing as true no-par stock. All stock in Virginia is in effect stated-value stock or stock

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34Formerly the New York rule as to liability of subscribers was much the same as the Virginia rule. See Christman v. Eno, 106 N. Y. 97, 12 N. E. 648 (1887) and Southworth v. Morgan, 205 N. Y. 293, 68 N. E. 490 (1912). A subscriber who agreed to pay $50 for a $100 par share and who had paid only $25 or $25 worth was liable to creditors for $25 and not $75. This rule has been changed by statute in New York, bringing New York in line with other states. See New York Stock Corporations Law, § 69.
of centrally recorded valuation. It is difficult to see what useful purpose is served by maintaining a distinction between par and no-par, so long as both are stated value stocks.

As a result of Virginia's having a unique capital theory which, strangely enough, permits the recorded capital figure to be lower than the result of the par value times the number of par shares, the story has gotten around that Virginia has no definite figure for capital. The Virginia statute, however, does, as the writer reads the statute, fix a precise figure for capital. "... the sum of the money values of the considerations received for the shares as valued and recorded with the S.C.C." This may be $50,000, when other states might fix capital at $100,000 because 1000 shares of so-called $100 par value have been issued. Although we must admit that capital is only $50,000, Virginia could keep that amount of capital intact, and hold that the company has a $25,000 capital deficit when it has only $25,000 net assets left. Rights of creditors, protection of liquidation preferences, prevention of dilution of value of one class of stock by another class, and the solution of many other practical problems require that a corporation should have a fixed quantity of money's worth of capital which does not shrink as assets dwindle away. The statute should be amended so as to permit dividend payments from only one source—"net assets in excess of capital." If the Riely case stirs up enough interest to cause Virginia lawyers to reread the statute thoughtfully and critically, this decision of the United States Circuit Court of Appeals may turn out to be a blessing in disguise. The whole patchwork of the statute needs a general overhauling.
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Raymon T. Johnson, Professor of Law in Washington and Lee University, died on March 25, 1948, at the age of 50.

Born in Minorsville, Kentucky, in 1897, Professor Johnson received the A.B. degree from the University of Kentucky in 1922 and the J.D. degree from the University of Chicago in 1925, where he made an excellent record as a law student and as a member of the debating team. He joined the Law Faculty of Washington and Lee University in the Fall of 1925. Except for two short periods of law practice—one year in Louisville, Kentucky and two years in the legal department of R.C.A.-Victor—Professor Johnson spent his whole professional life at Washington and Lee.

Commencing his career as a law teacher at the age of 27, he was regarded by his students as an outstanding teacher from the beginning. He combined clarity and force in presenting his material with a quick wit and lovable personality. He gave unsparingly of his time and effort toward the establishment of the Washington and Lee Law Review in 1939; he served with marked distinction in a difficult assignment as member of an investigating committee of the Association of American Law Schools; and a few days before his death, he was elected to membership in the American Law Institute.

The Editors of the Law Review mourn the loss of a colleague and friend.
THE LAW SCHOOL

The School of Law of Washington and Lee University opened its 100th session on October 14, 1948. On this date the School returned to the two-semester academic year, with beginning students admitted at both Fall and Spring Semesters.

Final registration for the Fall Semester, 1948 totalled 232, divided as follows:

- 1st Year, 1st Semester: 100
- 2nd Year, 3rd Semester: 31
- 4th Semester: 23
- 3rd Year, 5th Semester: 55
- 6th Semester: 23

Of the total Fall enrollment 209 students were veterans. All candidates for the degree of Bachelor of Laws had completed at least one-half of the requirements for a collegiate Bachelor's degree; 100 held a collegiate degree at the time of admission; 21 received a collegiate degree under the combined programs in Arts and Law or Commerce and Law; and 36 had completed at least three years of college work.

The permanent Law Faculty during the year 1948-49 includes Dean Clayton E. Williams, Professors Charles R. McDowell and Charles P. Light, Jr. and Associate Professors Charles V. Laughlin and Theodore A. Smedley. Miss Wanda Lee Spears, B.A., LL.B. was appointed Law Librarian and Mrs. C. R. McDowell continues as Law School Secretary. Mr. Carter Glass, III, of the Lynchburg Bar, continues to serve as Lecturer on Taxation, and Mr. William L. Martin, of the Roanoke Bar, as Lecturer on Virginia Procedure.

The late Professor Raymon T. Johnson's courses for the Spring Term, 1948, were completed by Messrs. Carter Glass, III, LL.B., LL.M., Joseph E. Blackburn, B.A., LL.B., and Paul M. Shuford, B.S., LL.B. During the Fall Semester, 1948, Mr. Edward S. Graves, M.A., LL.B., served as Lecturer on Domestic Relations and Mr. Wilson F. Miller, B.S., LL.B., as Lecturer on Criminal Law. Mr. Blackburn will continue during the Spring Semester, 1949, as Lecturer on Conflict of Laws.

Mr. Joseph H. Wolfe, B.S., J.D., presently Cook Fellow at the University of Michigan Law School, has been appointed Assistant Professor of Law commencing with the Fall Semester, 1949.

The value of the Menkemeller Memorial Law Scholarships has been increased, commencing 1949-50, to $1,350.00 for the six semesters of law study. These scholarships are offered to graduates of approved
colleges who are beginning the study of law. They are awarded on the basis of character, high scholastic attainment, and promise of future usefulness in the legal profession. Financial need is given consideration. A Menkemeller Scholarship will continue for the three years of law study, provided the holder maintains the standards set by the Law Faculty. The stipend is payable in the amount of $225.00 each semester, commencing 1949-50, which is equivalent to the total of all University fees for a semester.

The 100th anniversary of the establishment of the School of Law will be commemorated, during the Bicentennial of the University, by the inauguration of the John Randolph Tucker Memorial Lectures on May 10 and 11, 1949. The honorable John W. Davis, a distinguished member of the Law Class of 1895, is the Lecturer and has chosen as his subject: John Randolph Tucker—the Man and His Work. The first lecture will be delivered in Lee Chapel at 8:00 p.m., May 10th, and the second lecture at a Convocation in the Chapel at 12:00 noon, May 11th. The Law School Faculties in Virginia and neighboring states, members of the bar and alumni of the University will be invited to attend.

Members of the Law Faculty attended the Southern Law Review Conference at Baton Rouge, Louisiana, in April, 1948; the meeting of the American Law Institute at Washington, D.C., in June, 1948; the Judicial Conference of the Fourth Circuit at Asheville, N.C., also in June, 1948; the annual meeting of the Virginia State Bar Association at White Sulphur Springs, W.Va., in August, 1948; the winter meeting of the Section on Legal Education and Admission to the Bar at Richmond in December, 1948, as guests of the University of Richmond School of Law; and the annual meeting of the Association of American Law Schools at Cincinnati, Ohio, also in December, 1948.

The School of Law was host to the June, 1948, meeting of the Section on Legal Education and Admission to the Bar. The meeting was held in Tucker Hall and was attended by the Board of Bar Examiners and by members of the Law Faculties of the University of Virginia, the University of Richmond, the College of William and Mary and Washington and Lee University.

At the August, 1948, meeting of the Virginia State Bar Association, Dean Clayton E. Williams was elected to the Executive Committee, and Professor Charles R. McDowell was elected a Vice-President and reappointed Chairman of the Committee on Uniform State Laws. Professor Charles P. Light, Jr., completed his term as chairman of the Section on Legal Education and Admission to the Bar and was reappointed member of the Committee on Administrative Law.
Professor Theodore A. Smedley was elected Chairman of the Southern Law Review Conference for 1949.

The legal fraternities were active during 1948 in behalf of the entire School and their own membership. Tucker Inn of Phi Delta Phi and Staples Chapter of Phi Alpha Delta jointly presented an orientation program for first year law students, consisting of four lectures given at the beginning of the Fall Semester, 1948. Phi Alpha Delta sponsored a legal writing contest, with a prize of $50.00 in books, open to all law students except members of the Law Review staff. Six lectures on Legal Ethics were given for law students in November, 1948, by members of Phi Delta Phi. The lectures covered the field of ethical and moral responsibilities of the lawyer in his profession. A running docket of proceedings in the courts of Rockbridge County was prepared by Tucker Inn and posted on the bulletin board for the information of the law student body.

Speakers who addressed meetings of Phi Alpha Delta during the year were: Dean F. D. G. Ribble of the University of Virginia Law School, Mr. John L. Walker of the Roanoke Bar and Past President of the Virginia State Bar Association, Mr. Paul A. Holstein of the Lexington Bar, Congressman James E. Noland of Indiana, and Professor Charles P. Light, Jr., of the Law Faculty. Meetings of Phi Delta Phi were addressed by President Walker of the State Bar Association, Mr. Holstein, State Senator Earl Fitzpatrick of the Roanoke Bar, Colonel Francis Pickens Miller of Albermarle, Judge Floridus S. Crosby of the 18th Judicial Circuit, Superintendent Blalock of the Virginia Hospital for the Criminal Insane at Marion, Mr. Richard D. Auerbach, Head Agent of the F. B. I. for the Richmond area, Mr. Edward Osborne, Director, Federal Juvenile Detention Camp, Mr. Massie Yuille of Lynchburg and Mr. John Fishwick of the Legal Department, Norfolk and Western Railroad, Roanoke. During March and April four of the Democratic candidates for Governor of Virginia were brought to Lexington to speak under the auspices of the fraternity.

The Howard-Rogers Legal Society, composed of law students from West Virginia, invited to the School as speakers Mr. E. B. Pennybacker, West Virginia Compensation Commissioner, and Mr. Charles E. Mahan of the West Virginia Bar (Fayetteville).

Informal graduation exercises were held for the mid-year class of 1949 on February 14th, in Washington Chapel. The graduates were presented by Dean Williams to President Gaines who announced the award of the Bachelor of Laws degrees. The address was delivered by Justice Buchanan of the Supreme Court of Appeals of Virginia.