

February 1, 1934.

OUTLINE OF MAIN PROVISIONS TO BE INCLUDED

IN A FEDERAL CORPORATIONS LAW

I. Protection of Capital and Preventing Dilution of Stockholders' Interests:

1. Protection against stock watering. The Committee has already decided that provisions for protection against stock watering should be included in the proposed law. These provisions are to express the following principles:
 - (a) Full public disclosure of the circumstances of the promotion.
 - (b) Power given to the Corporation Commission to refuse to permit corporations to commence business if an unreasonable valuation is placed on the property.
 - (c) The imposition of liabilities for failure to make proper disclosure.

The Committee was also of the opinion that the proposed law should contain provisions regarding the payment of promoters' fees and organization expenses.

II. Shares:

1. Par Value versus No Par. Should the proposed law require all stock to have a par value or should no par stock be permitted?
 - (a) If it is decided that only par value shares are to be provided for, should permission to issue stock at a discount with the previous approval of the Corporation Commission be given in order to permit flexibility of corporation financing?

- (b) If no par stock is permitted, what provisions shall be included to prevent abuses?
- i. To prevent allocation of funds to surplus so as to permit the paying out of money which should be allocated to capital:
Should there be any limitation on the division of consideration received for no-par shares between capital and paid-in surplus? Should there be an arbitrary limitation of 10% which may be allocated to paid-in surplus? Should there be a requirement that all of the consideration be allocated to capital? Should the corporation be permitted to allocate as much of the consideration as it desires to paid-in surplus if two-thirds of the stockholders vote such allocation? Or should the funds realized from issues, subsequent to the original issue, be allocated to capital and surplus in proportion to the capital and surplus then existing in the corporation? If this latter suggestion is adopted, it will still be necessary to have an arbitrary limit or some other restriction upon the allocation of the original stock issue.
 - ii. To prevent giving away stock and dilution of existing stockholders' interest. Should provision be made to prevent the sale of subsequent issues of no par shares at an unreasonably low figure which would cause injury to

existing shareholders? Should this provision take the form of requiring the corporation to secure the consent of the Corporation Commission to the sale of shares below market value, or should the Commission be given the power to issue stop orders where the sale price is unreasonably low?

iii. Simplification of corporation law. Should par value stock be prohibited?

2. To prevent a paper corporation from commencing business and to prevent evasion of provisions regarding increases of capital stock.

(a) Authorized and Issued Capital. Should there be a requirement that a corporation must have a certain percentage of its authorized capital subscribed for before it commences business?

(b) Initial Cash Payment. Should there be a requirement that a stipulated percentage of the consideration be paid up in cash before a corporation can commence business?

III. To Prevent the Use of Corporation Funds to Redeem Stock of Favored Stockholders:

1. Redemption of Preferred Shares. Should the proposed law contain provisions regarding the redemption of preferred shares?

IV. To Prevent Impairment of Stockholders' Voting Right and of Right to Share in the Corporate Assets:

1. Preemptive Rights. Should the proposed law contain a provision strengthening the present rule as to preemptive rights and doing away with some of the present exceptions?

V. To Prevent Corporations From Speculating in Their Own Stock:

1. Treasury Stock. Should the acquisition of treasury stock be forbidden where it involves the expenditure of corporate funds, or should treasury shares be permitted with Commission control over purchase and resale of such shares?

VI. (1) To Protect Bondholders:

- (a) Standard clauses: Should the proposed law require that mortgage indentures contain standard clauses requiring the corporation to make proper provision for sinking fund and amortization, and giving bondholders a right to vote in the event that default is made?

- (b) Trustees: Shall the Corporation Commission be given power to object to the designation of a particular person as trustee under a mortgage indenture? Shall the Commission be given power to remove trustees on the application of a stipulated percentage of the bondholders?

- (2) To prevent dilution of stockholders' rights and stock watering through bonds convertible into stock:

- (a) Convertible bonds. Should the proposed law contain provisions regarding control by the Commission over the issue of convertible bonds?

VII. Amendment of Articles:

- 1. To prevent change of character of business to detriment of stockholders and creditors:

- (a) Change of object. Should there be a requirement for consent of the Commission to amendments of articles with respect to changing the objects of the corporation? Should there be a provision giving the Commission control over the initial objects of the corporation?

- 2. To prevent injury to creditors by distributing assets to shareholders:

- (a) Reduction of capital. Should there be a requirement for consent of the Commission to reduction of capital?

- 3. Should the Commission pass upon increases of capital?

VIII. To Prevent Improper Payment of Dividends, to insure Stability of the Corporation and to

Force Distribution of Dividends Where Properly Payable:

- 1. Cash Dividends. Out of what fund shall a corporation be permitted to pay dividends? Shall it be limited to paying dividends out of profits resulting from the operation of the business, or should it be permitted to pay dividends out of the excess of assets over liabilities?

2. Compulsory Reserves. Should corporations be required to set aside a percentage of the annual profits as a reserve to make up past losses of capital?
3. Compulsory Payment. Should there be a provision to enable shareholders to compel payment of dividends?
4. To minimize the necessity of financing through bonds during developmental periods. Should corporations be empowered to pay interest out of capital for a limited period where shares are issued to raise money for the construction of a plant?
5. Stock Dividends (to prevent gambling). Should corporations be prohibited from declaring stock dividends? If stock dividends are to be permitted, should the consent of the Corporation Commission be required before such dividends are declared?

IX. Accounts and Statements: It will probably be agreed that the proposed law should require corporations to submit to their shareholders and to the Corporation Commission annual balance sheets and profit and loss statements. Should corporations be required to submit further statements, viz:

1. A statement regarding directors and officers including
 - (a) amount of compensation
 - (b) allowance to directors and officers
 - (c) the existence of any interest of directors or officers in contracts made by the corporation.

(d) purchases and sales of stock of the corporation by directors or officers.

2. A quarterly statement of earnings.
3. A list of all shareholders holding more than 1% of the shares and of all shareholders who are directors or officers.
4. A list of any names of bondholders in the possession of the corporation. Should the corporation be required to insert in all mortgages a provision that the trustee retain a record of bondholders and submit this record to the corporation?

X. Auditors: Should auditors be appointed by the management, elected by the shareholders' meeting, or appointed by the Corporation Commission? Should the Corporation Commission be given the power to admit auditors to practice? Should the Commission be given the sole power to remove auditors (a) upon their own motion, (b) upon application of the directors, (c) upon application of the stockholders, or (d) upon application of the bondholders?

XI. Inspection: Should the Corporation Commission be given the power to order an inspection of the affairs of the corporation upon the application of shareholders? On its own motion? On application of the bondholders? Should the proposed law restate the common law rule regarding inspection of corporate records by shareholders, or should limitations be placed on the common law right?

XII. Voting Rights and Shareholders' Meetings:

1. Voting Rights. Should non-voting stock be permitted? Should non-voting preferred stock be permitted? Should there be a provision which would give a right to vote in proportion to the investment made by the shareholders?
2. Should Voting Trusts be Prohibited?
3. Proxies. Should general proxies be permitted or should proxies be limited to specific matters contained in notice of meeting? Should any of the following provisions be inserted:
 - (a) Proxies should be elected at the annual meeting and should be put under a fiduciary duty.
 - (b) Corporation funds are not to be used for the solicitation of proxies.
 - (c) No director or officer should be a proxy.
 - (d) Notice of solicitation of proxies should be registered with the Corporation Commission.
 - (e) The Corporation Commission should be given the right to solicit proxies.
 - (f) The Corporation Commission should be given the right to vote any stock not voted.
4. Election of Directors. Should there be a provision for absentee voting by ballot for directors?
5. Shareholders' Meetings. Should a specified percentage of the shareholders be permitted to call extraordinary meetings? Should shareholders be given the right to require that particular matters be put on the agenda? Should shareholders be

given the right to request from the directors information on the affairs of the corporation at meetings? Should any limitations be put on this right to request information?

XIII. Directors:

1. Should the Corporation Commission be given power to remove directors?
2. Should there be a requirement for qualifying shares to be held by directors?
Should these shares be impounded in the corporation's treasury?
3. Should there be any limitation placed on the extent to which directors may be given a share of the profits?
4. Should corporations be prohibited from making loans to directors, or should there be a requirement that loans to directors may be made only with the assent of the stockholders?
5. Should the law provide that directors shall stand in a fiduciary relation to stockholders? Should there be a provision preventing directors from making a profit at the expense of shareholders by dealing in the stock of the corporation?
6. Should individual stockholders be permitted to sue on behalf of the corporation to enforce liabilities of directors?

XIV. Dominant Shareholders: Should the proposed law attempt to deal with the problem of shareholders who dominate the corporation? Should they be placed under the same liability as directors and be required to disclose their interests in contracts? Should

dominant shareholders be placed under a fiduciary duty to other shareholders to disclose dealings in the securities of the corporation?

XV. Holding Companies: Should holding companies be prohibited? Should an exception be made permitting wholly-owned subsidiaries? If holding companies are to be permitted, in what way shall they be regulated? Shall this regulation be directed solely toward disclosure of intercorporate affairs, or shall there be any provisions to prevent diversion of income?

XVI. Reorganization: Should the proposed law contain provisions relating to the reorganization of federal corporations, or should this subject be left to other legislation? If this law is to deal with reorganization, should there be provisions for an official receiver? Should the law subject bondholders' committees and deposit agreements to control by the Commission? Should the Commission be given the power to approve reorganization plans, or to draw up its own plan?