

**OPINION
57-180**

October 28, 1957 (OPINION)

SECURITIES

RE: Salesmen - Registration

Under date of October 15, 1957, we received from you a letter inquiring as follows:

Does an unincorporated group of promoters for a yet to be formed, and chartered, Canadian Corporation require licensing by the Securities Commissioner before receiving contributions from a number of individuals in North Dakota, New York, and Canada, towards the organization of the anticipated foreign corporation?"

The proposed agreement with the party paying the money is attached and we find it states that Gene Orndorf of Deering, North Dakota, is referred to as party of the first part and _____ of _____ is referred to as party of the second part,
Witnesseth:

There is nobody named as party of the second part but we deem that as unimportant from the following facts as stated in the proposed agreement. It is stated that, Whereas, First Party, Gene Orndorf of Deering, North Dakota, and several other parties are about to form a corporation under the laws of the Province of Manitoba, Canada, with home offices in the City of Winnipeg, to be known as Canadian-American Records, Ltd., for the purpose of producing and promoting phonograph records; said proposed corporation to have a capital stock of one million dollars (\$1,000,000.00) all of which is to be common stock, and which shall consist of ten thousand (10,000) shares of the par value of one hundred dollars (\$100.00) per share, said corporation to have a Board of Directors consisting of not less than five and not more than fifteen persons, five of whom shall be the persons above named.

It provides that one Herb Brittain has agreed to act in the capacity of a technical advisor in the making and promoting of records, selecting talent and musical numbers for a period of three years without salary, and for which he will receive five percent of the stock of said corporation. And it further provides that whereas said Jeff Hand has agreed to act for a period of three years, without salary, as technical adviser, and as a contact between the corporation and the record buying public in exchange for five percent of the stock of said corporation, and whereas Gene Orndorf agrees to devote his full time to organizing said corporation in furtherance of which he has spent several months of time in securing facts and in exploring the feasibility of such a corporation, in exchange of fifteen percent of the stock of the corporation, when formed, and the corporation is set up, Gene Orndorf agrees to manage the affairs of said corporation on a full-time basis for a period of three years in consideration of an annual salary of \$7500.00, and an option to purchase ten percent more of the capital stock at the same price as

is accorded to party of the second part.

It further provides that said R.C. Orndorf, in exchange for five percent of the stock, has agreed to act as business adviser to said corporation, and said T.H. Luedke, in exchange for five percent of the stock of said corporation will act as salesman for said corporation, if and when said corporation is organized. It then provides further that it is necessary to obtain \$50,000.00 in order to finance the organization of said corporation, secure talent, promote the sale of records, etc.

We call your attention to the fact that such agreement is contrary to the Constitution and statutes of the State of North Dakota. Section 138 of the Constitution of the State of North Dakota provides 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."

Section 10-0317 of the North Dakota Revised Code of 1943 provides as follows:

No corporation shall issue stock or bonds except for money or for labor done or property actually received by it, estimated at its true money value, and all the officers 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 liable jointly and severally 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."

It is plain that the agreement referred to violates the provisions of both the Constitution and the statute of North Dakota herein cited and an intention is made to issue stock before they have collected any value therefor. We further find in the proposed agreement that it is proposed that in the event said corporation is organized that ten percent of the stock of said corporation shall be exchanged for specific services rendered by individuals or otherwise, to the proposed corporation. It is, therefore, plain that the stock is to be issued under the proposed agreement which in itself shows that there is no corporation in existence at the time of executing such agreement. It further provides that twenty percent of said stock shall be retained as treasury stock to be disposed of at the discretion of the Board of Directors; and that twenty-five percent of said stock shall become the property of the persons, including party of the second part, who advance the initial \$50,000.00 for the purpose hereinbefore stated.

We must herein point out that the corporate stock they intend to issue has not been paid for as provided by the Constitution and statutes of North Dakota in order to provide issuance of stock.

The agreement further provides the American State Bank of Minot, North Dakota, shall hold moneys in escrow and when \$50,000.00 is raised the Canadian-American Records Ltd. shall, upon its being organized, deliver to said party of the second part, one share of its common stock for each \$20.00 deposited by second party with the American State Bank.

We have, therefore, the following amounts authorized to be issued in stock before they have received value for the stock, namely, ten percent for services rendered by the individuals before incorporation, twenty percent as treasury stock and twenty-five percent to persons, including party of the second part, who advance the initial \$50,000.00. All of this is for stock where the corporation has received no value from the parties procuring the stock. It is further provided that the party of the second part shall receive common stock for each \$20.00 deposited, which would mean that he would received five shares of par value which would show that the stock is considerably watered.

We find a law in this state as well as in other states that: According to the weight of authority a corporation is not under any liability to pay for services rendered or expenses paid or incurred by the promoters in bringing it into existence. This citation is found in 14 C.J. page 282, paragraph 332, Note 61. Under said citation is found Supreme Court decision holding to that effect in the following states: Arkansas, Conn., Ga., Illinois, Indiana, Iowa, Ky., La., Mich., Minn., Missouri, New York, Texas, Utah, Vermont. We also find a court decision by the Court of the United States and of the courts of England and also from the following Canadian Provinces of Alberta, Manitoba, and Ontario. We call particular attention to the laws of Manitoba by the following decision of the court of that province. Colonial Assur. Co. v. Smith, 23 Man. 243, 12 DomLR 113, 24 WestLR 105, Von Hummell v. International Guarantee Co. 23 Man. 103, 10 DomLR 306, 23 WestLR 248, AnnCas. 1913E 1163; Re Crown Mutual Hail Ins. Col, 8 W.L.R., 18 Man. L.R. 51.

In 14 Corpus Juris 255, paragraph 289, we find the following: "Since the promoters of a corporation are not in any legal sense its agents before it comes into existence, it is a well-settled rule that a contract made by them, even though it may be made for and in the name of the proposed corporation, is not binding on the corporation when formed." Citing numerous cases under Note 57. Among them is the case of Cross v. Farmers' Elevator Company, 31 N.D. 116, 153 NW 279; Montgomery v. Whitbeck, 12 N.D. 385, 96 NW 327.

It then becomes necessary to point out that this proposed agreement is for the purpose of selling stock. For the consideration of such contract is, that they may receive stock upon the creation of the corporation. It, therefore, comes under the law of our state, section 10-0410 of the 1953 Supplement to the North Dakota Revised Code of 1943, which reads as follows:

No dealer or salesman shall offer for sale or sell any

securities within or from this state, except in transactions exempt under section 6-(10-0406), unless he is registered as a dealer or salesman pursuant to the provisions of this section."

Since the promoters offer stock in exchange for cash, it plainly comes within this statute and they must have licenses and be registered as provided by said section.

The courts of the State of Georgia in the case of Felton v. Highland Hotel Company, 165 Ga. 598, 141 S.E. 793, 57 A.L.R. 987 provides as follows:

Under the provisions of Section 13 of the law just cited (Laws 1920, p. 256), in whatever character or capacity they may appear, persons as well as firms and corporations who purpose either to issue or sell stock in an existing or proposed corporation must file with the securities commission the statement prescribed by law, and failure to file such statement avoids the subscription, thereby relieving the subscriber, and entitling him to the return of any payments made upon the illegal contract."

The text of this case fully supports the statement in the syllabus.

It is, therefore, the view of this office that the parties you mention in your letter of the fifteenth must register before they can sell the securities therein.

LESLIE R. BURGUM

Attorney General