SENATE . . . . No. 562

The Commonwealth of Massachusetts.

EXECUTIVE DEPARTMENT, BOSTON, May 22, 1913.

To the Honorable Senate and House of Representatives:

Herewith I return without my approval Senate Bill 415, being An Act Relative to the Issue of Stock and Bonds by Electric Light and Power Companies and to the Issue of Preferred Stock by Certain Corporations.

Chapter 725 of the Acts of 1912, Part 2, Section 4, provided that railroad corporations might issue bonds to the amount of twice their paid-in capital, provided that such bonds are secured by a mortgage.

The present bill grants this right to electric light and power companies but sweeps away the provision concerning mortgages. The bill says that such companies may issue mortgages, but does not obligate them to do so.

The practical effect of the bill is therefore a declaration by the Massachusetts Legislature that these public service corporations may bond their property to twice the amount of the capital, and to twice the amount now allowed by our laws, but without the safeguard of a mortgage.

The second section of the bill, by the use of the word "twice" after the words "exceeding at any time", enlarges the power to issue preferred stock until it may be double the common stock. The existing law, which is to be found in section one of Chapter 441 of the Acts of 1902, allowed the issue of preferred stock only up to the amount of the par value of the common. The provision for preferred stock was new in our law in 1902. There was an earlier provision

existing since 1870 providing for what was called "special stock" which, however, could only be issued under certain very carefully prescribed restrictions. While the Act of 1902 allowed preferred stock to an amount equal with the common, this section allows preferred stock to twice the amount of the common. For an illustration of the effect of the two sections thus far described, it may be noted that a corporation desiring to issue $900,000 of securities might divide them into bonds $600,000; preferred stock $200,000; common stock, $100,000. The title of the bill, which mentions only electric light and power companies as affected by the Act, is also to some extent misleading, since all companies acquiring any rights in the streets, such as the street railways, come within its provisions.

Section 3 of the bill changes radically the law as now fixed by section 58 of chapter 110 of the Revised Laws. Sections 58 and 59 impose a contingent liability for the debts and contracts of the corporation upon the president and directors when the "debts exceed its capital"; upon the president, directors and treasurer when the property conveyed in payment of stock is "not taken at a fair valuation"; upon the president, directors and other officers for the "debts contracted before the original capital has been fully paid in"; upon the stockholders or members of the corporation for "debts contracted before the original capital is fully paid in"; where "special stock" is created "until the special stock shall have been fully redeemed" and "for all money due the operatives for services rendered within six months before demand made upon the corporation and its neglect or refusal to make payment." Section 3 of this bill provides that all of the statutory liabilities above cited of section 58 may be defeated by covering the debts described by a mortgage or pledge "of all or any part of the property of the corporation," and such a course is absolutely and without limitation in the power of the corporation.

There is probably no restriction at common law upon the power of a corporation to mortgage a portion of its property. There may be some question as to the right and propriety in mortgaging all of its property, especially corporations of

this class referred to in the bill, but the requirements of section 58 may be entirely defeated by a mortgage of even a portion and it may be a small portion of the company's property, respecting which its right to mortgage may be unquestionable. The original necessity for section 12 of chapter 121, expressly permitting a mortgage and providing for the rights of the mortgagee, was solely for the purpose of enabling the corporation to mortgage all of its property and its franchise. The limitation of bonds in section one of the bill to twice the capital stock applies to bonds only, while section three now under discussion includes obligations of all other kinds. There is no restriction in the existing law nor in the present bill upon the amount of such obligations, except that which may be indirectly due to the contingent liability which section 58 imposes and which it is now proposed by this bill to virtually repeal.

The policy of the Commonwealth toward its public service corporations, in view of the fact that they are so largely and essentially monopolies, has been one of conservatism in respect to the issue of their securities, recognizing the importance of such restrictions to the interests of the customers of such companies, as well as of the investors whose money makes possible the existence of such companies and the extension of their facilities.

One purpose of the existing limitation upon the amount of bonds and preferred stock was undoubtedly to secure for the corporation the benefits resulting from the active interest of those possessing a substantial share in the securities of the company. Bondholders have no voting power, preferred stockholders frequently have none, that power being usually vested in holders of the common stock only, who, however, under this bill may have in all not more than approximately a ten per cent interest in the property. A larger interest responsible for the actual management of the property would undoubtedly tend to increase security for all classes of the company's investors. Control by a small interest invites more to stock speculation and corporate manipulation than to economical operation and management.

It is fair to say that nothing has yet occurred to indicate

a need by existing gas or electric light companies for abandoning the limitation in the present law. With rare exceptions, these companies are financed under existing laws by the issue of a single class of stock and not at all by bonds, nor are they likely to need such legislation for the promotion of the public interest, unless hereafter, through mismanagement or the issue of an undue burden of securities, their stock issuing credit shall become seriously impaired. The aggregate capital stock of the gas companies in this State is now $36,426,283, but they have only $1,644,000 bonds. The aggregate capital stock of the electric lighting companies is $26,647,250, but they have only $2,957,200 of bonds outstanding.

It will not answer my objections to say that these new issues are contingent upon the approval of the Gas and Electric Light Commissioners. The bill makes no such provision, and even if it be held that our existing law to this end will still be binding, even so, the Legislature, having now declared for the general principle of issuing twice the amount of bonds now allowed, cannot look to other public agencies to nullify its provisions and ignore its declaration of a perverted policy, when once that policy has become spread upon our statutes.

The bonds and stocks of our present electric light and power companies have been issued upon a conservative basis and are regarded as high-class securities. They have been bought by trustees and individuals upon the assumption that the Commonwealth would protect their intrinsic value and not permit it to be diminished through any wild cat scheme of financeering.

If our public service corporations are now to receive permission to swell their bond issues in some instances to double or more than double the present amount, then all outstanding issues of stock and bonds must suffer proportionately; and these securities, which have until now been held in high estimation, will depreciate.

Thus Massachusetts, now holding a most honorable position as regards the securities of her corporations, would stand as sponsor for a policy of inflated and insecure financeering.

Moreover, these present securities, being sound, are saleable at a low rate of interest. This interest is paid out of earnings and these are contributed by the public. Therefore the public is vitally concerned to keep these securities sound, and their interest rate low, so that the burden of interest charges borne by the public shall be low.

If you now weaken the securities of these corporations by permitting inflated issues of imperfectly secured bonds, then these bonds will not be saleable at a low interest rate and a higher interest rate must be guaranteed. The interest charges will immediately increase, and the public must contribute them through increased rates and poorer service.

I have watched with amazement the complacency with which this Legislature has favored several schemes of this same character; and the final enactment of this bill (the first of its class to reach me) bodes ill for the financial future of this Commonwealth, unless the people succeed in holding their representatives to a higher ideal of public duty.

If the Legislature is acting under the impression that this policy can be foisted upon the State, then it greatly underestimates the intelligence and the temper of the people of Massachusetts.

EUGENE N. FOSS.