

The device of raising capital by the sale of contracts, or "bonds," is the product of the past ten years, and appears to be a New Zealand invention. This method of finance has been very successful in encouraging investment in land-utilization companies, and the aggregate of "bond" moneys raised by such companies has been substantially greater than that raised by share companies of the orthodox type. The organization and practice of companies using this method of raising finance differ in detail, but exhibit certain general well-defined characteristics.

The common practice is that a small group of people form a company which purchases, or agrees to purchase, an area of land, or obtains an option over land. This may, or may not, be free from encumbrances. Normally, though not universally, the paid-up capital is small, both absolutely and in relation to the proposed undertaking. The company then proceeds to issue a "prospectus" inviting the public to subscribe for "bonds" or other forms of "contract."* Apparently the "sales resistance," especially of the experienced investor who normally buys securities through his broker, is too strong to permit of the sale of any considerable number of bonds without a special sales organization, and the sale of bonds tends to become the function of specialized concerns. These employ "high-powered" salesmen who have usually adopted the method of door-to-door canvass or "hawking."

In the formation procedure the bond-selling company may be a private company preceded by other companies or syndicates which are interposed between the original vendor of land and the bond-issuing company. At a later stage the bond-issuing company may be converted into a public company and issue a prospectus inviting subscription for shares. By the device of a private company, and of precedent syndicates and companies, transactions in land and the particulars of other material contracts may be effectively concealed.

Usually the value of the bond issues provided for (and issued) is very much greater than the nominal capital, and especially than the subscribed or paid-up capital. This is illustrated in Table II (page 29). The summarized results are as follow:—

The original nominal capital of fifteen land-utilization companies was approximately £210,000, the subscribed capital £147,000, and the paid-up capital £114,000, of which £54,000 was paid up in cash and £60,000 for considerations other than cash. According to the latest return the nominal capital was £860,000, subscribed capital £657,000, and paid-up capital £601,000. Of the paid-up capital £315,500 was received in cash and £285,600 for considerations other than cash. The aggregate bond-moneys received amounted to £5,265,591, and the value of bonds the issue of which was provided for was about £7,165,000. The value of bond issues provided for up to June, 1934, was over sixty times the original paid-up capital, including shares issued for considerations other than cash, and nearly twelve times the paid-up capital at that date. The amount received from the sale of bonds in June, 1934, was over forty-six times the original paid-up capital, and nearly nine times the paid-up capital at that date.

In considering the implications of the above figures it should be noted that in many cases the value of the consideration for which fully-paid shares have been received is entirely fictitious, while it is by no means certain that shares described as paid up in cash always represent a genuine cash transaction. It is interesting to note that included in the above amount of £285,600 for consideration other than cash are the shares of one company, represented as £146,000 fully paid up, which are issued in exchange for shares to the value of £13,007 in another company governed by the same directors, the assets of which were (fictitiously) written up eleven-fold.

Bonds are issued in denominations varying from £20 to £55 per bond. They consist of a contract to transfer to the bondholder on a specified date (or to a trustee appointed to look after his interests) a certain unencumbered area of land duly planted and maintained. In the case of forestry companies, the contract covers an acre of land per bond. In the case of flax, tobacco, and tung-oil companies, the area is usually one-quarter, one-third, or one-half acre per bond. The contract covers an agreement to replant areas which have failed or been destroyed. In some cases the company agrees to plant an area in excess of that covered by bonds sold, as an additional security.

The bondholder does not normally have title to a particular individual acre, but he shares his rights in common with other bondholders over the particular area of land to which his bond-series relates. His right consists in a share in a particular area in the proportion that his holding of bond bears to the total bonds issued against the area, and in an equivalent proportion of the proceeds from the realization of the area. In some of the earlier issues of forestry companies, they contracted to pay interest on bonds. Forestry companies soon abandoned this practice, but it is still common for tobacco, tung-oil, and flax companies to pay interest for a stated period of years, at the end of which the plantations are expected to be ready for realization.

In some cases provisions relating to the transfer of title are ambiguous, and in one or two cases the bondholders have no title to the land, but only to the proceeds from the crops when they are marketed.

The function of the "parent" company is to acquire the area, sell or arrange for the sale of bonds, plant the area as bonds are sold, and maintain it until the lands are transferred. It makes its profits out of the difference between the value of bonds sold and the sum of the costs involved in promotion, land-purchase, bond-selling, planting, administration, and maintenance.

*The use of the term "contract" to describe the subject-matter of a subscriber's interest is of recent adoption, and the company's officials tend to shelter behind it when the question of the precise nature of the instrument is discussed. As between salesman and intending purchaser, however, the term "bond" or "debenture" has been, and is, used, and the idea carefully fostered that the instrument represents a "gilt-edged" class of security. This idea is strengthened by the use of a prospectus, which is a procedure legally necessary to the sale of debentures and such securities to the public, but quite unnecessary, legally, to the procuring of "contracts" in series.