[HIGH COURT OF AUSTRALIA.]

KNOWLES . . . . . APPELLANT;
DEFENDANT,

AND

BALLARAT TRUSTEES, EXECUTORS AND AGENCY COMPANY LIMITED AND OTHERS . . . . . RESPONDENTS.
PLAINTIFFS AND DEFENDANTS,

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HASLEM . . . . . APPELLANT;
DEFENDANT,

AND

BALLARAT TRUSTEES, EXECUTORS AND AGENCY COMPANY LIMITED AND OTHERS . . . . . RESPONDENTS.
PLAINTIFFS AND DEFENDANTS,

ON APPEAL FROM THE SUPREME COURT OF VICTORIA.

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MELBOURNE, *Sept.* 12, 13, 14, 15, 18; *Oct.* 13.

Griffith C.J., Barton, Isaacs, Gavan Duffy and Rich JJ.

*Will—Tenant for life and remainderman—Shares in company—Dividend—Accumulated profits—Distribution of assets—Income or capital.*

For the purpose of determining the rights of life tenants and remaindermen entitled under a will respectively to the income and capital of shares in a company which has power to increase its share capital, the term capital is not necessarily limited to sums of money appropriated by the company out of its accumulated profits to an increase of its share capital and in that form distributed among the members, but may also include payments of cash made by the company out of such profits to its members if such payments are in fact intended to be a distribution of capital as distinguished from dividends.

So *held*, by *Griffith* C.J. and *Barton*, *Gavan Duffy* and *Rich* JJ. (*Isaacs* J. dissenting).

*Bouch* v. *Sproule*, 12 App. Cas., 385, discussed and distinguished.

A company which had power to increase its share capital in addition to paying a "dividend" and a "bonus," made a distribution in cash out of its accumulated profits among its members equal in amount to the amount paid up on the shares, and purported to do so by way of "distribution of assets."

*Held*, by *Griffith* C.J. and *Barton*, *Gavan Duffy* and *Rich* JJ. (*Isaacs* J. dissenting), that under the circumstances the sum received pursuant to such "distribution of assets" by a trustee in respect of shares to the income of which life tenants were under a will entitled should be deemed to have been paid to and accepted by the trustee as a distribution of capital of the company, and should, therefore, as between the life tenants and the remaindermen be treated as capital.

Decision of the Supreme Court of Victoria: *In re Hassall; Ballarat Trustees, Executors and Agency Co. Ltd.* v. *Haslem*, (1916) V.L.R., 29; 37 A.L.T., 139, affirmed.

APPEALS from the Supreme Court of Victoria.

Thomas Hassall, who died on 10th July 1898, by his will, dated 28th June 1898, appointed the Ballarat Trustees, Executors and Agency Co. Ltd. his executors and trustees. He gave to Thomas Richard Haslem "as long as he lives the net income derived from 1,000 of the shares I hold in the Melbourne Tramway and Omnibus Co. Ltd. (hereinafter called the Tramway Company) and at his death I give the said shares to his children but failing child or children the said shares shall revert to my estate." He further directed that the income of his residuary estate should be divided in equal shares annually amongst a number of persons with remainders over. Part of the assets of the testator at his death consisted of 13,364 shares in the Tramway Company of which in 1913 the trustees sold 9,000 shares.

An originating summons in the Supreme Court was taken out by the trustees for the determination of, among other questions, the question, substantially, whether a sum of money received by the trustees from the Tramway Company as being a "distribution of assets" at the rate of 10s. per share was to be treated as income and paid to the life tenants, or as capital and held for the remaindermen.

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The defendants to the originating summons were Thomas Richard Haslem; Joseph Gilbert Haslem, who was sued as representing himself and any other children of T. R. Haslem; Henry Knowles, who was sued on behalf of himself and all other persons beneficially interested in the income of the estate of the testator; and the Ballarat District Benevolent Asylum and Lying-In Hospital, which was sued on behalf of itself and all other charitable institutions and churches and all other persons beneficially interested in the residue of the testator's estate.

The circumstances under which the distribution was made by the Tramway Company are fully stated in the judgments hereunder. It is only necessary to add that the articles of association of the Tramway Company contained the following clauses :—

"35. The directors may with the sanction of a special resolution of the Company previously given in general meeting increase its capital by the issue of new shares such aggregate increase to be of such amount and to be divided into shares of such respective amounts as the Company in general meeting directs or if no direction be given as the directors think expedient."

"77. The directors may declare a dividend to be paid to the members in proportion to their shares.

"78. No dividend shall be payable except out of the profits arising from the business of the Company.

"79. The directors may out of the profits of the Company, before declaring any dividend, make such provision as they think proper, as a reserve fund to meet contingencies, or for equalizing dividends or for return of capital, or for repairing, maintaining or renewing the works connected with the business of the Company or any part thereof, and for such other purposes as the directors shall think conducive to the interests of the Company, and to invest the several sums so set aside upon such investments (other than shares of the Company) as they may think fit, and from time to time to deal with and vary such investments and dispose of all and any part thereof for the benefit of the Company, and to divide the reserve fund into such special funds as they think fit, with full power to employ the assets constituting the reserve fund in the

business of the Company, and that without being bound to keep the same separate from the other assets."

The summons was heard by the Full Court, which held that the money received by the trustees should be treated as capital: *In re Hassall; Ballarat Trustees, Executors and Agency Co. Ltd.* v. *Haslem* (1).

From that decision Henry Knowles and Thomas Richard Haslem appealed to the High Court. The two appeals were heard together.

*Weigall* K.C. (with him *Ian Macfarlan*), for the appellant Knowles. By a gift of the income from shares of a company such as the testator has made in this case, he means that all lawful distributions of assets made by the Company, which are not returns of share capital authorized by the *Companies Act*, in respect of the shares while it is a going concern are to go to the life tenant. That is an established principle of construction. A company can lawfully distribute only its profits, and all distributions of profits are included in what are called dividends or bonuses and are to be treated as income and not capital. There are only two ways in which a company which has power to increase its capital can, while it is a going concern, dispose of its accumulated profits among its shareholders. It can either appropriate them to an increase of its share capital or it can distribute them as dividends or bonuses among its shareholders: *Bouch* v. *Sproule* (2). It cannot at once distribute its profits in specie among its shareholders and treat that which is distributed as capital. Unless the company has *de jure* appropriated its accumulated profits to capital they remain undivided profits. If the company legally distributes those undivided profits among the shareholders, and whether the directors call the distribution a dividend or a bonus or a distribution of assets, the distribution remains a distribution of hitherto undistributed profits. [He referred to *Mitchell* v. *Hart* (3); *Jarman on Wills*, 6th ed., vol. II., p. 1223; *White and Tudor's Leading Cases*, 8th ed., vol. I., p. 877; *In re Alsbury*; *Sugden* v. *Alsbury* (4); *In re Palmer*; *Palmer* v. *Cassel* (5); *In re Woolcott*; *Woolcott* v. *Woolcott* (6); *In re Armitage*;

(1) (1916) V.L.R., 29; 37 A.L.T., 139.
(2) 12 App. Cas., 385.
(3) 19 C.L.R., 33.
(4) 45 Ch. D., 237, at p. 243.
(5) 28 T.L.R., 301.
(6) (1905) V.L.R., 599, at p. 605; 27 A.L.T., 19.

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*Armitage* v. *Garnett* (1); *In re Malam*; *Malam* v. *Hitchens* (2); *In re Piercy*; *Whitwham* v. *Piercy* (3).]

[RICH J. referred to *In re Thomas*; *Andrew* v. *Thomas* (4); *McLouth* v. *Hunt* (5); *In re Hopkins' Trusts* (6).

ISAACS J. referred to *Carson* v. *Carson* (7).]

The intention of the company is only material for the purpose of ascertaining whether there was an actual distribution intended. If the facts are looked at, there appears to be no reason for suggesting that the distribution now in question should be treated otherwise than as income.

[RICH J. The most material evidence as to the intention of the Company, namely, the minutes of the meetings of directors at which the payments in question were resolved on and those of the general meetings of the Company at which the directors' reports were adopted, is absent.]

*Davis*, for the appellant Haslem. The words of the will are colourless as to what is to be treated as income from the shares. The real question is: Has the Company validly converted the money which was afterwards distributed to the shareholders into capital —that is, share capital? That is distinctly laid down in *Bouch* v. *Sproule* (8). Unless it has done so, the money cannot be divided as capital. It is not competent for a company to deal with money as capital which is not capital. The intention of the company is immaterial unless it is validly expressed. The lawfulness of this distribution is not questioned, and therefore the only intention of the Company can have been to make a payment in the nature of a dividend. Where a company has power to increase its capital by the issue of shares and has not done so, the creation of reserves out of profits cannot in any circumstances convert the accumulated profits into capital, and any part of those reserve funds distributed among the shareholders while the company is a going concern is income.

[RICH J. referred to *In re Bridgewater Navigation Co.* (9).

(1) (1893) 3 Ch., 337, at p. 344.
(2) (1894) 3 Ch., 578.
(3) (1907) 1 Ch., 289.
(4) (1916) 1 Ch., 383; 32 T.L.R., 530.
(5) 154 N.Y., 179.
(6) L.R. 18 Eq., 696.
(7) (1915) 1 I.R., 321.
(8) 12 App. Cas., 385.
(9) (1891) 2 Ch., 317.

ISAACS J. referred to *In re Rolland*; *Trustees, Executors and Agency Co.* v. *Black* (1).]

*Mitchell* K.C. (with him *Braham*), for the respondent trustees. The question is whether the payment made by way of "distribution of assets" was a payment of a dividend pursuant to article 77, or was a payment either under article 79 or by way of distribution of capital. The rule laid down in *Bouch* v. *Sproule* (2) is not exhaustive, and in unusual circumstances like those of the present case there may be a third alternative case.

*Walker*, for the respondent Haslem. The payment made by way of a "distribution of assets" was not a dividend but was a distribution of capital, that is, a distribution of the common fund or stock of the Company. The payment was not made as a dividend pursuant to article 77, but the directors were anticipating the liquidation of the Company and the work of the liquidator. See sec. 186 of the *Companies Act* 1915. The tenant for life is not entitled to anything except payments made by way of dividend: *In re Armitage*; *Armitage* v. *Garnett* (3); *Ward* v. *Combe* (4); *Gibbons* v. *Mahon* (5). Even if the payment was called a dividend the facts must be looked at to see whether it was in fact a dividend: *In re Thomas*; *Andrew* v. *Thomas* (6)).

[ISAACS J. referred to *In re Crichton's Oil Co.* (7); *Straker* v. *Wilson* (8).]

*J. R. Macfarlan*, for the respondent Hospital. The intention of the testator was that the life tenants should have what was paid by the Company as dividends and bonuses. In determining what in fact the Company did, all the circumstances must be looked at. The fact that the Company has or has not the power of increasing its share capital is only one of the circumstances. The decision in *Bouch* v. *Sproule* (9) is merely that in the circumstances of that case the distribution was by way of capital. It is not a decision, nor is

(1) 30 N.Z.L.R., 494.
(2) 12 App. Cas., 385, at p. 397.
(3) (1893) 3 Ch., 337, at p. 345.
(4) 7 Sim., 634.
(5) 136 U.S., 549.
(6) (1916) 1 Ch., 383, at p. 392.
(7) (1902) 2 Ch., 86, at p. 95.
(8) L.R. 6 Ch., 503.
(9) 12 App. Cas., 385.

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it a part of the *ratio decidendi*, that a company having power to increase its share capital cannot have capital which is not share capital, and it recognizes that such a company may have capital in addition to and apart from its share capital. That case does not lay down a general principle of law applicable to all cases. The decision was that in the case of such a company the mere fact that it has made a distribution which it calls a dividend does not necessarily make it a dividend so as to give it to the tenant for life. The passage in Lord *Herschell's* judgment (1) following his quotation from the judgment of *Fry* L.J. for the Court of Appeal (*In re Bouch*; *Sproule* v. *Bouch* (2) ) is quite unnecessary to the decision of the case, and should be treated as *obiter*.

[GRIFFITH C.J. referred to *Dominion of Canada* v. *Province of Ontario* (3).]

That passage is quite inconsistent with all prior authorities. [He referred to *Irving* v. *Houston* (4); *Price* v. *Anderson* (5); *In re Barton's Trust* (6).]

[ISAACS J. referred to *In re Accrington Corporation Steam Tramways Co.* (7); *In re Evans*; *Jones* v. *Evans* (8).]

The circumstances which show that the payment was a distribution of capital are that the fund distributed was the accumulation of past years, that the accumulation had been going on for a long period, that the Company was a short-lived one, that the distribution was called a " distribution of assets " and not a dividend, and was distinguished from a dividend and a bonus, that what was being done was practically a winding up of the Company, that the proportion borne by the distribution to the paid-up capital was so large, and that the accumulations had been used as a dividend-producing fund and for capital purposes.

*Davis*, in reply, referred to *Baroness Wenlock* v. *River Dee Co.* (9); *Palmer's Company Precedents*, 11th ed., Part I., pp. 30, 633; *Ooregum Gold Mining Co. of India* v. *Roper* (10).

(1) 12 App. Cas., at p. 398.
(2) 29 Ch. D., 635, at p. 653.
(3) (1910) A.C., 637.
(4) 4 Paton Sc. App., 521.
(5) 15 Sim., 473.
(6) L.R. 5 Eq., 238.
(7) (1909) 2 Ch., 40, at p. 48.
(8) (1913) 1 Ch., 23.
(9) 36 Ch. D., 675*n*.
(10) (1892) A.C., 125.

[ISAACS J. referred to *Re Paget*; *Listowel* v. *Paget* (1).]

*Weigall*, in reply, referred to *Palmer's Company Precedents*, 11th ed., Part I., p. 861; *Trevor* v. *Whitworth* (2).

*Cur. adv. vult.*

The following judgments were read :—

GRIFFITH C.J. The question raised upon these appeals is whether two distributions of funds made by the Melbourne Tramway and Omnibus Co. to its members in the years 1914 and 1915 are, in the case of shares settled upon successive trusts, to be regarded as payments by way of income or as accretions to the capital of the trusts. The question is one between life tenant and remainderman, and not between the members of the Company *inter se*, although in the long argument to which we have listened the two questions have been a good deal confused with one another.

Thomas Hassall, who died in 1898, by his will made a gift in these words : " I give to Thomas Richard Haslem as long as he lives the net income derived from 1,000 of the shares I hold in the Melbourne Tramway and Omnibus Company Limited and at his death I give the said shares to his children." He made a gift of the residue of his estate, which included a large number of shares in the same company for the benefit of several persons, of whom the appellant Knowles is one, for life, with remainders over. The respondents the Ballarat Trustees, Executors and Agency Co. are the trustees and executors of the will. The issued shares in the Company are 960,000 of £1 each, paid up to the extent of 10s. per share.

I take the following statement of the facts relevant to the nature of the Company and of the fund from which the payments in question were made from the judgment of *Cussen* J. :—" The Company is and was, as he " (the testator) " must be taken to have known in 1898, when he died, a company of exceptional character. It has and then had a paid-up capital which, compared with its undertaking, is very small. Its chief asset was a lease of about thirty years' duration, ending in 1916, which gave it a right to use tramcars

(1) 9 T.L.R., 88.

(2) 12 App. Cas., 409.

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in the streets of Melbourne and some of the surrounding municipalities. The tramways were constructed by means of moneys borrowed by a trust formed by a combination of representatives of these municipalities, and the Company had to provide from its earnings interest on its borrowed moneys, and also a sinking fund: See *Melbourne Tramway &c. Co.* v. *Mayor &c. of Fitzroy* (1). For this and other reasons it had large liabilities, actual or possible, and it was thought desirable, both before testator's death and afterwards, to accumulate large reserves. The Company was prosperous, and this almost necessarily resulted (having regard to the fact already mentioned that the paid-up capital was very small) in the shareholders getting dividends which represented a high percentage on that paid-up capital, and consequently in a large increase in the value of the shares due to these dividends, the anticipation of future similar dividends, and also to the accumulation of large reserves.

"As the expiration of the lease was drawing near, and no renewal had been arranged, there was no longer, in the opinion of those managing the affairs of the Company, any necessity to retain the large reserves previously mentioned, and the question of their distribution came to be considered. It seems clear, even if the Company is not wound up on the expiration of the lease, that the character of its business must in the near future be profoundly changed. In these circumstances, the directors determined to use their power of dividing moneys amongst shareholders for the purpose, not only of declaring what are ordinarily called dividends and bonuses for the particular years 1914 and 1915, but also for the purpose of distributing almost the whole of the reserve funds, amounting to over one million pounds, amongst the shareholders.

"This distribution represented in, though perhaps not for, the years 1914 and 1915, the payments of ten shillings and eleven shillings per share respectively already referred to. These payments were undoubtedly made out of accumulations of profits, but they seem to possess the following characteristics—they were made out of accumulations extending over the whole term of the leases; they were very large, representing together more than twice the

(1) 25 V.L.R., 5; 21 A.L.T., 20.

paid-up capital; they were made by a company of a special character, the nature of whose chief asset (which was of a wasting character, and which is now rapidly approaching extinction) I have already referred to; they were made out of funds which are the result of, and may be said in fact to have taken the place of, that asset, and, finally, they were made in anticipation of either a winding-up or a profound change in the character of the business to be carried on by the Company."

The question to be determined by us depends upon the intention of the testator as expressed in his will. What does a testator mean when he gives the income of shares in a joint stock company to one set of persons and the capital or corpus to another? *Primâ facie*, I should think the answer to this question is that he intended that the remainderman should have the benefit of the aliquot part of the assets of the company of which the testator was the beneficial owner, however large or small the value of that aliquot part may be, and that the tenant for life should have the benefit of any annual or periodical payments made by the company to its members by way of dividend in the ordinary acceptation of that term. If he means that the tenant for life is to have his share of all the profits made by the company during his life, he can, no doubt, say so. But the word "income" does not of itself connote that idea. I will return to this point later.

I propose to follow the course adopted by *à Beckett* J. in the Supreme Court, and to approach the question upon the general principles applicable to ownership of property, including the property of joint stock companies, and the nature of the ownership of the individual members of such companies, and to draw such conclusions as may be drawn from them with the aid of reason and common sense, and then to inquire whether the Court is precluded by authority from acting on the conclusions so drawn. Mr. *Weigall* in one part of his argument, and to a lesser degree Mr. *Davis*, invited us to follow the first part of this road, but finally they both appealed to authority and nothing else.

I remark in the first place that the term "share," as a word of the English language, apart from any artificial meaning given to it under the laws relating to joint stock companies, denotes an

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aliquot part of a common fund or other common property of which several persons are joint beneficial owners. In the case of joint stock companies the term has a secondary meaning, namely, a legal entity which connotes a right to an ascertained part of the property of the company and is evidenced by documents, which include a share register and share certificates.

It is common knowledge that the market value of shares, using the term in the latter sense, is estimated on this basis, and the aggregate value of the assets of a company is commonly estimated by multiplying the value of a single share by the number of shares. It is also common knowledge that the market value of a share as property, that is, as capital of the shareholder, depends to a large extent upon the probable income to be derived from it by way of dividend. If the company has accumulated part of its profits and invested the accumulations in income-earning property, the amount which it will have for distribution as dividends will be proportionately increased, and the right to share in such distributions adds correspondingly to the capital value of the individual shares.

When, therefore, shares are settled upon successive interests, the settlor may be presumed to intend that what he settles is, in substance, the capital value of the aliquot part of the company's property which is evidenced by the shares which he settles, so that the tenant for life shall take the income derived from that capital value, and the remainderman shall take the capital value intact. If the shares are sold, this is the obvious consequence. The appellants ask us to disregard all these matters, and to deal with the case upon certain technical rules which they say compel us to do so.

Their contention, shortly put, is that it is necessary first to ascertain whether a particular part of the funds of a company is to be regarded in the abstract as capital or as income; that all profits are to be regarded as income until they have been formally, in some manner authorized by positive law, converted into capital, whatever that means; and that all payments made out of unconverted profits must be treated as dividends. This argument involves two obvious fallacies, arising from the common error of using the same word in different senses in the same argument. The word "capital" is used in the double sense of "authorized share capital" and of

"capitalized profits," which are quite different concepts. And the word "dividend" is used in the double sense of such a periodical distribution of profits as is commonly called a dividend, and as including any distribution of a fund.

I have already adverted to the danger of confounding a controversy which may arise between members of a company *inter se* on the question whether profits have been capitalized, with a controversy on the question whether a sum of money paid to the trustees of shares held for successive interests is paid as income, or as an accretion to the capital of the trust.

The first controversy rarely arises, and can, indeed, only arise, if under the constitution of the company special rights are given to certain members in respect of uncapitalized profits. For ordinary purposes it is quite immaterial how they are regarded.

An instance of such a controversy is afforded by the case of *In re Bridgewater Navigation Co.* (1). The articles of association of that company authorized the company by resolution to increase its capital (*i.e.*, by the issue of new shares). The articles also authorized the directors in priority to any dividend to set aside out of "profits" any sums as a reserve fund for any purpose of the company, and to invest the sums so set aside, and directed that any interest derived from such investments should be dealt with as profits, and that subject thereto "the entire net profits of each year" should belong to the shareholders. Subsequently the company increased its capital by the issue of new shares carrying a preferential dividend. Reserve funds were created, to which, year by year, part of the profits was carried, and the remaining profits, after payment of the preferential dividend, were distributed among the ordinary shareholders.

The company's undertaking was eventually sold by virtue of a special Act of Parliament at a price which left a surplus in excess of the liabilities of the company and the amount of both the ordinary and preferential shares. Large sums were standing to the credit of the reserve funds. They were not represented by any separate investments, but were merely book-keeping entries represented by property of various kinds.

(1) (1891) 2 Ch., 317.

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The preferential shareholders claimed that they were entitled as shareholders to share in the distribution of all the assets of the company, including that part which represented accumulated profits. The ordinary shareholders, on the other hand, claimed that the provisions of the article under which they were entitled to the entire net profits of each year applied only to ordinary shareholders, and still attached to so much of the surplus funds as represented such profits.

The Court of Appeal accepted the latter view, on the ground that the money standing to the credit of the reserve funds still represented undrawn profits uncapitalized, and was divisible amongst the ordinary shareholders only. The question as to whether undistributed profits can, under any circumstances, be treated as capital was discussed at length, but it did not occur to anyone to suggest that the only way in which they could be treated as capital was by converting them into additional share capital. Sir *Horace Davey* on this point only contended that a clear intention to treat them as capital must be shown.

*Lindley* L.J. said (1) :—" It remains, however, to be considered whether these undrawn profits have been capitalized or so dealt with that they have become the property of both classes of shareholders instead of the property of the ordinary shareholders only. Carrying undrawn profits to a suspense account or to a reserve account does not necessarily change their character, still less their ownership ; they remain the undrawn profits of those persons to whom they belonged, dedicated, no doubt, to certain purposes and applicable to those purposes, but not otherwise altered in their character or ownership. If the purposes for which such profits are set apart fail, or if the profits are not required for such purposes, they become divisible, not as capital, but as undrawn profits. When capital and profits belong to the same persons and in the same proportions, it becomes unimportant to distinguish the one from the other, and capitalization for convenience may be inferred from slight evidence. But when capital and profits belong to different persons, or to the same persons in different proportions, the effect of capitalizing profits is to change their ownership, and an intention

(1) (1891) 2 Ch., at p. 327.

to do this must be shown before conversion of profits into capital can be properly inferred."

The learned Lord Justice, it will be observed, points out that when capital and profits belong to the same persons and in the same proportions capitalization "for convenience" may be inferred from slight evidence (*cf.* the language of *Fry* L.J. in *In re Bouch*; *Sproule* v. *Bouch* (1), where he pointed out that the manner in which the Bank of England had dealt with profits had more than once been treated as converting them into capital). The learned Lord Justice was speaking with reference to the controversy then before the Court, which was whether such a conversion had taken place as to deprive the ordinary shareholders of their exclusive vested right to a fund which represented the entire net profits after payment of dividends.

*Lopes* L.J. concurred in the judgment of *Lindley* L.J. *Kay* L.J. pointed out that a transaction authorized by a resolution of a general meeting to which he referred proved conclusively that the shareholders did not consider that the act of reserving the funds had converted them from income into capital. He then examined the evidence, and found that there was nothing else to show an intention to convert.

Before the principle of this case can be applied to a case as between tenant for life and remainderman it must be shown that the tenant for life has a vested interest in accumulated profits which cannot be divested from him. It is clear that he has no such interest.

I will next advert to the right of a joint stock company to deal with its own property. In my judgment a joint stock company has all such ordinary rights of ownership as are necessary to enable it to do what is fairly and reasonably necessary to effectuate the objects for which it is formed, except so far as such rights are limited by positive law or by the mutual contract between its members evidenced by the memorandum and articles of association (*Attorney-General* v. *Great Eastern Railway Co.* (2)). Thus a joint stock company is prohibited from returning its subscribed capital except under certain conditions. It is, of course, common knowledge that the purposes to which the funds of a company may be applied are limited by its memorandum of association, and that the mode of

(1) 29 Ch. D., 635, at p. 656.

(2) 5 App. Cas., 473.

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application may be controlled by the articles. But, with these limitations, a company, like any other owner of property, may do what it will with its own. In the case of *In re Patent File Co.*; *Ex parte Birmingham Banking Co.* (1), *James* L.J. said :—" By the law of England a body corporate can hold property and dispose of it as freely as an individual, unless it is specially prohibited from so doing." The question in that case was as to the power of a company to mortgage its property. *Mellish* L.J. said (2) :—" It was urged that no company can mortgage unless expressly authorized to do so. Now, the company has property which it is authorized to deal with, and I should say that the true rule is just the contrary, namely, that the company can mortgage unless expressly prohibited from doing so." The learned Lords Justices did not, in my opinion, mean to suggest that a company could mortgage its property except as incidental to carrying out the purposes for which it is incorporated. Subject, then, to such restrictions as I have mentioned, a company may sell its real and personal property and dispose of its funds as it likes. I take the case of a company constituted (like the Melbourne Tramway and Omnibus Co.) for a definite purpose, as, for instance, a one-ship company, which is a very common form of investment in the United Kingdom. Suppose the ship to be lost and its value paid to the company by the insurers. Suppose also that it has no creditors, and that there are ten shareholders each holding one-tenth of the shares. Subject to any question that might be raised as to such part of the fund as is equal to the subscribed capital, I can see no reason why the shareholders should not resolve to divide the fund equally between them without formally winding up the company. The case of *Burland* v. *Earle* (3) establishes that a Court cannot interfere with the internal management of companies acting within their powers. It was contended that the case of *Baroness Wenlock* v. *River Dee Co.* (4) laid down the rule that a joint stock company may not do anything which it is not expressly authorized to do by its articles. All that was decided in that case was that on a proper construction of the private Acts of Parliament by which a company was governed it had no power

(1) L.R. 6 Ch., 83, at pp. 86-87.
(2) L.R., 6 Ch., at p. 88.
(3) (1902) A.C., 83.
(4) 10 App. Cas., 354.

to do the particular act the validity of which was impeached. In the case of *Irvine* v. *Union Bank of Australia* (1) it appeared that the directors of a company had power to borrow money to a limited extent. It was held by the Judicial Committee that the limitation of the power of borrowing was merely a limitation of the power of the directors, and was not part of the constitution of the company, and that a borrowing by the directors of the company in excess of the limit might be ratified by the shareholders at a general meeting. Other cases are to the same effect.

It follows, in my opinion, that a distribution of the assets of a company not forbidden by law or by its constitution is within the general powers of the company, and that the Court cannot interfere with such disposition.

When, therefore, a company disposes of part of its assets by distributing them, as such, amongst its members to be held by them in lieu, wholly or in part, of the share of those assets to which they are entitled by virtue of their membership, the nature of the ownership is not changed. The property of the shareholders is the same in value and character as it was before the distribution. The only change is in the form in which that property is held.

It is an accepted general rule applicable to the construction of gifts of shares in joint stock companies upon successive interests that the donor is to be taken to have had regard to the common knowledge as to the internal management of joint stock companies, and to the well-known fact that under the ordinary constitution of a company (in this case its actual constitution) the directors have a discretionary power to make periodical appropriations of a portion of the profits by the name of dividend or bonus, and that a member's right to claim a dividend is dependent upon the exercise of that power.

In the present case, the Company, in 1914, under the circumstances already recited, distributed amongst its members out of money standing to the credit of its reserve funds and representing accumulated profits, a sum of ten shillings per share (equal to the whole paid-up capital), and in the following year out of the same money a further sum of eleven shillings per share.

(1) 2 App. Cas., 366.

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The actual minutes of the resolutions of the directors under which the payments were made are not in evidence, nor are the minutes of the annual general meetings of the shareholders held after the distributions had been respectively declared, to which the action of the directors was reported. But it is not suggested that there was any dissentient voice among the members. We are not, however, without information as to what the directors did, for it appears that on 1st July 1914 a circular was sent to each member of the company to the following effect :—

"Dear Sir,—Enclosed please find a cheque for

Dividend of 6d. per share

Bonus of 6d. per share

Distribution of assets, 10s. per share,"

carrying out the amounts according to the number of shares held by the member.

Upon these facts it appears to me that one conclusion only can be drawn if the view of the law which I have expressed is correct, namely, that the directors of the Company declared a dividend and a bonus, each of 6d. per share, and distributed a sum of 10s. per share by way of a partition of assets.

When the trustees of the will received this sum I think that they were bound either to accept the payment on the terms in which it was expressed to be made or to return it. *Solvitur in modo solventis.* They could not accept the 10s. per share as a sum given to them by way of capital, that is, for the joint benefit of all the beneficiaries of the trust, and then treat it as a payment made for the benefit of the tenant for life only. This would be so whether the payment was or was not proper as an act of administration of the Company's funds. The exercise by the directors of their discretion to declare or not to declare dividends or bonuses, which is essential to the concept of a dividend or bonus, cannot, when they say they do not intend to declare a dividend or bonus, be converted by the recipient into an exercise of a power to do that which they expressly say they do not intend to do.

What answer then is offered to these conclusions ? It is contended that we are bound by the decision of the House of Lords in the

case of *Bouch* v. *Sproule* (1), a case which has, in my opinion, been much misunderstood by some learned text-writers, and requires careful examination. In that case the directors of a joint stock company which had power to increase its capital by the issue of new shares proposed to distribute certain accumulated profits as "a bonus dividend," to allot new shares (partly paid up) to each shareholder, and to apply the bonus dividend in part payment of the new shares. The articles of the company authorized the directors before recommending a dividend to set aside out of the profits such sums as they might think proper "as reserve funds for meeting contingencies and equalizing dividends and for repairing or maintaining the company's works." They also authorized the company—a power which it had previously exercised—to increase its capital by the creation and allotment of new shares to its members according to their respective interests and crediting them with a sum as paid on each share from its reserved or undivided profits. I will read from the judgment of *Stirling* J. in *In re Malam*; *Malam* v. *Hitchens* (2) as to the effect of the decision of the House of Lords:—"The general principle applicable is thus stated in *Bouch* v. *Sproule* (3): 'When a testator or settlor directs or permits the subject of his disposition to remain as shares or stock in a company which has the power either of distributing its profits as dividends, or of converting them into capital, and the company validly exercises this power, such exercise of its power is binding on all persons interested under him, the testator or settlor, in the shares, and consequently what is paid by the company as dividend goes to the tenant for life, and what is paid by the company to the shareholder as capital, or appropriated as an increase of the capital stock in the concern, enures to the benefit of all who are interested in the capital.' It was further laid down by the House of Lords in the same case that in considering whether a company has distributed its accumulated profits as dividends or converted them into capital regard must be paid both to the form and the substance of the transaction; and that House, upon the question of fact, came to a different conclusion from the Court of Appeal, and held that shares allotted, under circumstances

(1) 12 App. Cas., 385.
(2) (1894) 3 Ch., 578, at p. 585.
(3) 12 App. Cas., at p. 397.

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which bear a resemblance to those of the present case, were an accretion to the corpus of the testator's estate, to no part of which the tenant for life was entitled. The principle of law thus laid down is binding on me; the decision on the question of fact is not, unless indeed the facts be substantially the same."

The material facts of that case were that the directors in their report of 12th August 1880, after recommending the payment of a dividend out of the profits for the preceding year, recommended that a sum of £100,000 standing to the credit of the reserve fund and a further sum of £38,000 should be distributed as a "bonus dividend" of £2 10s. per share, and that there should be issued 18,400 new shares of £10 each, of which £7 10s. should be payable concurrently with the payment of the bonus dividend. They concluded by saying: "Every member of the company . . . would consequently receive one new share in respect of every three shares he holds, such new shares having, like the existing shares, £7 10s. paid thereon." The report was adopted, and a new article authorizing the action recommended was also adopted. The creation of the new capital and its allotment as proposed were also authorized by special resolution. The question for determination was whether certain new shares which were issued to a trustee under these resolutions were to be treated as between tenant for life and remaindermen as income or capital. The Court of Appeal, reversing the decision of *Kay* J. (who proceeded on another ground), held that the bonus dividend and the shares representing it belonged to the tenant for life. The House of Lords reversed this decision. In the argument before the House it was contended for the appellants that funds representing accumulated profits must be regarded as capital, so that, whenever a dividend or bonus is declared out of such profits, it is an accretion to the capital of the trust fund, and the corpus belongs to the remainderman. For the respondents it was contended that a bonus dividend becomes income as soon as it is declared, whether as bonus or dividend, unless the company has already made it capital, and that the question always is whether the company has already done so. No one disputed that capital distributed retains its character as such. The House of Lords did not accept either view.

In dealing with the appellants' argument a good deal was said relevant to the manner in which under the general law a company can convert accumulated profits into capital—a point which the House considered immaterial—and much reliance was placed by the appellants in the present cases on these observations.

The Lord Chancellor (Lord *Herschell*), after an elaborate review of previous decisions, none of which he thought governed the case, expressed his approval of the language of *Fry* L.J., delivering the judgment of the Court of Appeal, of which the passage which I have read from the judgment of *Stirling* J. in *In re Malam* (1) is a quotation. It is to be observed that the cases in which payments by the company to its members are said to enure to the benefit of all who are interested in the capital are two, namely, what is paid by the company to the shareholders "as capital" (not "out of capital"), and what is appropriated as an increase of the capital stock in the concern. The appellants rely upon a passage in the judgment of the Lord Chancellor immediately following this expression of approval, which I will read (2): "And it appears to me that where a company has power to increase its capital and to appropriate its profits to such increase, it cannot be considered as having intended to convert, or having converted, any part of its profits into capital when it has made no such increase, even if a company having no power to increase its capital may be regarded as having thus converted profits into capital by the accumulation and use of them as such."

In my opinion, this language must be read in the light of the subject matter under discussion. If it is read as meaning that, although a company which has no power to increase its capital by appropriating profits to such increase may be regarded as having converted profits into capital by the accumulation and use of them as such, a company by acquiring power to increase its capital in this new way is deprived of any power which it would otherwise have had, it is difficult to reconcile the dictum with recognized principles of law. The conferring of a new power upon a company does not *primâ facie* deprive it of any existing power, and the existence of a power to capitalize profits by proper means is treated

(1) (1894) 3 Ch., at p. 585. (2) 12 App. Cas., at p. 398.

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in the cases to which I have referred as well recognized. But, in truth, the question for determination is, as I have endeavoured to show, not whether as between the members of a company a part of its funds is to be regarded as having been capitalized (whatever the effect of capitalization may be), but whether a sum of money paid to trustees of settled shares has been paid *to them* as capital. The dictum has therefore no application to the case before us. The Lord Chancellor could not have intended to contradict the statement of law which he had just quoted from the judgment of *Fry* L.J., as to the effect of a payment made by a company to its shareholders "as capital."

The Lord Chancellor then proceeded: "I come now to the question whether the company did in the present case distribute the accumulated profits as dividend, or convert them into capital." After referring to a contention that a shareholder might have refused to take the proposed bonus dividend otherwise than as income, and expressing his agreement with that contention, he pointed out that by doing so the shareholders in that particular case would have obtained about £1,500 instead of £4,000 worth of property. Upon consideration of all the facts he came to the conclusion that the substance of the transaction was and was intended to be to convert the undivided profits into paid-up capital upon newly created shares. He concluded by saying (1): "Upon the whole, then, I am of opinion that the company did not pay, or intend to pay, any sum as dividend, but intended to and did appropriate the undivided profits dealt with as an increase of the capital stock in the concern."

The facts in the present case are very different, and, as pointed out by *Stirling* J. in *In re Malam* (2), we are not bound by the decision of the House of Lords on a question of fact. The matter depends upon the question of the intention of the company or the directors. In *Bouch* v. *Sproule* (3), as in other cases relied on by the appellants, the only question for determination was which of two things the company intended to do, and the judgments must be read as dealing with that question. In the present case the Company did

(1) 12 App. Cas., at p. 399.

(2) (1894) 3 Ch., 578.

(3) 12 App. Cas., 385.

not intend to do either of those things, and an entirely different question arises for determination. It is clear that they did not intend to pay the sums in question as dividends. Nor did they intend to appropriate the amount distributed as "an increase in the capital stock in the concern," but, as I have already shown, this is only one of two alternative permissible ways of appropriating accumulated funds as capital, and their intention to appropriate them in one of those permissible ways was shown as clearly as words can show it. So far, therefore, as the reasoning of the Lord Chancellor is to be regarded, it is conclusive of the present case against the appellants' contention. The speeches of the other Lords who took part in the decision are to the same effect.

I do not refer in detail to the numerous authorities reviewed by the House in *Bouch* v. *Sproule* (1), but I may point out that in two of them, *Ward* v. *Combe* (2) and *Price* v. *Anderson* (3), it had been held that a division of profits not made as dividends was to be regarded as given by way of increase of capital of a trust estate. These cases were treated as well decided. In *In re Alsbury* (4), before *North* J., the question of what I may call the internal capitalization of profits by a company was much debated. The learned Judge referred at length to the case of *Bouch* v. *Sproule* and pointed out that the House of Lords did not decide the case on the ground that the profits had been capitalized by being carried to a reserve fund, but on the ground that they had been capitalized, although by a transaction of a different nature. He found that the money in question in the case before him, whether it came from a reserve fund or from the profits of the year, was dealt with as an interim dividend declared by the directors, and added (5): "Except as an interim dividend, the directors had no power to pay it at all; although a general meeting might have confirmed what the directors had done." There can be no doubt, therefore, how that learned Judge would have decided the present case.

In *In re Armitage*, where a similar question arose, *Lindley* L.J. said (6):—"What does a man mean when he leaves shares

(1) 12 App. Cas., 385.
(2) 7 Sim., 634.
(3) 15 Sim., 473.
(4) 45 Ch. D., 237.
(5) 45 Ch. D., at p. 247.
(6) (1893) 3 Ch., 337, at p. 346.

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to a tenant for life? He means that that tenant for life shall have the income arising from the shares in the shape of dividends or bonuses declared during the lifetime of the tenant for life. He does not mean that the tenant for life shall receive profits in any other sense. . . . This conclusion is completely in accord with *Bouch* v. *Sproule* (1), which . . . established the rational principle that what a tenant for life is to take under an ordinary bequest of shares is what is declared as dividends or bonuses in the shape of dividends during the lifetime of that tenant for life." After referring to a passage in the speech of Lord *Bramwell* in that case, he added (2):—"It is true that this property has never been capitalized by the company, neither has it ever been declared as a dividend or a bonus by the company; the company has not dealt with it in either one shape or another. But when you come to ask yourself whether it is to go to the tenant for life or to the remainderman, there can be but one answer—it is to go to the remainderman."

In the very recent case of *In re Thomas* (3) *Sargant* J. and the Court of Appeal (4) said that in all such cases the Court must inquire whether the benefits in question are really and not merely nominally received in respect of a division of dividend, or are really received by way of a distribution of capital.

The only decision to a contrary effect is *In re Piercy* (5), in which *Neville* J. held that a sum of money paid (without authority) to shareholders as a return of capital was, notwithstanding the expressed intention of the directors to the contrary, to be treated as a dividend. I am unable to reconcile this decision with the law clearly established by other cases of great authority. In any view it would only apply to the present case on the assumption that the distributions now in question were not authorized and could not be ratified by the shareholders.

For these reasons I am of opinion that the decision of the majority of the Supreme Court was right, and that the appeals should be dismissed.

(1) 12 App. Cas., 385.
(2) (1893) 3 Ch., at p. 347.
(3) (1916) 1 Ch., 383.
(4) 32 T.L.R., 530.
(5) (1907) 1 Ch., 289.

BARTON J. Thomas Hassall of Ballarat made his will on 28th June 1898, and died on the following 10th July. He gave to the appellant Thomas Richard Haslem the "net income" from 1,000 of his shares in the Melbourne Tramway and Omnibus Co., with remainder to his children; and he directed also as follows:—"If during the lifetime of Thomas Richard Haslem the Melbourne Tramway and Omnibus Company has by operation of law or otherwise to repay to its shareholders the money invested by them in the said Company then in such a case my trustees shall be at liberty to reinvest the money produced by the 1,000 shares in some other way but so that the income derived therefrom shall be for the use of the said Thomas Richard Haslem and his children after him." This does not imply, I think, that money accepted by the trustees as capital was to be handed over to the tenant for life.

The respondent trustees raised by originating summons the question whether a sum of 10s. per share paid as "a distribution of assets" by the Company, in pursuance of a recommendation of its directors by their report for the year ended 30th June 1914, was to be attributed to capital or income of Hassall's estate in respect of the rights of the appellant and his children respectively. A similar distribution of 11s. per share was made in the succeeding year, and though this took place after the date of the originating summons the appropriation of that sum must follow the result of this appeal. An appeal by Henry Knowles is made under similar circumstances. The two cases were argued together, and the judgment is to determine both of them.

The first question is as to the intention of the testator. The best criterion in such a case as this is given by the judgment of *Lindley* L.J. in the case of *In re Armitage* (1). He said (2):—"What does a man mean when he leaves shares to a tenant for life? He means that that tenant for life shall have the income arising from the shares in the shape of dividends or bonuses declared during the lifetime of the tenant for life. He does not mean that the tenant for life shall receive profits in any other sense." But whether the distribution in the particular case is in the shape of dividends or bonuses declared depends on the action of the company in which

(1) (1893) 3 Ch., 337. (2) (1893) 3 Ch., at p. 346.

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the shares are held, and so far as it abstains from transgressing the contractual limits fixed by its memorandum and articles the company can do as it likes with its own. In *In re Bouch*; *Sproule* v. *Bouch* (1) *Fry* L.J. delivered the judgment of the Court of Appeal, in which he said (2), after discussing the authorities :—" These cases are sufficient to show that there has been no such continuous and unbroken current of authorities as would be required to establish such a doctrine as was contended for, viz., that payments out of accumulated profits were necessarily to be treated as payments out of capital. On the contrary, as is reasonable, the authorities leave the inquiry as one of fact upon the circumstances of each case." Though the judgment of the Court of Appeal was reversed by the House of Lords in *Bouch* v. *Sproule* (3), the reversal was only on the question of fact whether the particular distribution was appropriated to the tenant for life as income or to the remainderman as capital. The law of the Court of Appeal was approved, and a rule laid down by them was adopted by the House as a sound one. I shall advert to it presently.

In the first instance, then, the inquiry must be as to the facts antecedent to and connected with this distribution.

The Melbourne Tramway and Omnibus Co. held, under a body called the Tramways Trust, a lease for thirty years, under which and under statutory powers it used tramways constructed on certain public streets and roads. That lease expired in July 1916. The Trust borrowed the money for the construction of the tramways, and the Company was to pay, and did pay, to the Trust the interest paid by it on the borrowed capital, and was to form, and did form, a sinking fund which, accumulating at interest, was to extinguish, and did extinguish, the amount of the borrowed capital. The Company was to supply plant and equipment and to lay, repair, and renew the tramways, and hand them over to the Trust at the end of the lease in good condition. The *Tramway Board Act* of 1915 provided for the termination of the lease on 30th June 1916, and for the dissolution of the Tramways Trust on that date, whereupon the newly created Board was " in law " to succeed the Trust. In

(1) 29 Ch., 635.

(2) 29 Ch., at p. 658.

(3) 12 App. Cas., 385.

any event, the Company had to keep in view the termination of the lease in 1916.

The construction of the tramways having been provided for by loan, and the extinction of the loan provided for by sinking fund, the Company's need of capital was only for plant, equipment, maintenance, repairs, renewal, and working expenses. Therefore, although its nominal capital was £2,000,000, it had to call up only £400,000 in cash, and £80,000 seems to have been provided for by paid-up shares. There were 960,000 shares of £1 each, 800,000 of them paid up to 10s. each and 160,000 rated as paid up to the same extent. No calls appear to have been made. Consequently, if its operations were successful, a comparatively small sum would pay a dividend. A dividend of 5 per cent. on the sums paid up amounted to 6d. per share, and needed only £24,000, while the operations of the Company were, of course, very extensive. After a few years the Company became, and continued, very prosperous. For instance, in 1898 its dividends amounted to £24,000 after carrying £222,000 to reserves. In 1912 the dividends paid were £96,000 and the reserves amounted to over £930,000. In the report of 24th September of that year, referring to a special bonus of 1s. a share declared out of accumulated profits, the directors said: "They think it would be well for shareholders to consider some part of this and future bonuses as on account of the ultimate realization of assets." In 1914 the Company paid dividends of £192,000 and its reserves came to £1,067,000, including for the first time a reserve "for return of capital" amounting to £480,000. In 1915 £192,000 were paid in dividends and the reserves amounted to £1,049,000, including £480,000 for "return of capital"; but the total of the reserves was reduced to £569,000 by reason of "realized assets distributed 1st July 1914" £480,000, which means that the then reserve for the "return of capital" was distributed as realized assets to the same amount. But on the day after the termination of that financial year the Company distributed a further 11s. per share, or £528,000, in the same way, and these payments, amounting together to £1,008,000, reduced to £41,000 the reserves standing in the books before that day. But the Company still held very large values of freeholds, rolling stock, and plant, though their

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leasehold had been written down to £1,600 odd. I have quoted figures from the reports and balance-sheets before us. They show that the operations were greatly profitable, with the profits ever increasing.

In August 1905 the dividend, called a "dividend bonus," was as low as 2½ per cent., but in and from 1908 the payments under the heads of dividend and bonus were very large, as the reports and balance-sheets disclose.

In connection with the payments to July 1914, notices were sent by the Company to the shareholders, each enclosing a cheque for a sum the items of which were stated as follows :—

"Dividend of 6d. per share

"Bonus of 6d. per share

"Distribution of assets, 10s. per share,"

the amount of each item and the aggregate sum being specified.

I have adverted to the advice given by the directors to the shareholders in September 1912. But it is apparent that the Company was increasing its payments in view of the expected end of the lease; the payment of 10s. per share for 1st July 1914 was called in the balance-sheet of 1915 "realized assets distributed," and it absorbed the reserve of equal amount for "return of capital." The same may be said of the subsequent payment of 11s. per share. Both were accompanied with a notice such as I have described, distinguishing separately the dividend, the bonus, and the distribution of assets.

Now the phrase "distribution of assets" is exactly that used in the *Companies Act* in stating the consequence of a voluntary winding-up, and is applied to the final distribution of the company's belongings when turned into money, upon which distribution there is no question that the shareholders receive their respective portions as capital. Had the distribution of assets been left until liquidation upon the conclusion of the Company's operations the present question could not have arisen. "After the commencement of a winding-up dividend is no longer payable" (*per Stirling* L.J. in *In re Crichton's Oil Co.* (1) ).

It is well to remember, in considering what the Company denoted

(1) (1902) 2 Ch., 86, at p. 95.

by the words "distribution of assets," that the scheme upon which it worked, involving large liabilities for loan and other purposes, necessitated large savings for the liquidation of those liabilities within the life of the Company's lease. These savings took the form of reserves in the periodical balance-sheets. When the liabilities were provided for, a great surplus remained. Also the great prosperity of the Company, in operations conducted on a relatively small capital, entailed large dividends, and their recurring payment, together with the aggregation of great reserves, made the shares as proportionate parts of the Company's assets valuable much beyond their face amount. This is an imperative inference from the exhibits, although the actual value of the shares in the market is not in evidence. Thus, as the end of the Company's tenure approached without renewal, a necessarily insistent question arose—that, namely, of the manner of the distribution of that surplus of the continually mounting reserves, which exceeded due provision for repayment of liabilities, and which, in any event, must soon be distributed among the shareholders. It is hence, no doubt, that the Company found itself bound to make divisions in the later years of its tenure, not only in the shape of dividend and bonus, but also for the disposal of the surplus reserves in view of the division which must have succeeded the termination of operations. It is easy then to understand why the Company called the payments of 10s. and 11s. per share a distribution of assets. It was clearly intended as a division anticipating that which otherwise must follow liquidation.

Now, the controversy which arises in this case is not a dispute between shareholders whether sums (being in this case great savings) have been capitalized or not. The question now for determination is how these sums of 10s. and 11s. a share, which the trustee respondents have received, are to be appropriated by them in view of the terms of the will coupled with the objects to which the Company applied them. Are the trustees to give them to the life tenant, or are they to hold them for the remaindermen? If the life tenant has established his claim to them as income of the shares, the appeal succeeds. Otherwise it fails.

I turn again to the passage quoted above from the judgment of

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*Lindley* L.J. in the case of *In re Armitage* (1). Upon that criterion the appellants should have only the income arising from the shares in the shape of dividends or bonuses declared during their lifetime. If there was not, and there is not, a context which alters the sense of the bequest, the testator did not mean that the tenant for life should receive profits in any other sense. He did not give any other profits; and the Company has distinguished in plain terms between dividend or bonus and distribution of assets. In its balance-sheets it has shown that the sums divided on the latter head are given by it as return of capital; and it would be hard to say how the Company could have better differentiated between this payment and a dividend or bonus than by using, in the document covering its cheque, terms which set the dividend and bonus as items separate from the distribution of assets, and by employing in the last-mentioned expression a phrase identical with that by which the Statute denotes an operation usually carried out at a time when dividends are no longer payable.

Counsel for the appellants seem to think that their purpose was achieved by showing that the three payments were alike made out of profits. But the only profits receivable by the tenant for life from the trustees are those assigned by the Company to the shares in the shape of dividends or bonuses. In the case already mentioned of *In re Armitage* (1) *Lindley* L.J., speaking of the conclusion which he founded on the passage already quoted, went on to say:— "This conclusion is completely in accord with *Bouch* v. *Sproule* (2), which at last, after reviewing a great mass of conflicting cases, established the rational principle that what a tenant for life is to take under an ordinary bequest of shares is what is declared as dividends or bonuses in the shape of dividends during the lifetime of that tenant for life. The exact point we have to decide is not quite covered by *Bouch* v. *Sproule*, and there are passages in the judgment of Lord *Bramwell* which have been relied upon by Mr. *Byrne* as showing that everything is divisible as income until it is capitalized. For the purposes of that case that language is perfectly accurate, but it is not quite exhaustive. It is true that this property has never been capitalized by the company, neither

(1) (1893) 3 Ch., at p. 346. (2) 12 App. Cas., 385.

has it ever been declared as a dividend or a bonus by the company; the company has not dealt with it in either one shape or another. But when you come to ask yourself whether it is to go to the tenant for life or to the remainderman, there can be but one answer—it is to go to the remainderman." In that case a residue had been left to A for life, and after her death upon further trusts. Part of the residue consisted of £10 shares in a company with £8 per share paid up. Some years after the testator's death the company was wound up and reconstructed, and the new company paid for the testator's shares £1 5s. 6d. more than had been paid up. This excess arose partly from profits retained to meet contingencies and partly from a fund created by the articles for equalization of dividends. This excess had never been converted into share capital by the company, and if the arguments advanced to us had been correct the tenant for life would have been entitled to his proportion of it, because it consisted of profits. But it had never been declared as a dividend or a bonus, and it was held that the claim of the tenant for life failed.

In a claim like this the real question seems to me to be whether, under a bequest which the testator has defined in simple terms as a gift of the income to the tenant for life, with the shares themselves for the remaindermen, the Company has ever placed the money claimed in the category of dividend or bonus assignable to such income. As it has never done so it seems to me to be far from the claimant's purpose that the Company has declared the money to be distributed as assets in contradistinction to bonus and dividend. If the money is not within either of the two last named, it does not help his claim to find that it has been devoted to another purpose. I say this even if the Company had not the power to devote the money to the purpose to which it specifically appropriated it. For even then the trustees, having accepted the payments under the three several items, had still, if they did not return the 10s. and the 11s. per share, to settle whether, having received them as capital, they had any right to pay the latter sums over to the tenant for life. I do not think they could do so, and as they ask the Court to say whether they could, I feel bound to answer in the sense I have indicated. But is it certain that the Company had not power,

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having decided what it would distribute as dividend and bonus, to go on and pay these other sums as capital—for that is what I think it did in fact? I do not think it correct to say that a company has never any right to deal with its assets in any manner not prescribed by its articles. So far as the articles command or prohibit this course or that, the shareholders are bound by them as their mutual contract. Further, they are bound by the actual directions of law, as, for instance, by a Statute of their own, or by provisions of the *Companies Act*. But there is also the common law, which applies so far as the Statute does not displace it; and that law does not withhold from them the ordinary rights of ownership where neither Statutes nor articles stand in the way. And I do not think the course taken by the Company is prohibited by any law.

I do not find any of the articles which justify discussion except those relating to capital and to dividend. Article 35 empowers the directors, if they gain the sanction of the Company by special resolution, to increase the share capital by the issue of new shares. That, however, does not mean that unless share capital is increased no funds shall be distributed except as dividend. It is a power intended to meet the necessity for extended operations—a necessity which did not arise in 1914 and 1915. There could be no benefit from the increase of the stock at that time, because it was the termination, and not the extension, of the Company's operations that had come into view. Article 37 seems to help one to see that the increase of capital by further share issues is a process associated in the minds of the contracting parties with the necessity for further outlay, or possibly with the occasion for a "watering" of the stock. Article 39 relates only to the reduction of share capital and the return of paid-up share capital. There was nothing in the position of the Company at the time which could suggest any of these steps. Trading capital was superabundant in the shape of reserves, and the problem was how to deal with this surplus when the necessity for trading with it had ceased. Although it might be called profit it had really been the source of a large income itself, and its accumulation evidently suggested to the directors that it would be incongruous to expend a sum so great in dividends and bonuses when operations were near their end, and when a voluntary

liquidation would necessitate its being the subject of a distribution of assets. So they took a course which I think was not forbidden. To say that because the Company distributed these funds as assets in contradistinction to dividend or bonus it therefore gave the life tenant a claim to possess them as income of the latter kind would be a flat contradiction of the Company's decision as to its own money, and I cannot bring my mind to adopt such a conclusion.

As to article 79, under the heading of "Dividends," it cannot convey any inference that funds appropriated as these have been are by the contract to be diverted from the purpose chosen by the Company and devoted to another purpose expressly placed outside the Company's object.

The articles did not expressly or by implication forbid the course taken by the shareholders. Nor was any provision of Statute law cited to us which would have any real effect.

The passage I have quoted from the judgment of the Court of Appeal delivered by *Fry* L.J. in *In re Bouch*; *Sproule* v. *Bouch* (1), at p. 658 of the report, shows that that Court did not consider that authority had established the doctrine that payments out of undivided profits were "necessarily" to be treated as payments out of capital. But that statement, by the use of the word "necessarily," seems to allow that there are occasions on which such payments can be treated thus, and under the circumstances described I think this case is such an occasion, treating the inquiry, to use his Lordship's words, as one of fact. That which is called the rule in *Bouch* v. *Sproule* (2) is adopted from the judgment of the Court of Appeal. The rule concludes in these words: "what is paid by the company as dividend goes to the tenant for life, and what is paid by the company to the shareholder as capital, or appropriated as an increase of the capital stock in the concern, enures to the benefit of all who are interested in the capital." I draw attention to the words "what is paid by the company to the shareholder as capital."

I infer that the rule has regard to what the company pays "as dividend," or pays the shareholder "as capital," or devotes to increasing the share capital in the concern, rather than to what the company says is income, or says is capital. Hence in *In re Carson*

(1) 29 Ch. D., 635.

(2) 12 App. Cas., at p. 397.

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(1) a distribution of shares did not become income because the company called it a dividend—a mere misnomer on the face of its circular. But in the present case the Company has made clear what it pays as dividend or bonus and what it pays as capital.

In the analysis which the learned Chief Justice has made of the cases I content myself with an expression of agreement. The passage in *Bouch* v. *Sproule* (2), in which the Lord Chancellor, after stating the rule, goes on to express a view which was much relied upon by the appellants, is a dictum in the sense that it was not necessary to the determination of the case. If it was intended to be of general application without reference to the case in hand, it does seem to me to be at variance with the rule which had just been expressly adopted by verbatim quotation, and I think, with the learned Chief Justice, that it could scarcely have been intended to express such a variance.

The present case arises at a stage at which trustees have actually received three sums, under a distribution by the terms of which two are undoubtedly claimable by the life tenant, whose right to them is not disputed, and the third is paid by the Company as distributed assets and received by the trustees as such. The life tenant, by this appeal, claims this money too, but I do not think that he can be entitled to more than the moneys paid and received as dividend and bonus. Even if the distribution of assets were unlawfully made as such—and I think it was lawfully made—we cannot say that it was paid as dividend or bonus.

Agreeing, therefore, with the judgment of the majority of the Supreme Court, I think the appeal should be dismissed.

ISAACS J. The problem we have to solve may be thus stated: —A company having power to increase its capital distributed its accumulated profits among its shareholders without using the word "dividend" or "bonus" and without converting them into capital, and without taking any steps in the nature of winding up. As between tenants for life and remaindermen interested in shares, where no special direction is given in the will, to whom do the moneys so distributed belong?

(1) (1915) 1 I.R., 321.

(2) 12 App. Cas., at p. 398.

I may premise that, as was carefully pointed out by *àBeckett* J., no question arises as to whether the action of the Company, if challenged by its shareholders, could be successfully objected to, but the question to be determined is as to what are the rights of tenant for life and remainderman resulting from such action. His Honor accordingly—as did the whole Supreme Court—dealt with the matter on that basis. In this Court both sides took the same course. No argument was addressed to us touching the legality of the directors' act in making the distribution now under consideration. It was treated as lawfully made. The evidence on both sides asserts it was made by "the Company," so that, if *intra vires* the Company, it cannot be impeached. Had it been impeached, probably the Company itself must have been a party, but even then, in view of the fact that there are no restrictions upon the "profits" which may be divided (as there are sometimes—see *Fisher* v. *Black & White Publishing Co.* (1), where restrictive words were introduced) it is manifest that in the absence of such restrictive words such cases as *In re Alsbury* (2) and *Burland* v. *Earle* (3) would present serious obstacles to any contention of unlawfulness. Besides, I agree with the learned Chief Justice that the evidence shows that the balance-sheets and reports were, in accordance with the articles, duly submitted to the Company in general meeting, and I conclude were adopted and approved by the Company. There can be no doubt the distribution, whatever it was in law, was ratified and sanctioned by the whole body of shareholders (*Irvine* v. *Union Bank of Australia* (4) ).

This is not to be taken as suggesting that I, any more than the learned Chief Justice, see the least ground for imputing illegality. I merely confirm what *àBeckett* J. observed. And, as already said, no evidence and no argument was directed to establishing any unlawfulness, and the parties are bound by this course (*Browne* v. *Dunn* (5); *Neville* v. *Fine Arts* (6) ). *àBeckett* J., therefore, was quite right in the observation referred to, and all we have to determine, or have any right to determine, is the substantial question fought so strenuously between the parties.

(1) (1901) 1 Ch., 174.
(2) 45 Ch. D., 237, at p. 243.
(3) (1902) A.C., 83.
(4) 2 App. Cas., 366, at p. 375.
(5) (1894) 6 R., 67, at pp. 75, 76.
(6) (1897) A.C., 68, at p. 76.

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There has been a startling diversity of opinion in the Supreme Court and this Court on the subject, but, with the most unfeigned deference to the opposite view, I see no room for doubt. I hold the clear view that *Madden* C.J. and *Hood* J. were right. Many authorities have been cited and canvassed, including American cases. The latter I do not examine, because the question has already been decided for us one way or the other by practically authoritative English Courts, including the House of Lords, and it comes now to a simple matter of understanding what has been so decided. Those Courts have already considered the matter from all the standpoints of inherent reason, fairness and general principles, and I am not prepared to consider whether those decisions should be substantially overruled for Australia. I accept them.

*Bouch* v. *Sproule* (1) has for nearly thirty years been supposed by text-writers and many learned Judges to have laid down a definite guiding principle, where the company still remained a going concern and retained its profits. There can be no doubt that innumerable settlements and wills dealing with vast amounts of property not confined to Australian interests have been framed doubtless, at all events in most parts of Australia, in reliance upon the very distinct principles enunciated in that case by the eminent lawyers who sat and composed the authoritative tribunal by which it was determined. It is said that the formulation of the law by Lord *Herschell* and Lord *Watson* must be regarded by us as merely *obiter* and wrong. That is a most serious undertaking on a question of property law, and, in my opinion, not legally possible. At all events, if those clearly expressed and long-standing views, so uniformly acquiesced in, are now to be disregarded, I think that in the circumstances the responsibility of taking so far-reaching and drastic a step should be reserved for the ultimate tribunal.

The minority in the Supreme Court rely upon *Bouch* v. *Sproule* (1). The majority pass it by, two of their Honors not even mentioning it. But as I regard this case, its principles should govern our decision. In the circumstances it is apparent that some careful analysis of the judgments in *Bouch* v. *Sproule* is inevitable.

Lord *Herschell* first stated his opinion (2) that there could be

(1) 12 App. Cas., 385.

(2) 12 App. Cas., at p. 392.

no satisfactory rule to the effect that accumulated profits which *de facto* had formed part of the capital of the company must be treated as an addition to capital. Then he proceeded to consider the authorities up to 1887. He first dealt with *Brander* v. *Brander* (1), and found (2) that it rested on the same foundation as *Irving* v. *Houstoun* (3), viz., that the accumulated profits had become part of the floating capital of the concern. That was the rule his Lordship had already declared unsatisfactory.

Coming then to *Irving's Case* itself, he said he was bound by it because it was a decision of the House of Lords (4). He quoted Lord *Eldon's* judgment, adopting the ratio of *Brander's Case*. Then, added Lord *Herschell*, *Irving's Case* was followed by others he named. Nevertheless, said he (5), "a disposition was early shown to limit the operation of the rule," adding: "it is manifest that from the first it was felt not to rest on any stable principle." Examples of departure are given on pp. 395 and 396, the learned Lord himself feeling a difficulty in reconciling that departure with the judgment of the House of Lords. He regards, for instance, *Ward* v. *Combe* (6) as possibly inconsistent with *Preston* v. *Melville* (7), but says (8): "it is a clear recognition of the doctrine that a division of accumulated profits amongst the shareholders is to be regarded as given by way of increase of capital." In other words, *Ward* v. *Combe* is a recognition of the very doctrine that Lord *Herschell* had just declared unsatisfactory as a principle, but which, because it was adopted by the House of Lords in *Irving's Case*, and had continued to be recognized, bound him. Therefore, said he (9), he must still regard *Irving's Case* "as good law, unaffected by any counter-current of authority." But at this point the learned Lord felt himself at liberty to diverge from it. He drew a distinct line, confining that case and all the other cases in association with it, including *Ward* v. *Combe*, to one side of that line. The line is marked by *the power to increase capital*. If a company has no power to increase its capital, *Irving* v. *Houston* and its satellites

(1) 4 Ves., 800.
(2) 12 App. Cas., at p. 393.
(3) 4 Paton Sc. App., 521.
(4) 12 App. Cas., at p. 394.
(5) 12 App. Cas., at p. 395.
(6) 7 Sim., 634.
(7) 16 Sim., 163.
(8) 12 App. Cas., at p. 396.
(9) 12 App. Cas., at p. 397.

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apply. That is, Lord *Eldon's* reasoning applies. That reasoning is that every settlor or testator holding shares in such companies knows the practice of the company—if there be such a practice—to treat accumulated profits as capital, and must be taken in the absence of contrary direction to intend accordingly that whatever profits are so treated shall pass as capital to the remainderman. But, holds Lord *Herschell*, if a company has power to increase its capital, then it stands on the other side of the line, and another rule applies. On p. 397 the learned Lord says: "Apart from the authorities to which I have alluded, the general principle for the determination of such a question as that before us, and in my opinion *the only sound principle*, is that which is well expressed in the judgment of Lord Justice *Fry*." Then follows the now classical passage in that judgment, which I need not repeat. I will only say that the power which that passage predicates is one of doing either one of two things—(1) distributing profits as dividend, and (2) converting them into capital. No third course is assumed to be possible; nor is it, so long as the company retains the profits, and continues as a live concern.

It is all important to observe that in adopting that passage—and it is that adoption which gives it for us the commanding force it possesses—the learned Lord adopts it with this authoritative declaration (1): "It appears to me that *where a company has power to increase its capital and to appropriate its profits to such increase, it cannot be considered as having intended to convert, or having converted, any part of its profits into capital when it has made no such increase.*"

It is idle to say that Lord *Herschell* adopts the statement of *Fry* L.J. in any other sense than that in which he expressly says he understands it.

Having laid this down as the basis of the law, Lord *Herschell* proceeded to consider which of the two things the company had done—viz., (1) distribution as dividend, or (2) conversion into capital. And the controlling consideration in this respect appears to have been this, that the company did not intend that the money nominally divided among the shareholders should ever be paid to them,

(1) 12 App. Cas., at p. 398.

but should still remain in the company's hands—no longer as the company's profits but in the changed character of the company's capital. In this connection I refer to *Mitchell* v. *Hart* (1), and may further observe that the line of reasoning adopted by Lord *Herschell* in this respect is practically identical with that of Lord *Hatherley* (then *Wood* V.C.) in *Baring* v. *Ashburton* (2).

I come now to Lord *Watson's* judgment. After shortly dealing with the prior class of decisions, in effect agreeing with Lord *Herschell*, he pointed out that the company in the case before the House had a certain power. That power was to increase its capital by issuing new shares to its members, and "crediting them" (the members) "with a sum as paid on each share from its reserved or undivided profits."

That, I may observe in digression, is an instance of permitted "appropriation" of profits as an increase of the capital stock, referred to by *Fry* L.J., as distinguished from the ordinary case of a person, member or outsider, independently paying for the new shares he gets. See also *In re Alsbury* (3). "Appropriation" does not, as is pointed out, mean the mere "treatment" of profits as capital in the sense of being used in the business. If that were so, then, as Lord *Herschell* said (4), most, if not all, the profits of the Consett Company would have to be regarded as capital. This view he explicitly rejected.

Reverting to Lord *Watson's* judgment, we find the following formulation at p. 401 :—"Where the company has power to determine whether profits reserved, and temporarily devoted to capital purposes, shall be distributed as dividend or permanently added to its capital, the interest of the life tenant depends, in my opinion, upon *the decision of the company.*"

Again, we find the two possibilities enumerated as the only possibilities—(1) distribution as dividend, and (2) permanent capitalization. But, ran one criticism, it is the "*life tenant*"—not the remainderman—whose interest depends upon the "decision." If (it was said) the company does not decide on a "dividend," and does not decide to "capitalize," but merely "distributes," then there is no such "decision" as Lord *Watson* predicates. The

(1) 19 C.L.R., 33.
(2) 16 W.R., 452, at p. 453.
(3) 45 Ch. D., 237, at p. 247.
(4) 12 App. Cas., at pp. 393, 394.

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result, according to the contention, is that the remainderman gets the money because the company has not decided on a dividend, or the Court must decide on the facts to see what the company "intended" to do, and did do, as a third course.

In the first place, as a matter of construction, I cannot read Lord *Watson's* words in that way. When he spoke of the company's decision he assumed a distribution (otherwise *cadit quæstio*), and he contemplated that that distribution must have been decided upon by a company then having the power to decide in one or other of the two characters he specifically mentioned. Such an ellipsis as is suggested is to me unimaginable. But, if doubt were possible, it is resolved by his Lordship's quotation from the judgment of Lord *Hatherley* (while Vice-Chancellor) in *In re Barton's Trust* (1), where the two alternative courses are brought into sharp and exhaustive contrast. As if to emphasize this necessity of choosing between the two courses specified if any distribution takes place at all, Lord *Watson* (2) repeats them, categorically.

As to the facts, he adopts the same test as Lord *Herschell*, namely, whether the bonus was intended as a *money payment* to the shareholders to be kept by them, or was it to be *retained* in the company's coffers. I need not specifically refer to the judgments of Lord *Bramwell* and Lord *Fitzgerald*, for they only confirm the preceding judgments.

I wholly reject the argument that the House of Lords simply repelled the application of the rigid rule of the earlier cases, and left the whole matter open, without guide or rule, where the company has power to increase its capital, except a conclusion of fact from the circumstances, external and internal, the tribunal being left at large. The difficulties of a trustee in such a condition of affairs may be imagined from some of the considerations in the judgments from which I have the misfortune to differ. Of course, it is always a question of fact whether or not the company has intended to convert its profits into capital, but the principle laid down in *Bouch* v. *Sproule* (3) is, in my opinion, that where the company has power to do so that is the only ultimate question of fact.

(1) L.R. 5 Eq., 238, at p. 244.
(2) 12 App. Cas., at pp. 402, 403.
(3) 12 App. Cas., 385.

The Court is invited to proceed upon the principle as to how the company intended to regard the money it handed over, independently of any intention on its part to convert profits into its own capital. Stripping the matter of non-essentials, the argument is that the company is to be a dictator as between tenant for life and remainderman as to which of them shall have the moneys distributed, irrespective of whether those moneys are the company's profits or the company's capital. According to that, a company, for instance, could, disregarding its actual powers, say arbitrarily, "So much is to be capital for the remainderman, and so much income for the tenant for life," and could even discriminate between different trusts. Any such view is, I feel confident, in conflict with *Bouch* v. *Sproule* (1). It is obviously contrary to the view held by *Fry* L.J. See 29 Ch. D., at p. 650.

The root conception of *Bouch* v. *Sproule*, as I understand it, is that where a company has power to convert profits into capital, the tenant for life and remainderman must each take the chance of whether the company (1) leaves the profits to continue as its profits, or (2) lawfully converts them into its capital in the true sense. If the company decides to really and effectually distribute the money itself, and while retaining its character of profits, the tenant for life gets it; if the company decides to convert it into capital, then any so-called distribution, whatever formalities transpire, is not intended to be and is not really a "money payment" at all, and the remainderman gets the benefit, though he does not and cannot get the money, because that remains in the company's coffers. That is the view taken, not only in the text-books, but also in decided cases such as *Baring* v. *Ashburton* (2) which practically anticipated *Bouch* v. *Sproule* though not cited in it.

In *Re Paget* (3) *Chitty* J. put the question most explicitly. After quoting Lord *Herschell* and Lord *Watson* in *Bouch* v. *Sproule*, the learned Judge said: "It is evident from this, and, indeed, it is plain, that *the decision required so to bind is a final decision for the permanent addition of the previous profits to the company's capital.*" So the rule is stated in *In re Piercy* (4). So also *per North* J. in

(1) 12 App. Cas., 385.
(2) 16 W.R., 452.
(3) 9 T.L.R., 88, at p. 89, col. 2.
(4) (1907) 1 Ch., 289, at p. 294.

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*In re Alsbury* (1), who says : " The company has power to increase its capital ; it has passed no resolution to do so ; and has not increased its capital." That case directly supports the appellants' view.

The latest case, and after *Bouch* v. *Sproule* (2) the most authoritative case relative to the present, is *Re Thomas* ; *Andrew* v. *Thomas* (3), where the Court of Appeal affirmed *Sargant* J. Again the two possibilities, (1) dividend or (2) conversion into capital, were considered as the only two possible courses. Lord *Cozens-Hardy* M.R. said (4) :—" The company did not want the capital. They did not want to capitalize the sum ; and we are asked really to go in the teeth of the written document if we take any other view. . . . I quite agree that we must look to see what is the real intention of the parties. Here it is called a dividend." And then the learned Lord asks this crucial question : " Is there anything to suggest an intention on the part of any human being to capitalize this sum ? "

*Pickford* L.J. says that the principle was correctly stated in *In re Evans* (5) by *Neville* J. :—" In my opinion, in all these cases it is a question of fact, and the decision must turn upon what was the intention of the company. The intention of the Collieries Company, as expressed by their resolution and by the documents before us, undoubtedly was to distribute this reserve fund as dividend, and not to take it and use it and convert it into capital—*not to make it capital.*"

*Neville* J. points out that, in answer to the argument that the company took the course it did to avoid the legal difficulty of *Trevor* v. *Whitworth* (6), the *motive* is not to be regarded for which the course actually taken was adopted, but only the *intention* the company had in doing what it did. I shall revert to this observation later, because I think there is an analogy in the present case. His Lordship subsequently says : " Thereupon the transaction, so far as the combine is concerned, is over, and their object has been achieved without the slightest necessity for capitalizing any part of the reserve fund." It is to be noted that though *Sargant* J. was of opinion that the case was of the *In re Armitage* (7) type

(1) 45 Ch. D., 237, at p. 245.
(2) 12 App. Cas., 385.
(3) 114 L.T., 885.
(4) 114 L.T., at p. 890.
(5) (1913) 1 Ch., 23.
(6) 12 App. Cas., 409.
(7) (1893) 3 Ch., 337.

rather than of the *Bouch* v. *Sproule* (1) type, the Court of Appeal expressly rested solely on the principle of *Bouch* v. *Sproule*.

In view of the argument, it is not out of place to refer to the two words "capital" and "dividend." Lord *Lindley*, in his work on *Companies*, 6th ed., p. 544, defines "The capital of a company" as "the money intended to be contributed, or agreed to be contributed by its members for carrying out its objects." And in *Bouch* v. *Sproule* (1) the learned Lords are most careful to insist that "capital," in the sense in which they use the word, must be understood strictly.

As to "dividend," much reliance was placed on the fact that the Company had not used the word "dividend" in connection with the distribution of the 10s. and the 11s. per share. It was said that that showed, or helped to show, that the Company did not "intend" those sums as dividends. Now, if such payments *are* dividends, the Company must have intended them as such. By Statute law in force then, and now consolidated in the *Companies Act* 1915, sec. 277, a trading company must not declare dividends except out of profits. To contravene this is penal; and "dividend" is declared to include bonuses and payments by way of bonus. Is a company able to escape this by simply declaring a "distribution" of what is not profit? I think not.

In the leading case of *Henry* v. *Great Northern Railway Co.* (2) Lord *Cranworth* L.C. regarded a "dividend" as meaning primarily, if its derivation be looked to, a fund to be divided, but according to ordinary usage the share of a person in that fund. *Knight Bruce* L.J. said (3) "the word 'dividend' carries no spell with it."

In *Lamplough* v. *Company of Proprietors of the Kent Waterworks* (4) *Collins* M.R., referring to the argument that in the section then under consideration the word dividend meant "the total divisible sum," observed: "The sense in which ordinary persons use it is the sum received and paid as a quotient." See also *Halsbury*, vol. v., p. 271, sec. 442.

Consequently, I apprehend, when *Farwell* L.J. and Lord *Herschell*

(1) 12 App. Cas., 385.
(2) 1 De G. & J., 606.
(3) 1 De G. & J., at p. 642.
(4) (1903) 1 Ch., 575, at pp. 580, 581.

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and Lord *Watson* in *Bouch* v. *Sproule* (1) used the word " dividend " they used it in the ordinary sense as the share receivable by each shareholder out of the fund of profits by the company. If a company determines that a certain amount of profits shall be divided among its shareholders in proportion to their shares, the aliquot part receivable by a member in respect of a share is his " dividend," whether the company calls it a dividend, or a bonus, or a share in distribution. In *Bouch* v. *Sproule* the share was called a " bonus " (see 29 Ch. D., at p. 644) ).

Where dividend and bonus are differentiated by context, the former may mean a periodical payment and the latter an occasional payment, both probably recurring, the latter less frequently or regularly (see *In re Griffith* ; *Carr* v. *Griffith* (2) ). Differentiating again the expression " distribution of assets," it may be taken to be a payment in the nature of a bonus, that is not to be expected to recur. But in the case of a live company not repaying capital under the prescribed statutory procedure for the purpose, it must be " profits " to be lawful. But, as already stated, the word " dividend " as used by the House of Lords was manifestly intended as a generic term to mean all money payments to a shareholder as such out of what were legally profits of the company.

I now come to a point very much pressed, but which, with the greatest respect, I think entirely beside the question when once it is understood. It is said that the Company, about two years before the tramway system was to be taken over, determined on this distribution of accumulated profits, by way of anticipating a winding-up. Therefore, it is said, it must be regarded practically as if it were a winding-up, and consequently the distribution must be regarded in strict law as a distribution by capital. That, as *Neville* J. said in *Andrew* v. *Thomas* (3), might have been the *motive* of the Company (or it might not) for doing what it did. But it cannot be taken as governing the question of the *intention* of the Company in the actual distribution. If a man, knowing he will probably die in a year, makes a gift *inter vivos* so as to avoid the necessity of disposing of the property by will, he cannot be said to intend a

(1) 12 App. Cas., 385.
(2) 12 Ch. D., 655, at p. 661.
(3) 114 L.T., 885, at p. 891.

testamentary disposition. He avoids one. So the Company, merely because it deliberately set itself to avoid a distribution in liquidation, with the consequences set out in sec. 186 of the Act of 1915, cannot, in my opinion, be said to have therefore intended to do what it intended to avoid. The contention seems to me to disprove itself. *In re Armitage* (1) was cited, however, as supporting that contention. But in that case the company was actually in voluntary liquidation, and the Lords Justices regarded that as the cardinal fact. *Lindley* L.J. said (2) :—" The moment the company got into liquidation there was an end of all power of declaring dividends and of equalizing dividends, and the only thing that the liquidator had to do was to turn the assets into money, and divide the money among the shareholders in proportion to their shares. That is what he has done."

Now, we have to remember, first, that no dividends can be declared after liquidation—for which not only the passage quoted is a high authority, but also the statement of *Stirling* L.J. in *In re Crichton's Oil Co.* (3). Then we must bear in mind the central fact, so often pointed out, as, for instance, by Lord *Hatherley* (when Vice-Chancellor) in *In re Barton's Trust* (4), that the only dividend to which a tenant for life is entitled is the dividend which the company chooses to declare ; and, I would add, the dividend which the company has power to declare. All else goes to the remainderman.

*Lindley* L.J., in *In re Armitage* (2) says that all a tenant for life of shares is entitled to is the income arising from dividends and bonuses declared during his life. That excludes anything not declared before liquidation. It also excludes profits obtained by realization of shares by the company, because the money represents the shares in another form, and does not represent any dividend declared by the company as payable to the former shareholder.

The Lord Justice said *Bouch* v. *Sproule* (5) is not quite exhaustive. That case assumed the company had acted in respect of the profits while a going concern. But in *In re Armitage* (1), as the Lord

(1) (1893) 3 Ch., 337.
(2) (1893) 3 Ch., at p. 346.
(3) (1902) 2 Ch., 86, at p. 95.
(4) L.R. 5 Eq., at p. 244.
(5) 12 App. Cas., 385.

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Justice said, the company had not dealt with the fund either as dividend or by way of capitalizing it. There having been no distribution whatever by the company while it could declare a dividend, the tenant for life had no claim on it. Similarly held *Lopes* L.J.

But the reasoning is wholly inapplicable to the case of a company that while its legal powers are unimpaired does deal with its profits by either distributing them simply as a dividend or by capitalizing them. See *In re Palmer* (1) and *In re Rolland* (2).

I am of opinion that the appeal should be allowed.

GAVAN DUFFY and RICH JJ. We think that the decision of the Supreme Court is right, and we adopt the reasoning of *Cussen* J., but the able argument that has been addressed to us on behalf of the appellants makes it desirable that we should add something to what was said by that learned Judge.

The payments to shareholders of 10s. in July 1914 and 11s. in July 1915 under the name of distribution of assets were made out of funds standing to the credit of a number of reserve accounts, the permanent existence of which, during the Company's life, had apparently been considered necessary for the safe and efficient conduct of the Company's business. These moneys had long represented a large proportion of the market value of the shares, and were released by the impending termination of the Company's control of the city and suburban tramway service. The directors might have retained the moneys for distribution in the course of winding up, but as it was uncertain when the winding-up would take place it would have been difficult to reinvest them satisfactorily in the meantime. It was argued that the directors had no power to make payments out of accumulated profits except by way of dividend under clause 77 of the articles of association, and that they must be assumed to have acted within their powers, and so under that clause, and the case of *In re Piercy* (3) was cited as an authority for this proposition. To this it was answered that the directors, with the assent of a general meeting of shareholders, had power to make distributions of capital, and that the distributions

(1) 28 T.L.R., 301. (2) 30 N.Z.L.R., 494.

(3) (1907) 1 Ch., 289.

in question were made with such assent. It is unnecessary for the purpose of this case to define the powers of the directors either with or without the assent of a general meeting.

We are satisfied, on the evidence, that the directors did not act or purport to act under clause 77, but intended to distribute the assets of the Company, reserving only sufficient to provide for the return of the share capital and for other payments which would become necessary in the course of winding up. The trustee knew the facts, and accepted the payments without condition or protest, and he is bound by his acceptance, and is not at liberty to say that he will hold the moneys as if they had been paid to him under clause 77. Finally it was urged that the intention of the directors was immaterial because the distributions were not distributions of capital as defined in *Sproule* v. *Bouch* (1) and *Bouch* v. *Sproule* (2). In those cases it was argued for the remainderman that where a sum, whether called bonus or dividend, is distributed by a company among its shareholders, it must, if it is paid out of the accumulated profits of past years, be treated between tenant for life and remainderman as capital. The Court of Appeal refused to accept this argument and stated the general principle thus :— "When a testator or settlor directs or permits the subject of his disposition to remain as shares or stock in a company which has the power either of distributing its profits as dividend, or of converting them into capital, and the company validly exercises this power, such exercise of its power is binding on all persons interested under him, the testator or settlor, in the shares, and consequently what is paid by the company as dividend goes to the tenant for life, and what is paid by the company to the shareholder as capital, or appropriated as an increase of the capital stock in the concern, enures to the benefit of all who are interested in the capital. In a word what the company says is income, shall be income, and what it says is capital, shall be capital" (3).

It is to be observed that the word "capital" in this statement is not confined to share capital, but includes accumulated profits treated as capital by the company. We shall not pause to consider

(1) 29 Ch. D., 635. (2) 12 App. Cas., 385.
(3) 29 Ch. D., at p. 653.

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whether the general principle thus enunciated applies to distributions like those in question here, which probably would not have been anticipated by the testator. We shall assume that it does apply to them, without deciding the question.

The Court examined the cases, and then said :—" These cases are sufficient to show that there has been no such continuous and unbroken current of authorities as would be required to establish such a doctrine as was contended for, viz., that payments out of accumulated profits were necessarily to be treated as payments out of capital. On the contrary, as is reasonable, the authorities leave the inquiry as one of fact upon the circumstances of each case. The authorities appear to us further to establish this proposition, that in most, if not in all, cases, the inquiry as to the time when the profits were earned by the company is an immaterial one as between the tenant for life and remainderman. Their rights have been made dependent on the legitimate action of the company, and (subject to any rights arising from the law of apportionment, with which we are not now dealing) we are of opinion that their rights are determined by the time, not at which the profits are earned by the company, but at the time at which they are by the action of the company made divisible amongst its members."

" Such being the law applicable to the present inquiry, we have to consider whether the present company did by any act prior to the distribution in question make the accumulated profits part of their capital. A portion of the moneys in question had been carried to the reserve fund, which, by the 109th article of association, was appropriated for any of the following purposes : (1) meeting contingencies ; (2) equalizing dividends ; (3) repairing or maintaining the works connected with the business of the company. It appears to us to be plain that whilst some of these objects would be demands on capital, others, such as the payment of dividends and of the repairs and maintenance of the works of the company, are essentially payments out of income, consequently we are of opinion that the carrying of moneys to the reserve fund was not a capitalization of them " (1).

It would seem to follow from these passages that in the present

(1) 29 Ch. D., at pp. 658, 659.

case the moneys standing to the credit of some of the reserve accounts should be regarded as intended to be capitalized and the moneys standing to the credit of other of the reserve accounts should not be so regarded, and that distributions made indiscriminately out of these funds would not necessarily be distributions of capital. Whether they were or were not so would be a question of fact depending on all the surrounding circumstances.

The Court next proceeded to inquire whether the way in which the declaration of a bonus or dividend was coupled with the creation of new share capital authorized by resolutions of the company amounted to a capitalization of the bonus paid out of the mixed fund, and came to the conclusion that the two transactions were not so connected as to produce that result, and that the payment of the bonus was therefore in its nature a mere distribution of profits kept *in medio* down to the time of its appropriation by the resolutions of the company, and not converted into capital by those resolutions.

The House of Lords accepted the law as laid down by the Court of Appeal, but treated the question at issue as one of fact and reversed the judgment of that Court on the ground that the bonus or dividend, though paid to the shareholders, was paid under such conditions as practically secured its return to the company as the price of new shares to be issued by the company, and that therefore "looking at all the circumstances the real nature of the transaction was that the company did not pay or intend to pay any sum as dividend, but intended to and did appropriate the undivided profits as an increase of the capital stock" (1).

Lord *Herschell*, however, in adopting the principle formulated by the Court of Appeal, omitted the last sentence, and added this statement: "And it appears to me that where a company has power to increase its capital and to appropriate its profits to such increase, it cannot be considered as having intended to convert, or having converted, any part of its profits into capital when it has made no such increase, even if a company having no power to increase its capital may be regarded as having thus converted profits into capital by the accumulation and use of them as such" (2).

(1) 12 App. Cas., at p. 385. (2) 12 App. Cas., at p. 398.

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It is said that the words "to increase its capital" necessarily refer to "share capital," and that the moneys distributed by the Melbourne Tramway and Omnibus Co., not having been appropriated to the increase of "share capital," were not converted into capital, but were distributed as profits, and were received by the trustee as income. It is doubtful whether Lord *Herschell's* statement has any application to the present case. The company there had a special power of increasing its share capital by the creation and allotment of new shares to its members and of crediting them with a sum as paid on each share as from its reserve or undivided profits (see *per* Lord *Watson*, (1) ). The Melbourne Tramway and Omnibus Co. has no such power. But if it be assumed that the statement is relevant to the present case it is an authority for the proposition that such a company cannot be supposed to hold profits as capital unless it has shown its intention of doing so by appropriating such moneys to an increase of its share capital, not for the proposition that it cannot be supposed to distribute them as capital unless it first so appropriates them. It seems absurd to suggest that a company desiring to distribute a portion of its cash assets, and having the power to do so, must be held not to have done so because it has not done something quite inconsistent with a distribution in cash.

We think that nothing that was said either in the Court of Appeal or in the House of Lords precludes us from deciding that the two sums in question were paid to and received by the trustee as capital of the Melbourne Tramway and Omnibus Co., and should be held by him as corpus for the benefit of the sons of Thomas Richard Haslem.

*Appeal dismissed. Costs of all parties as between solicitor and client to be paid out of the testator's residuary estate.*

Solicitors for the appellants, *M. Mornane*; *Madden & Butler.*

Solicitors for the respondents, *Elder & Graham*; *A. Phillips*; *Davies & Campbell.*

B. L.

(1) 12 App. Cas., at p. 401.