[HIGH COURT OF AUSTRALIA.]

THORNLEY AND OTHERS . . . . APPELLANTS;
DEFENDANTS,

AND

BOYD AND OTHERS . . . . . RESPONDENTS.
DEFENDANT AND PLAINTIFFS,

ON APPEAL FROM THE SUPREME COURT OF VICTORIA.

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MELBOURNE, *Oct.* 19, 20, 29.

Knox C.J., Isaacs and Rich JJ.

Will—Construction—Gift of income—Sheep station carried on by trustees—Sale for purpose of winding up business—Profits on sale of sheep—Corpus or income.

A testator, who during his lifetime had carried on the business of a grazier on four stations, three of which were freehold, by his will gave all his property, which substantially consisted of the stations and the sheep thereon, to his trustees on trust for sale and conversion and investment. He directed that the trustees should hold the whole of the proceeds upon trust to pay the income to his children in certain shares and after their deaths upon trust for their children. He also directed that the trustees were not to sell his real estate until ten years after his death; he empowered them to postpone the sale of his real estate and the conversion of his personal estate in their discretion, and he authorized them to lease or manage and work his real estate, and for that purpose to use any sheep or stock and plant belonging to the estate or to purchase sheep, stock or plant. The trustees carried on and worked the stations for some years after the expiration of the ten years.

Held, that, on a sale by the trustees of one of the stations and the sheep thereon for the purpose of putting an end to that business, none of the profit realized on the sale of the sheep was income, but that the whole of the proceeds of sale was corpus.

Decision of the Supreme Court of Victoria (Full Court): *In re Thornley; Boyd* v. *Thornley*, (1925) V.L.R. 569; 47 A.L.T. 52, affirmed.

APPEAL from the Supreme Court of Victoria.

William Boyd and the Union Trustee Co. of Australia Ltd., the trustees of the will and estate of Nathan Thornley, by originating summons sought a determination of the question (among others) whether, having regard to the construction of the will, the whole or any and what portion of the amounts realized at the clearing sales of live-stock belonging to the estate, held on 4th February 1924 on the station known as Woperana and held on 31st May 1924 on the station known as Warrambeen respectively, should be appropriated to corpus. The defendants to the summons were the sons and daughters of the testator, namely, Edmund Ashworth Thornley, Geoffrey Prestwick Thornley, Edith Theresa Boyd, Florence Louisa Nicholson and Violet May Lillies, and Douglas Thornley Boyd on behalf of himself and the other grandchildren of the testator. The material provisions of the will and the other facts are stated in the judgments hereunder.

The Full Court, to which the summons was referred, answered the question by declaring in effect that in the case of each sale the whole of the sum by which the amount realized at the sale exceeded the value at which the sheep stood in the books kept by the trustees should be appropriated to corpus: *In re Thornley*; *Boyd* v. *Thornley* (1).

From that decision the sons and daughters of the testator now appealed to the High Court.

The other material facts are stated in the judgments hereunder.

Owen Dixon K.C. (with him *Clayton Davis*), for the appellants. The whole of the sums in question was income within the meaning of the will and not corpus. The sheep on the stations were the circulating capital and not the fixed capital of the business. They were trading stock of the business carried on upon the stations, and are in the same position as the trading stock of a drapery business, for instance. Any increase in the value of that trading stock, so long as the stock is unrealized, is income of the business, and when the stock is realized the amount of the income is ascertained. The occasion of the realization should not be looked at but the manner in which the proceeds of realization are earned (*Anson* v. *Commissioner*

(1) (1925) V.L.R., 569; 47 A.L.T. 52.

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of Taxes (1); *Gloucester Railway Carriage and Wagon Co.* v. *Inland Revenue Commissioners* (2); *In re Spanish Prospecting Co.* (3); *De Grey River Pastoral Co.* v. *Deputy Federal Commissioner of Taxation* (4)).

[KNOX C.J. referred to *Joshua Bros. Pty. Ltd.* v. *Federal Commissioner of Taxation* (5); *Whiting* v. *Whiting* (6); *Bradley* v. *Denne* (7); *McIntyre* v. *McIntyre* (8).

[RICH J. referred to *In re Flood*; *Macpherson* v. *Whiston* (9).]

The sums in dispute are due to the natural increase of the sheep, to the gradual increase in the market price of sheep over a period of years, to the increase in value of the sheep due to the growth of the wool since the previous shearing and to the fact that the ewes became in lamb. Money which arises in that way is income, and was intended by the testator to be treated as income. The flock of sheep was intended by the testator to be used by the trustees as an instrument for the production of income by sales, and the whole of the proceeds of sales was intended to be carried to revenue account for the purpose of determining what was income. Taking the capital value of the sheep at the commencement of the period, everything added to that value belongs to the life tenant.

Gregory, for the respondent Douglas Thornley Boyd. Looking at the will to find the testator's intention and at the nature of the property and the manner in which it was worked, namely, by keeping up the flock and selling the wool and the surplus stock, the sums in question were corpus and not income. The word "income" throughout the will means, not unrealized products, but money produced by realizing products, that is, the ordinary annually recurring income. The increase in value, either by increase in the market value or by improvement in the quality of the sheep, is not income. All the decisions in Australia support that view. [Counsel was stopped.]

Tait, for the respondent trustees.

Cur. adv. vult.

(1) (1922) N.Z.L.R. 330.
(2) (1925) A.C. 469.
(3) (1911) 1 Ch. 92, at pp. 98, 106.
(4) (1923) 35 C.L.R. 181.
(5) (1923) 31 C.L.R. 490.
(6) (1841) 5 Jur. 1127.
(7) (1911) 29 N.S.W.W.N. 2.
(8) (1914) 15 S.R. (N.S.W.) 45.
(9) (1912) 12 S.R. (N.S.W.) 144.

The following written judgments were delivered :—

KNOX C.J. The appellants are the surviving sons and daughters of the testator Nathan Thornley ; the respondent Douglas Thornley Boyd is a grandson of the testator who has been appointed to represent in these proceedings all the other grandchildren, and the respondents William Boyd and the Union Trustee Co. are the trustees of the will of the testator. The testator, who died in the year 1903, was at the date of his death the owner of certain station properties known as Woperana, Warrambeen, Kangatong and Barwidgee, which he had for some years carried on as sheep stations, and of the sheep depasturing on those properties. The stations were managed and carried on as one business, sheep being transferred from one station to another as occasion required. It is not stated in what form the accounts of this business were kept during the testator's lifetime.

By his will the testator, after bequeathing certain legacies and life annuities, devised and bequeathed all his real and personal estate to his trustees upon trust to sell his real estate and to call in and convert into money his personal estate and to stand possessed of the proceeds of such sale calling in and conversion upon trust, after payment of his debts and funeral and testamentary expenses and of the legacies bequeathed by his will, to invest the same in the manner therein directed. After providing for the application of portion of the income and the accumulation of the balance during the life of his wife, the testator directed that after the death of his wife the trustees should hold the whole of the proceeds then existing of his estate and the accumulations upon trust that the same should be appropriated, or considered as appropriated, to his six children as tenants in common, but so that the share of each son should be double the share of each daughter, and as to each of these shares he declared that it should be held upon trust, so far as now relevant, "to pay the income of such share to such son or daughter during his or her life and after his or her death to stand possessed of the same trust premises in trust for the child or children of such son or daughter" in manner therein mentioned.

The will also contained provision for postponing the sale of the real estate and the conversion of the personal estate and for the

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management thereof until sale in the words following :—" Provided always and I hereby expressly declare that my said trustees shall not before the expiration of ten years from my death nor during the life of my said wife sell any of my said real estate nor without the written consent of my said wife the household furniture and household effects of any description in or appropriated to my residence situated in Grandview Grove and known as 'Radcliffe' And after the expiration of the said ten years and the death of my said wife my said trustees shall have the fullest discretionary power to postpone the sale of the whole or of any part of my said real estate for so long as they shall in their uncontrolled discretion think fit and they shall not be responsible for any loss which may arise in consequence of such postponement And I declare that it shall be lawful for my executors and for the trustees for the time being of this my will to defer and postpone the sale conversion and collection of the whole or any part or parts of my said personal estate not only during the period of one year from my death but also so long as to such executors or trustees shall in their uncontrolled discretion seem proper and they shall not be responsible for any loss which may arise in consequence of such postponement . . . And it is my desire that my said real estate other than my said residence shall be either managed and worked or leased for grazing or dairying purposes in portions and I authorize my said trustees to let the said real estate in such lots as they may from time to time think fit and that each lot may from time to time be let from year to year or for any term not exceeding five years at a time and so that any lease shall take effect in possession or within one year after the making thereof and upon such terms and conditions and subject to such rents as my said trustees may from time to time think fit and to erect homesteads and other buildings on any of the said lots for the purpose of effecting any such lease or to manage and work all or any part of my said real estate and use for that purpose any sheep or stock and plant belonging to my estate or to purchase any sheep stock or plant as they may think fit And I declare that all the rents and income received in respect of my estate of whatever form it may consist and whatever its state of investment may be shall be applicable as income for the purposes

of my will in the same manner as if the same proceeded from investments in stocks funds securities and debentures hereinbefore authorized."

From the time of the testator's death the trustees carried on and managed the station properties in the same manner as they had been managed in his lifetime, but after 1904, when the lease of Barwidgee came to an end, operations were confined to the three remaining properties, which were freehold, the sheep formerly on Barwidgee being transferred to Kangatong and Woperana. The reasons for judgment delivered in the Supreme Court contain a statement in detail of the manner in which the accounts of the station business were kept by the trustees, which need not be repeated here. It is sufficient for the purpose of this opinion to say that in these accounts the sheep on hand on each station at the beginning and at the end of each accounting period, including natural increase, and the sheep transferred from one of the stations to another were taken in at a fixed or standard value per head having no necessary relation to the true value, while purchases and sales of live-stock were taken in at the prices paid or received therefor. It is not suggested that the method of keeping the accounts adopted by the trustees was improper or in any respect unusual, having regard to the nature of the business. The testator's widow died on 20th November 1914, when the trust for accumulation came to an end and the appellants became entitled to receive their respective shares of the income of the estate accruing after that date. After the death of the testator's widow the accounts of the estate were balanced on 30th June in each year, and the amount shown to the credit of the income account, which included the balance of the working or trading account of each station, was divided among the persons entitled to participate in the income. At the date of testator's death the total number of sheep depasturing on the station properties was 36,779, at the date of the death of testator's widow 33,411, and in 1924 about 34,607.

On 4th February 1924 the trustees sold Woperana station with all live-stock thereon on a " walk-in walk-out " basis, the purchase-money including the sum of £21,507 18s. 4d. as the agreed price of the sheep to the number of 14,460 then depasturing thereon. These

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sheep stood in the books at the standard or fixed value of 10s. per head, or £7,230 in all. On 31st May 1924 the trustees held a clearing sale of the live-stock on Warrambeen. All the sheep depasturing on that station to the number of 2,784 were sold at that sale and realized £4,900 18s. 4d. These sheep stood in the books at the standard or fixed value of 12s. 6d. per head, or £1,740 in all. The land was sold separately.

The question now raised for decision relates to the sum by which the proceeds of these sales of sheep exceeded the amount at which the sheep sold stood in the books, namely, £14,277 18s. 4d. in respect of the Woperana sheep and £3,160 18s. 4d. in respect of the Warrambeen sheep, or £17,438 16s. 8d. in all.

The appellants claim that the whole of this sum represents income earned in the carrying on of the grazing business, and as such is divisible among the beneficiaries entitled to share in the income of the estate. Alternatively, they claim that the amount by which the proceeds of these sales respectively exceeded the real value at the death of the testator's widow of the sheep then depasturing on the respective stations is distributable as income. In the Supreme Court it was held that the whole sum in question should be appropriated to corpus. The question at issue depends on the intention of the testator expressed in his will.

In ascertaining the intention of the testator, who up to the time of his death was carrying on the business of a grazier on these stations, he must be regarded as a person acquainted with the usual method of conducting a business of that nature and with the rules which should be observed by trustees who are directed or authorized to carry on and manage it. This is so because the question for determination is not whether the sum in question is theoretically to be regarded as capital or as income, but whether on the true construction of his will the testator has expressed the intention that it shall belong to the persons to whom he has given the income of his estate. The business carried on both by the testator and by his trustees was that of woolgrowing and breeding and fattening sheep. In the ordinary course of that business sheep were from time to time bought and sold as occasion might require, the number on hand from time to time varying by reason

of natural increase and deaths and, presumably, also by reason of weather conditions. It is apparent that in the prudent management of such a business it is desirable that the number of sheep should be maintained in conformity with the carrying capacity of the land, regard being had to the condition of the country, the expectation of the seasons and other relevant conditions, and that the quality of the sheep should be kept up or improved. It follows that the number of sheep sold or bought, as the case may be, may vary considerably in different years, and that such variations when they occur must affect the income of the business. It is common knowledge also that the market value of sheep is liable to considerable fluctuations, and it cannot be supposed that a prudent manager of a business of this kind would take into account the current market value of sheep at the beginning and end of a given period as a factor in ascertaining the income of the business for that period. Hence the adoption of a fixed or standard value for the sheep on hand at the beginning and end of each accounting period. The testator must, I think, be taken to have been aware of the difficulty of applying hard and fast rules to the ascertainment of the periodical income of a business of this nature, and he abstained from prescribing by his will any method of ascertaining it. It is true that the will provides that all income received in respect of testator's estate in whatever state of investment shall be applicable as income for the purposes of the will as if proceeding from authorized investments, but this provision does no more than negative the application of the rule in *Howe* v. *Earl of Dartmouth* (1); it throws no further light on the question now under consideration.

Before considering in detail the provisions of the will, it may be well to see what it is that the appellants claim as income of the business carried on by the trustees. The sum claimed represents the difference between the market value of the sheep when sold in 1924 and the market value as at the death of testator's widow of the sheep then depasturing on the same stations. The sales in question were made, not in the course of carrying on the grazing business on these stations, but for the purpose of putting an end to that business, and were made in conjunction with, or as incidental

(1) (1802) 7 Ves. 137.

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to, sales of the land on which the business had been carried on. It is for the appellants to establish that the money so realized passes as income of the business under the terms of the will. It is not enough for them to show that this sum represents a profit made for the estate of the testator, or that the profit is due to the fact that the business was carried on under the power to postpone a sale instead of being wound up at an earlier date. They must show, in effect, that the testator has by his will given to them the whole increment in the value of the sheep used in the business which should accrue during the continuance of the business and be realized on its winding up, or, what is the same thing from another point of view, that he has given for the benefit of those entitled to the corpus of his residuary estate, not the sheep used in the business when it should be wound up and its assets converted into money, but only the value as at the date of his widow's death of the sheep then so used. In my opinion, it is impossible to establish either proposition on the true construction of this will. Apart from some inconsiderable legacies and annuities, the testator by his will gave all his property real and personal to his trustees on trust for sale and conversion into money and directed how the money realized by such sale and conversion, with certain accumulations of income added, was to be invested. By a later provision the trustees are directed not to sell the real estate for ten years after testator's death, and are empowered to postpone the sale of the real estate and the conversion of the personal estate in their discretion. So far it is clear that the whole proceeds of sale and conversion of the real and personal estate, whenever sold and converted, were to be treated as corpus. Then the trustees are authorized to lease or to manage and work the real estate, and to use for that purpose any sheep or stock and plant belonging to the estate or to purchase sheep, stock or plant. No direction is given as to the income of the grazing business if the trustees decide to manage and work the properties, except that the income received by the trustees from that source, whatever it may be, is to be treated as if it proceeded from an authorized investment of the corpus of the estate. The sheep, if retained and used by the trustees, are still treated as corpus from the use of which income may be derived by the trustees. It cannot be denied that the sheep

depasturing on the station at testator's death or at the death of his widow formed part of his estate, so that, if the trustees had elected to let the land and to sell the sheep instead of carrying on the business, the proceeds of sale of the sheep would have been corpus. The sheep which were on the stations at the time of the sales in 1924 were the progeny of or the substitutes for the sheep which were there at the testator's death. They were part of the testator's estate no less than the sheep which they replaced. They were sold, not in the ordinary course of management of the business, or for the purpose of carrying it on under the power conferred on the trustees in that behalf, but under the trust for conversion of the personal estate of the testator. Why, then, should not the proceeds of sale form part of the corpus of the estate ? It was not suggested, as I understood the argument, that the method adopted by the trustees for ascertaining the distributable income of the business while it was being carried on was incorrect, or that, but for the sale, the tenants for life would have been entitled to receive as income of the business any portion of the enhanced value of the sheep from time to time remaining unsold and depasturing on the stations so long as the business was carried on. But it was said that the sale of the sheep disclosed that, as a result of carrying on the business, a profit had been made over and above the amount distributed as income of the business, and that such profit when realized was income to which the tenants for life were entitled. This argument rests on the assumption that profit made by the sale of sheep employed in a grazing business is in all cases income of the business. That proposition cannot be maintained. No doubt, when sheep are sold in the ordinary course of management of such a business, the profit made on such sales is properly taken into account in ascertaining the income of the business, and in the present case this has been done and the tenants for life have had the benefit. But, where the profit is the result, not of sales made in the ordinary course of management, but of a sale of the whole of the sheep made for the purpose of putting an end to the business, the profit, in my opinion, cannot be properly regarded as income of the business or as income derived or received from the business. Under this will the proceeds of sale and conversion are corpus, and

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the tenants for life are entitled only to the income received by the trustees either from authorized investments of such proceeds or from the use by the trustees of the unconverted assets belonging to the estate. The amounts now in question represent, in my opinion, accretions to the value of capital assets, and not income of the business. As *Lindley* L.J. said in *In re Armitage*; *Armitage* v. *Garnett* (1), "when a person gets out of a concern more than he puts into it the difference is profit. If I put £100 into a concern and get out £105, I get £5 profit. In that sense of the word this £1 5s. 6½d. is profit, being the excess of the money produced by the sale of the investment over the amount of money invested. But is it income to which the tenant for life is entitled? That is a totally different matter, and I say that it clearly is not." Subject to any specific directions given by a testator or settlor, the duty of trustees empowered to manage and carry on a grazing business is to manage it according to the method which would be pursued by a prudent owner of the business, and to keep the accounts of the business in the manner usually adopted by such an owner. Accounts so kept should show at the end of each accounting period the sum which may properly be regarded as the distributable income of the business, and in the absence of special circumstances a person entitled to the income of the business should receive as such income this sum and no more. No such special circumstances exist in this case, and in my opinion the appellants have failed to establish that they are entitled to any part of the sums which they now claim. For these reasons I think the appeal should be dismissed.

ISAACS J. The respective rights of the parties of necessity depend upon the provisions of their common charter—the will of the testator. When that instrument is looked at and the accepted facts are borne in mind, the position seems to me uncommonly simple. When the testator died the property he left was, of course, corpus. He directed it to be converted into money—if not existing or collectable in that form—and the proceeds of conversion would also be corpus, being a mere transformation. He imposed certain restrictions as to time and events and these were duly

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

observed. He desired his trustees in the interim period preceding conversion to carry on the business of grazing and for that purpose to use any sheep, stock, or plant they thought fit or to purchase more. This they did, and whatever actual profits they made thereby were doubtless income. No claim is made as for income based on notional conversion. It is admitted that, except for the particular claim actually made, all income was properly paid.

On 4th February 1924 the trustees in their discretion determined to terminate the interim process and to exercise their primary power. They accordingly sold two stations and the stock thereon as a conversion. It follows practically automatically that the proceeds are corpus, though it is claimed that so much as represents the value of sheep over and above the number in 1914 is income. The Supreme Court thought the whole sum obtained on realization was corpus, and I agree with that conclusion.

The appeal should, in my opinion, be dismissed.

RICH J. I have had the opportunity of reading the judgment of the Chief Justice and agree with it.

Appeal dismissed with costs.

Solicitors for the appellants, *Malleson, Stewart, Stawell & Nankivell.*
Solicitors for the respondents, *Blake & Riggall*; *H. W. C. Simpson.*

B. L.