1934

* May 17
* June 15.

# IN THE MATTER OF THE ESTATE OF EDWARD H. KEATING, DECEASED

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

*Will—Administration and distribution of estate—Postponement of conversion into money of testator's shares of stock in company—Shares apparently unsaleable and no dividends received—Ultimate realization on shares on liquidation of company—Rights as between tenants for life and remaindermen as to moneys realized—Manner of distribution among shareholders of moneys received by company for its assets—Directions of will.*

K. died in 1912. In his will, after certain bequests, he devised and bequeathed the remainder of his property to his trustee to carry out the trusts of the will, which included conversion into money "in such manner and at such times as he may deem proper," direction to invest and power to change investments, direction for payments

* PRESENT:—Duff C.J. and Rinfret, Cannon, Crocket and Hughes JJ.

to K.'s widow out of income for maintenance, direction for division, after the widow's death (which occurred in 1916), of the balance of the net income of the estate among his children, and, by para. 14, direction that the capital of the estate be kept intact until at least one year after the death of K.'s last surviving child or of K.'s last surviving grand-child which might be living at K.'s death, whichever event should last happen, and then that the whole estate be distributed in a manner set out.

The estate left by K. included 250 ordinary shares of the capital stock of a company, of the par value of £10 each. No dividends were paid and the shares were apparently unsaleable, until an expropriation of the company's property which was followed in 1920 by a voluntary liquidation of the company for the purpose of distributing its assets, which apparently consisted wholly of the sum awarded for the expropriation and interest thereon. This interest was distributed on account of the arrears of dividends accumulated on the company's preference shares. The principal sum awarded was distributed "by way of return of capital" *pro rata* among the preference and ordinary shareholders pursuant to a direction of the court in England. In the years 1920-1922 the trustee of K.'s estate received from the company's liquidator sums aggregating $20,212.78.

Appellant, one of K.'s children, contended that the said sum of $20,212.78 received by the trustee should be apportioned between capital and income in accordance with the rule laid down in *In re Earl of Chesterfield's Trusts*, 24 Ch. D. 643; that the postponement of conversion of the shares was for the benefit of the estate—for the benefit both of the remaindermen and of the life tenants; and the said rule should be applied, so as to do justice as between life tenants and remaindermen, by dividing the funds received in such a way that they would respectively be in the same position as if it had been possible to convert the shares to advantage on the testator's death or within one year thereafter; that even if the sums when received by the trustee were capital realizations, that fact would not exclude the application of the equitable principle invoked.

*Held:* (1) The adjudication of the English court that the principal sum of the award should be distributed "by way of return of capital," etc., was not conclusive upon the parties to this appeal, as that direction was made on an originating proceeding to determine the respective rights of the preference and ordinary shareholders upon the winding up of the company, and was not also a determination of the respective rights of the life tenant and reversioner under the will of any shareholder.

(2) The sums when received by the trustee were clearly capital realizations (*In re Armitage*, [1893] 3 Ch. 337; *Inland Revenue Commissioner* v. *Burrell*, [1924] 2 K.B. 52; *Hill* v. *Permanent Trustee Co. of New South Wales Ltd.*, [1930] A.C. 720). The will itself excluded the application of the rule invoked. The application thereof asked for by appellant would effect a reduction of capital and be contrary to the said express direction in para. 14 of the will. The sums in question must remain in their entirety as part of the capital of the estate.

Judgment of the Court of Appeal for Ontario, [1934] O.R. 71, affirmed in the result.

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APPEAL (on leave granted by the Court of Appeal for Ontario) by C. Sedley Keating, one of the children of Edward H. Keating, deceased, from the judgment of the Court of Appeal for Ontario (1), dismissing (Middleton, J.A., dissenting) his appeal from the judgment of Jeffrey J. (on motion for determination of a question arising in the administration of the estate of said deceased), holding that the whole of certain sums of money realized by the executor of the estate of the said deceased out of 250 shares of the common stock of the Halifax Graving Dock Co. Ltd., part of the assets of the said estate, (said sums being realized upon the winding-up of the company), should be credited to capital only.

The appellant is one of the beneficiaries under the will of the said deceased, being entitled as life tenant to a share in the net income from the residuary estate after the payment of certain legacies and annuities. He claimed that the moneys realized as aforesaid should be apportioned as between income and capital in accordance with the rule in *In re Earl of Chesterfield's Trusts* (2). This claim was rejected by the judgments appealed from.

The material facts of the case are sufficiently stated in the judgment now reported, and are indicated in the above headnote. The appeal was dismissed with costs.

*R. L. Kellock* for the appellant.

*McGregor Young K.C.* for infant respondents and respondent charities.

*K. F. MacKenzie K.C.* for the executor and trustee of the deceased's estate.

The judgment of the court was delivered by

HUGHES J.—The late Edward H. Keating died on the 17th day of June, 1912. Among the assets which passed to the trustee were 250 ordinary shares of the capital stock of the Halifax Graving Dock Company, Limited, of the par value of £10 each. This company was an English company incorporated about the year 1886. In 1890 preference stock was created, amounting to 7,400 5% cumulative

(1) [1934] O.R. 71; [1934] 1 D.L.R. 510.

(2) (1883) 24 Ch. D. 643.

shares of the par value of £10 each. When the company went into liquidation, as hereinafter mentioned, there were 7,400 preference shares outstanding and 7,365 ordinary shares of the same par value. The company carried on the business of a dry dock until an explosion occurred on the 6th day of December, 1917, when the property was severely damaged. About the time the repairs were completed, namely in May, 1918, the property was expropriated by the Dominion Government.

Compensation amounting to about $1,400,000 was awarded to the company by the Exchequer Court of Canada on July 6, 1920, with interest at 5% from the date of expropriation. Thereafter the company went into voluntary liquidation for the purpose of distributing its assets, which apparently consisted wholly of the moneys received from the expropriation proceedings. No dividends had been paid on either preferred or ordinary shares of the company, and apparently there was no accumulated income available for distribution as dividends, as the only income distributed on the liquidation was the interest received from the Dominion Government upon the award. This interest was distributed on account of the arrears of dividends accumulated upon the preference shares. The principal amount of the award was distributed "by way of return of capital" *pro rata* among the preference and ordinary shareholders pursuant to a direction of the court in England.

Upon the distribution of the assets, the Royal Trust Company, executor and trustee of the estate of the late Edward H. Keating, received from the liquidator the sum of $20,212.78 in the following amounts at the following times:

| | |
|---|---|
| Nov. 13, 1920 | $ 9,250 00 |
| May 23, 1921 | 10,029 37 |
| Oct. 19, 1921 | 905 25 |
| Apr. 19, 1922 | 28 16 |

It should also be mentioned that in the inventory filed by the trustee on the application for letters probate, the shares were listed as of no value. They were then unsaleable, and continued to be apparently unsaleable and of no value until the expropriation.

By his last will and testament, the testator made certain specific bequests and then devised and bequeathed the

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whole of the remainder of his real and personal property to the trustee to carry out the trusts created by the will.

Some of the remaining provisions are very important.

4. In trust that the said trustee may sell, collect and convert into money all such parts of my estate as shall not consist of money in such manner and at such times as he may deem proper.

5. I direct that after paying my just debts and funeral expenses all moneys belonging to my estate not already well invested are to be invested by my trustee for the benefit of my estate and in such securities as he may consider proper and best and that the said trustee may from time to time at his discretion vary or transpose any investments for others which may be deemed preferable.

6. I direct that my said wife is to be paid monthly out of the net income from my estate the sum of three hundred and fifty dollars or four thousand two hundred dollars per annum during her lifetime for her use and maintenance and for the maintenance of my unmarried daughter Jessie and that this is to be a first charge against the revenues of my estate after paying the annuities in the next succeeding clause 7.

* * * *

8. After the death of my said wife if she survives me or after my death if I survive her I direct that the following disposition is to be made, viz.,

* * * *

10. I direct that the balance of the net income of my estate after deducting the annuities and amounts reserved in the three preceding clauses, 7, 8, and 9, is to be divided equally among my surviving children, Jessie, Heloise, Agnes and Sedley, and paid in monthly or quarterly instalments subject to the following express provision and stipulation, viz., that if in any year the share coming to my daughter Jessie under such division should amount to less than two thousand dollars per annum I direct that she is to receive that amount (viz: $2,000) in full per annum until her marriage and that the remaining balance only is in that event to be equally divided between Heloise, Agnes and Sedley my intention being that she is to be assured and is to receive at least $2,000 per annum for her sole use and enjoyment until her marriage.

* * * *

14. I direct that the capital of my said estate shall be kept intact and only the income derived therefrom distributed as I have in this my last will and testament directed until at least one year after the death of my last surviving child or of my last surviving grand-child which may be living at the time of my death which ever event shall last happen—when I direct that the whole of my said estate shall be distributed amongst my next-of-kin as provided by "The Statute of Distribution" or any other law providing for the devolution of estates in force in the Province of Ontario in so far and providing that my said next-of-kin are my own lineal descendants. In the event of there being no lineal descendants of my own then living I direct that the whole of my said estate shall in that case be distributed equally among the following charitable institutions or among so many of them as may then exist, viz:

The Toronto Dispensary for the relief of the Sick Poor.
The Nursing Mission (Hayter Street), Toronto.
The Nursing Mission (Beverley Street), Toronto.
The West End Creche, Toronto.
The Sick Children's Hospital, Toronto.

The Home for Incurable Children, Toronto.
The Children's Aid Society, Toronto.
The Association for the Relief of the Poor, Halifax, N.S.
The Benevolent Fund of the Canadian Society of Civil Engineers, Montreal.
The Benevolent Fund of the Institution of Civil Engineers, London, G.B.

15. I appoint the Royal Trust Company of Canada my executor and trustee for the purposes aforesaid and I request that a copy of this my will be furnished to each of my children as soon as it can conveniently be done after my death.

The testator's widow died on December 3, 1916.

The appellant contends that upon the true construction of the last will and testament of the deceased the said sum of $20,212.78 received by the trustee should be apportioned between capital and income in accordance with the rule laid down in *In re Earl of Chesterfield's Trusts* (1). An application was made by the appellant and Heloise J. Macklem before Mr. Justice Jeffrey by way of originating notice for determination of the question. Mr. Justice Jeffrey held that the whole sum should be credited to capital only. From this order an appeal was taken to the Court of Appeal for Ontario and the Court of Appeal, by a majority judgment, dismissed the appeal.

From this order the appellant, C. Sedley Keating, now appeals to this Court.

In *In re Earl of Chesterfield's Trusts* (1), it was decided that where a testator has bequeathed his residuary personal estate to trustees upon trust for conversion, with power to postpone such conversion at their discretion, and to hold the proceeds upon trust for a person for life with remainders over, and such residue includes outstanding personal estate, the conversion of which the trustees, in the exercise of their discretion, postpone for the benefit of the estate, and which eventually falls in some years after the testator's death—as, for instance, a mortgage debt with arrears of interest, or arrears of an annuity with interest, or moneys payable on a life policy—such outstanding personal estate should, on falling in, be apportioned as between capital and income by ascertaining the sum which, put out at interest at 4 per cent. per annum on the day of the testator's death, and accumulating at compound interest calculated at that rate with yearly rests and de-

(1) (1883) 24 Ch. D. 643.

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ducting income tax, would, with the accumulations of interest, have produced, at the day of receipt, the amount actually received; and the sum so ascertained should be treated as capital, and the residue as income.

It was contended by the respondents that the adjudication of the court in England that the principal amount of the award should be distributed "by way of return of capital" *pro rata* among the preference and ordinary shareholders was conclusive and binding upon the parties to the appeal. That direction, however, was made on an originating proceeding to determine the respective rights of the preference and ordinary shareholders upon the winding up of the company, and was not also a determination of the respective rights of the life tenant and reversioner under the will of any shareholder.

In *Hill* v. *Permanent Trustee Company of New South Wales, Limited* (1), a company sold substantially the whole of its lands and other assets and ceased to carry on business. In 1926 a dividend was declared and paid as "a distribution of capital assets in advance of the winding up." No question arose in the appeal as to that dividend. In November, 1927, the company declared and paid a dividend, stating that it was paid out of the sale of breeding stock. Upon an originating summons issued by trustees, who held over two-thirds of the shares issued, the Supreme Court held that the dividend should be treated as capital of the trust estate. Upon appeal to the Privy Council, it was held that the dividend should be treated as income of the trust estate. In delivering the judgment of the Judicial Committee, Lord Russell of Killowen said, at page 729:—

> These being the relevant facts of the case the point for decision is capable of statement thus: Is the sum of £19,380 "net income or profits to be derived from such investment or investments," or is it "capital of my said trust estate?"
>
> The question which thus arises is one which may frequently occur when investments, representing a settled trust fund, include shares in a limited company which are not restricted to a fixed rate of dividend. So long as such a company is a going concern and is not restricted as to the profits out of which it may pay dividends, it may distribute as dividends to its shareholders the excess of its revenue receipts over expenses properly chargeable to revenue account. The balance to the credit of profit and loss account may in many cases be divided as dividend even if the company's capital account is in debit; and such

(1) [1930] A.C. 720.

a distribution by way of dividend would, prima facie, be "income or profits" of the trust share, and belong to the tenant for life; it would not be "capital of my trust estate." On the other hand, if the company instead of distributing the same balance as dividends, resolved upon liquidation, the shareholder would be repaid his share capital and in addition the share of surplus assets in the liquidation attributable to his shares. The moneys received by the shareholder in the liquidation may be swollen by reason of the fact that the company has in its possession undivided profits, but no part thereof would belong to a tenant for life as income; it would all be corpus of the trust estate.

From this it would appear that moneys paid in respect of shares in a limited company may be income or corpus of a settled share according to the procedure adopted, i.e., according as the moneys are paid by way of dividend before liquidation or are paid by way of surplus assets in a winding up. Each process might appear to involve some injustice, the former to the remainderman, the latter to the tenant for life.

And at pages 730 and 731:—

A limited company when it parts with moneys available for distribution among its shareholders is not concerned with the fate of those moneys in the hands of any shareholder. The company does not know and does not care whether a shareholder is a trustee of his shares or not. It is of no concern to a company which is parting with moneys to a shareholder whether that shareholder (if he be a trustee) will hold them as trustee for A. absolutely or as trustee for A. for life only * * * If such moneys or any part thereof are to be treated as part of the corpus of the trust estate there must be some provision in the trust deed which brings about that result. No statement by the company or its officers that moneys which are being paid away to shareholders out of profits are capital, or are to be treated as capital, can have any effect upon the rights of the beneficiaries under a trust instrument which comprises shares in the company.

And at page 734:—

Their Lordships desire to say a word in reference to *In re Armitage* (1). * * * The legal position in that case was quite plain. The old company had sold its assets (including accumulated profits) to the new company for a price which produced surplus assets in the winding up of the old company to the amount of £9 5s. 6d. for each share of the old company upon which only £8 per share had, in fact, been paid up. Upon no theory could it be said that any part of the £9 5s. 6d. was payable to the tenant for life. The moneys paid were all surplus assets distributed in a winding up and took the place in the trust estate of the shares themselves. The difference between the £9 5s. 6d. and the £8 was a profit to the trust estate, just as if the shares had been sold and had realized £9 5s. 6d. per share; but no part of the £9 5s. 6d. was income of the tenant for life.

In *In re Armitage; Armitage* v. *Garnett* (1), a testator gave his estate upon the usual trusts for conversion and investment, with a power to postpone conversion and a direction that during the interval all income produced by the property in its actual state should be treated as income

(1) [1893] 3 Ch. 337.

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for the purposes of his will. He bequeathed one-third of the residue 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 reconstituted and the new company paid for the testator's shares £9 5s. apiece, being £1 5s. per share more than had been paid up. This excess arose from two funds, one of which consisted of profits which the directors had retained to meet contingencies. It was held, on appeal, that the right of the tenant for life of shares is only to receive dividends and bonuses in the shape of dividends declared during his life, and that the £1 5s. per share, though it was profits, was not income to which the tenant for life was entitled but must go to capital. Lord Justice Lindley said, pages 345 and 346:

> The company was wound up, and the assets of the company were distributed amongst the registered shareholders * * * Those undivided profits of course could have been divided as dividends if the company had so thought fit. * * * 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. * * * 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. He does not mean him to have such profits, for example, as arise by a realization of shares; he never dreamed of such profits going to the tenant for life. * * * This conclusion is completely in accord with *Bouch* v. *Sproule* (2), which at least, 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.

Lopes, L.J., was also of opinion that as the company was voluntarily winding up and had not previously declared dividends in respect of the excess, the latter was not income but capital and did not go to the tenant for life. A. L. Smith, L.J., agreed with Lord Justice Lindley.

The appellant pointed out that the shares of the Halifax Graving Dock Company, Limited, were retained by the trustee until the receipt by him of the proceeds of the shares in the winding-up, and that it was for the benefit

(2) (1887) 12 App. Cas. 385.

of the estate that the conversion of the shares should be postponed rather than that they should have been sold at a sacrifice in the years 1912 or 1913. He urged that the postponement was for the benefit of the remaindermen as well as for the benefit of the life tenants, and submitted that the rule set out in *In re Earl of Chesterfield's Trusts* (1) was evolved for the purpose of doing justice as between life tenant and remainderman, by dividing the funds received in such a way that they would respectively be in the same position as if it had been possible to convert the shares to advantage on the death of the testator or within one year thereafter.

Now there is no doubt that the sums of money received by the trustee, when received, were capital realizations. *In re Armitage; Armitage* v. *Garnett* (2); *Inland Revenue Commissioner* v. *Burrell* (3); and *Hill* v. *Permanent Trustee Company of New South Wales Ltd.* (4). The appellant, however, contends that, although the sums when received by the trustee may have been capital realizations, there is nothing in that fact to exclude the application of the equitable principle illustrated by *In re Earl of Chesterfield's Trusts* (1). In my opinion, however, the will itself excludes the application of the rule. By paragraph 14 of the will, the testator directs that the capital of the estate is to be kept intact, and only the income derived therefrom distributed until at least one year after the death of the last surviving child or of the last surviving grand-child living at the death of the testator, whichever event may last happen. The application of the rule asked by the appellant would effect a reduction of capital and would, in my opinion, be contrary to the express direction of the testator as set out in paragraph 14 of the will.

I am, therefore, of opinion that the sums in question must remain in their entirety as part of the capital of the estate, as was held by Mr. Justice Jeffrey and by the majority of the Court of Appeal.

The appeal, therefore, should be dismissed with costs.

*Appeal dismissed with costs.*

(1) (1883) 24 Ch. D. 643.
(2) [1893] 3 Ch. 337.
(3) [1924] 2 K.B. 52.
(4) [1930] A.C. 720.

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Solicitors for the appellant: *Mason, Foulds, Davidson, Carter & Kellock.*

Official Guardian (for infant respondents): *McGregor Young.*

Solicitor for the Public Trustee (representing respondent charities): *C. M. Garvey.*

Solicitors for the respondent The Royal Trust Company (executor and trustee of the will of deceased): *MacKenzie & Saunderson.*

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* PRESENT:—Duff C.J. and Rinfret, Lamont, Cannon, Crocket and Hughes JJ.