

tingent on the heir's survivance for the period prescribed by the statute.

It is not within the defender's power to surrender the real estate in England to the uses of the will, and it follows, in my opinion, that the defender's right to the legacies bequeathed to him is not conditional on his making such surrender. In other words, he is not bound to elect between his right as heir and his right under the will.

I do not add more on this point, because I agree with all that is said by the Lord Ordinary regarding it, and adopt entirely his Lordship's interpretation of the decisions in which this subject is discussed.

The Lord Ordinary has left open the liability of the real estate to contribute to the payment of debts and legacies. If the claim of the trustees under this head was confined to the subject of the right to charge a proportion of the debts and personal legacies on the real estate, we should be in a position to dispose of the question at present. But the trustees claim the right to charge a proportional part of the charitable bequests on the English estate, and it is evidently impossible to separate the two questions so as to give an effectual decision applicable to the one class of testamentary charges while the other point is left open.

Since this case came into the Inner House a suit has been instituted in the Chancery Division of the Supreme Court in England, for the purpose of ascertaining the rights of the heir-at-law and the trustees in relation to the English estate.

If the administrative title of the trustees is sustained as relative to the real estate, it will then be for the Court to determine to what extent the English estate can be affected with payment of debts and legacies, consistently with our recognition of the invalidity of the disposition of that estate in part to charitable uses.

If the trustees do not succeed in establishing their administrative title a different question will arise, viz., the question whether the claim of the trustees to burden the English estate with debts and personal legacies can be made good by withholding payment of the pecuniary legacy payable to the defender.

Nothing that we decide this day is intended to prejudge their claims. In the meantime I agree with Lord Kinnear that the case is not in shape for the decision of any question except the question of election, which we are now considering, and I suggest that your Lordships should affirm the Lord Ordinary's interlocutor and sist proceedings in the meantime, leaving it to the parties to move, when by the decision of the English suit or from other causes the difficulty I have referred to may be removed.

LORD ADAM and LORD KINNEAR concurred.

LORD ADAM intimated that the LORD PRESIDENT, who was absent, concurred in the opinion of Lord M'Laren.

The Court adhered.

Counsel for the Pursuers—Graham Murray—C. S. Dickson—J. Brodie Innes. Agents—Davidson & Syme, W.S.

Counsel for the Defender—Asher, Q.C.—Lorimer. Agents—Morton, Smart, & Macdonald, W.S.

Friday, March 20.

## FIRST DIVISION

### THE NIDDRIE & BENHAR COAL COMPANY, LIMITED, AND ANOTHER v. HURLL.

*Public Company—Memorandum of Association—Preference Share—Division of Profits.*

The memorandum of association of an incorporated company declared the capital to be divided into A or preference, and B or ordinary shares, and provided that the A shares should rank prior to the B shares on the profits of each year for a 10 per cent. dividend; that the "B" shares should rank on the balance of the profits of each year after the preferential dividend was paid; and that no deficiency in dividend in any year should be made good out of the profits of future years.

For several years a loss on the ordinary revenue account of the company resulted in a debit balance on that account. The debit balance was subsequently reduced, and in the year ending 30th April 1890 profits were earned which were not applied as dividend, but applied in further reducing the debit balance. During the following year profits were earned sufficient to wipe out the debit balance, to pay 10 per cent. of preference dividend to the A shareholders, and to leave a surplus available for division.

Held that the A shareholders were not entitled to have this surplus applied in payment of a preference dividend on the A shares as for the year ending 30th April 1890, and that the surplus fell to be applied in payment of a dividend to the B shareholders for the current year.

The Niddrie and Benhar Coal Company, Limited, were incorporated under the Companies Acts 1862 to 1880 on the 16th day of August 1882, with a memorandum and articles of association. By the memorandum of association the capital of the company was declared to be £152,500, divided into 15,000 shares, therein termed A or preference shares of £5 each, and 62,000 shares, therein termed B or ordinary shares of £1, 5s. each, having the following rights and privileges, as set out in the memorandum of association, namely:—"The A shares shall rank prior to the B shares on the profits of each year, ending on the 31st day

of December [now 30th April], for a dividend at the rate of 10 per cent. per annum on the amount paid up thereon. . . . The B shares shall, for the purpose of calculating dividends from profits, be credited with £3, 15s. per share as paid thereon, in addition to such part of the said £1, 5s. as may be paid up thereon at the time. The B shares shall rank on the balance of the profits of each year remaining after payment of the said preferential dividend on the A shares for a dividend of 10 per cent. per annum, calculated after crediting each B share with £3, 15s. as aforesaid. Any surplus divisible profits which may remain after payment of the said dividends shall belong to both classes of shares without any priority between them—the B shares always receiving credit as above mentioned. No deficiency in dividend in any year shall be made good out of the profits of future years.” . . .

For some years prior to 30th April 1886 there was a loss on the ordinary revenue account of the company, resulting in a debit balance on that account as at that date of £12,065, 13s. 8d. This debit balance was, by the transactions of the subsequent year, reduced to £7867, 0s. 2d., at which figure it stood as at 30th April 1889, the 30th April being the date on which the annual accounts of the company were made up. During the year, from 30th April 1889 to 30th April 1890, net profits were earned to the amount of £6909, 8s. 7d. This sum was not available for division and was not divided among the shareholders by way of dividend owing to the debit balance on the profit and loss account from previous years. Deducting this sum of £6909, 8s. 7d. from the debit balance with which the year ending 30th April 1890 commenced, there was left a debit balance of £957, 11s. 7d. as at the close of the year on 30th April 1890. During the year commencing 1st May 1890 profits were earned sufficient to wipe out the debit balance of £957, 11s. 7d., and also to leave a surplus available for division. A question arose between the A and the B shareholders as to how the balance of the surplus was to be disposed of after the A shareholders had been paid a preferential dividend of 10 per cent.

The present special case was accordingly presented by (1) the company and a holder of 760 ordinary or B shares, and (2) a holder of 400 A or preference shares. The second party claimed that he was entitled to have the said balance, to the extent necessary for that purpose, applied in payment of a 10 per cent. dividend to A shareholders as dividend for the year ending 30th April 1890, in respect that the profits for that year were not available for division, or were not actually divided and paid as dividend, owing to a debit balance on revenue account from previous years. He claimed that, under the provisions of the memorandum of association, as between the two classes of shareholders, there was to be an annual accounting, and that the loss in a previous year was not to be wiped out by the profits of a succeeding year in such a way as ultimately to deprive the A shareholders of dividend for the year in which such profit was earned.

The first parties, as for the B shareholders, claimed on the other hand that they were entitled to have the balance applied in paying dividend to them as for the current year. They contended that under the memorandum of association no deficiency in dividend in any year was to be made good out of the profits of future years; and that, as the profits earned during the year ending 30th April 1890 were *de facto* not available for division, there was a deficiency in the sense of the clause in the memorandum of association, and that such deficiency could not be made good out of the profits of a future year.

The following questions were submitted for the opinion of the Court:—“Is the second party, as the holder of A shares, entitled to have the balance of the profits of the current year (after satisfying the 10 per cent. dividend for the current year) applied, to the extent necessary for that purpose, in payment of a preference dividend on the A shares as for the year ending 30th April 1890? or, Are the B shareholders entitled to have the said balance applied in payment of a dividend to them for the current year without deduction of such dividend to the A shareholders for the year ending 30th April 1890?”

Argued for the first party—The claim of the second party was excluded by the clause in the memorandum, which declared that no deficiency in dividend in any year should be made good out of the profits of future years. The A shareholders were not entitled to any dividend at all for the year ending April 1890, because no profits available for division were earned that year, and they were not entitled to have a share of the current year's earnings applied to a dividend which never was earned. The case of *Henry v. The Great Northern Railway Company* did not apply, because in that case there was no clause as here restricting the preference shareholders to the profits of the current year.

Argued for the second party—The A shareholders were entitled to have the profits of the year applied in payment of a dividend for the previous year because they were preference shareholders. Preference shares implied cumulative dividends. When a profit was earned any year the right of the A shareholders emerged. If that profit was devoted to the payment of debts for the previous year the rights of the A shareholders lay over. The real meaning of profits was earnings unalotted by the directors—*Henry v. Great Northern Railway Company*, 1 De Gex & Jones, p. 637; *Crawford v. The North Eastern Railway Company*, 3 Kay & Johnston, 743; *Dent v. London Tramway Company*, L.R., 16 Ch. Div. 344.

At advising—

LORD ADAM—The question raised in this special case is one between A and B shareholders of the Niddrie and Benhar Coal Company as to the disposal of the profits earned, or which will be earned, during the year now current ending on 30th April 1891.

The facts which raise the question are

set forth in the special case, and are these. It seems that by the memorandum of association of the Niddrie and Benhar Coal Company the capital of the company is declared to be £152,500 divided into 15,000 shares, therein termed A or preference shares of £5 each, and 62,000 shares, therein termed B or ordinary shares of £1, 5s. Then the rights and privileges of these respective shares are these. It is provided that the A shares shall rank prior to the B shares on the profits of each year ending on the 31st day of December (now changed to 30th April) for a dividend at the rate of 10 per cent. per annum on the amount paid thereon. Then the rights of B shares are these. The B shares shall, for the purpose of calculating dividends from profits, be credited with £3, 15s. per share as paid thereon in addition to such part of the said £1, 5s. as may be paid up thereon at the time. Then there is this very material paragraph—the B shares shall rank on the balance of the profits of each year remaining after payment of the said preferential dividend on the A shares for a dividend of 10 per cent. per annum calculated after crediting each B share with £3, 15s. as aforesaid. Then there is a clause dealing with the disposal of the surplus remaining over after these two payments, and directing that it shall be divided equally. Then the next article is this—No deficiency of dividend in any year shall be made good out of the profits of future years. The company has power to redeem the A shares, and we are told that of the preference shares 10,000 are in issue and are fully paid up. It is said that for some years prior to 30th April 1886 there was a large loss resulting in a debit balance on the ordinary revenue account of the company, as at that date, of £12,065, 13s. 8d. This debit balance was, by the transactions of the subsequent year, reduced to £7867, 0s. 2d., at which figure it stood as at 30th April 1889, the 30th April being the date on which the annual accounts of the company are made up. During the year from 30th April 1889 to 30th April 1890 net profits were earned to the amount of £6909, 8s. 7d. This sum was not available for division, and was not divided among the shareholders by way of dividend owing to the debit balance on the profit and loss account from previous years. Then it is stated that deducting this sum of £6909, 8s. 7d. from the debit balance with which the year ending 30th April 1890 commenced, there was left a debit balance of £957, 11s. 7d. as at the close of the year on 30th April 1890; that is to say, at the commencement of the present current year there was a debt on the revenue account against the company of £957, 11s. 7d. Then the fifth article is this—During the current year commencing 1st May 1890 profits have been earned sufficient both to wipe out the said debit balance of £957, 11s. 7d. and leave a surplus available for division. Both parties admit that out of said surplus the A shareholders are entitled to a preferential dividend of 10 per cent. as for the current year. They are, however, not agreed as to the disposal

of the balance of the said surplus after paying the said preference dividend, and it is that that raises the question.

Now, as I understand that article, although the current year is not completed the company have already earned sufficient to pay 10 per cent. of preference dividend to the A shareholders, to pay the debit balance at the beginning of the year of £957, 11s. 7d., and to leave a surplus over for division.

That is the state of the fact which raises the question between the parties, and the questions which we are asked are these—Is the second party, as the holder of A shares, entitled to have the balance of the profits of the current year (after satisfying the 10 per cent. dividend for the current year) applied, to the extent necessary for that purpose, in payment of a preference dividend on the A shares as for the year ending 30th April 1890? or, Are the B shareholders entitled to have the said balance applied in payment of a dividend to them for the current year without deduction of such dividend to the A shareholders for the year ending 30th April 1890? These are the questions put, and which we are asked to answer. The question put just comes to this—Whether the A shareholders are entitled to have the profits of this year applied in payment of a dividend for the previous year? That is the contention shortly stated on the part of the A shareholders.

The first article of the memorandum of association which bears upon this is the one first in order—The A shares shall rank prior to the B shares on the profits of each year (ending on 30th April) for a dividend at the rate of 10 per cent. per annum on the amount of the paid up capital. That is the right of the A shares. Now the first question is—Were the A shares entitled to any dividend at all for the year ending 30th April 1890? And that depends upon the question whether there were any profits available for dividend. That raises the question—What are profits properly so called? and in that I quite agree with Mr Buckley's definition, which is, that profits are the excess of the ordinary receipts over the expenses properly chargeable to revenue account. I also agree with him when he says that when a loss on the revenue account has been sustained, there is, of course, no profit until that loss has been made good either by set-off of previous undivided profits still in hand, or by profits subsequently earned. Now, that is the case we are dealing with here. We are dealing with a case of proper revenue account—with a proper revenue account showing a debit balance of £957, 11s. 7d. at the end of last year—and accordingly on a proper statement of accounts it is clear that there was no profit earned by the company last year at all—I mean profit available for dividend; and if that was so, then the first thing is that the A shareholders were not entitled to dividend last year at all. Now if that is so, they cannot be entitled to have a share of the current year's earnings applied to a dividend which

never was earned. The statement printed makes that very clear, because during the year from 30th April 1889 to 30th April 1890 net profits were earned amounting to £6909, 8s. 7d.; but although that is called net profit, according to the definition which I have read net profit only arises on the debit balance on the revenue account being made good, so that this cannot properly be called profit. That is done in this case—the whole of these so called profits were applied towards the extinction of the debit balance as amounting to £7867, 0s. 2d. Therefore upon that ground I should say that the only answer that can be given to the question is that the A shareholders are not entitled to have any part of the profits of the current year applied to payment of a dividend which was not earned last year. The clause in the memorandum says that the A shares shall rank prior to the B shares on the profits of each year. That is the whole right. And the fourth article distinctly says that no deficiency of dividend in any year shall be made good out of the profits of future years. Now, how in the face of articles in these terms can it be said that the dividend which amounted to nil in 1890 is to be made good out of the profits of the current year?

We were referred, as dealing with this question, to the case of *Henry v. The Great Northern Railway Company*. What was decided in that case was this—where a company having power so to do, issued preference capital carrying a dividend of 10 per cent. per annum payable half yearly, and with no words to restrict the preference shareholders to the profits of the current year, it was held that if the profits in any one year were insufficient to pay 10 per cent. in full, the deficiency was as between the preference and ordinary shareholders to be made good out of the subsequent profits. Now, that shows that we have here exactly what was desiderated in the case of *Henry*, because we have in the memorandum and articles of association words restricting the preference shareholders to the profits of the current year. Therefore I think the case of *Henry* has really no bearing upon this question.

I am quite aware that a company having articles such as are contained in this memorandum of association may be liable to abuse, because it is obvious enough—as was pressed upon us—that the directors by manipulating the accounts might by carrying large sums from profits to a reserve fund, or in other ways, at the expense of the A shareholders, benefit the B shareholders. That is quite true, but if any attempt of that sort was made I have no doubt the Court would find a remedy.

I am therefore of opinion that the proper disposal of the surplus which the company has earned is, first, to extinguish the debt of £957, 11s. 7d.—although that question is not before us—and in the next place, that the A shareholders are entitled to 10 per cent., and after that the B shareholders are entitled to have the balance applied in payment of dividend to them, the remainder, if there is any, to belong to both.

I therefore move that we answer the first question in the negative, or, in other words, that we answer the second question in the affirmative.

LORD M'LAREN—I concur in the view of your Lordship in the chair. It was contended by one of the parties that profit means merely the result of the operations of the financial year; the difference between the income and the expenditure of that year. I think that is an incomplete definition, and is neither consistent with the law nor with sound commercial accounting. Profit and loss in my view represent the aggregate of all the commercial transactions of the company from the time when it commenced business, and the way in which it is represented is by bringing into the account of any year the balance of profit or loss resulting from the close of the previous year's transactions; and when that principle is applied it is plain enough in this case that the supposed profit has no real existence, because it is only obtained by leaving out of account the loss which falls to be extinguished, and which was at the debit at the commencement of the year's account.

LORD KINNEAR—I have come to the same conclusion. The A shareholders are to have a preference to the profits of each year. Now, the word "profits" no doubt may have various meanings, but I agree with your Lordship in the chair that the word must be taken to mean here the excess of the receipts in any year over the expenditure which has been incurred in order to earn those receipts. Now, the preference shareholders having that right over the profits, there is a further stipulation in the contract that no deficiency in dividend in any year shall be made good out of the profits of future years; and that of course must mean that if the profit in the sense in which your Lordship defined in any one year is insufficient to pay any dividend, or to pay the full dividend, to which the preference shareholders are entitled, they must submit to the failure, and cannot make good the deficiency of that year out of the larger profit of any subsequent year. So far there does not seem to be very much difficulty in considering the matter.

But then these definitions do not solve the practical question which is raised in this case, and which may be one of difficulty, because it must always be a question in the conduct of business what is the expenditure which is to be deducted in order to ascertain the excess of earnings over the expense of realising them; and that is a question which may sometimes be one of difficulty. If the company has sustained losses, there may be a question for the members or administrators of the company to consider whether such losses are payable out of current receipts, or whether they are not so payable; and I presume that in the ordinary case that is a question which would be determined by a majority of the members of the company—by a majority of the partners if it was an ordinary firm, and

by a majority of members if it was a company of this kind, unless there was any provision in the contract which would over-ride the judgment of the majority. It appears to me that it might be a question in the absence of such provision in the contract whether the excess of earnings in any year might not be divided as profits although some portion of the capital might have been lost. That might possibly be; there is no rule of law so far as I know which would prevent a copartnership so treating their accounts. But then the difficulty arises where according to the constitution of the company the shareholders are divided into two classes having adverse interests; and in such a case it would be impossible to hold that the shareholders having a preference, or being subject to postponement as the case might be, were necessarily to be bound by the judgment of the whole shareholders having a different interest from theirs merely because the one body was larger than the other. It therefore appears to me that the question which is raised in the statement of fact which is put before us might be one of some delicacy.

It is said that there had been a loss upon the ordinary revenue account of the company, resulting in a debit balance at 30th April 1886, and that it so remained until 30th April 1889, and that during that year profits had been made to the amount of £6909, 8s. 7d., and these net profits were applied by the company in wiping out the debit balance on the profit and loss account of previous years. Now, I must say that if I were required to determine whether that was a proper mode of treating the account or not, I would require some further information. But then I do not think that is a question which is raised for our determination at all, not only because there is nothing set forth in the special case to challenge the method in which the accounts were stated, but because upon the face of the special case the parties are agreed that that was a proper mode of treating the account. When parties are agreed to present a special case to the Court, and ask for their opinion and judgment upon any questions arising out of it, then they are bound by the judicial contract between them; all the statements of facts, or statements of mixed law and fact, which the special case contains are conclusive and binding, and not only so, but are exhaustive of all the facts which are necessary to enable the Court to give judgment upon the questions arising. Now, that being so, I take it that the parties are agreed that in consequence of the existence of this debit balance there was no sum available for division among the shareholders by way of dividend. If that mode of dealing with the account were right, then of course there was no profit which could be allocated to the preference shareholders; if it were wrong, then it follows equally of course that the dividend which ought to have been paid to the preference shareholders was wrongly applied in wiping out the debit upon the account. Therefore it ap-

pears to me that when the second party in this case claims to have a dividend which might have been payable to him in that year made good out of the larger profits of the subsequent year, he is merely in a position to maintain that he is entitled to recover from the company—that is, from the other shareholders—moneys which have been improperly applied. That is the meaning—and the only meaning—which can be put upon the argument which was addressed to us in support of the special case. If the thing was rightly done, there was no dividend; if it was wrongly done, then money was improperly applied which ought to have gone to preference shareholders; and when the question is put in that way, it becomes quite obvious that the second party cannot maintain that position, because it is a statement of fact upon which he has agreed, and which is binding upon him and upon the other party, that there was no part available for division in the year in which this sum of £6909, 11s. 7d. was applied to wipe out the debit balance. Therefore it appears to me to be quite clear upon the statements in the case that there was a deficiency of dividend in the sense of the memorandum of association in that year which he is not entitled to have made good out of the profits of the present year.

The LORD PRESIDENT was absent.

The Court answered the first question in the negative and the second question in the affirmative.

Counsel for the First Parties—Salvesen. Agents—Drummond & Reid, W.S.

Counsel for the Second Party—Clyde. Agents—Stuart & Stuart, W.S.

Friday, December 19, 1890.

## FIRST DIVISION.

[Lord Kinnear, Ordinary.]

JAMES BROWN & COMPANY v.  
M'CALLUM AND OTHERS.

*Bankruptcy—Reduction—Illegal Preference—Title to Sue—Act 1696, c. 5—Bankruptcy Act 1856 (19 and 20 Vict. c. 79), secs. 10, 11.*

The right of an individual creditor to reduce an illegal preference granted by his debtor in contravention of the Act of 1696, c. 5, is not excluded upon the sequestration of the debtor in respect of the right to reduce "for behoof of the whole body of creditors" conferred upon the trustee by the 11th section of the Bankruptcy (Scotland) Act 1856.

This was an action at the instance of James Brown & Company, venetian blind manufacturers, Glasgow, against John M'Callum and Robert Bowie, for the reduction of a disposition in their favour dated 16th and recorded 17th March 1888. The defenders were cautioners in a cash-credit bond granted to the Clydesdale Bank