Judgment of the Lords of the Judicial Committee of the Privy Council on the Appeal of ***Edgar*** **v.** ***Plomley*** *and Another, from the Supreme Court of New South Wales; delivered* 15*th May* 1900.

Present at the Hearing:

LORD HOBHOUSE.
LORD MORRIS.
LORD DAVEY.
SIR RICHARD COUCH.

[*Delivered by Lord Hobhouse.*]

The question in this suit arises in the administration of the estate of William Shepherd, in connection with which other questions have been discussed before this Board. That gentleman, who died in the year 1855, devised his real estate to be divided amongst his wife and children when the youngest child should attain the age of 21 years. Each child was to take a life interest with remainder to his or her children. The testator left eight children of whom one was named James. The youngest child attained 21 in the year 1876. In the year 1879 James Shepherd was appointed a trustee of the will, and in the year 1882 he became sole trustee.

Francis James Plomley the Respondent in this Appeal purchased the interest of some of the devisees, and in August 1885 he instituted a suit against James Shepherd and all the other beneficiaries, praying for a sale of the testator's land with a view to distribution of the proceeds according to the interests of the parties to be

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ascertained by the Court. A decree for sale was made on the 3rd December 1885. The suit is numbered 3840.

On the 29th March 1888 a decree was made on further consideration by which it was ordered that eight separate accounts should be opened, the fourth of which was headed "The account "of James Shepherd and his children." The purchase moneys of the testator's land were to be paid to the several accounts in certain specified proportions. And as to Account No. 4 it was ordered "That all moneys which shall at "any time hereafter during the life of the "Defendant James Shepherd be carried over to "the credit of the said Account Number Four "(4) in respect of the interest or income arising "from unpaid purchase moneys of the said "hereditaments, or otherwise received or credited "to the said account in respect of interest or "income, and all interest and income that may "arise from the investments if any of the said "moneys or any part thereof respectively which "may from time to time be authorised by this "Court, be paid from time to time as and when "the same shall have been carried over or "credited as aforesaid to the Defendant James "Shepherd or his duly authorised attorney or "attorneys until further order." As regards some of the accounts it was ordered that nothing should be paid out of Court without notice to the persons mentioned, but no such order was made to affect Account No. 4.

On the 26th September 1893 the Respondent and Anne Jones, who was one of the testator's children, jointly instituted a suit against James Shepherd alone. This suit is numbered 6542. The Plaintiffs stated that some of the land was still unsold, and they prayed for an account of rents and profits received by James Shepherd, and so far as necessary for administration of the

trusts of the will. The Plaintiffs did not suggest any breach of trust on James Shepherd's part, nor did they apply for a stop order against Account No. 4 in Suit 3840. On the 11th May 1894 a decree was made for an account of the rents and profits of the real estate of the testator received by James Shepherd.

On the 24th October 1895 James Shepherd assigned to the present Appellant all his interest in the testator's estate for the purpose of securing the sum of 725*l.* and interest. The mortgage deed specifies James Shepherd's interest under Account No. 4 in Suit 3840 to the credit of which there was then standing the sum of 5,158*l.* 6*s.* 5*d.*; and it gives to the Appellant full powers of application to the Court for procuring payment to himself. It does not mention Suit 6542 but the pendency of that suit was known to the Appellant.

On the 5th August 1896 the Master in Equity made a certificate under the decree in Suit 6542 by which he found that certain moneys were due from James Shepherd on the account of the testator's real estate to the other sharers in that estate. This certificate underwent some variations not now material to mention. By the decree made on further consideration on the 12th March 1897, the liability of James Shepherd was established, and he was ordered to pay into Court sums amounting to nearly 2,500*l.*, and also to pay certain costs.

In the meantime, on the 31st October 1896, the Respondents had filed a new claim against James Shepherd and the present Appellant by way of supplement to Suit 6542. James Shepherd had at that time been made bankrupt, and his assignee, Mr. Lloyd, was added as a Defendant to the suit. The Respondents claimed the same benefits of Suit 3840 as if the Appellant had been made a Defendant to it; and they claimed declarations that the sums due from James

Shepherd were charges on his interest under the will, and further that they had priority over the Appellant's mortgage.

The Appellant does not claim to enforce his mortgage against any interest of James Shepherd in the testator's estate except the fund standing to the credit of Account No. 4 in Suit 3840. That is now the sole question; whether, in the peculiar position in which that fund was placed by the decree of 29th March 1885, priority of charge should be given to the mortgagee of James Shepherd, or to the beneficiaries whose funds he has misapplied.

The learned Chief Judge in Equity gave the Respondents a decree in accordance with the prayer of their claim. He relied on the general principle that a defaulting trustee must make good his default before he is entitled to take any part of the trust estate for his own benefit, and that his assignee cannot stand in any better position. As for the effect of the decree carrying over funds to No. 4 Account, he considered that Suit 3840 was a mere partition suit, and that the order was nothing more than a declaration that, so far as that suit was concerned, the fund might be treated as the separate property of the persons named in the heading. No question of administration, he said, was or could have been raised in that suit. There was no *res judicata* between the parties, or if any, it was only that James Shepherd was entitled to the income of the fund until further order. The Appellant's contention that he was a *bonâ fide* purchaser for value is, in the opinion of the learned Chief Judge, displaced by the fact that he had notice of Suit 6542.

So far as regards the liability of James Shepherd and his assignee in bankruptcy this judgment cannot be and is not impeached. But as regards the position of the Appellant it raises a question of some subtlety and difficulty; and

it appears to their Lordships to be open to the remarks which they are about to make.

As regards Suit 3840 it is hardly correct to call it a mere partition suit or to say that no question of administration was or could have been raised in it. It is a suit for partial administration of the trusts of the will. It involved the necessity of ascertaining the legal interests of the several beneficiaries and of ascertaining and distributing the sums to which each was entitled. It also had the important effect of turning the testator's specific gifts of land into money, which on the attainment by each devisee of an absolute and indefeasible interest could and would be paid over if no claims were put forward by the others interested in the estate; who again were not entitled to receive notice of application for payment.

If on the proposal to carry over James Shepherd's share to Account No. 4 it had been suggested that he was a debtor to the estate inquiry would certainly have been directed, and care taken that he should not receive any part of the estate till his debt was made good. Or if it had been pointed out that he was still receiving trust funds and might become a debtor to the estate, care might and probably would have been taken either to leave his share to the general credit of the estate, or if it were carried to a separate account to frame the heading of that account in such a way as to show the claim which the estate might have against the fund, or in some other way to protect it against a transfer by him.

But nothing of this kind was done. As the account stands it would lead anyone to suppose that in a suit for partial administration the fund had (to use Lord Langdale's language *in re Jervoise* 12 Beavan 209) been released from the general questions in the cause and marked as being subject only to the questions arising on

the particular matter referred to in the heading of the account. The right of James Shepherd to receive what was designed for him by the will was one of the general questions in the cause arising under the prayer for distribution, and not one that arose between himself and his children; and from that question his fund was released, though the release would not of itself be a bar to any subsequent proceedings which might be taken to set aside or qualify the order.

As regards the question of notice on which the learned Judge lays great stress, all that the Appellant knew was that James Shepherd was trustee, and had been called on for an account in Suit 6542. Every trustee is known to be subject to that liability. Of course there was the legal possibility that he might be a defaulter and that his creditors might take steps to recall the fund placed to his separate account and make it available to answer their claim. But nothing of the kind was suggested by the frame of the suit, nor indeed could it be done except by some proceeding adapted to the legal position created by the existence of Account No. 4. In every case an executor or trustee is liable to account and may make default; the remedies for which may be worked out against his remaining interest in the testator's estate. But it would be a new thing to hold that such a possibility of itself disables an executor or trustee during the whole continuance of his executorship or trusteeship from making a good title to a *bonâ fide* purchaser of a separate portion of the estate which the testator has given to him.

A similar question arose in the case of *Price* v. *Price* 35 Ch. Div. p. 297. There a trustee, having committed a breach of trust, died. A *cestui que* trust sued his two executors, claiming payment, and afterwards by amended bill a general administration of the defaulter's estate if his executors should not admit assets.

The Plaintiff registered his suit as a *lis pendens* in May 1878. In November 1878 and July 1879 one of the executors created charges on part of the defaulter's estate specifically devised to him. In March 1880 the Plaintiff established the liability of the executors and obtained the usual creditors' decree. Sir Edward Kay pointed out that the suit was not one to administer a trust created by will for payment of debts, and that the registration of *lis pendens* did not indicate any purpose of making liable that portion of the defaulter's estate which had been specifically devised to and mortgaged by the executor. On that view of the case he gave priority to the executor's mortgagees.

In the case before their Lordships there was not only no indication prior to October 1895 of a purpose to enforce liability against the fund carried to Account No. 4, but the proceedings in the two suits when put together were such as to induce a belief that the fund appearing by the separate account to be free was really free by not being attacked in Suit 6542.

Their Lordships are disposed to agree with the learned Judge that it may not be quite accurate to apply the term *res judicata* to an order of this kind; because, though made in a suit in which one of the Respondents was the Plaintiff and the other a Defendant, the particular question which has now arisen was neither decided nor raised. But that is hardly more than a verbal question. The important point is that the order was made in the presence of all parties interested; and its intention was to treat this fund as so far separated from the estate that it could be dealt with by the separate donees without notice to the others. That is a step forward in the administration of an estate, and it saves a great deal of expense and trouble. This fund could not be actually paid out because nobody had acquired an absolute and indefeasible

interest in it; for the absolute interests acquired by the children were liable to variation in amount by the birth of more children. But the object of separate accounts is to relieve the subjects of each account from entanglement with the others, and to make the persons specified in each heading the owners of the fund carried to its credit, so far as is consistent with the necessity for retaining those funds in Court. The retention of the fund is not meant to prevent adult owners of interests in it from dealing with those interests. The division into separate accounts is intended to facilitate such dealings. Of course it is true that so long as any fund remains in Court, claims against its owners can practically be enforced against it which could not practically be enforced if it were paid out. It is open to the other parties to the suit to show that they have claims enforceable against a separate fund which were not known or not existent when the fund was separated, and by proper proceedings to enforce them notwithstanding the order for separating the fund. But until some step is taken for that purpose the separation is commonly and rightly looked upon, as showing that the separated funds are free from claims by the other sharers in the estate. Persons honestly dealing with those whom the Court declares to be the owners of such funds are justified in trusting to that declaration; and their Lordships hold it to be unjust to subject them to claims by the other sharers arising out of matters subsequent to the separation or latent at the time.

They are supported in this opinion by a case which was decided by Chitty J. and is reported in 45 Ch. Div. 458. P. E. Eyton, whose estate was being administered in the suit of *Bartlett* v. *Charles*, had bequeathed money to Mrs. Charles and her descendants. By the decree made on further consideration in August 1886 a fund was carried over to an account

headed "Annuity of A. P. Charles and her "issue" with a direction to pay the income to her for her life. She created charges on her interest and her creditors obtained stop orders in 1886 and 1887. In 1889 a decree was made in another suit charging the testator and Mrs. Charles jointly with breaches of a trust they had undertaken, and it was ordered that the liability should be made good out of the testator's estate. A motion was made by one of the parties to the suit of *Bartlett* v. *Charles* to make Mrs. Charles's separate fund answerable in priority to the encumbrances effected by her. That application was rejected by Chitty J. on the grounds that the matter was *res judicata* as between the applicant and Mrs. Charles, and that the separation of the fund by the Court had given to the encumbrancers a right to believe that the fund was clear.

The learned Judge below has subjected this decision to a very careful examination, and he summarises his reasons for thinking it inapplicable to the questions before him in the following terms:—

"Manifestly this case presents three serious points of "difference from *re* Eyton. In the first place the charge "sought there to be enforced was for an ordinary debt and not "for a breach of trust: (2) the order carrying the funds to a "separate account was made in another and entirely distinct "suit: and (3) there was no suggestion of any question of "notice."

As to the third ground of difference, their Lordships have already given their views on the point of notice. As to the first ground, the distinction between debts arising out of breaches of trust and other debts seems to their Lordships immaterial to the present question. In point of fact the claim made *in re* Eyton did arise out of a breach of trust, and we are not told by the Report whether the breach was or was not connected with the property left by the

testator. But how can this consideration affect the principle that the action of the Court amounts to a representation that as between the parties to the suit the separated fund is clear? If any distinction is to be drawn between the two cases with reference to the cause of the assignor's liability and to the assignee's knowledge of it, a presumption against the existence of claims connected with the estate under administration, whether entire or partial, would be stronger when a separate account has been established than the presumption against wholly independent claims. And the second ground of difference, viz., that the order establishing the separate account of Mrs. Charles was made in a separate suit from that in which her liability was established, is subject to precisely the same considerations. It is true as the learned Judge observes that Chitty J.'s decision is not binding in the present suit. But it is one founded on a similar practice and procedure and as it appears to their Lordships to be sound in principle and exactly in point, they are glad to avail themselves of it.

The decision is also rested on the authority of many cases cited to show that a trustee who has misappropriated trust funds must be taken to have received payment of his share by anticipation, and that he has nothing to assign except the excess of his share over that payment. The learned Judge applies the decisions thus:—

"If these cases correctly state the principle on which "the rule is founded, as I have no doubt that they do, "then it would seem that the case of the assignee is not "helped by the fund having been carried to a separate account, "nor is it affected by notice or want of notice. The answer "then to this case is:—'You bought the interest of a man "'under a will of which he was a trustee. True his share "'independently of any question of administration was fixed "'at so much and it was by order of the Court placed in such "'a position that it could be dealt with without reference "'to the other parties interested under the will, but it turns

" ' out that all the time he was entitled to nothing. He had
" ' in fact overpaid himself out of the rents of the estate and
" ' when he affected to give you a charge, there was in fact
" ' nothing on which the charge would operate.' "

In most of these cases, such as *Morris* v. *Livie* 1 Y. & C. C. C. 380, the liability enforced in priority to assignees was against portions of the estate still in bulk. The nearest to the present case is *Jacubs* v. *Rylance* 17 Eq. 341. In that case a Mr. Elkes was executor, and was in default. He had an interest in the estate which he mortgaged. Another fund was given to his children, and was carried over to their separate accounts. One child died, and his interest passed to Elkes. It was held that the liability to make the default good extended to Elkes's derivative as well as to his original interest. But so far is the case from deciding the present point that the report does not even mention the date of Elkes's mortgage, whether before or after the separation of the fund or the death of the child, nor the subject matter specifically assigned by it. The sole question was whether the general principle requiring trustees to make good defaults before receiving their shares extended to derivative interests. In none of the cases was a trustee's general liability to make defaults good enforced against funds so far administered as to be carried to a separate account and specifically assigned for value by a person entitled according to the terms of that account.

The result is that the decree cannot stand so far as it is adverse to the Appellant. The proper order will be to discharge the decree so far as it declares that the charges established by the Plaintiffs against James Shepherd have priority over the Appellant's mortgage, and so far as it awards an injunction against the Appellant, and so far as it orders that no part of the interest accruing on Account No. 4 shall be paid to the

Appellant, and so far as it directs the Appellant to pay costs. Instead thereof the decree should declare that the mortgage of the 24th October 1895 is as between the Plaintiffs and the Appellant a valid security and the first charge on the interests of James Shepherd thereby assigned; and should order that the income of the funds comprised in Account No. 4 shall be paid to the Appellant until further order; and that the Plaintiffs shall pay him his costs of suit. That will leave standing all those parts of the decree which relate to James Shepherd and to Mary MacGovern, and to the requisition of notice to the Plaintiffs before any principal money is paid out, and to the questions reserved for further consideration.

Their Lordships will humbly advise Her Majesty in accordance with this opinion. The Respondents must pay the costs of this Appeal.