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Henry R. Snyder Jr.  
*University of Kentucky*

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CHARACTER OF PARTNERSHIP REALTY UPON THE DEATH  
OF A PARTNER

With the passage of the Uniform Partnership Act in Kentucky, it has become important to examine some of the possible effects of the Act upon existing partnership law in this state.<sup>1</sup> One of the more vexatious problems facing courts in the past has been the manner of disposition of partnership realty upon the death of one or more of the partners, and the question of whether Kentucky law in that area has been affected by the Act is of considerable importance. This note proposes to present a brief history of this phase of partnership law in this State and to discuss the probable effects of the Act upon future disposition of partnership real estate.

Early decisions were agreed that when real estate was held by partners as co-tenants, the death of one of the partners caused legal title to his share of the partnership realty to descend to his heirs at law. The heirs, however, held the legal title subject to the equitable right of the surviving partners to utilize the firm property for the payment of partnership debts and the settlement of firm obligations. These rights were exercised through the creation by courts of equity of a fictional "conversion" of the partnership real estate, whereby the real property, for the purpose of winding up partnership affairs, was deemed to be personalty.<sup>2</sup>

As to the subsequent disposition of the partnership realty, however, there was wide divergence of judicial opinion. The English courts fairly consistently sustained the theory of "out-and-out conversion".<sup>3</sup> Where real estate was bought with partnership funds, to be used in carrying on and enlarging the business, it was impressed with the characteristics of personalty for all purposes, not only as between the partners themselves and the firm and its creditors, but also as to distribution between the administrator, distributees, and heirs. The theory underlying the English rule was that the share of a partner was nothing more than his share of the partnership assets after they had been turned into money and applied in liquidation of the firm debts.<sup>4</sup> The early English rule of out-and-out conversion was sub-

<sup>1</sup> Ky. Rev. Stat. secs. 362.150 to 362.360 (1955). The Act became effective in Kentucky on June 17, 1954. For an excellent general survey of the Act, see Ham, *Kentucky Adopts the Uniform Partnership Act*, 43 Ky. L.J. 5 (1954). Hereinafter the Ky. Rev. Stat. will be referred to by the abbreviation, "KRS".

<sup>2</sup> Crane, *Partnership*, sec. 45 (2d ed. 1952).

<sup>3</sup> 25 A.L.R. 389, at 405 (1923). For a Kentucky analysis of the English rule, see *Davidson v. Richmond*, 24 Ky. L. Rep. 699, 69 S.W. 794 (1902).

<sup>4</sup> *Darby v. Darby*, 3 Drew 495, 61 Eng. Rep. 992 (1856); 2 *Tiffany*, *Real Property*, 254 (3d ed. 1939); and cf. sec. 26 of the Act: "A partner's interest in the partnership is his share of the profits and surplus, and the same is personal property".

sequently enacted into the statutes, but was somewhat modified by a provision that real estate would maintain its heritable status where the partners had adequately manifested such an intent.<sup>5</sup>

The majority of American courts, rejecting the English view, adopted the pro tanto theory; the partners, holding the realty as tenants in common, did so subject to a trust for payment of firm debts and the adjustment of equities between the partners.<sup>6</sup> Thus, the heir who took an undivided interest did so subject to the trust in favor of the partnership, and could be compelled to convey his title for the purpose of settling partnership affairs.<sup>7</sup> After liquidation, or when the realty was not required for firm purposes, the partners were deemed to hold the real estate as tenants in common as though no partnership existed.<sup>8</sup> Thus, under the American rule, real estate was considered as personalty only for the limited purpose of winding up the affairs of the partnership and meeting the claims of creditors. After the payment of firm debts, the remaining realty resumed its historical incidents, including dower and curtesy rights, for distribution; the conversion was partial, or pro tanto, rather than complete.

The early Kentucky decisions followed a rather vacillating course, seemingly adopting a new rule or engrafting exceptions to existing rules whenever the courts were confronted with the necessity to do justice in hard cases.<sup>9</sup> These early conflicting decisions were later sought to be resolved by the Court of Appeals on the basis of the intent of the parties to the partnership, the Court favoring the pro tanto rule in the absence of express or implied intent to the contrary.<sup>10</sup>

The status of a deceased partner's share in realty in Kentucky remained equivocal until 1891, in *Carter v. Flexner*.<sup>11</sup> The Court of Appeals, in accepting the pro tanto rule, held that a conveyance by the heirs was necessary to pass a complete title to the purchaser from the surviving partner. In this case, since the heirs had not joined in

<sup>5</sup> Partnership Act, 1890, 53 & 54 Vict. chap. 39, sec. 22. For an early statement of the rationale behind the English rule, see *Darrow v. Calkins*, 154 N.Y. 503, 506, 49 N.E. 61 at 64 (1897):

This doctrine . . . is said to have grown out of the peculiar law of inheritance there, and to remedy the hardship of the rule which excludes all but the eldest child from the inheritance, and of the other rule which exempts real estate in the hands of the heir from all but the specialty debts of the ancestor.

<sup>6</sup> 2 American Law of Property 38 (1952).

<sup>7</sup> 2 Tiffany, Real Property, 249-250 (3d ed. 1939).

<sup>8</sup> 2 American Law of Property 38-39 (1952).

<sup>9</sup> Cf. *Galbraith v. Gedge*, 55 Ky. 631 (16 B. Mon. 1855), favoring the pro tanto rule, with *Cornwall v. Cornwall*, 69 Ky. 369 (6 Bush 1869), which affirmed the rule of out-and-out conversion.

<sup>10</sup> *Lowe v. Lowe*, 76 Ky. 688 (13 Bush 1878). The early Kentucky cases are collected in 25 A.L.R. 389, 397-400 (1923).

<sup>11</sup> 92 Ky. 400, 17 S.W. 851 (1891).

executing a conveyance of the realty, but were before the Court, their title was conveyed by the Commissioner, and the third person who had contracted to purchase the land was compelled to accept the deed tendered by the surviving partner. Moreover, the Court refused to consider a possible implied intent of the partners to treat firm realty as personalty for all purposes; implied intent was held to be necessarily the result of mere speculation, placing too great a burden on the chancellor. The opinion also refused to accept the distinction made by some courts that where a partnership has been formed for the purpose of dealing in land, the parties are assumed to have intended an out-and-out conversion.<sup>12</sup>

The case contained a note that it was not to be officially reported, which led at least one observer to believe that the statements of the Court regarding implied intent were not to be regarded as the Kentucky rule on the question.<sup>13</sup> *Carter v. Flexner*, however, has remained the law in this State, and succeeding cases have affirmed its rejection of the English rule.<sup>14</sup>

In addition to preserving dower rights in the share of a deceased partner, *Carter v. Flexner* also had a definitive effect upon the manner of conveyance of real property by the surviving partners. Since the heirs held legal title to the share of a decedent, subject to the equitable rights of the partners to sell the realty in settlement of firm affairs, a purchaser from the partners must require a conveyance from the heirs in order to obtain a complete legal title. Thus, in *Strode v. Kramer*,<sup>15</sup> a bank, as personal representative of a deceased partner who had been the surviving member of a partnership, could not convey partnership real estate in the absence of power conferred by the will of the deceased, since the conveyance would not have bound adult children to whom the property had passed under the will of the deceased. And, in *Baker v. Wides' Ex'r*,<sup>16</sup> the Court refused to modify the rule that the legal title must be conveyed by the heir. In the *Baker* case, since the heir was held as a prisoner of war by the Japanese, title was ordered to be conveyed by a judicial sale, the Court citing *Strode v. Kramer*.

<sup>12</sup> In *re Ransom*, 17 F. 331 (S.D.N.Y. 1883); *Mechem, Partnership*, sec. 163 n. 36 (2d ed. 1920).

<sup>13</sup> See the analysis of disposition of realty in Kentucky by Taft, Circuit J., in *Perin v. Megibben*, 3 C.C.A. 443, 6 U.S. App. 348, 53 F. 86 (CCA6 1892).

<sup>14</sup> *Bennett v. Bennett*, 137 Ky. 17, 121 S.W. 495 (1909): Widow's dower rights held to attach to husband's share of realty remaining after payment of partnership debts.

<sup>15</sup> 293 Ky. 354, 169 S.W. 2d 29 (1943).

<sup>16</sup> 299 Ky. 414, 185 S.W. 2d 699 (1945).

The framers of the Uniform Partnership Act were forced to take cognizance of the fact that much of the confusion and diversity of opinion involved in the disposition of partnership property arose from the application of ancient concepts of co-tenancy to situations for which they were unsuited. The Kentucky courts, for example, had treated the ownership of land by partners as a tenancy in common, the partnership realty being impressed with a trust for firm purposes while held by the tenants in common.<sup>17</sup> Under this view, there seems to be no valid reason for the employment of a fictional "conversion" of realty in cases where the problem of disposition of firm realty has arisen.<sup>18</sup>

Where courts have sought to reconcile the theory of joint tenancy with the necessities of the partnership relation, they were forced to evade the right of survivorship granted as an integral feature of this type of tenancy.<sup>19</sup> Thus, since the joint tenancy makes no provision for the heirs of the tenants, courts have generally, in the absence of statute, tended to construe the ownership of land by a partnership as a tenancy in common.<sup>20</sup> The tenancy in common, moreover, is far more flexible in its operation, requiring only the unity of possession. The shares of the tenants need not be equal nor acquired at the same time, and an attempt by one tenant to convey the whole estate will transfer only his own interest.<sup>21</sup>

In spite of the greater adaptability of the tenancy in common, it is nonetheless a cumbersome instrument for the effectuation of partnership purposes upon the death of one of the partners, as evidenced by the utilization of the trust theory. The National Conference of Commissioners on Uniform State Laws thus found it imperative to create a new tenancy, designated as a "tenancy in partnership", that would better lend itself to the exigencies of partnership affairs.<sup>22</sup>

In the clauses of this section those incidents of tenancy in partnership are stated with several practical results of value. In the first place the law is greatly simplified in expression. In the second place the danger of the courts reaching an inequitable conclusion by refusing

<sup>17</sup> *Wilhite's Adm'r v. Boulware*, 88 Ky. 169, 171, 10 S.W. 629, 630 (1889).

<sup>18</sup> 2 *American Law of Property* 39 (1952). For definitions of the tenancy in common in Kentucky, see *Saulsberry v. Saulsberry*, 121 F. 2d 318 at 321 (CCA6 1941), and *McLeod v. Andrews*, 303 Ky. 46 at 54, 196 S.W. 2d 473, 477-8 (1946).

<sup>19</sup> For disadvantages of the joint tenancy, see *American Bar Association, Section of Real Property, Probate and Trust Law, Proceedings* 17, 23 (1952).

<sup>20</sup> 2 *Tiffany, Real Property*, 201-202 (3d ed. 1939). While a conveyance to two or more persons will ordinarily, in the absence of words to the contrary, create a joint tenancy, see *KRS* sec. 381.050 (1955): Conveyance to husband and wife creates a tenancy in common unless the right of survivorship is expressly provided for.

<sup>21</sup> 2 *Tiffany, Real Property* 212 (3d ed. 1939).

<sup>22</sup> See the Commissioners' note to sec. 25 of the Act, 7 U.L.A., U.P.A., pp. 144 and 145:

to modify the results of applying the legal incidents of joint tenancy is done away with. Finally, ground is laid for the simplification of a procedure in those cases where the separate creditor desires to secure satisfaction of his debtor's interest in the partnership.

Section 8 of the Act defines what is included in partnership property.<sup>23</sup> The Act provides that "A partner is co-owner with his partners of specific partnership property holding as a tenant in partnership",<sup>24</sup> but, without consent of the other partners, with no right of enjoyment except for partnership purposes.<sup>25</sup> On the death of a partner the partnership property vests in the surviving partner or partners or his legal representatives if he is the sole surviving partner, but none of them has a right to possession except for partnership purposes.<sup>26</sup> The property is not subject to dower, curtesy, or allowances to widows, heirs, or next of kin.<sup>27</sup> The Act further provides that upon dissolution in any way, except in contravention of the partnership agreement, each partner may have the partnership property applied to discharge its liabilities, and the surplus applied to pay in cash the net amount owing to the respective partners.<sup>28</sup> Moreover, a partner's interest in the partnership is his share of the profits and surplus, to be considered as personal property.<sup>29</sup> Realty can be acquired in the partnership name,<sup>30</sup> and if this is done it can be conveyed in the partnership name by any partner,<sup>31</sup> including of course a surviving partner who is authorized to wind up the affairs of the partnership. Where, however, the real property is in the name of the deceased partner or a third person, the survivor can transfer only the equitable interest,<sup>32</sup> although he can, no doubt, compel the holder of the legal title to perfect the transfer.<sup>33</sup>

These provisions of the Act have been considered by a comparatively small number of courts, but they have almost uniformly held the Act to embody the English rule of out-and-out conversion. The leading case is that of *Wharf v. Wharf*,<sup>34</sup> involving a partnership dealing in real estate, organized by the complainant and his father. During the operation of the partnership they had divided the profits

<sup>23</sup> The Act, sec. 8; KRS sec. 362.185 (1955).

<sup>24</sup> The Act, sec. 25(1); KRS sec. 362.270(1) (1955).

<sup>25</sup> The Act, sec. 25(2)(a); KRS sec. 362.270(2)(a) (1955).

<sup>26</sup> The Act, sec. 25(2)(d); KRS sec. 362.270(2)(d) (1955).

<sup>27</sup> The Act, sec. 25(2)(e); KRS sec. 362.270(2)(e) (1955).

<sup>28</sup> The Act, sec. 38(1); KRS sec. 362.335(1) (1955).

<sup>29</sup> The Act, sec. 26; KRS sec. 362.275 (1955).

<sup>30</sup> The Act, sec. 8(3); KRS sec. 362.185 (3) (1955).

<sup>31</sup> The Act, sec. 10(1); KRS sec. 362.195 (1) (1955).

<sup>32</sup> The Act, sec. 10(4); KRS sec. 362.195 (4) (1955).

<sup>33</sup> 3 American Law of Property 636 (1952).

<sup>34</sup> 306 Ill. 79, 137 N.E. 446 (1922). The Act was passed in Illinois in 1917, becoming law without the approval of the governor.

equally, and although at the father's death there were firm debts outstanding, there were fifty-eight unsold lots held in the names of the partners individually, and not required for the settlement of the partnership affairs. The complainant sought a decree awarding him an undivided half of the unsold lots, free from dower rights, and vesting the remainder of the lots in the heirs at law according to the laws of descent.

The Supreme Court of Illinois affirmed the decision of the circuit court, which had sustained a demurrer by the deceased partner's widow, and held that the Act had adopted the English rule of out-and-out conversion. Therefore the complainant had stated no ground for equitable relief, since title to the specific partnership property had vested in him under the Act, and he had the right to sell and convey to purchasers, and to distribute the proceeds. Said the Court:

The provision that a partner's interest in the partnership is his share of the profits and surplus, and the same is personal property, and that, when dissolution is caused by death, each partner, as against his copartner and all persons claiming through them, in respect to their interest in the partnership, unless otherwise agreed, may have the partnership property applied to discharge its liabilities and the surplus applied to pay in cash the net amount owing to the respective partners, is inconsistent heretofore held that upon the settlement of the partnership affairs real estate resumes its original character and descends to heirs. It seems that the legislative intention was to adopt the English rule that real estate which becomes personal property for the purposes of a partnership remains personal property for the purposes of distribution.<sup>35</sup>

The Court, as did the Kentucky Court of Appeals in *Carter v. Flexner*, refused to put into a separate category those partnerships which deal in real estate for profit. The right of dower in the deceased partner's share of firm realty was abrogated, and the surviving member might convey a complete legal title; in effect, title to the realty never passes to the heirs at law, and any surplus remaining after settlement of the firm affairs passes as personalty.<sup>36</sup>

Succeeding cases adhered to the reasoning of *Wharf v. Wharf*, embracing its unequivocal adoption of the out-and-out conversion rule

<sup>35</sup> *Ibid.*, at p. 449. Note that prior to passage of the Act in Illinois, the pro tanto rule had been firmly established in that State. See: *Strong v. Lord*, 107 Ill. 25 (1883); *Galbraith v. Tracy*, 53 Ill. 54, 38 N.E. 937, 28 L.R.A. 129 (1894).

<sup>36</sup> For affirmance of *Wharf v. Wharf* by the Illinois Court, see *Swirsky v. Horwich*, 382 Ill. 468, 47 N.E. 2d 452 (1943): Partnership property, though composed partly of real estate, was held to have the status of personalty, thus giving the widow of a deceased partner no freehold interest as would sustain the Illinois Supreme Court's jurisdiction of a direct appeal under the state statutes.

under the Act, and the rationale of that decision<sup>37</sup> has continued to acquire judicial favor.<sup>37</sup>

Tennessee has agreed that the Act abolishes the distinction formerly made in the case of partnerships dealing in realty for profit.<sup>38</sup> Where partners, for firm purposes, acquired real estate, the realty was required to be disposed of as personalty upon the death of two of the partners. Therefore the share of one of the deceased partners did not descend to his after-born child to the exclusion of his widow. The Court stated:

It is true that in the Wharf case the partnership was solely for the purpose of dealing in real estate and that the general rule is that real estate partnerships are considered as personalty and must be distributed as such. But we agree with the Wharf case that the rule is changed to all partnerships, whether real estate or otherwise, by reason of the passage of the Uniform Partnership Act.<sup>39</sup>

A recent Utah case has held that where a wife, who had been in partnership with her husband, renounced his will and claimed instead her one-third distributive share of all real property possessed by him during their marriage, the rule of out-and-out conversion prevailed under the Act.<sup>40</sup> The case was remanded for a determination of the manner of acquisition of the partnership realty, the Court stating that if the widow had brought the real estate into the firm as her contribu-

<sup>37</sup> For related cases based upon the out-and-out conversion construction of the Act, see:

In re Dumarest's Estate, 146 Misc. 442, 262 N.Y.S. 450 (1933):

Under the Act, a wife has no conjugal rights in the specific property of a partnership in which her husband was a member, since a partner has no individual property in any specific assets of the firm.

State v. Elsbury, 63 Nev. 463, 175 P. 2d 430 (1946):

Conviction for grand larceny of partnership property by one of the partners was reversed on the ground that the complaining partner did not own any specific share in the property, but only a share of the surplus which may remain after discharging all demands upon the firm. Dissent: Since the Act states that a partner is co-owner with his partners of specific partnership property holding as a tenant in partnership, that part of the criminal statutes should have been applied which states that it shall be no defense to a prosecution for larceny that the money appropriated was partly the property of another and partly the property of the accused.

Cf. Hannold v. Hannold, 4 N.J. Super. 381, 67 A. 2d 352 (1949):

Under the Act, land is regarded as personalty only for such time as is necessary for payment of partnership debts, and then reverts to the status of realty. But note that the court referred solely to sec. 26 of the Act in basing its opinion on three cases decided prior to passage of the act in New Jersey.

<sup>38</sup> Cultra et al. v. Cultra et al., 188 Tenn. 506, 221 S.W. 2d 533 (1949).

<sup>39</sup> *Ibid.*, at p. 535. The Tennessee Court also ruled that under the Act, no conveyance of the partnership realty need be made by the heirs, under the rationale of Wharf v. Wharf. For a subsequent case in the same year, see in re Moore's Estate, 34 Tenn. App. Rep. 131, 234 S.W. 2d 847 (1949), where the court asserted its intent to adhere to the Cultra decision.

<sup>40</sup> In re Ostler, 4 Utah 2d 47, 286 P. 2d 796 (1955).

tion, it became personalty to which her interest as a wife would not attach on her husband's death. If, however, the decedent had been seized of the property, held in his own right, or conveyed to the partners without a release of the wife's interest, her claim would be allowed.<sup>41</sup>

The questions relevant to disposition of a deceased partner's share of firm realty were unresolved prior to passage of the Uniform Partnership Act to such an extent that the equitable rights of surviving partners were effectuated only by the employment of trust and conversion strategems to circumvent the ancient rules of co-tenancy. By creation of the tenancy in partnership, the National Conference of Commissioners on Uniform State Laws sought to eliminate the anomalies then existing in the disposition of partnership real estate.

While its provisions have been interpreted as an adoption of the English rule of out-and-out conversion, the language of the Act is by no means unequivocal.<sup>42</sup> Nevertheless, the weight of authority and the comments of those responsible for the original promulgation of the Act lend strength to the interpretation of the Act in the *Wharf* case.<sup>43</sup>

It may be presumed that the Kentucky legislature, by passage of the Act, desired to give a greater degree of commercial stability to partnerships, and also to further define the status of partnerships in this State. The writer therefore submits that when the question of disposition of a deceased partner's share of real estate again arises in Kentucky, the Court of Appeals will in all probability view the pertinent provisions of the Act as have the courts in the above-discussed cases, and in the light of those well-reasoned opinions, adopt the rule that partnership realty is converted into personalty for all purposes, upon the death of a partner.

*Henry R. Snyder, Jr.*

<sup>41</sup> Cf. *Beers v. Beers*, 204 Ore. 636, 283 P. 2d 666 (1955): Without deciding if the out-and-out conversion rule applied in Oregon under the Act, the court held that the heirs at law of a deceased co-partner were necessary and indispensable parties to a suit involving the status of realty as constituting partnership property, even though the realty was treated as personalty for the settlement of partnership affairs.

<sup>42</sup> See 3 American Law of Property (1952):

It is certainly arguable that sec. 26 was merely intended to declare that the partnership property is personalty for the purpose of working out the rights of partnership creditors and of the partners inter se, and should not affect the former law for the purpose of declaring the respective rights of those interested in the estate of the deceased partner.

But the writer goes on to predict continued judicial adherence to the out-and-out conversion theory under the Act.

<sup>43</sup> See *Lewis*, *The Uniform Partnership Act*, 24 Yale L.J. 617, 637 (1915).