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Partnership-Power of Liquidating Partner to Bind the Partnership

RECENT CASE NOTES

PARTNERSHIP—POWER OF LIQUIDATING PARTNER TO BIND THE PARTNERSHIP.—Suit by receiver of a bank against the estate of one Betts upon two notes executed after the death of Betts by the surviving partners of the firm of which he had been a member at the time of his decease. The notes were made to evidence a loan of funds which were borrowed for the purpose of being used and were actually used in completing the performance of a construction contract with a railroad company. Although the written contract with the railroad company was not executed until after the death of Betts, yet prior to Betts' death the firm had submitted a bid, and had so conducted itself as to give reasonable inference of its acceptance of the counter offer thereupon made by the railroad company. Since the two surviving partners have become bankrupt, the receiver attempted to collect from the deceased partner's estate. Held: the actual contract of construction was made before the dissolution of the partnership and the making of the loan was incidental to winding up the affairs of the partnership; and therefore, the estate of Betts is liable on the note.[1]

Upon the death of a partner, the partnership is dissolved by operation of law, without any notice or judicial decree.[2] The legal title to all the partnership personalty immediately passes to the surviving partner or partners, it being held in trust for the purpose of and in the performance of their duty of liquidating the firm's assets.[3] Since the average business firm cannot immediately stop operations, turn all its assets into cash, and close up, the liquidating partner or partners must have a reasonable time in which to wind up the affairs.

As is generally known, during the regular operation of the firm each partner has implied authority to act as agent to bind the firm in any matter within the scope of the partnership business. However, after dissolution effected by the death of one of the members this implied authority is limited to winding up the affairs of the firm. The rule had been stated that whatever a partner, as survivor or liquidator, does that is reasonably necessary to the completion of the firm's existing obligations is within the scope of his authority.[4] But when the application of this general rule defining the agency is studied, one finds that courts of various jurisdictions have in many cases reached opposite results.

Most courts hold that one partner can nowhere create new obligations or enter into new business so as to bind the other members of the dissolved firm and continue the winding up indefinitely.[5] They agree, also, that where a partnership is a party to an executory contract, the death of a partner does not terminate the contract, nor relieve its members of the duty of performing

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1 Feucht v. Corbett (Indiana, 1938), 12 N. E. (2d) 957. The question of whether or not a good contract with a valid offer and acceptance existed prior to the death of the decedent is a very close one. However, the court seems to be correct in concluding that the written instrument was but a memorial of the contract instead of a condition precedent thereto. The Appellate Court in Evan v. Citizen Loan & Trust Co. (1932), 94 Ind. App. 161, 180 N. E. 23, held on the same construction contract, that no valid contract was consummated prior to the dissolution. At least for the purposes of this note the validity of the court's argument is conceded.

2 It has been said that by agreement the members can provide for carrying on after the death of one of the partners, but technically this is actually a new partnership, assuming the obligations and assets of the old one.

3 Mechem on Partnership, Section 402; also, see Barry v. Briggs (1871), 22 Mich. 201. A surviving partner stands in the same relation to the partnership property as an administrator or trustee to his trust; Harrah v. State (1906), 38 Ind. App. 495, 76 N. E. 443.

4 King v. Leighton (1885), 100 N. Y. 386, 3 N. E. 594; Little v. Caldwell (1894), 101 Cal. 553, 36 P. 107; Gilmore on Partnership, Sec. 118.

5 Boss Co. v. Granite City Co. (1902), 116 Ga. 176, 42 S. E. 415; Maryland Casualty Co. v. Little (1930), 102 Cal. 205, 282 P. 968.

the unfulfilled contract, except in the case of contracts which call for the personal skill and efforts of the deceased partner.[6] Among the other powers conceded to the liquidating partner are the power to sell firm goods,[7] collect the credits,[8] and pay firm debts.[9] But when the liquidating partner has borrowed money, even to be used in paying the firm debts, the authorities are in direct conflict. One of the leading cases on this problem is the English case of *Butchart v. Dresser*,[10] in which the liquidating partner borrowed money and pledged shares of stock as security, in order to have funds to enable him to fulfill a contract made prior to dissolution. The English Court of Appeals held that this was within the power of the liquidating partner and bound the firm members. In the United States, the New York court in *Durant v. Pierson*,[11] after admitting the general rule that there is no power or authority in the surviving partners to engage in new transactions, contracts or liabilities on account of the firm, said, "When a partnership is dissolved by death of a partner, the survivor is entitled to the possession and control of the joint property for the purpose of closing its business, and to that end and for that purpose he may, according to the settled principles of partnership law, administer the affairs of the firm, and by sale, mortgage or other reasonable disposition of the property make provision for meeting its obligations. He may, for that purpose, borrow money, and give a valid pledge of the co-partnership property for its repayment."[12]

However, contrary to the view of the Butchart and Durant cases are the many cases holding that a firm note cannot be given by the liquidating partner, even in renewal; or negotiable paper endorsed, even to pay existing obligations.[13] The theory underlying this rule is that since the dissolution operates as a revocation of all authority for making new contracts and since the giving of a promissory note or the acceptance of a bill or draft is the making of a new contract, although it may be for an antecedent debt, the creation of such new obligations is beyond the power of the liquidating partner.[14]

In the instant case, even if it be conceded that the construction contract was made prior to dissolution, the Indiana Supreme Court, in applying the

[6] Kimmell v. State (1920), 75 Ind. App. 168, 128 N. E. 708, Weiss v. Hamilton (1909), 40 Mont. 99, 105 P. 74; Stem v. Warren (1916), 161 N. Y. S. 247.

[7] Robbins v. Fuller (1862), 24 N. Y. 570.

[8] Gillilar v. Sun Ins. Co. (1869), 41 N. Y. 376.

[9] Milliken v. Loring (1854), 37 Me. 408.

[10] (1853), 43 Engl. Repr. 619.

[11] (1903), 124 N. Y. 44, 26 N. E. 1095. Also, see Rowley on Modern Law of Partnership, Sec. 618.

[12] Also, supporting this view, State Bank of Wheatland v. Bagley Bros. (1932), 44 Wyo. 307, 11 P. (2d) 592; Rosenthal v. Hasberg (1903), 84 N. Y. S. 290. In Stenback v. Smith (1917), 34 Cal. App. 223, 167 P. 189, the court said it would be no different for same amount due, but only a different person.

[13] Hamilton v. Seaman (1848), 1 Ind. 185; Conklin v. Ogborn (1856), 7 Ind. 553; Heide v. Beuttler (1935), 11 F. Supp. 290; Simpson v. Shadwell (1932), 264 Ill. App. 480. Also, see Wood v. Todd (1918), 251 F. 530—admitting this to be the rule except when the law of a state differs, and that Pennsylvania gives liquidating partner authority to execute notes in renewal of obligations made before dissolution.

[14] Bank of Montreal v. Page (1881), 98 Ill. 109.

rule that the liquidating partner may borrow in the firm name and use firm property as security for such purposes, as an exception to the general rule that a surviving partner cannot borrow money and bind the partnership after dissolution, appears to be making an inroad upon the prior rulings in Indiana on this subject.[15] I. K.

TRUSTS—BANKS AND BANKING—SET-OFFS AGAINST TRUST FUNDS.—Appellee Tractor Company delivered a tractor to an Equipment Company, an independent sales agency, under a conditional sales contract, the Equipment Company executing its note for the wholesale price and assigning the purchase order of its customer and all moneys due thereunder to appellee. The customer, through its treasurer, issued a warrant to the Equipment Company, who indorsed it and deposited it in appellant bank to credit its checking account. The Equipment Company was indebted to the bank on an overdue note, and appellant credited a part of the deposit to its overdue note. Upon suit by appellee for the amount applied to the note, recovery was allowed, and appeal taken. Held, affirmed. The bank, not having changed position in reliance on the buyer's apparent title, nor having given value, could not set off the buyer's pre-existing debt to the bank against a deposit to defeat the conditional seller's claim to the deposit. A bank may not appropriate funds deposited by a trustee in his own name to payment of a personal pre-existing debt of the trustee, even if the bank had no knowledge of the true owner's interest at the time of appropriation of the funds.[1]

There is no doubt that where no other right is involved, money deposited in a bank creates the relation of debtor and creditor between the bank and the depositor, the money becoming the property of the bank, and the bank having the right to apply a sufficient amount of the deposit to the payment of any debt due from the depositor to the bank.[2] At the other extreme, there is no doubt that where the bank knows a third person has an interest in a deposit made in another individual's name, the bank is precluded from applying those funds to the depositor's indebtedness to the bank.[3] However, between these two extremes is an intermediate step in which trust funds are deposited to the trustee's personal account and the bank, not knowing they are trust funds, attempts to apply them to the depositor's indebtedness to the bank.

On this last point, there is a great split of authority, and there has been a further split by distinguishing between cases where the depositor's consent

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[15] Hamilton v. Seamon (1848), 1 Ind. 185; Conklin v. Ogborn (1856), 7 Ind. 553. Also, see Hayden v. Cretcher (1881), 75 Ind. 108.

[1] Peoples State Bank v. Caterpillar Tractor Co. (1938, Ind.), 12 N. E. (2d) 123.

[2] Bedford Bank v. Acoam (1890), 125 Ind. 584, 25 N. E. 713; Lamb, Receiver, v. Morris (1888), 118 Ind. 179, 20 N. E. 746; Second National Bank v. Hill (1881), 76 Ind. 223, 40 A. R. 239; Aurora National Bank v. Dils (1897), 18 Ind. App. 319, 48 N. E. 19.

[3] Shepard v. Meridian National Bank (1897), 149 Ind. 532, 48 N. E. 346; Bundy v. Town of Monticello (1882), 84 Ind. 119; Davis v. Indiana National Bank (1920), 73 Ind. App. 563, 126 N. E. 489; Miami County Bank v. State (1915), 61 Ind. App. 360, 112 N. E. 40; Martin v. First National Bank (1931), 51 F. (2d) 840.