

Real Estate Partnership Partition

Term Paper

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Case laws indicate that when real estate partners established their partnerships, for the most part they did not have initial problems. Partnerships are based on various forms: family-based partners jointly invested into real estate income properties, partners who established a corporation and the corporation severally owned real estate; or partners who simply established partnerships, invested in real estate, and held title as joint tenants and tenants in common, to name a few. Usually years after the start of the partnership, and upon the idea of the dissolution of the partnership, the partners get themselves into trouble.

When voluntary partnership partition fails among partners, the choices in how to partition are limited. If the partners turn to courts for a resolution on their partnership partition and the court orders a judgment to dissolve the partnership, then this judicial partition is known as 'compulsory' partition.

Partnership partition cases in real property are not limited to income properties. There have been cases where partners owned simply lands and they had issues in terminating their ownership of land among themselves. Ownership of land gets tricky when one or more partners own a very large parcel of land and one's ownership is very small. For example, the small partner may own one-tenth of the land and a large partner may own nine-tenth of the land. If the large partner wants to sell his share or wants to finish the partnership, now the small partner can easily hold him up by severing communication, hostility, or complete lack of cooperation. One article of this subject saw the small partner as a kidnapper asking for ransom; whereby the small partner can cause the large partner a lot of trouble and in fact may

ask for a large sum of money for his consent for the sale of the land, and hence the dissolution of the partnership.

The pressure of resistance and lack of cooperation in dissolution of real estate partnership is not limited to small partners, where small partners physically own a smaller portion of the real property in partnership. Although all partners have implied fiduciary duties toward each other, the existence of an initial partnership agreement does make a difference when it comes time for partition. The initial partnership agreement may have specified the fiduciary duties in writing. There have been cases when general partners attempted to acquire interests, for their own benefits, in assets owned by the limited partners. Where the general partners have failed in their outmost due diligence of their fiduciary duties to the limited partners and have even failed to provide full disclosure of facts, the limited partners has had no choice but to turn to courts.

Courts have indicated in their rulings that whether there had been an initial agreement between the general partners and the limited partners requiring and specifying the fiduciary duties of the general partners toward the limited partners, “the Civil Code does, and it would be against public policy to permit a partnership agreement to immunize a general partner from damage claims for breach of a fiduciary relationship”.

As long as the fiduciary duties of the general partners to the limited partners have not been breached, the courts are willing to grant the exercise of the rights and powers given to

the general partners, including the right to acquire partnership assets or units of ownership in the limited partnership.

Under the common law, joint owners of real estate do have the right to seek partition, or physical division, of the land. The physical division of land, known as ‘partition in kind’, may cause all sorts of problems to arise. For example, a small partner of the land may find himself owning a piece of land of much less market value because of its location within the larger parcel, or even its lack of accessibility, than when his portion was part of the entire parcel. In this case, the best solution may be to sell the land for the highest market price possible and divide the proceeds of the sale among the partners.

Modern statutes do allow courts to order a sale of the land if the loss in value from division is substantial, with proportionate division of the proceeds among partners. Not all land sales start at a fair market value price. If the land is auctioned, then the partner with much larger asset and financial credit may over-bid the other partner in the land sale auction, leaving the small partner, who has much less asset and financial credit, with much less cash than he deserved.

Considering that the physical division of the land potentially leads to inefficient fragmentation of the land and incurs subdivision costs associated with it, the sale of the entire parcel of the land at fair market value ordered by the courts may be the best alternative.

Real property partnership partition gets far more complicated as the number of partners increase. The more partners end up with court actions and disputes, more attorney and law suit costs they have to incur.

The courts have to engage in a balancing test between ordering a forced sale of real property in disputes among partners only in cases where the resulting fragmentation would materially reduce the aggregate value of the land, and the physical partition of the property.

In certain cases, the courts may favor partition in kind knowing that the physical partition of the land reduces the market value by rendering them dysfunctional for resale. For example, one partner may be an elderly person who lives in a small portion of the parcel. The courts may order the partition in kind in order to preserve the property ownership of the elderly person.

Question arises on why a big partner would end up with a small partner. Inheritance might have brought them together in the first place; whereby the smaller partner had received a small portion of the land in partnership of another fellow.

In the United States, partition was established by statute in each of the individual states. Unlike the partition in kind, which existed under early common law, the forced judicial partition sale was an American innovation. Dividing property may promote industry and enterprise, and prevent the land from sitting in the hands of unhappy cotenants. The

common law traditionally favored partition in kind of real property held by more than one owner in a tenancy in common or joint tenancy when one or more of the owners seeks to sever the common ownership. For the compulsory partition, a partner must assert that he has the right to partition and a physical partition would be infeasible. For the partner to petition and win a judicial partition of sale of the entire real property, he must present a number of arguments, among which an argument of the difficulty in dividing the property due to its unique topographical features stands out. As a matter of fact, many courts have used the rationale in ordering sale where land containing unique resources, such as hot springs and other water sources, hunting and fishing grounds, or other special attributes, would make actual division complex. However, the property's unique qualities are often the precise reason why parties are resisting sale.

One of the most commonly found reasons for ordering a partition by sale is the existence of too many interests in the commonly held property. Courts find partition in kind impracticable if it requires a division of the property into so many pieces that the property's economic value is diminished. Once the court finds that compulsory partition by way of judicial sale is necessary, it orders the entire property sold at market price, applying a quasi-liability rule. The court's primary focus is whether there would be injury to a cotenant seeking partition, if partition is denied. Injury is most often defined as economic loss.

References

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