

Partnership

Definitions

The Act of a Firm

An act of a firm means any act or omission by all the parties, or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm.

Business

Business means every trade, occupation and profession.

Third Party

Third party used in relation to a firm or to a partner therein means any person who is not a partner in the firm.

Types of Partnership

Partnership at Will

Where no provision is made by contract between the partners for the duration of their partnership, or for the determination of their partnership, the partnership is called partnership at will.

Particular Partnership

When a partnership has been formed for a particular undertaking or adventure, it is known as a particular partnership.

Subject to an agreement between the partners, a particular partnership is dissolved by the completion of the adventure or the undertaking for which the partnership was formed.

Essential Elements of a Partnership

Partnership has been defined by the Partnership Act as the relation between persons who have agreed to share the profits of a business carried on by all or anyone of them acting for all. Persons who have entered into partnership with one another are called individually as partners, and collectively as firm and the name under which their business is carried on is called the firm name.

From the definition it follows that to constitute a partnership the following are the essential elements:

- (a) There must be a business.
- (b) There must be more than one person associated with the business. But in no case the number of partners should exceed twenty, in case of ordinary partnership business.
- (c) There must be a contract between the persons.
- (d) The object of the business must be earning of profit and not that of rendering humanitarian services and the like.
- (e) The business must be carried on by all or any of them on behalf of all.

Registration of Partnership Firms

Before 1932, firms were not legally required to be registered. They were, as such, more or less mysterious organisations, subject to no control or regulation. The Partnership Act of 1932 made provision for the registration of firms.

Effect of Non-registration

The Law does not require that every firm must be registered. But if a firm is unregistered:

- (a) No partner can bring a suit in any court against the firm or his co-partner in the firm;
- (b) The firm cannot file a suit against any third party.

Evidently, the consequences of non-registration are so serious that hardly any firm will like to remain unregistered.

Method of Registration

Partners who want their firm to be registered should fill in the prescribed form for the purpose and send it on to the Registrar of Firms together with the prescribed fee. The form must state:

- (a) the firm's name;
- (b) the place or the principal place of business of the firm;
- (c) the names of any other place where the firm carries on business;
- (d) the date when each partner joined the firm;
- (e) the names in full and permanent addresses of the partners, and
- (f) the duration of the firm.

The above statement should be signed by all the partners and verified in the prescribed manner.

The firm's name should not contain such words as 'Crown', 'Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal'; all words expressing or employing the sanction, approval or patronage of the Crown or the Government.

When the Registrar is satisfied that the above provisions have been duly complied with, he shall make an entry in the Register of Firms and the firm will thus become registered.

Notification of Subsequent Changes

Whenever any change in the constitution or nature of the firm takes place, the registrar of firms should be informed accordingly. The change must be notified when (1) an alteration is made in the firm's name or in the principal place of business; (2) branches are closed or opened; (3) the name or permanent address of any partner changes; (4) the constitution of the firm changes by the entry or withdrawal of a partner, or (5) when the partnership is dissolved.

Partnership firms shall no longer be the sole concern of their partners and their constitution, etc. no longer a mystery to outsiders. Any person can have a look at the Register of Firms on the payment of the prescribed fee. A copy of any entry or portion thereof in the Register of Firms, certified by the Registrar, can also be obtained on the payment of the prescribed fee.

Partnership be

The following o

- (a) If all or all b
- (b) If the busin
- (c) If the part
- (d) If a firm
- (e) If a part
- (f) If the f
- (g) If ther

Distinction

The distin

1. It is
2. It is ship
3. Ev
4. A
5. A
- 6.

7.

8.

Partnership becoming Illegal

The following circumstances, among others, make partnership illegal:

- (a) If all or all but one partner become insolvent.
- (b) If the business transacted by a firm becomes illegal.
- (c) If the partnership was for a limited period and that period has expired, or after the completion of the agreed venture or after the death or insolvency of partner, unless otherwise provided in the Partnership Deed.
- (d) If a firm continues after a partner has given a notice that partnership should be dissolved provided that is partnership at will.
- (e) If a partnership continues after its dissolution by the court.
- (f) If the firm is unregistered.
- (g) If there are more than 20 partners in a firm (or more than 10 in the case of banking business).

Distinction between Partnership and Company

The distinction between partnership and company is explained below:

Partnership	Company
1. It is not a legal entity.	1. It has a legal entity distinct from members.
2. It is governed by the provision of the Partnership Act, 1932.	2. It is governed by the Companies Ordinance, 1984.
3. Every partner in a firm is jointly and severally liable for all debts incurred by the firm.	3. Liability of a shareholder is limited to the nominal value of the share held.
4. A partner can bind the firm and his co-partners so long as he acts within the ordinary scope of the business.	4. A shareholder has no power to bind the company or to bind the other shareholders.
5. All partners can take part in the management of the business of the firm.	5. A shareholder has no right to inspect the books except as may be allowed by the articles.
6. All partners have access to its books.	6. A shareholder has no right to inspect the books except as may be allowed by the articles.
7. The partner can make any agreement they like, and can vary the terms of the partnership as and when they please.	7. A company is bound by its memorandum and articles of association and these can be altered only to limited extent as provided by law.
8. There is no statutory provision requiring a partnership to do so.	8. A company must keep proper books of accounts under the Companies Ordinance, 1984.
9. There is no such statutory provision in the Partnership Act, 1932.	9. It must have the accounts audited.

Partnership	Company
10. A partnership can be brought to an end by an agreement at any time.	10. A company's existence can be brought to an end only by: <ol style="list-style-type: none"> being dissolved by an order of Court. being wound up in a legal manner. its name being struck off by the Registrar.
11. Death or retirement of a partner dissolves the partnership in the absence of a contract to the contrary.	11. A company, having legal existence, continues irrespective of the death or retirement of a member or members.
12. A partner cannot contract with his firm.	12. A shareholder can contract with the company.

Distinction between Partnership and Private Company

The distinction between a partnership and a private company is explained below:

Partnership	Private Company
1. It is governed by the provisions of the Partnership Act, 1932.	1. It is governed by the provisions of the Companies Ordinance, 1984.
2. Each partner is jointly and severally liable for all the debts of the firm.	2. The liability of the members is limited to the nominal value of the shares held by them.
3. It is dissolved on the death of a partner unless there is a contract to the contrary.	3. It has a legal entity separate from its members and is not dissolved on the death of a member.
4. The share of a partner cannot be transferred without the consent of the co-partners.	4. Its member can transfer shares to another subject to the restrictions of the articles of association.
5. Every partner is an agent of the firm and of other partners for the purposes of the partnership business and is entitled, in the absence of a contract to the contrary, to take an active part in the management.	5. A member is not an agent and is not entitled to take active part in its management.
6. Its powers are governed by the Partnership Deed which may be freely altered if all the partners agree.	6. Its general powers are governed by the Memorandum of Association which can be altered only with the consent of the court and is to a limited extent.

Distinction

The distinct

1. It signi person name
2. It is th
3. It ne thoug
4. A pa
5. A pa othe

6. A p has

Partne

After signed differer

The to hav Partne

Th

(a)

(b)

(c)

Distinction between Partnership and Co-ownership

The distinction between partnership and co-ownership is given as under:

Partnership	Co-ownership
1. It signifies the association of more than one person in a business with a common purpose, namely the sharing of profits and losses.	1. It implies the ownership of any particular thing being vested in more than one person.
2. It is the result of an agreement.	2. It does not necessarily arise out of agreement.
3. It necessarily involves a sharing of profits though not of losses.	3. It does not necessarily involve sharing of profits or losses.
4. A partner is the agent of the other partners.	4. A co-owner is not the agent of his owners.
5. A partner cannot, without the consent of the other partners, transfer his right to strangers.	5. A co-owner can, without the consent of the other co-owner, transfer his rights and interest to a stranger.
6. A partner being an agent of the other partners has lien on the partnership property.	6. A co-owner has no lien on the property for expenses or for a common debt.

Partnership Agreement

After having selected the right person for partnership, a Partnership Agreement should be drawn up and signed by the partners. Partners are very friendly at the commencement of the business but later on differences arise between them. They can be easily resolved with reference to the partnership agreement.

The Partnership Agreement may be written on paper or entered into verbally, but it is always advisable to have it in writing. The Partnership Agreement is also known as 'Deed of Partnership' or 'Articles of Partnership'.

The Partnership Agreement must state the following:

- (a) The name of the firm or the designation under which it is to work;
- (b) The nature of the business to be carried on;
- (c) The term or duration of partnership. It may be at will, if no limit has been fixed to its duration so that it can be dissolved at any time; or, it may be for a term, if the time of dissolution has been previously fixed by the original agreement;
- (d) The amount of capital each partners is to contribute;
- (e) The drawing, i.e. the sums the partner can withdraw during a given period;
- (f) The interest to be allowed on capital and charged on drawings;
- (g) Conduct and powers of partners;
- (h) Remuneration to partners;
- (i) Method of division of profits and losses;
- (j) Method to be followed in the event of the death of a partner, dissolution, etc.;
- (k) Goodwill;

- (l) The keeping of proper books of accounts preparation of Balance Sheet, Profit and Loss Account/ Income and Expenditure Account and audit;
- (m) Arbitration clause, laying down the procedure to be followed in the event of disputes.

Rights and Liabilities of the Members of a Partnership Firm

Since partnership is the creation of a contract between the partners, the mutual rights and liabilities of the partners may be determined by contract between the partners, and such contract may be expressed or may be implied by course of dealing. Two principles govern the rights and duties of partners:

- (a) Partners are bound to carry on the business of the firm to their common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner or his legal representative. Thus it was held in *Green Vs. Howell (1910)*/Ch 459/, that even where a partnership agreement provided that a partner may be expelled for breach of certain specified articles, such a clause will not justify the expulsion of a partner where the motive for expulsion is really to purchase the interest of the expelled partner on unfavourable terms.
- (b) Every partner must indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

Apart from these two provisions, the partners may regulate their rights and duties by any agreement. But subject to contract between the partners, the following rules, as laid down by the Partnership Act, will be deemed to regulate the rights and duties of the partners:

- (a) Every partner has a right to take part in the conduct of the business.
- (b) Every partner is bound to attend to his duties in the conduct of the business.
- (c) Any difference arising as to ordinary matters connected with the business may be decided by a majority of the partners, and every partner shall have the right to express his opinion before the matter is decided, but no change may be made in the nature of the business without the consent of all the partners.
- (d) Every partner has a right to have access to and to inspect and copy any of the books of the firm.
- (e) A partner is not entitled to receive remuneration for taking part in the conduct of the business.
- (f) The partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm.
- (g) Where a partner is entitled to interest on the capital subscribed by him, and interests shall be payable only out of profits. But in the absence of agreement no partner is entitled to receive interest on the capital contributed by him.
- (h) For the purposes of the business, if any partner makes a payment or advance beyond the amount of capital he agreed to subscribe is entitled to interest thereon at 6 per cent per annum from the date of the advance.
- (i) A partner shall indemnify the firm for any loss caused to it by his willful neglect in the conduct of the business of the firm.
- (j) The firm shall indemnify a partner in respect of payments made and liabilities incurred by him
 - (i) In the ordinary and proper conduct of the business, and

- (ii) In doing such act, in any emergency, for the purpose of protecting the firm from loss, as would be done by a person of ordinary prudence, in his own case under similar circumstances.

Personal Profits earned by Partners

- (a) If a partner derives any profit for himself from any transaction of the firm or from the use of property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm and share it with his co-partners.
- (b) If a partner carries on any business of the same nature and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business and share the same with his co-partners.

The Property of a Firm

The property of the firm shall be held and used by the partners exclusively for the purposes of the business.

Implied Authority of a Partnership

Subject to the provisions of the Partnership Act, a partner is the agent of the firm for the purposes of the firm. Therefore, a transaction entered into by one partner on behalf of the firm is binding on the firm and makes every partner liable, provided the following conditions laid down in Section 19(1) of the Partnership Act are satisfied. The authority of a partner to bind the firm conferred by this section is called his 'Implied Authority':

- (a) The transaction must be related to the normal business of the firm. If A and B carry on business as partners in a shoe shop, a contract signed by A in the firm-name to supply books would not be binding on the firm or B unless it is made with the express authority of B for the supply of books, is not connected with the normal business of a shoe shop.
- (a) The transaction must be an act for carrying on business in the usual way. It is difficult to lay down any criterion as to the usual way of carrying on any business. It is for the court to decide from all the facts and circumstances of each case as to what is an act for carrying on business in the usual way.
- (b) The transaction must be executed in the firm name, or in any other manner expressing or implying an intention to bind the firm.

But in the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to

- (a) submit disputes relating to the business of the firm to arbitration;
- (b) open a banking account on behalf of the firm in his own name;
- (c) compromise or relinquish any claim or portion of a claim by the firm;
- (d) withdraw a suit or proceeding filed on behalf of the firm;
- (e) admit any liability in a suit or proceeding against the firm;
- (f) acquire immovable property belonging to the firm;
- (g) enter into partnership on behalf of the firm; or
- (h) acquire immovable property on behalf of the firm.

It should be noted that the partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partner. But notwithstanding any such restriction, any act done by a partner or behalf of the firm which falls within his implied authority binds the firm, unless the person with whom he is dealing knows of the restriction or does not know or believe that partner to be a partner.

A partner has also authority, in an emergency, to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstances, and such acts bind the firm.

Principle of Holding Out

Anyone who, by words spoken or written or by conduct, represents himself or knowingly permits himself to be represented as a partner in a firm is liable as a partner of that firm to anyone who has on the faith of any such representation given credit to the firm, whether the person representing himself or allowing himself to be represented as a partner does or does not know that the representation has reached the person so giving credit. This often happens when a partner retires but nevertheless allows himself to appear as if he still were a partner.

This is the rule of liability which is commonly known as arising out of the principle of holding out. It rests on the principle of estoppel as laid down by Section 115 of the Evidence Act.

Minor as a Partner

Since partnership is the product of a contract alone, a minor cannot be a partner in a firm for the simple reason that he has no contractual capacity. A minor may, however, be admitted to the benefits of partnership if all the partners for the time being consent to such admission.

When a minor is thus admitted, he has a right to such share of the property and of the profits of the firm as may be agreed upon between the partners. He may also have access to and inspect and copy any of the accounts of the firm.

Such a minor is not personally liable for the liabilities of the firm. His share in the business alone is liable for such liabilities.

After the attainment of majority, the minor's position as regards the firm is determined by the attitude he takes thereafter. At any time within six months of his attaining majority, he may give public notice that 'he has elected to become or that he has elected not to become a partner in the firm'. If he fails to give such a notice, he will become a partner in the firm on the expiry of the said six months.

When a person becomes a partner in the above way, his rights and liabilities as a minor continue up to the date on which he becomes a partner, and he also becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership. His share in the property and profits of the firm shall be the share to which he was entitled during minority.

When such a person elects not to become a partner, his rights and liabilities shall continue to be those of a minor up to the date on which he gives the public notice required. His share shall not be liable for any acts of the firm done after the date of the notice. And he shall be entitled to sue the partners for his share of profits when he serves his connections with the firm.

Reconstitution of a Firm

A firm is said to be reconstituted when (a) a new partner is introduced, (b) any of the partners retires, (c) any of the partners is lawfully expelled, (d) any of the partners becomes insolvent, or (e) any of the partners dies.

(a) Introduction of

Under Section 33, a person shall be introduced into a firm as a partner, if an existing partner unless all the partners consent to his admission as a partner.

In the absence of his admission as a partner.

(b) Retirement

A partner may retire by the partners, if his intention to do so is declared in a special agreement.

A retiring partner is liable for the debts of the firm.

(c) Expulsion

A partner may be expelled from a firm unless the express consent of all the partners is obtained.

An expelled partner is not liable for the debts of the firm.

(d) Insolvency

A partner who becomes insolvent is not liable for the debts of the firm.

(e) Death

Unless a partner dies, the firm is not dissolved. The death of a partner does not dissolve the firm.

Dissolution

A firm is dissolved when the partners agree to dissolve it.

(a)

A firm is dissolved when the partners agree to dissolve it.

(b)

(c)

(d)

(e)

(a) Introduction of a New Partner

Under Section 31 of the Act, in the absence of any contract to the contrary between the partners, no person shall be introduced as a partner into a firm without the consent of all the existing partners. As a result, if an existing partner sells his share in the partnership, the purchaser of the share does not become a partner unless all the other partners agree to such transfer. But even by agreement a minor cannot be made a partner.

In the absence of special agreement, a new partner does not become liable for debts of the firm prior to his admission as a partner.

(b) Retirement of the Partner

A partner may retire (i) with the consent of all other partners, (ii) in accordance with an express agreement by the partners, or (iii) where the partnership is at will by giving notice in writing to all other partners of his intention to retire. The mode of retirement of partners in any firm may, however, be specified by a special agreement between the partners.

A retiring partner has to give public notice of retirement in order to obtain freedom from liability for the debts of the firm as from the date of such notice.

(c) Expulsion of a Partner

A partner cannot be expelled except in the manner specified by the contract between the partners and unless the expulsion has been made in good faith.

An expelled partner cannot claim damages. His only right is to seek reinstatement. A legal expelled partner stands on the same footing as a retired partner as regards his liabilities for the debts of the firm.

(d) Insolvency of a Partner

A partner ceases to be a partner as soon as he is adjudged an insolvent. But the firm is not dissolved unless all the partners or all partners but one are adjudged insolvent.

(e) Death of a Partner

Unless otherwise provided by the contract of partnership, the death of a partner has the effect of dissolving the partnership. Where under a contract between the partners, the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after the death.

Dissolution of a Partnership

A firm may be dissolved with the consent of all the partners, or according to the terms of the partnership agreement. It may also be dissolved in the following cases:

(a) Compulsory Dissolution

A firm is compulsorily dissolved if all the partners, or all of the partners but one, become insolvent, or if the business of the firm becomes unlawful.

(b) Dissolution on the Happening of Certain Contingencies

Subject to an agreement between the partners a firm is dissolved:

- (i) if constituted for a fixed term, by the expiry of the term;
- (ii) if constituted to carry out one or more undertakings, by the completion thereof;

- (iii) by the death of a partner;
- (iv) by the adjudication of a partner as an insolvent.
- (c) Dissolution by Notice of Partnership at Will

Where the partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partners of his intention to dissolve the firm.

- (d) Dissolution by the Court

At the suit of a partner, the court may dissolve a firm on any of the following grounds: (i) that a partner has become of an unsound mind; (ii) that a partner, other than the partner filing the suit, has become in any way permanently incapable of performing his duties as a partner,

For example: through transportation for life; (iii) that a partner, other than the partner filing the suit, is guilty of misconduct prejudicial to business; (iv) that a partner, other than the partner filing the suit, wilfully or persistently commits breach of Partnership Agreement; (v) that a partner other than the partner filing the suit, has in any way transferred his interest in the firm to a third party; (vi) that the business of a firm cannot be carried on except at a loss; or (vii) on any other ground that renders it just and equitable that the firm should be dissolved.

A public notice of dissolution should be given as soon as possible; otherwise the partners continue to be liable to third parties for any act done on behalf of the firm thereafter as if the firm is not dissolved.

Settlement of Accounts on Dissolution

In settling of the accounts of a firm after dissolution, the following rules shall, subject to agreement by the partners, be observed:

- (a) Losses, including deficiencies of capital, shall be paid first out of the profits, next out of capital and lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits.
- (b) The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order:
 - (i) In paying the debts of the firm to third parties;
 - (ii) In paying to each partner rate ably what is due to him from the firm for advances distinguished from capital;
 - (iii) In paying to each partner rate ably what is due to him on account or capital, and
 - (iv) The residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

Dissolution of Partnership: Rights and Obligations of Partners

The rights and obligations of partners on dissolution are as follows:

- (a) Notwithstanding the dissolution of a firm, the partners constitute to be liable as such to third parties for any act done by any of them which would have been an act of the firm if done before the dissolution, until public notice is given by any partners:

Provided that the estate of partner is not liable for acts done after (i) he dies, (ii) he is adjudicated insolvent, and (iii) he retires from the firm and the person dealing with the firm after that date does not know him to be a partner.

For example: A and B, partners in a trade agree to dissolve the partnership and execute a deed for that purpose, declaring the partnership dissolved as from 1 January, but they do not give notice of the dissolution on 1 January. A endorses a bill in the partnership's name to C, who is not aware of the dissolution. The firm is liable to pay the bill and both A and B are liable as well.

A bill is drawn on a firm in its usual name of Ahmed & Co., and accepted by an authorised agent A was formerly a partner in the firm, but not to the knowledge of B, the holder of the bill, and ceases to be so before the date of the bill. B cannot sue A for the bill.

- (b) On the dissolution of a firm every partner or his legal representative (i.e. his heir or executor or administrator) is entitled as against all other partners or their representative to have the property of the firm applied in payment of the debts and liabilities of the firm and to have the surplus distributed among the partners or their representative according to their rights. This involves amongst others the right to account and to have a Receiver appointed of the assets of the firm for the purpose of preserving the assets of the firm until the accounting is completed and the assets distributed.
- (c) After the dissolution of a firm the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners, continue notwithstanding the dissolution so far as may be necessary to wind up the affairs of the firm and to complete transactions begun but unfinished at the time of the dissolution, but not otherwise.

Provided that the firm is in no case bound by the act of a partner who has been adjudicated insolvent, but this proviso does not relieve the liability of any person who has after the adjudication represented himself or knowingly permitted himself to be represented as a partner of the insolvent.

- (d) Where a partner has paid a premium on entering into partnership for a fixed term and the partnership is dissolved before the term, he is entitled to recover his premium unless the dissolution is due to death of one of the partners or to his own misconduct or is in pursuance of an agreement containing no provision for the return of premium paid.

TEST QUESTIONS

1. Define partnership and state its difference from a private company.
2. What are the essential elements of a partnership?
3. Must a firm be registered? What are the effects of non-registration?
4. Differentiate between partnership and co-ownership.
5. Discuss the rights and liabilities of members of a partnership firm.
6. When does a partner have implied authority to bind the firms? Give details. For what act is the authority to bind the firm not implied?
7. What do you understand by the principle of 'holding out' in case of a partnership?
8. Can a partner on his own authority send a dispute related to the firm to arbitration or acquire immovable property of the firm?
9. What are the rights and obligations of partners after dissolution of a partnership?
10. Under what circumstances is a firm said to be reconstituted?
11. Discuss the various situations in which a firm may be dissolved.