DISSOLUTION OF A FIRM

39. Dissolution of a firm – The dissolution of partnership between all the partners of a firm is

called the “dissolution of the firm”.

40. Dissolution by agreement – A firm may be dissolved with the consent of all the partners or

in accordance with a contract between the partners.

41. Compulsory dissolution – A firm is dissolved -

a) by the adjudication of all the partners or of all the partners but one as insolvent or

b) by the happening of any event which makes it unlawful for the business of the firm to be

carried on or for the partners to carry it on in partnership:

Provided that, where more than one separate adventure or undertaking is carried on by the

firm, the illegality of one or more shall not of itself cause the dissolution of the firm in respect of

its lawful adventures and undertakings.

42. Dissolution on the happening of certain contingencies – Subject to contract between the

partners a firm is dissolveda) if constituted for a fixed term, by the expiry of that term;

b) if constituted to carry out one or more adventures or undertakings, by the completion

thereof;

c) by the death of a partner; and

d) by the adjudication of a partner as an insolvent.

43. Dissolution by notice of partnership-at-will-

(1) 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.

(2) The firm is dissolved as from the date mentioned in the notice as the date of dissolution or,

if no date is so mentioned, as from the date of the communication of the notice.

44. Dissolution by the Court – At the suit of a partner, the Court may dissolve a firm on any of

the following grounds, namely:-

a) that a partner has become of unsound mind, in which case the suit may be brought as well

by the next friend of the partner who has become of unsound mind as by any other partner;

a) that a partner, other than the partner suing, has become in any way permanently incapable

of performing his duties as partner;

a) that a partner, other than the partner suing, is guilty of conduct which is likely to affect

prejudicially the carrying on of the business, regard being had to the nature of the business;

a) that a partner, other than the partner suing, willfully, or persistently, commits breach of

agreements relating to the management of the affairs of the firm or the conduct of its business,

or otherwise so conducts himself in matters relating to the business that it is not reasonably

practicable for the other partners to carry on the business in partnership with him;

a) that a partner, other than the partner suing, has in any way transferred the whole of his

interest in the firm to a third party, or has allowed his share to be charged under the provisions

of rule 49 of Order XXI of the First Schedule to the Code of Civil Procedure, 1908, or has

allowed it to be sold in the recovery of arrears of land-revenue or of any dues recoverable as

arrears of land-revenue due by the partner;

a) that the business of the firm cannot be carried on save at a loss; or

a) on any other ground which renders it just and enquitable that the firm should be dissolved.

45. Liability for acts of partners done after dissolution – (1) Notwithstanding the dissolution of a

firm, the partners continue 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 of the dissolution:

Provided that the estate of a partner who dies, or who is adjudicated an insolvent, or of a

partner who, not having been known to the person dealing with the firm to be a partner, retires

from the firm, is not liable under this section for acts done after the date on which he ceases to

be a partner.

(2) Notices under subsection (1) may be given by any partner.

46. Right of partners to have business wound up after dissolution – On the dissolution of a firm

every partner or his representative is entitled, as against all the other partners or their

representatives, 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 representatives

according to their rights.

47. Continuing authority of partners for purposes of winding up – 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 acts of a partner who has been adjudicated

insolvent; but this proviso does not affect 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.

48. Mode of settlement of accounts between partners – In settling 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 profits, next out of capital,

and, lastly, if necessary, by the partners individually in the proportions in which they were

entitled to share profits.

a) 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 orderi) in paying the debts of the firm to third parties;

ii) in paying to each partner rateably what is due to him from the firm for advances as

distinguished from capital;

ii) in paying to each partner rateably what is due to him on account of capital; and

ii) the residue, if any, shall be divided among the partners in the proportions in which they were

entitled to share profits.

49. Payment of firm’s debts and of separate debts- Where there are joint debts due from the

firm, and also separate debts due from any partner, the property of the firm shall be applied in

the first instance in payment of the debts of the firm, and, if there is any surplus, then the

share of each partner shall be applied in payment of his separate debts or paid to him. The

separate property of any partner shall be applied first in the payment of his separate debts, and

the surplus(if any) in the payment of the debts of the firm.

50. Personal profits earned after dissolution- Subject to contract between the partners the

provisions of clause (a) of section 16³ shall apply to transactions by any surviving partner or by

the representatives of a deceased partner, undertaken after the firm is dissolved on account of

the death of a partner and before its affairs have been completely wound up:

Provided that where any partner or his representative have bought the goodwill of the firm,

nothing in this section shall affect his right to use the firm name.

51. Return of premium on premature dissolution- Where a partner has paid a premium on

entering into partnership for a fixed term, and the firm is dissolved before the expiration of that

term otherwise than by the death of a partner, he shall be entitled to repayment of the

premium or of such part thereof as may be reasonable, regard being had to the terms upon

which he became a partner and to the length of time during which he was a partner, unless -

a) the dissolution is mainly due to his own mis-conduct, or

b) the dissolution is in pursuance of an agreement containing no provision for the return of the

premium or any part of it.

52. Rights where partnership contract is rescinded for fraud or misrepresentation – Where a

contract creating partnership is rescinded on the ground of the fraud or misrepresentation of

any of the parties thereto, the party entitled to rescind is, without prejudice to any other right,

entitleda) to a lien on, or a right of retention of, the surplus or the assets of the firm remaining after

the debts of the firm have been paid, for any sum paid by him for the purchase of a share in

the firm and for any capital contributed by him;

b) To rank as a creditor of the firm in respect of any payment made by him towards the debts

of the firm; and

c) To be indemnified by the partner or partners guilty of the fraud or misrepresentation against

all the debts of the firm.

53. Right to restrain from use of firm name or firm property- After a firm is dissolved, every

partner or his representative may, in the absence of a contract between the partners to the

contrary, restrain any other partner or his representative from carrying on a similar business in

the firm name or from using any of the property of the firm for his own benefit, until the affairs

of the firm have been completely wound up:

Provided that where any partner or his representative has bought the goodwill of the firm,

nothing in this section shall affect his right to use the firm name.

54. Agreements in restraint of trade- Partners may, upon or in anticipation of the dissolution of

the firm, make an agreement that some or all of them will not carry on a business similar to

that of the firm within a specified period or within specified local limits : and notwithstanding

anything contained in section 27 of the Contract Act, 1872, such agreement shall be valid if the

restrictions imposed are reasonable.

55. Sale of goodwill after dissolution – (1) In settling the accounts of a firm after dissolution,

the goodwill shall, subject to contract between the partners, be included in the assets, and it

may be sold either separately or along with other property of the firm.

(2) Rights of buyer and seller of goodwill – Where the goodwill of a firm is sold after dissolution,

a partner may carry on a business competing with that of the buyer and he may advertise such

business, but, subject to agreement between him and the buyer he may not -

(a) use the firm name,

(b) represent himself as carrying on the business of the firm or

(c) solicit the custom of persons who were dealing with the firm before its dissolution.

(3) Agreements in restraint of trade – Any partner may, upon the sale of the goodwill of a firm

make an agreement with the buyer that such partner will not carry on any business similar to

that of the firm within a specified period or within specified local limits, and, notwithstanding

anything contained in section 27 of the Contract Act, 1872, such agreement shall be valid if the

restrictions imposed are reasonable.