

## PARTNERSHIP ACT 1932

### Definition :- Section 4

“Partnership is the relation between persons who have agreed to share the profit of business carried on by all or any one of them acting for all.”

In short the term is defined as a voluntary contract between two or more competent persons to place their money, effects, labour and skill or some or all of them in lawful business with the understanding that there shall be sharing of profit between them.

### Partners firm and firm's name

Persons who have entered into partnership with one another are called individually. Partners' and collectively 'A firm' and the name under which their business is carried on is called the firm name.

### Essential elements of partnership :

#### (i) Association two or more persons :

At least two persons should join together to constitute a partnership. Minimum two persons are required to constitute a partnership and maximum no. of members is ten in case of banking business and twenty in case of other business.

#### (ii) Agreement :

There must be an agreement entered into by all such persons. Partnership can only arise as a result of agreements express or implicit, between two or more persons. Partnership is thus created by a contract; it does not arise by the operation of law. Joint ownership may arise by the operation of law, but not partnership. Thus, on the death of a person, his children may inherit the family property jointly with the family business and may share the profit of the business equally but they are not for that reason partners.

The contract which is the foundation of partnership must itself be founded on good faith and must be for a lawful object and purpose, and between competent person.

#### (iii) Sharing of profit :

Basically, the word, 'partnership' is derived from the word, 'To Part' means 'To Divide' Thus division of profit is one of the most important feature of partnership Section 4 only says about the sharing of profit and is silent about the sharing of losses. But Section 48. of partnership Act provides that " In the absence of a contract to the contrary the losses are to be shared in the proportion in which they were entitled to share profit " .

It means a person may become a partner with clear understanding that he shall not be liable to share the losses but it will be binding to partners only and not for third party. However if two or more persons associate for charitable or religious purpose they can not be called as a partner because such association do not have an intention of making profit and sharing them.

#### (iv) Existence of a business :

A term 'Business' has been defined in Section 2 to include every trade, occupation and profession. This definition which has been adopted from the English Act is very general and offers very little assistance while dealing with borderline cases.

The object of the agreement or contract is to carry on business and the business which the partners carry on must of course be legal. However the mere fact that several persons own something in common which produces returns and that such persons divide those returns according to their respective interest does not make them partners.

**For Example :** 'A' and 'B' are co-owners of a house net rent between themselves. A and B are not partners because receiving the rent of house let at a tenant is not a business. Business may be temporary or permanent but it must be in existence. In agreement to carry on business at a future time does not result in a present partnership.

**(v) Mutual Agency :**

"The business must be carried on by all the partners or any one of them acting for all ". This shows that the persons or the group who conduct the business do so as agent for all the persons in the group and are therefore liable to account to all. Thus, the relation of principal and agent amongst the partners i.e. mutual agency is the true test of partnership. In fact it has been especially provided by Section 80 that, " Subject to the provisions of this act a partner is the agent of the firm for the purposes of the business of the firm".

The principal of agency is the essence of partnership. A partner is both a principal and an agent, while the relation between the partners is that of principals, they are agent of the firm and of one another in relation to third parties for the purpose of the business of the firm.

**\* Test of Partnership:**

In order to determine the existence of partnership between a group of persons a definition in **Section 4**. is used as a test i.e. one must look to the agreement between them. If the agreement is to share the profit of a business and the business is carried on by all or any of them acting for all, there is a partnership otherwise not. The difficulty arises when there is no specific agreement constituting partnership or agreement does not specifically speak of partnership. In such case we have to take help of section 5 and section 6.

**Section 5** lays down that the relation of partnership arises from contract and not from status. **Section 6** lays down that in determining whether a group of persons is or is not a firm or whether a person is or is not a partner in a firm. The relation between the parties is to be determined from all the facts i.e. the written or verbal agreement surrounding circumstances at the time when the contract was entered into conduct of the parties and other relevant facts i.e. books of account, correspondence, evidence of employees etc. These facts are taken collectively and their cumulative effect is taken into consideration.

Section 5 or section 6 also lays down that certain persons are not to be deemed to be partners.

**\* It is expressed laid down that the following are not partners :**

**(i) Joint owners sharing gross returns :** Joint owners of some property sharing profits or gross returns arising from the property do not become partners.

**(ii) Sharing of Profits :** The sharing of profits is a prima face a powerful evidence of partnership. But the fact that there is sharing of profits between some person will not automatically make them the partners. Therefore, receipt by a person of share of the Profits of a business or payment contingent upon the earning of profit or varying with the profits

earned by a business does not of it self make him a partner with the person carrying one business.

(a) When a person has lent money to person engaged or about to engage business, and received a rate of interest varying with the profit.

**Example :** A advanced money to two merchants who agreed to carry on the business subject to the control of in several respects. A was to receive commission of 20% on total profit. Held there was no partnership.

(b) Where a servant or, agent is engaged in business & receives his remuneration as a share of profit.

**Example :** A contractor for loading & unloading railway wagons appointed a servant to manage it.

The servant was to receive 50% of the profit and was to bear all losses if any. Held the servant was the agent of and not his partner.

(c) Where a widow or child of a diseased partner receives a portion of the profit.

(d) Where a person has sold his business along with its goodwill and receives a portion of the profit in consideration of the sale. Although the sharing of profit of a business is a strong test of partnership, yet whether the relation of partnership does or does not exist must depend upon the real intention and conduct of the parties.

#### **Property of the firm & its application ( section ) :**

Section 14 and 15 lays down that the property of the firm includes all property. and rights and interest in the property originally into the stock of the firm or acquired by purchase or otherwise, by or for the firm or for the purposes and in the course of the business of the firm and includes also the goodwill of the business unless a contrary inter appears, property acquired with money belonging to the firm are deemed to have been acquired for the firm.

It may be noted that just because property belong to one partner is used for the purpose of the firm's business. It does not become the property of the firm. But if there is anything to show the intention of the partner to make it so, then it will become the firm property.

Example : Where the owner of a mill agreed to carry on the manufacture in partnership with others and the owner partner was credited in it firms account with the value of the mill as his capital. It was held that the mill had become the firms property.

#### **\* Types of partner :**

(i) Active Partner

(ii) Dormant or sleeping or Nominal partner.

(iii) Partner by holding out (Sec 28) (SN)

Section 28 of the Act deals with what is known as liability by holding out. Any one 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 in that firm, to anyone who has, on the faith of any such representation, given credit to the firm, whether the person representing himself, or represented to be a partner, does or does not know that the representation has reached the person so giving credit.

In other words, the doctrine of holding out is part of the principle of estoppel which lays down that where one person by words or conduct, induces another to believe him and act upon the existence of a particular

state of facts, he can not afterwards, as regards that person deny the existence of such facts. **Example** : A is in the habit of representing himself to be a partner of a particular firm, B on strength of such representation and without giving any such notice to A supplies goods on credit to the firm. **Held**. A would be liable as a partner to B for the price of the goods. Essentials ( Section 28) In order to stop a person from denying that he is a partner on the doctrine of holding out, two important elements must co-exist.

- (1) A person must represent himself to be a partner in a firm or, knowingly permit himself to be represented.
- (2) Another person must have given credit to the firm on the faith of such representation.

**\* Additional points in connection to the doctrine of holding out :**

- (1) The representation may be express or implied.
- (2) It need not be made by person himself, but may be made by others.
- (3) A general representation to the world at large is not sufficient unless the person who gives credit can satisfy the court that he was aware of and acted upon it.

**\* Effect of holding out :**

If a person holds himself out to be a partner of a firm, he becomes personally liable. He does not thereby become a partner in the firm and he is also not entitled to any rights against those who are in fact partner in the firm. He does not become an agent of the firm. He merely makes himself personally liable for the credit given to the firm on the faith of the representation.

**\* Registration of firm :**

Before the Amendment Act 1984 Indian partnership Act 1932 does not make registration of a firm compulsory nor does it impose any penalty for non-registration. It is optional for a firm to get itself registered or not. Section 58 of partnership Act as amended by the Maharashtra Amendment Act 1984 maintains the same position that is registration of a firm is not compulsory but said amendment provides, those who want the firm to be registered, should send the statements in prescribed form to the registrar of the firm within a period of one year from date of constitution of the firm and if there is a delay. Late registration can be done under new section 59A-1 but a penalty of Rs. 100/- per year delay has to be paid.

**\* Effects of Registration :**

Section 68 lays down a rule of conclusive proof and enable a certified copy of an entry in the Registrar of the firm to be tendered in evidence of

- (a) The registration of the firm to which the entry relates.
- (b) The contents of any statement, intimation or notice recorded or, noted there in. The result is that although the law does not make registration of a firm compulsory, from the practical angle, it is highly advisable to do so.

**\* Effects of Non-registration :**

As seen above Indian Partnership Act has provided for the registration of firm but has not imposed any penalties for non-registration. Non-registration does not make the partnership agreement of any transaction between the partner and the third parties, void. But no prudent partner or

a firm should hesitate to get his or its name registered at the earliest possible opportunities, for the effect of non-registration is rather serious.

**(i) No suits between partners and firm :**

A partner of an unregistered firm can not sue the firm or any of his present or past co-partner to enforce a right arising from a contract or confirmed by this act. Unless the firm is registered and the name of the partner suing appears in the register of the firm as a partner in the firm. But Maharashtra State Amendment provides, suit filed by the legal heirs of a diseased partner registration of firm is not required.

**(ii) No-suits by a firm :**

An unregistered firm can not sue any third party for enforcement of a right arising from a contract unless the firm is registered and the persons suing are or have been shown in the register of a firm as partners in the firm. But unregistered firm can sue to enforce a right arising otherwise than from contract i.e. injunction against infringement of trademarks, trade name and patent. It is also important to note that the act does not lay down that any transaction of an unregistered firm will be invalid. It merely says that a firm will not be allowed to take the assistance of a civil court.

**(iii) No right to counter claim or set off :**

No unregistered firm or partner, when sued, be entitled to counter claim or set off to enforce a right arising from a contract.

**\* Exceptions :**

Non-registration of firm does not affect following rights.

- (i) The right of third parties to sue the unregistered firm or its Partners.
- (ii) The right of partner to sue for dissolution of firm.
- (iii) The power of official Assignee, court receiver to realise the property of an insolvent partner.
- (iv) Suit for amount not exceeding Rs.100/-

It may be noted that above disabilities are those of a firm and partners, and not for third parties. Hence third party can always bring a suit against a firm whether registered or not.

**Relation of Partner to Third Parties implies Authority of Partner : ( Implied Authority of Partner )**

A partner is both the principal and an agent. The partner exercises his authority expressly or implicitly. An express authority of one, which a partner has a right to enjoy under the deed of partnership. In the absence of an express authority, the partner may do any act in the firm's name in the usual course in the conduct of the business, it is called implied authority. Such authority is not required to be stated in the partnership deed.

For the purpose of the implied authority business are divided into two categories :

**(a) When a partner has implied authority :** Implied authority in commercial or Trading Business. In this case a partner may carry on behalf of the firm usual commercial activities like

- (1) Buying & selling the goods.
- (2) Receiving & giving payments.
- (3) Employing persons for the firm.
- (4) Repaying the loans on behalf of the firm.

(5) He may draw, make, sign endorse, accept, transfer, negotiable instrument in the name of firm.

**(b) When a partner has no implied authority :**

Following limitations as regards implied authority of a partner which will not bind the firm, they are as follows :

- (1) To open a bank A/c in his own name on behalf of the firm.
- (2) To compromise or relinquish any right or claim of the firm.
- (3) To withdraw a suit or proceeding

## **Rights and Duties of Partners**

The mutual right & duties of partners of a firm may be determined by contract between the parties. In the absence of express contract between the partners, the relation between partners are governed by section 9 to 16 & 25 of the act.

**Right of a Partners :**

**(1) To take part in the business :** Every partner has a right to take part in the conduct & management of the business, subject to any contract between the partners.

**(2) To share the Profit :** In the absence of any agreement the partner has a right to share equally in the profits of the business earned & are liable to contribute equally to the losses sustained by the firm.

**(3) To have access to the accounts :** Every partner has a right to have access to & to inspect & copy any of the books of the firm.

**(4) To be indemnified :** Every partner has a right to be indemnified by the firm in respect of payment made & liabilities incurred in the ordinary conduct of business or doing any act in emergency.

**(5) To be Consulted :** Every partner has a right to be heard & to be consulted if the matter's differences of opinion & also has a right to express his opinion.

**(6) To interest on Capital :** The partnership agreement may contain a clause to the right of the partners to claim interest on capital at a certain rate such interest subject to contract between the partners is payable only out of profit, if any, earned in the firm.

**(7) To retire :** A partner has a right to retire according to the nature of partnership.

**(8) To use Partnership property :** The property of the firm shall be held & used by the partners exclusively for the purpose of business. No partner has a right to treat it as his individual property.

**(9) To have business wound up after dissolution :**

On the dissolution of a firm every partner or his representative, to have the property of firm applied in payment of the debts & liabilities of firm & to have the surplus distributed among the partners or representatives.

**(10) Right to interest on advances :**

Where a partner makes for the purposes of the business of the firm any advances beyond the amount of capital he is entitled to interest on each advance at the rate of 6% P.A. such interest is not only payable out of the profit of the business but also act the assets of the firm.

### **Duties & Liabilities of a Partner :**

**(1) To carry on a business to common advantage :**

**Every partner is bound to:**

- (a)** Carry on the business to the greatest common advantage.
- (b)** Be just & faithful to each other.
- (c)** Use reasonable care & skill in performing his duties.
- (d)** Render true account & full information.

**(2) To indemnify :**

**\* Every partner shall indemnify the firm for any loss caused to it by :**

- (a)** His fraud in the conduct of the business of the firm .
- (b)** Wilful neglect of duty conduct of the business of the firm. All partner are jointly & severally liable for acts of the firm.

**(3) To be diligent :**

Every partners is bound to attend diligently to his duties in the conduct of the business.

**(4) No remuneration :**

A partner is not entitled to receive remuneration for taking part in the conduct of the business. It is, however, usual to allow some remuneration to the working partners provided there is a specific agreement to that effect.

**(5) To account for personal profit made :**

If a partners derives any benefit, with all the consent of the other partners from partnership transaction or by used of partnership property name or business connection, he must account for it & pay 'A' Tao the firm.

**(6) Not to Carry on competing business :**

No partners shall carry on any business of the same nature as competing to the business of the partnership firm. If partners carries the business & then he shall account for & pay to the firm all the profit made by him in that business.

**(7) To share losses :**

Subject to the contract between the partners, partner in liable to contribute equally to the losses sustained by the firm, some partners may exclude their liability to share losses.

**(8) Liable for acts of the firm :**

Every partner has implied. authority, where he exceeds the authority conferred on him & the firm, suffers a loss, he shall have to compensate the firm for any such loss.

### **(Section 30) Minor's Position in Partnership :**

According to section II of contract Act & the principles laid down in the case of **Mohribibi V/s Dharmadas Ghosh**, a minor is incompetent to contract & a contract by a minor is **void ab initio**. Since partnership is a contract, therefore minor's entry in a partnership firm, as a rule has been barred. But the second part of section 30 opens the door for the person who is a minor to become a partner in a firm. A minor may admitted only to the profit or benefit of the partnership with consent of all the partners

of the firm. Moreover, a partnership firm cannot be formed with only minor persons as partners, so at least two major partners should be there.

**Right of a Minor :**

- (a) To share profit
- (b) To inspect the books of A/c
- (c) To filed suit for A/c's of profit against other partner.
- (d) To elect to become a partner - on attaining majority.
- (e) To elect not to become partner - on attaining mjrjority.

**Liabilities of Minor :**

- (a) Minors share is liable for the act of the firm.
- (b) On attaining majority if he elects to be a partner, he becomes personally liable.
- (c) Within 6 month of his attaining majority, he must give public notice offer his election to become a partner or he has elected not become a partner of the firm. If minor fails to give public notice, it is presumed that he has elected to become a partner & held liable for personally for all losses & liabilities form the date of admission.

When he elect not to become a partner his rights & liabilities continue to be those of a minor upto the date on which he gives the public notice. His share in the profit shall not be liable for any act of the firm done after the date of public notice. He can sue the firm for his share in the profit.

**Mohori Bibi V/s Dharmodas Ghose :**

Minor mortgaged his house in favour of money lender to secure a loan of Rs. 20,000/, part amount of Rs. 10,500/- actually paid to the minor. After taking advance, minor filed a case, stating that he was a minor who had mortgaged his house & mortgage should be cancelled on the ground of the minority , Court cancelled the mortgage deed. Money lender requested the court to direct the minor to repay advance of Rs.10,500/-. But Court refused to order the return of money & It was held that minors agree't not only void but it is void-ab-intio.

**DISSOLUTION OF A FIRM**

**Meaning :**

Dissolution of a firm means a firm ceases to exist. The relationship existing between the partner discontinues. The dissolution of partnership between all the partners of a firm is called the dissolution of the firm.

Dissolution of a firm is different from dissolution of partnership. Dissolution of a firm involves total breakdown or, relation of partnership between all the partners comes to an end. On dissolution of partnership relation of partnership between a few partners comes to an end.

**Mode of Dissolution :**

**Section 40 to 44 lays down various modes of dissolution of a firm, which can be classified as follows :**

**1. By an act of the Parties :**

- (a) **By Agreement :** A firm can be dissolved as per the mutual agreement between the parties or expressed terms in the partnership deed.



**(b) By Consent :** A firm may be dissolved at any time with the consent of all partners. This applies to all cases, whether firm is for a fixed period or otherwise.

**(c) By Notice :** In case of “partnership at will” the firm may be dissolved by any partner giving notice in writing to all other partners of his intention to dissolve the firm. A notice once given cannot be withdraw with at consent of all the partners.

## 2. **By Operation of Law :**

**(a) Compulsory dissolution**

**(b) On happening of certain contingencies.**

### **(a) Compulsory dissolution :**

**(i) Insolvency of partner :** When all the partners or all the partner except one, are adjudicated insolvent, the firm is compulsory dissolved.

**(ii) When some event making partnership business unlawful :** When some event happens, which makes it unlawful for the business to be carried on in partnership.

E.g. A wine shop carrying on the business of selling liquor is valid when business started, but new legislation comes into force which prohibits the sale of liquor, it would become an unlawful business. Where business is declared as unlawful, the firm must be compulsorily dissolved.

**(iii) Illegal Partnerships :** Where two partners in a firm are carrying on business & one of the partner is a foreigner & there was a outbreak of war between the country, foreign countries declare as an enemy country the partnership between the two partner become an illegal partnership & firm has to be compulsory dissolved.

### **(B) On happening of certain contingencies :**

**(i) By expire of term :** Where a partnership has been constituted for a fixed period, the firm is automatically dissolved on the expire of such fixed period .

**(ii) By completion of undertaking :** Where a partnership has been constituted to carry out one or more adventures or undertaking the firm is automatically dissolved on completion of such adventure or undertaking.

**(iii) By Death of a partners :** Where a partner in a firm dies, the firm is automatically dissolved on the death of the partner.

**(iv) By insolvency of a Partner :** In the absence of where a partner is declared insolvent by a court he ceases to be a partner forthwith & the firm is dissolved.

## 3. **By Intervention of the Court :**

**(a) By insanity of a partner :** When a partner becomes a lunatic, either his relative or friend or any other partner can file a suit for dissolution this is because a contract by a lunatic is void & so business cannot be carried on with such person.

**(b) Permanent incapacity of Partner :** Where a partner becomes permanently incapable of performing his duties as a partner, on suit being filed by other partner, the court may order a dissolution of firm.

**(c) By mis-conduct of a partner :** If a partner is guilty of conduct which is likely to affect prejudicially the business of the firm, any other partner can sue for dissolution of the firm E.g. Mis appropriation of customer money.

**(d) By persistent breach of agreement :** Where a partner wilfully or continuously commits breach of partnership agreement, relating to the management of the affairs, of the firm or the conduct of the business, any partner can file a suit for dissolution.

**(e) By transfer of interest :**

**(i)** When one partner has transferred the whole of his interest in the firm to a third party.

**(ii)** allowed his interest to be charged in execution of a decree against him

**(iii)** He has allowed his share to be in recovery of arrears of land revenue. Any other partner can sue for dissolution .

**(f) Business Running at loss :** When the business of the firm can not be carried on except at the loss then the firm can be dissolved. The object of partnership is to earn profit & if it cannot be fulfilled then the firm cannot exist.

**(g) Just & Equitable ground :** When on any other ground the court finds it just & equitable to dissolve a firm, it can order so. E.g. dead lock in the management.

### **Consequences of Dissolution :**

On dissolution, the firm comes to an end. When the firm is dissolved by the order of the court, the dissolution stands from the date of the judgement.

### **Right of a partner of dissolution :**

**(1) To on equitable lien :** line means retain, partner has the right to deal with the goods while in his possession, so he can hold the goods.

**(2)** The authority of each partner to bind the firm & their mutual rights & obligation continue to wind up the affairs of the firm & complete the unfinished transaction.

**(3)** To have the debt of the firm settled, out of the property of the firm.

**(4)** To account for personal profit after dissolution where partnership is dissolved by fraud or misrepresents every partner may retain any other partner from use of the firm name or, property.

### **\* Liabilities :**

**(1)** Until public notice is given partner continue to be liable to third parties.

**(2)** To wind up the affairs of the firm & for complete the unfinished transaction.

**(3)** If any profit is earned after the dissolution it must be shared with the other partner.