

# PARTNERSHIP ACT, 1932

## LAW OF PARTNERSHIP

**Definition:** Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all.

### **Essential Elements of Partnership (Test of Partnership):**

- 1) **Association of Persons:** In order to constitute a partnership, there must be at least two persons because a single person cannot be a partner with himself. The maximum limit of membership is twenty. However in case of partnership of professionals, the maximum limit may exceed twenty.
- 2) **Agreement:** The relation of partnership arises from a agreement and agreement alone and
  - not from status as in the case of the member of a hindu undivided family carrying on a family business
  - not be legal process as in the case of a company
  - not by succession
  - not be inheritance

Such agreement between partners may be expresses or implied. It is called partnership deed if this agreement is in written form. A contract which is the foundation of the partnership must be a valid contract i.e. all the essential elements must be present in it.

- 3) **Business:** A partnership can exist in business and business alone. It includes every trade, occupation and profession. Speaking broadly, it is taken to refer to any activity which is successful would result in profit. Thus a partnership is not for a charitable purpose. Business must be a lawful business.
- 4) **Sharing of Profits:** The word partnership is derived from the phrase “to part” which means to divide. The essential motive in making a partnership agreement is the making of profit. Thus an agreement to share profit is essential but an agreement to share losses is not an essential agreement. No person is a partner unless he has a right to share a profit of a business. But every person who received profits is not necessarily a partner (such as a creditor of the firm). Thus sharing of profit is only a prima facie evidence of existence of partnership.
- 5) **Agency:** The fundamental principle of a partnership is that partners carrying on the business of the firm are agents as well as partners. The question
  - whether a person is a partner or not depends in nearly all cases upon,
  - whether he has the authority to act for those who are admittedly partners, and
  - whether those admittedly partners have the authority to act for him.

### **General / Fundamental / Absolute Duties:**

- 1) **Duty of good faith:** Partnership is a fiduciary relationship. It is the duty of partners to be just and faithful to each other.

- 2) **Duty to work for the greatest common advantage:** It is the duty of the partners to carry on the business of the firm to the greatest common advantage. All the efforts of a partner must be to secure a maximum profit for the firm.
- 3) **Duty to render accounts:** It is the duty of every partner
  - to maintain fair and correct accounts of the firm and
  - to render the accounts to any partner or his legal representative, if and when required by the other.
- 4) **Duty of Disclosure:** It is the duty of every partner to give full information of all the things affecting the business of the firm to his co-partners.
- 5) **Duty to indemnify:** It is the duty of every partner to indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.
- 6) **Duty in case of emergency:** In case of emergency, it is the duty of every partner to do 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 under similar circumstances.
- 7) **Duty to be liable:** It is the duty of every partner to be liable jointly (with all the other partners) and also severally for all acts of the firm done while he is a partner.
- 8) **Duty to act within authority:** It is the duty of every partner to act within the scope of his actual or implied authority.

### **Qualified Duties:**

Subject to contract between the parties:

- 1) **Duty to attend diligently:** Every partner is bound to attend diligently to his duties in the conduct of the business of the firm.
- 2) **Duty to work without remuneration:** It is the duty of the partner to work without receiving remuneration for taking part in the conduct of the business of the firm.
- 3) **Duty to indemnify:** It is the duty of every partner to indemnify the firm for any loss caused to it by his willful neglect in the conduct of the business of the firm.
- 4) **Duty to apply property of the firm:** It is the duty of every partner to hold and use the property of the firm exclusively for the purposes of the business of the firm.
- 5) **Duty to account for personal profits:** It is the duty of every partner not to make any personal profit and if he does it, then he is bound to account for such profits and pay the same to the firm if derived from
  - any transaction of the firm
  - the use of the property of the firm
  - the business connection of the firm
  - the use of the name of the firm

- 6) **Duty not to carry on any business:** It is the duty of every partner not to carry on any business similar to with the business of the firm. If a partner does it, he is bound to pay to the firm all profits made by him in that business.
- 7) **Duty not to compete:** It is the duty of every partner not to carry on any business in competition with that of the business of the firm.
- 8) **Duty not to transfer interest:** It is the duty of every partner not to transfer his right and interest in the firm (without the consent of his co-partners) to an outsider so as to make him a partner in the firm.

### **Rights of Partners:**

Subject to contract between the partners:

- 1) **Right to take part:** It is the right of every partner to take part in the conduct of the business of the firm.
- 2) **Right to be consulted:** It is the right of every partner to be consulted in all matters affecting the business of the firm and to express his opinion before the matter is decided.

Ordinary matters connected with the business of firm may be decided by majority of the partners but fundamental matter may only be decided by unanimous consent of all the partners.

- 3) **Right to have access to the books:** It is the right of every partner to have access to and to inspect and copy any of the books of the firm.
- 4) **Right to share profit equally:** It is the right of every partner to share equally in the profit earned by the firm.
- 5) **Right to interest on capital:** It is the right of every partner to receive interest on the capital subscribed by him.
- 6) **Right to interest on subsequent advances:** It is the right of every partner to receive interest on making for the purpose of the business of the firm) any payment or advances (beyond the amount of capital he has agreed to subscribe) @ 6% per annum.
- 7) **Right to indemnity:** It is the right of every partner to be indemnified in respect of payments made and liabilities incurred by him
  - in the ordinary and proper conduct of the business of the firm, or
  - in an emergency for the purpose of protecting the firm from loss.
- 8) **Right of joint ownership of firm's property:** It is the right of every partner to own the partnership property jointly with his co-partners and to have an equal share in it.
- 9) **Right to retire:** A partner may retire:
  - where it is part of partnership agreement that a partner might retire without seeking the dissolution of the firm.

- Where all the partners consent to his retirement, if there is no such provision in partnership contract.
- Where the partnership is at will by giving notice in writing to all the other partners of his intention to retire.

	<b>Partnership</b>	<b>Joint - Ownership</b>
1) Agreement	Partnership is necessarily the result of an agreement.	Joint ownership may or may not arise from agreement, it may also arise by status.
2) Business	Business is necessary for the existence of partnership.	Joint ownership can exist without it.
3) Share of Profits	Partnership involves community of profit or loss.	Joint ownership not necessarily involves such interest.
4) Transfer of Interest	A partner cannot transfer his share to a stranger without the consent of the other partner.	A joint-owner can transfer interest as such. In such a case, the transferee becomes a substitute for joint-owner who transfers his share.
5) No. of members	In partnership, the number of members cannot exceed the statutory limit.	In a joint ownership, there is no limit on maximum number.
6) Agency	A partner is the agent of his co-partner.	A joint owner is not the agent of the other joint-owner.
7) Partition of Property	A partner cannot sue for the partition of partnership property in specie but he can sue his co-partner for the dissolution of firm and accounts.	A joint owner can sue for the partition of the property.
8) Lien for expenses	A partner has a lien on partnership property for expenses incurred by him on such property on behalf of the firm.	A joint owner has no such lien.

### **Ostensible Partner (Partner by Estoppel / Holding Out)**

**Definition:** Where a person

- holds himself out as a partner or
- allows other to do it

he is then properly estopped from denying the character he has assumed and

- upon the faith of which the creditors may be presumed to have acted.

### **Requirement:**

- 1) **Direct Representation:** The person to be held out must have made the representation (by words written or spoken or by conduct) that he was a partner.
- 2) **Indirect Representation:** Such a person must have knowingly permitted himself to be represented as a partner to the other person.

- 3) **Knowledge of the third party:** The other party must have knowledge of representation and must have acted on the basis of such representation.

### **Applications:**

- 1) **Retiring Partner:** A partner who retires and public notice of retirement is not given remains liable
- for the acts of the firm done after his retirement
  - with the old clients of the firm who have no knowledge of his retirement.
- 2) **A Minor (on attaining majority):** If a minor (who has admitted to the benefit of an existing partnership) after attaining majority
- does in fact act as a partner before giving public notice
  - he will be liable as a partner by estoppel.

### **Exceptions:**

- 1) **Deceased Partner:** The estate of a deceased partner is not liable for any act of the firm done after his death even if the business is continued by the surviving partners in the same style and place and even if his name appears in the name and affairs of the firm. Death is a notice by itself.
- 2) **Insolvent Partner:** Insolvency of a partner also terminated his liability immediately. A person ceases to be a partner of the firm from the date of his insolvency and his estate is no more liable for any act of the firm done after his insolvency whether notice has been given or not.

### **Transfer of Interest:**

#### **Rights of Transferee:**

- 1) **Right to share profit:** He is entitled to receive share of profits as the transferring partner was entitled.
- 2) **Right on the dissolution of firm:** It is only if and when dissolution occurs that transferee would be entitled as against the remaining partners to ask for accounts as from the date of dissolution and to receive his share of the assets of the firm and to which transferring partner was entitled.

#### **Disabilities of Transferee:**

- 1) No status of a partner
- 2) Disability to interfere in the conduct of the business of the firm.
- 3) Disability to require accounts
- 4) Disability to inspect the books of the firm
- 5) Disability to challenge the accounts of profit agreed to by the partners.
- 6) Disability to sue for dissolution of the firm.

## **Implied Authority of a Partner (Mode of doing act to bind firm):**

The act of a partner done by him:

- as an agent of the firm
- in the course of the business of the firm
- - in the name of the firm, or  
- in any other manner expressing an intention to bind the firm

**is an act of the firm.** This is known as implied authority of the partner.

### **Restriction on the implied authority of a partner:**

**A) Statutory Restriction:** In the absence to any usage or custom of the trade to the contrary, the implied authority of a partner does not empower him to do the following:

- 1. Arbitration:** He cannot submit a dispute relating to business of firm to arbitration.
- 2. Bank Account:** He cannot open a bank account on behalf of the firm in his own name.
- 3. Composition:** He cannot compromise or relinquish any claim by the firm.
- 4. Withdraw of suit:** He cannot withdraw a suit or proceeding filed on behalf of the firm.
- 5. Admission:** He cannot admit any liability in a suit or proceeding against the firm.
- 6. Acquire Immovable property:** He cannot acquire immovable property (by way of purchase mortgage or lease) on behalf of the firm.
- 7. Transfer of Immovable property:** He cannot transfer (by way of sale, mortgage or lease) immovable property belonging to the firm.
- 8. Partnership:** He cannot enter in to partnership on behalf of the firm.

**Effects:** Statutory restriction are effective against whole world whether a particular person dealing with firm has knowledge of them or not.

**B) Restriction by Partnership Deed:** Restriction on the implied authority of partner may be imposed by partnership contract.

**Effects:** These restrictions are effective against only those dealing with the firm has knowledge of the restriction.

**Admission of Minors to the benefits of partnership:** Partnership is a relation resulting from a contract and a minor agreement is altogether void. Accordingly, a minor being incompetent to enter into contract cannot become a partner nor a partnership can be created with a minor as a partner. But a minor may be admitted to the benefit of:

### **Requirements:**

- existing partnership firm
- consent of all the partners

However even after such admission, he does not become one of the group of persons called a firm. When a minor is admitted to the behalf of a firm, he has some rights and liabilities.

### **1) Position of a Minor before attaining majority:**

#### **A) Rights:**

- 1) Right to share profits and property of the firm.
- 2) Right to have access to accounts of the firm.
- 3) Right not to be adjudged insolvent of the debt of the firm.

**B) Liabilities:**

- 1) He is not personally liable for any debt of the firm.
- 2) His share is liable for any act of the firm.

**C) Disabilities:**

- 1) No status of a partner.
- 2) Not entitled to have access to the books of the firm other than accounts.
- 3) No suit against partners for profits and property except when he severs his connection with the firm. Moreover, such a suit by a minor does not dissolve the firm.

**2) Position of a Minor on attaining Majority:** At any time within six months:

- on his attaining majority, or
- of his obtaining knowledge that he had been admitted to the benefits of the partnership, (whichever date is later)

Such person make a public notice whether he is elected or not to become a partner in the firm. if he fails to give such notice, he shall become a partner on the expiry of six months.

**A) Where such person elects to become a partner:**

- His share in the property and profits of the firm shall be shared to which he was be entitled as a minor.
- He becomes personally liable to third person for all acts of the firm done since he was admitted to the benefits of the partnership.

**B) Where such person elects not to become a partner:**

- His rights and liabilities shall continue to be those of the minor upto the date of public notice.
- His share shall not be liable for any act of the firm done after the date of the notice.
- He shall be entitled to sue the partners for his share of the property of profits.

	<b>Partnership</b>	<b>Company</b>
<b>Regulating Act</b>	A partnership firm is governed by the provision of the Partnership Act, 1932	A company is governed by the provision of the Companies Act, 1956.
<b>Number of Members</b>	The maximum number of members in the case of the partnership is 20 for any business.	No such maximum limit is fixed in the case of the public company.
<b>Entity</b>	A partnership firm has no separate legal entity distinct from the members composing it.	A company is a separate legal entity different from its members.

<b>Liability</b>	Here, each partner has unlimited liability and is personally liable for all the debts of the firm.	Here, a shareholder has a limited liability to the extent of the amount guaranteed by him to be his contribution in case the company is wound up.
<b>Management</b>	All the partners of the firm are entitled to take part in the management of the business of the firm.	Here, the right and control and management of the business is vested in the Board of Directors elected by the shareholders
<b>Registration</b>	A partnership firm may or may not be registered	A company registration is essential.
<b>Authority of Members</b>	In partnership each partner has an implied authority to bind his co-partner by act done within the ordinary course of the business.	In a company, there being no mutual agency between various shareholders.
<b>Transfer of Interest</b>	A partner cannot transfer his interest in the firm without the consent of his co-partner.	In case of the public company, a shareholder can transfer his shares freely without restriction. However in private companies permission of Board of Director is required.
<b>Audit</b>	The audit of the accounts of the firm is not as such a legal necessity except in special circumstances.	The audit of the accounts of the company is legal necessity.
<b>Winding Up</b>	It can be wound up at any time by any partner, if it "at will" without legal formalities.	Here no one member can require it to be wound up at will and winding up involves legal formalities.

### **Reconstitution of Firm (Incoming and Outgoing Partners) (Dissolution of Partnership):**

Introduction of a Partner	Incoming Partner
Retirement of a Partner	Outgoing Partner
Expulsion of a Partner	Outgoing Partner
Insolvency of a Partner	Outgoing Partner
Death of a Partner	

**Definition:** Reconstitution of a firm means a readjusted in the firm is the collection of partners. It has no independent legal existent. If there is a change in the numbers and status of partner, the firm is said to be reconstituted (whenever there is change in the constitution, there is necessarily a change in the partnership relation but the firm continues as a new firm or a reconstituted firm.

#### **Introduction of Partner**

A new partner may be admitted into an existing firm with the mutual consent of all the partners but even by agreement, a minor cannot be made a partner.



**Liabilities:**

- 1) The liability of an incoming partner commences from the date of his admission into the firm.
- 2) An incoming partner may be liable for the past liabilities if:
  - the new firm assumes the liability of the old partner
  - the creditors accept the new firm as their debtors to discharge the old firm from its liabilities.

**Retirement of a Partner**

The word retire is confined to cases where a partner withdraws from a firm and the remaining partners continue to carry on the business of the firm, without dissolution of partnership with them.

**Modes of Retirement:**

- 1) Partnership agreement
- 2) Consent of all partners
- 3) By Notice (Partnership-at-will)

**Liabilities of Retired Partner:**

- 1) **Liability for acts done before retirement:** A retiring partner may continue to be liable to third persons for
  - the acts of the firm done before his retirement,
  - transactions of the firm begun but unfinished at the time of his retirement.A retired partner will be discharged of his past liability by a tripartite agreement between the retired partners, the survival partners and the third persons.
- 2) **Liability for acts done after retirement:** A retired partner may be liable for the debts incurred by the firm after his retirement (until public notice is given) on the principle of holding out.

**Rights of Retired Partner:**

- 1) **Rights to carry on completing business:** A retired partner may carry on a business completing with that of the firm and he may advertise such business. In the absence of any special contract, following restrictions are imposed on him:
  - a) He cannot use the name of the firm, he cannot use the name similar to that of firm so as to mislead the public to believe that it is the old business.
  - b) He cannot represent himself as carrying on the business of the firm.
  - c) He cannot solicit the custom of person who are dealing with the firm, before he ceased to be a partner. Since, the restriction in the respect of the customer prior to his retirement, it will not apply in respect of the customer who was subsequent to his retirement.

Agreement in restrained of trade: If there is a clause in the partnership contract, then a retired partner cannot carry on any business similar to that of the firm within a specified period or within specified local limits provided the restrictions are reasonable.

- 2) **Right to share subsequent profits:** If there is no final settlement, the retiring partner is entitled either,
  - to claim interest 6% per annum on the amount of his share in the property of the firm, or
  - to share profits earned by the firm after retirement as may be attributable to the use of his share of property of the firm

## **Expulsion of Partner**

### **Requirements:**

A partner cannot be expelled from a firm except:

- 1) if it is permissible under the partnership contract
- 2) if decided by the majority of the partners
- 3) if the power is exercised in good faith

An expelled partner stands on the same footing as that of a retired partner as far as his rights and liabilities are concerned.

## **Insolvency of a Partner**

The consequences resulting from the insolvency of the partners are:

- 1) The partner adjudicate as insolvent ceases to be a partner
- 2) He cease to be a partner on the date on which the order of adjudication is made.
- 3) The state of the insolvent is not liable for any act of the firm done after the date of the order of adjudication.
- 4) The firm cannot be held liable for any act of insolvent done after the date of adjudication.
- 5) As far as his position after expulsion is concerned, he stands on the same footing as that of a retired partner.

## **Death of a Partner**

The estate of a deceased partner is not liable for any act of the firm done after his death.

**Dissolution of the Firm:** The dissolution of partnership between all the partners of a firm is called the dissolution of the firm.

### **Modes of Dissolution:**

#### **A) Dissolution without the intervention of the Court:**

- 1) **Dissolution by Agreement:** A firm may be dissolved with
  - the consent of all the partners or
  - in accordance with a contract between the partners
- 2) **Compulsory dissolution:** A firm is dissolved:
  - a) **Insolvency:** by the insolvency of all the partners or of all the partners except one.
  - b) **Subsequent Illegality:** 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. However 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 undertaking.
- 3) **Contingencies:** Subject to the contract between the parties:
  - a) **Expiry of Term:** if constituted by a fixed term by the expiry of that term.

- b) **Completion of business:** if constituted to carry out one or more adventures or undertakings, by their completion.
  - c) **Death:** by the death of a partner
  - d) **Insolvency:** by the adjudication of the partner as an insolvent
- 4) **By Notice:**
- a) Where the partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partner of his intention to dissolve the firm.
  - b) The firm is dissolved as from the date mentioned in the notice of the date of dissolution or of (if no time so mentioned) as from the date of the communication of the notice.
- B) By the Order of the Court:** Dissolution of a firm by the court is necessitated when there is a difference of opinions between the partners regarding the dissolution of the firm. At the suit of a partner disagreed the court may dissolve a firm on any of the following ground:
- 1) **Insanity:** When a partner becomes insane. It permits not only any of the partners but also the next friend of the insane partner to file the suit for the dissolution of the firm.
  - 2) **Permanent Incapacity:** When the partner other than the partner suing becomes permanently incapable from performing his duties as the partner.
  - 3) **Misconduct:** When the partner other than the partner suing, is guilty of misconduct, which is likely to affect prejudicially the carrying on of the business of the firm.
  - 4) **Persistent breaches:** When the partner other than the partner suing, commits frequently breaches of the partnership agreement or otherwise so conducts himself in matters relating to business that other partner finds it impossible to carry on the business in partnership with him.
  - 5) **Transfer of Interest:** When the partner other than the partner suing, has transferred the whole of his interest in the firm to a third party or has allowed his share to be sold in execution of a decree.
  - 6) **Perpetual Loss:** that the business of the firm cannot be carried on except at loss
  - 7) **Just and Equitable:** When on any other ground which renders a just and equitable that the firm should be dissolved.

### **Public Notice**

**When to give public notice:** A public notice has to be given:

- on retirement of a partner

- on expulsion of a partner
- on attaining majority by a minor
- on dissolution of the firm

**How to give public notice:** The notice relating to the above matter is given:

- by notice to the registrar of the firm
- by publication in official gazette
- by publication in at least one vernacular newspaper circulating in the district where the firm to which it relates has its place or principal place of business.

In case of a registered firm. However in case of non-registered firm notice to the registrar of firm is out of question.