UNIT 7 : THE INDIAN PARTNERSHIP ACT, 1932

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7.1 LEARNING OBJECTIVES

After going through this unit, you will able to :

- understand the meaning of partnership,
- discuss the essential characteristics of a partnership,
- know how a partnership is formed,
- distinguished between partnership and other forms of organisations,
- know about various rights and duties of a partner,
- know how a partnership is dissolved.

7.2 INTRODUCTION

You are aware of the fact that one of the form in which business can be carried out is partnership. In India partnership forms of business is widespread. Partnership business in India is governed by the Indian Partnership Act, 1932, which came in to effect from 1st October, 1932, Except Section 69 relating to registration of firm which came in to force on 1st October, 1933. This Act repeals Sec. 239 to Sec. 266 of the existing Contract Act. The Act extends to the whole of India except the state of Jammu & Kashmir.

In this chapter we will discuss about various provisions of partnership Act. Which deal with formation of partnership, rights and liabilities of parterner, dissolution of partnership etc.

7.3 DEFINITION UNDER THE ACT

In the Act, unless there is anything repugnant in the subject or context,

a) an “act of a firm” means any act or omission by all the partners, or by any partner or agent of the firm which gives rise to a right enforceable by or against the firm;

b) “business” includes every trade, occupation and profession;

c) “prescribed” means prescribed by rules made under this Act; (c-1) “Registrar” means the Registrar of Firms appointed under sub-section (1) of section 57 and includes the Deputy Registrar of Firms and Assistant Registrar of Firms appointed under sub-section (2) of

that section;

d) "third party" used in relation to a firm or to a partner therein means any person who is not a partner in the firm.

7.4 DEFINITION OF "PARTNERSHIP", "PARTNER", "FIRM" AND "FIRM-NAME" (Sec-4)

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

A partnership firm has no separate legal entity distinct from its members. Hence, unlike a company which has a separate legal entity distinct from its member, a partnership firm cannot posses property. While selecting the name of the firm the partners need to keep in mind the following points :

1) The name must not be too identical to the name of another existing firm doing similar business.
2) The name must not contain words like King, Queen, Crown, Emperor, Empress, Empire, Imperial, Royal or words expressing or implying, the sanction, approval or patronage of government except when the state government signifies its consent to the use of such words as part of the firm name by order in writing.

7.5 ESSENTIAL CHARACTERISTICS OF PARTNERSHIP

After having understood the meaning of the term partnership as defined in section 4 of the Act, let us discuss the essential characteristic of a partnership, which are discussed as under :

A) Agreement : Partnership is the outcome of an agreement or contract between persons. The relation of partnership arises from the formation of a contract and not from status or birth. The agreement may be oral or in writing but it must satisfy all the essentials of a

valid contract. If a proprietor gives a share in profits to his employee it will not be called a partnership unless there is an agreement of partnership between the two.

B) **Association of two or more Persons :** To form a partnership there must be at least two persons. According to Sec 11 of the Indian Partnership Act, 1932, the maximum number of persons in a partnership should not exceed 10 in case of banking business and 20 in other types of business. If the number of partners exceeds the prescribed limit, it would become an illegal association of persons. A firm cannot become a partner of another firm though its partners can join any other firm as partners.

C) **Carrying on of Business :** A partnership can be formed only for the purpose of carrying on a business. An association of persons who jointly own a house without carrying on a business is not partnership. Moreover, the business carried on by the partners must be lawful. Illegal acts such as theft, dacoity, smuggling, etc., cannot be called partnership. Associations created for charitable, religious or social purpose are not regarded as partnership because such organisations are not associated with business. It may also be noted that an agreement to carry on business at a future time does not result in partnership unless that time arrives and the business is started. [R R Same, vs. Heuberr] Another point which is worth noting is whether business should be temporary or permanent. So long there is a valid agreement to carry on legal business there exist a partnership. An agreement for Partnership can be for a specified period, specified project or for an undefined period or purpose.

Example : Two brothers were living together with their father. The father who was a proprietor of a business dies. The sons inherited the business but does not become partners automatically after death of their father unless there is an agreement between them expressed or implied to carry on the business as partners.

D) **Sharing of Profits :** The agreement between the partners must be

to share the profits of business. There can be no partnership without the intention of mutual gain. The profits must be distributed among the partners in an agreed ratio. The section does not insist upon loss sharing. Thus a, provision for loss sharing is not essential [Walker West Development vs. FJ Emmett (1978)252EG1171] However, sharing of profits is not a conclusive proof of partnership. For example, a manager may be given a share in profits of the firm, it does not mean that the manager is a partner of the firm.

E) Mutual Agency : Partnership business can be carried on by all the partners or by any of them acting on behalf of the others. In other words, every partner is an implied agent of the other partners and of the firm. Each partner is liable for acts performed by other partners on behalf of the firm. The use of the words 'carried on by all or any of them acting for all' in Sec 4 clearly emphasizes the agency relationship. The partners are agent for each other and principals for themselves. Their relationship is governed by the law of agency. The partners are largely regulated by the law of Principal and agent. The above mentioned features are the real tests of partnership.

F) Utmost Good Faith : The relations between partners are based upon mutual trust and confidence. Every partner is expected to act in the best interests of other partners and of the firm as a whole. He must observe utmost good faith in all the dealings with his co-partners. He must render true accounts and make no secret profits from the business. The concept of utmost good faith is stressed in section 9 of the Partnership Act which lays down general duties of a partner. Section 9 lays down that partners are bound to carry on the business of the firm to the greatest 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 representatives. This we will be discussing in subsequent section dealing with right and duties of partners.

G) Unlimited Liability : Every partner is jointly and severally liable to an unlimited extent for the debts of the partnership firm. In case the

assets of the firm are insufficient to pay the debts in full, the personal property of each partner can be used to pay the creditors of the firm.

H) **Restriction on Transfer of Interest :** No partner can transfer his share in the partnership without the prior consent of all other partners. As per Section 29 a partner cannot assign his rights and interest in the firm to an outsider so as to make him the partners of the firm. He can however, assign his share in the profits and share in the assets of the firm. But the transferee will not be entitled to take part in the business of the firm, but in the share of profit only.



CHECK YOUR PROGRESS

Q.1 : Mention four Characteristics of Partnership.

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7.6 REGISTRATION OF A PARTNERSHIP FIRM

According to the Partnership Act, 1932 it is not legally compulsory to register the firm for its formation. But if the registration is not done then there may arise some difficulties. So, it is always useful to get the firm registered. The Partnership Act, 1932 provides that if the partners so desire, may register their firm with the "Registrar of Firms" of the state in which the partnership firm is situated.

In order to get itself registered, a partnership firm must submit an application in a prescribed form along with the prescribed fee to the "Registrar of Firms". The application must contain the following details:

- Name of the firm
- The head office of the business
- Names of the other places where the firm has business
- Full names and addresses of the partners

- Date of entry of the partners in the firm
- Period of the firm, if any
- Signatures of every partner or his representatives.

When the Registrar of the Firm, after scrutiny, is satisfied with the statements, he shall make entry of the firm in the register of firms and the firm gets registered and certificate which is called "Certificate of Registration" which is issued by the Registrar. After getting the certificate, the firm becomes a registered firm.

7.6.1 Penalty for Furnishing False Particulars (Section 70)

Any person who signs any statement, amending statement, notice or intimation under this Chapter containing any particular which he knows to be false or does not believe to be true or containing particulars which he knows to be incomplete or does not believe to be complete, shall be punishable with imprisonment which may extend to three months, or with a fine or with both.

7.6.2 Alterations

Any alterations, subsequent to Registration shall be notified to the registrar.

- **Change in firm name and principal place of business (Section 60)** shall require sending of a new application form to the registrar along with the prescribed fee, duly signed and verified by all the partners.
- **Change relating to opening and closing of branches. (Section 61) :** When a registered firm discontinues business at any place or begins to carry on business at any place, such place not being its principal place of business, any partner or agent of the firm may send intimation thereof to the Registrar.
- **Change in the name and permanent address of any partner (Section 62) :** When any partner in a registered firm alters his name or permanent address, an intimation of the alteration may

be sent by any partner or agent of the firm to the Registrar

- Under Section 63(2), when a minor who has been admitted to the benefits of partnership in a firm attains majority and elects to become or not to become a partner, he or his agent specially authorized in this behalf, may give notice to the Registrar that he has or has not become a partner.

7.6.3 Effect of Non-Registration (Section 69)

Through registration of partnership firm in not necessery. But a non registered. firm canont avail some fecility. These are discuss bellow:

- A partner of an unregistered firm cannot file a suit in any court against the firm or other partners for the enforcement of any right arising from a contract or right conferred by the Partnership Act unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.
- No suits to enforce a right arising from a contract shall be instituted in any Court by or on behalf of a firm against any third party unless the firm is registered and the persons suing are or have been shown in the Register of Firms as partners in the firm.
- An unregistered firm or any of its partners cannot claim a set off (i.e. mutual adjustment of debts owned by the disputant parties to one another) or other proceedings in a dispute with a third party. Hence, every firm finds it advisable to get itself registered sooner or later. However, non-registration of a Partnership firm shall not affect.
  - The rights of third parties to sue the firm and/or its partners.
  - The firms or partners in the firms which have no place of business in the territories to which this Act extends, or whose places of business in the said territories are situated in areas to which the act does not apply.
  - The enforcement of any right to sue for the dissolution of a firm or for accounts of a dissolved firm, or any right or power

to realise the property of a dissolved firm.

- The powers of an official assignee, receiver or Court under the Presidency-towns Insolvency Act, 1909 (3 of 1909), or the Provincial Insolvency Act, 1920 (5 of 1920), to realise the property of an insolvent partner.

7.7 PARTNERSHIP AND OTHER ASSOCIATIONS

7.7.1 Distinction Between Partnership and HUF

Partnership and Hindu Undivided Family (HUF) : In Hindu Undivided Family business all members of an Undivided Hindu family are engaged in the business. The business is manage and controlled by the eldest male member of the family. Following are

Point of	Partnership	HUF
Differences Regulation	Partnership business is governed by the provisions of the Indian Partnership Act, 1932	A Joint Hindu Family business is governed by the principles of Hindu law (Succession) Act, 1956.
Mode of creation	A partnership arises out of a contract between the partners.	A Joint Hindu Family business arises by the operation of law and is not the result of a contract.
Admission of new members	For admission of a new partner in a partnership consent of all the existing partners is required,	In the case of a Joint Hindu Family business a new member is admitted just by birth.
The position of females	In a partnership women can be full-fledged partners.	While in a Joint Hindu Family business membership is restricted to male members only.

Number of members	In partnership the maximum number of partners is 10 for banking business and 20 for other business.	There is no such maximum limit of members in the case of joint Hindu family business.
Liability of members	In partnership, the liability of the partners is joint and unlimited. Each partner is personally and jointly liable to an unlimited extent and in case the partnership fail to pay its debts each partner's separate personal property is liable for the debts of the firm.	In a joint Hindu family business only the 'Karta' is personally liable to an unlimited extent. Other coparceners' liability is limited to the extent of their interest in the joint family property and they do not incur any personal liability.
Share in profits	In a partnership business each partner is entitled to claim his separate share of profits.	A member of a joint Hindu family business has no such right.
Effect of death of a member	A partnership business is dissolved on the death of a partner.	A joint Hindu family firm is not dissolved on the death of a coparcener.

7.7.2 Distinction Between Company and Partnership :

Company	Partnership
i) A Company is treated as an artificial legal person.	Partnership is not a legal person.
ii) Company has perpetual succession.	Partnership firm does not have perpetual succession.

Company	Partnership
iii) Registration of a Company under Companies Act is mandatory.	For a partnership firm registration is not compulsory. It is guided by Indian Contract Act and Partnership Act.
iv) A Private Limited Company shall have at least 2 members and maximum 50 members. Public Ltd Company shall have minimum 7 members and there is no maximum limit.	Partnership firm shall have at least 2 members and maximum 20 members and for banking business, maximum 10 members.
v) Shares of a company can be transferred with ease.	Partners can transfer his share but the assignee does not become a partner. He is only entitled to share of Profits.
vi) Liability of a member is limited by shares or guaranty.	Liability of partners is unlimited.
vii) Ordinary members cannot take part in management of a company. Only director members can take part in management	All Partners can take part in management of a firm.
viii) Private limited company shall have a minimum paid up capital of Rupees One Lakh and public limited company of Rupees Five Lakh.	There is no minimum paid up capital for a partnership firm.
ix) Member cannot bind the company by his act.	Partner is an agent of firm and other partners.Partner can bind the firm by his act.



CHECK YOUR PROGRESS

Q2 : Write two differences between partnership and company.

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7.8 TYPES OF PARTNERSHIP

Various types of partnership can be classified on the basis of duration of partnership and liability of partners. They are :

7.8.1 On the Basis of Duration

- **Partnership at Will :** When a partnership is formed which is not for a specific period of time or for a particular project but for an indefinite period of time such partnership is termed as partnership at will. Continuity of such partnership depends on the will of the partners. It may be dissolved, if any partner gives notice of withdrawing from the partnership.
- **Particular Partnership :** When a partnership is formed to complete a particular venture, trade or project, such partnership is called particular partnership. As soon as the objective of forming the partnership is achived the partnership comes to an end. For example, if a partnership is formed to construct a bridge, it will be the case of a particular partnership and it will come to an end as soon as the construction of the bridge is completed.

7.8.2 On the Basis of Liability of Partners

- **General Partnership :** In a general partnership, partners have

unlimited liability and they enjoy the right to participate in the management of the firm. Partners are bound together with mutual agency. Withdrawal of any partner from the partnership due to death, lunacy or any other reason leads to dissolution of the firm.

- **Limited Partnership :** In a partnership where all the partners except one, have their liability limited to the capital invested by them such partnership is known as limited liability partnership. A limited partner has no right to participate in the management of the firm. Death, lunacy or insolvency of a limited partner has no effect on the existence of the partnership firm.

7.9 TYPES OF PARTNERS

There are various types of partners in a partnership firm. They are as follows :

a) **Active Partner :** An active partner is one who not only contributes capital in the firm but also takes active part in management and day to day functioning of the firm. He may also be called 'actual' or 'ostensible' partner. He is an agent of the other partners in the ordinary course of business of the firm and considered as a full fledged partner in the real sense of the term. His liability is unlimited for all the debts of the firm.

b) **Nominal Partner :** A nominal partner neither contributes any capital nor shares in the profits or take part the management of the firm. He only allows the firm to use his name and the firm take advantage of the goodwill of that person. Though he is not given any right in the firm but he is liable to the third parties for all the liabilities of the partnership.

c) **Sleeping or Dormant Partner :** A sleeping or dormant partner does not take any active part in the management of the business. He contributes capital and shares the profits which are usually less than that of the active partners. A sleeping partner has unlimited liability for the debt of the firm but his relationship with the firm is not disclosed to the general public.

d) **Partner in Profits only :** A partner who shares in the profits only without being liable for the losses is known as partner in profits. He does not take part in the management of the firm but his liability for all the debts of the firm is unlimited.

e) **Secret Partner :** Partners who contributes capital and actively participate in the activity of the firm but his association with the firm is not disclosed to the public such partners are known as secret partner. His liability for all the debts of the firm is unlimited.

f) **Partner by Estoppel :** When a person falsely represents himself as a partner or acts in such a way that others have on impression that he is a partner of the partnership firm, such a person is called partner by estoppel. The third parties who deal with such a partner and suffers loss, can held the partner by estoppel liable for the less. For example : A and B are partners in a pertnership firm and if C (an outsider) represents himself as a partner of the firm and transacts with X (third party) and if X suffers loss, he can held C liable for such loss.

g) **Partner by Holding out :** If the partners of a partnership firm declares another person as a partner of the firm and the person remains silent, such a partner is called partner by holding out. Any third party transacting with the firm on the pritext that the partner by holding out is a real partner of the firm, the third party can held the partner by holding out liable for any loss. For example : A and B are partners in a partnership firm and declares C as a paertner and C remains silent, C is called the partner by holding out.

h) **Minor Partner :** A partner is called a minor partner if his age is less than 18 years. Partnership arises from contract and a minor is not competent to enter into contract. Therefore, strictly speaking, a minor cannot be full-fledged partners. But with the consent of all the partners he can be admitted into partnership for benefits only. He is not personally liable for the debts of the firm, his liability is limited only to the amount he has invested in the firm as capital. He has no right to buy or sell goods or sign any contract with any other party on behalf of the firm. During minority a minor has right to receive agreed share

of profit, right to have access and copy of the account of the firm. Section 30 lays down the rights and liabilities of a minor who has been admitted in the partnership which are:

1) The minor is entitled to receive his agreed share of the property and of the profits of the firm.
2) The minor has the right to inspect and take copies of the books of accounts of the firm. However, he has no such right in respect of books other than accounts.
3) The minor is not personally liable to the third parties for the debts of the firm, but his liability is limited only up to his share in the partnership assets and profit. If the assets of partnership fall short in discharging the debts of the firm the personal property of the minor cannot be applied for payment of the firm debt.
4) The minor is not entitled to take part in conduct of the business as he has no representative capacity to bind the firm.
5) The minor cannot bring about any suit against the partners for an account or payment of his share of the property or profits of the firm except when he severs his connection with the firm.
6) On attaining majority, if he continues as a partner, his liability will become unlimited with effect from the date of his original admission into the firm and he will be having all the rights which are available to a normal partner. For this, he has to give his consent or public notice or declaration that he wants to continue in the firm as a partner. If he does not give his consent it will be assumed that he wants to continue as a partner and in that case his liability will be unlimited.
7) Where the minor does not become a partner:
   i) His rights and liabilities continue to be those of a minor up to the date of his giving public notice;
   ii) After the date of the public notice his share is not liable for any acts of the firm;
   iii) He can sue the other partners for his share of the property and profit in the firm;

8) After attaining majority but before choosing to become a partner If, the minor represents or knowingly permits himself to be represented as a partner in the firm, he will be personally liable to anyone who has on the faith of such representation granted credit to the firm on the ground of 'holding out'.



CHECK YOUR PROGRESS

Q.3 : Who is a sleeping partner?

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7.10 RIGHTS AND DUTIES OF PARTNERS: MUTUAL RIGHTS AND DUTIES

"Subject to the provisions of this Act, the mutual rights and duties of the partners of a firm may be determined by contract between the partners, and such contract may be express or may be implied by a course of dealing.

Rights of Partners : The Partnership Act confers the following rights upon the partners of a firm:

1) **Right to take part in the conduct of the business** [Sec. 12 (a)]. Every partner, irrespective of the amount of capital contribution, has an inherent right to take part in the conduct of the business of the firm. Although one may not to participate in the management of the business.
2) **Right to express opinion** [Sec. 12 (c)]. Every partner has a right to be consulted and heard before any matter is decided. Any difference arising as to ordinary matters connected with the business may be decided by a majority of the partners. But no change may be made in the nature of the business or the constitution of the partnership, e.g., admission of a new partner, without the consent of all the partners.
3) **Right of access to books** [Sec. 12(d)]. Every partner has a right to have access to and to inspect and copy any of the books of the firm.

4) **Right to share the profits** [Sec. 13(b)]. Every partner, irrespective of the amount of capital contribution or business expertise, has a right to share equally in the profits earned by the firm.
5) **Right to interest on capital** [Sec. 13(c)]. Where a partner is entitle to interest on capital subscribed by him, such interest shall be payable only out of profits.
6) **Right to interest on advances** [Sec. 13(d)]. Where a partner makes, for the purpose of the business, any payment or advance beyond the amount of capital he has agreed to subscribe, he is entitled to interest thereon at the rate of six per cent per annum.
7) **Right to indemnity** [Sec. 13(e)]. Every partner has a right to claim indemnity from the firm in respect of payments made or liabilities incurred by him (a) in the ordinary and proper conduct of the business, and (b) in doing such act, in an 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.

Duties of Partners : For the sake of clarity we shall be studying the duties of partners inter se under the following two heads: ‘

I) Absolute duties.
II) Qualified duties.

I) Absolute Duties : These duties are mandatory in nature imposed by law and are not subject to a contract to the contrary. Being mandatory in nature, these duties are applicable to all partnership and cannot be varied by agreement among the partners. The following are the absolute duties of partners:

1) *Duty to carry on the business to the greatest common advantage* (Sec. 9). Every partner is bound to carry on the business of the firm to the greatest common advantage. It implies that every partner must use his knowledge and skill for the benefit of the firm and not for his personal gain.
2) *Duty to be just and faithful inter-se* (Sec. 9). An ideal partnership is one where there is mutual trust and confidence, and spirit of helpfulness and goodwill among the partners. As such every partner must be just and faithful to his co-partners.

3) *Duty to render true accounts* (Sec. 9). Every partner must render true and proper accounts to his co-partners. It implies that each partner must be ready to explain the accounts of the firm and produce vouchers in support of the entries. No partner should think of making a secret profit at the expense of the firm.

4) *Duty to provide full information* (Sec. 9). Every partner must give full information of all things affecting the firm to his co-partners.

5) *Duty to indemnify for loss caused by fraud* (Sec. 10). A partner can cause loss to the firm by hi's neglect or want of skill or omission or fraud while acting in the ordinary course of business. The general practice is that where a partner acts bona fide the loss caused by his neglect or want of skill or omission is borne by the firm. But when the loss is caused by fraud committed against a third party by a partner, the same must be recovered from the guilty partner and cannot be shared among all the partners.

6) *Duty to be liable jointly and severally* (Sec. 25). Every partner is liable, jointly with all other partners and also severally, to third parties for all acts of the firm done while he is a partner. The liability of all the partners is not only joint and several but is also unlimited.

7) *Duty not to assign his interest* (Sec. 29). No partner can assign or transfer his partnership interest to any other person so as to make him a partner in the business without the consent of all other partners. He can, however, assign his share of the profit and his share in the assets of the firm but the transferee shall not have any right to interfere in the conduct of the business.

II) **Qualified Duties :** Qualified duties are those which depend upon the contract between the paartners and it is only in the absence of a contract to the contrary that these duties, as laid down by the Partnership Act, are applicable. In other words, the partners are free to vary these duties by mutual agreement, express or implied, and if the partnership agreement is silent then only the duties contained in

the Partnership Act will be the duties of the partners. Subject to contract between the partners, the Partnership Act prescribes the following duties of partners :

1) *Duty to attend diligently to his duties* [Sec. 12(b)]. Every partner is bound to attend diligently to his duties in the conduct of the business.
2) *Duty to work without remuneration* [Sec. 13(a)]. A partner is not entitled to receive remuneration for taking part in the conduct of the business.
3) *Duty to contribute to the losses* [Sec. 13(b)]. The partners are bound to contribute equally to the losses sustained by the firm, irrespective of the amount of capital contribution by each one of them.
4) *Duty to indemnify for willful neglect* [Sec. 13(/)]. Every partner is under a duty to indemnify the firm for any loss caused to it by his wilful neglect in the conduct of the business of the firm. The expression 'wilful neglect' means the failure to perform a duty, or to do something which a partner ought to have done, intentionally and deliberately. An act done in good faith and bona fide or a mere error of judgment cannot be termed as wilful neglect.
5) *Duty to use firm 's property exclusively for the firm* (Sec. 15). It is the duty of every partner to use the property of the firm exclusively for the purposes of the business. No partner should use property of the firm for his personal benefit.
6) *Duty to account for personal profits derived* [Sec. 16(a)]. If a partner derives any profit for himself from any transaction of the firm or from the use of the property or business connection of the firm or the firm name, he must account for that profit and pay it back to the firm.
7) *Duty not to compete with the business of the firm* [Sec. 16(b)]. A partner must not carry on any business which is similar to or likely to compete with the business of the firm. If he does that,

he is bound to account for and pay to the firm all profits made by him in that business. A partner may, however, carry on a non-competing business and may retain the profits of that business to himself.



CHECK YOUR PROGRESS

Q.4 : Mention two rights of a partner.

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Q.5 : Mention two duties of a partner.

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7.11 LIABILITIES OF A PARTNER / PARTNERSHIP TO THIRD PARTIES

i) **Liability of a Partner for Acts of the Firm (Sec. 25) :** Every partner is liable, jointly and severally with all other partners for all acts of the firm done while he is a partner. Further, the liability of all the partners is unlimited. Because of this liability, the creditor of the firm can sue all the partners jointly or individually.

ii) **Liability of the Firm for Wrongful Act of a Partner (Sec. 26) :** If any loss or injury is caused to any third party or any penalty is imposed because of wrongful act or omission of a partner, the firm is liable to the same extent as the partner. However, the partner must act in the ordinary course of business of the firm or with authority of his partners.

iii) **Liability of the Firm for Misutilisation by Partners (Sec. 27) :** Where (a) a partner acting within his apparent authority receives money or property from a third party and misutilises it, or (b) a firm receives money or property from a third party in the course of its business and any of the partners misutilises such money or property, then the firm is liable to make good the loss.

iv) **Liability of an Incoming Partner :** An incoming partner is liable for the debts and acts of the firm from the date of his admission into the firm. However, the incoming partner may agree to be liable for debts prior to his admission. Such agreeing will not empower the prior creditor to sue the incoming partner. He will be liable only to the other co-partners.

v) **Liability of a Retiring Partner :** A retiring partner is liable for the acts of the firm done before his retirement. But a retiring partner may not be liable for the debts incurred before his retirement if an agreement is reached between the third parties and the remaining partners of the firm discharging the retiring partner from all liabilities. After retirement the retiring partner shall be liable unless a public notice of his retirement is given. No such notice is required in case of retirement of a sleeping or dormant partner.

7.12 DISSOLUTION OF PARTNERSHIP AND DISSOLUTION OF FIRM

7.12.1 Dissolution of Partnership

Dissolution of partnership refers to the change in the existing relations of the partners. The firm continues its business after being reconstituted. This may happen on admission, retirement or death of a partner or change in profit sharing ratio in the firm. Example:

L, M and N are three partners in a firm. M retires. The partnership between L M N comes to an end and new partnership between M and N comes into existence. This new partnership between M and N shall be known as reconstituted firm'. Thus, on retirement of partner, the old partnership stands dissolved but the firm continues its business with remaining partners M and N. This is a case of dissolution of partnership.

Partnership may be dissolved in the following circumstances :

a) At the time of admission of a new partner;

b) On the retirement/death of an old partner;

c) At the time of change in profit sharing ratio among existing partners;
d) If any partner is declared insolvent;
e) On the expulsion of any partner;
f) On the expiry of the period of partnership.

Thus this is clear from the above discussion that in the case of dissolution of the partnership the firm may continue under a new agreement whereas in the case of dissolution of partnership firm the business of the firm comes to an end.

7.12.2 Dissolution of Firm

Dissolution of a firm means the dissolution of partnership between all the partners of a firm. In such a situation, the business of the firm is discontinued, its assets are realised, the liabilities are paid off and the surplus (if any) is distributed among the partners according to their rights.

7.12.3 Modes of Dissolution of Firm

A partnership firm can be dissolved in any of the following ways :

A) By the order of the Court : Any partner to firm may apply to the court for getting the firm dissolved. On getting such application by any of the partner the court may proceed to order the dissolution of the firm in the following circumstances: (Sec. 44)

i) If any of the partner becomes insane. [Sec. 44(a)]
ii) If a partner, other than the partner filing the suit has become disabled to perform his duties as a partner. [Sec. 44(b)]
iii) If a partner, other than the partner filing the suit is guilty of misconduct. [Sec. 44(c)]
iv) If a partner, other than the partner filing the suit is guilty of intentionally and persistently committing a breach of the partnership agreement. [Sec. 44(d)]

v) If a partner, other than the partner filing the suit has transferred whole of his interest in the firm to a third party without the consent of the other partners.[Sec. 44(e)]

vi) If the court is satisfied that the business of the firm cannot be carried on except with a loss. [Sec. 44(e)]

vii) If the court considers it just and equitable to dissolve the firm due to some other reasons. [Sec. 44(f)]

B) Without the Intervention of the Court

i) Dissolution by Agreement : A firm may be dissolved with the consent of all the partners or in accordance with a contract between the partners.

ii) Compulsory Dissolution : (Sec. 41) A firm is compulsorily dissolved under any of the following circumstances:

a) When all the partners or all except one partner, become insolvent or insane making them incompetent to sign a contract;

b) Where the business becomes illegal;

c) Where all the partners except one decide to retire from the firm;

d) Where all the partners or all except one partner dies;

e) Where the partnership deed includes any provision regarding the happening of the following :

i) Expiry of the period for which the partnership was formed;

ii) Completion of the specific venture or project for which the firm was formed.

C) Dissolution on the Happening of Certain Contingencies (Sec. 42) : Subject to contract between the partners a firm is dissolved:

a) 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.

D) Dissolution by Notice of Partnership at Will (Sec. 43) : 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. 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.

7.12.4 Sales of Good will after Dissolution

The provisions relating to sales of good will after dissolution of a firm are as follows :

1) In settling the accounts of the firm after dissolution, the good will 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) Where the goodwill of the 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 the person who were dealing with the firm before its dissolution.



7.13 LET US SUM UP

- Partnership business in India is governed by the Indian Partnership Act, 1932, which came in to effect from 1st October, 1932.
- "Partnership" is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.
- Essential characteristics of a partnership firm are presence of agreement, association of two or more persons, sharing of profit, unlimited liability, utmost good faith etc.

- Registration of a partnership firm is not mandatory. But, provisions in the Indian Partnership Act has been made in such a way, that if a firm is registered, the firm avail certain privileges and firms which are not registered they cannot avail those privileges.
- Depending upon nature of participation and functions partners are classified as active partner, sleeping partner, silent partner, partner for profit only, partner by estoppels etc.
- With the consent of all the partners a minor can be admitted into partnership for benefits only.
- A partnership firm can be dissolved in any of the two ways: A) By the order of the court; B) without the intervention of the court.



7.14 FURTHER READINGS

1) *Indian Partnership Act*, 1932, (2014). New Delhi : Lawmann's.
2) Kapoor, N. D., *Elements of Mercantile Law*. New Delhi : S. Chand & Co. ltd.
3) Shukla, M. C. (2007), *Mercantile Law*, New Delhi : S. Chand & Co. Ltd.



7.15 ANSWERS TO CHECK YOUR PROGRESS

Ans. to Q. No. 1 : Four essential characteristics of a partnership firm are presence of an agreement, association of two or more persons, sharing of profit, unlimited liability.

Ans. to Q. No. 2 : Following are the two differences between company and partnership firm :

i) A Company is treated as an artificial legal person but Partnership is not a legal person.

ii) Company has perpetual succession but Partnership firm does not have perpetual succession.

Ans. to Q. No. 3 : A sleeping or dormant partner does not take any active part in the management of the business.

Ans. to Q. No. 4 : i) Right to take part in the conduct of the business

ii) Right to express opinion.

Ans. to Q. No. 5 : i) Duty to work without remuneration

ii) Duty to attend diligently to his duties.



7.16 MODEL QUESTIONS

Q.1 : Define partnership. What are the essential elements of a partnership?

Q.2 : What are the differences between partnership and joint stock company?

Q.3 : Discuss the various kinds of partners in a partnership firm?

Q.4 : Can a minor be admitted to a partnership? Discuss.

Q.5 : What is the procedure for the registration of a firm? What are the consequences of non-registration of a firm?

Q.6 : What are the mutual rights and duties in between the partners in a partnership firm?

Q.7 : What are the different modes in which a firm may be disolved?

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