

CHAPTER

9

PARTNERSHIP ACT, 1932

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**EXPECTED
MARKS COVERAGE
(5 to 10)**

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PARTNERSHIP ACT, 1932

INTRODUCTION

The Indian Partnership Act, 1932, came into force w.e.f. 1st October, 1932 except section 69, which came into force on the 1st day of October, 1933.

It lays down the **important provisions** relating to **partnership contracts**.

However, the **general principles of the Indian Contracts Act, 1872** which formally contained the provisions of the **law of partnership** shall apply so far as *they are not inconsistent with this Act*. (Section 3)

PARTNERSHIP - DEFINITION

According to Section 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”.

FOUR ELEMENTS OF PARTNERSHIP

When analysed, the definition tells us that in order that persons may become partners, it is essential that:

There must be at least two persons

There must be a relationship arising out of an agreement between two or more persons to do a business

The agreement must be to share the profits of a business

The business must be carried on by all or any of them acting for all

All these four elements must be present before a group or an association can be held to be partners.

In other words, it can be said that all the aforesaid **four elements must co-exist** before a partnership can be said to come into existence. If any one of them is not proved to be present, there cannot be a partnership.

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PARTNERS, FIRM AND FIRM 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”. (Section 4)

In law,

“a firm” is *neither a legal entity, nor is it a person as is a corporation*;

it is a collective name of the members of a partnership.

FIRM NAME

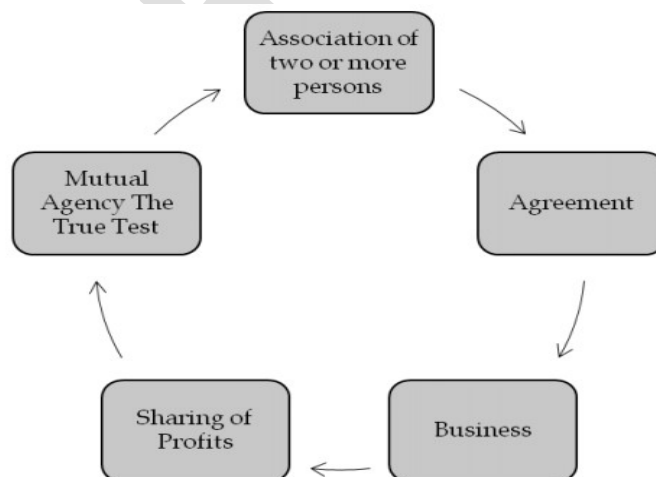
As regard the “firm name”, partners have a right to carry on business under **any name and style** which they choose to adopt, *provided they do not violate the rules relating to trade name or goodwill*.

They must not adopt name calculated to **mislead the public** into confusing them with a firm of repute already in existence with a **similar name**.

They must not use a name implying the sanction of **patronage** (*financial support*) of the Government.

A partnership firm cannot use the word “**Limited**” as a part of its name.

ESSENTIALS OF A PARTNERSHIP AND TRUE TEST OF PARTNERSHIP



(1) ASSOCIATION OF TWO OR MORE PERSONS

There must be a contract **between two or more persons**.

Persons **must be competent** to enter into a contract.

They may all be **natural or artificial** or some natural and other artificial.

Thus a **corporation or limited partnership may itself be a partner** in a general partnership.

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(2) AGREEMENT

Section 5 of the Act states that the relation of partnership arises from **contract**

Such an agreement between the partners may be **express or implied**.

Further, the agreement must be a valid agreement and for a **lawful object** and purpose and between the persons **competent to contract**.

(3) BUSINESS

Partnership implies business and when there is no association to carry on business there is no partnership.

As per **Section 2(b)** of the Act the term “*business*” *includes every trade, occupation and profession*.

(4) SHARING OF PROFITS

To constitute a partnership, the parties must have agreed to **carry on a business and to share profits** in common.

Sharing of profits also involves sharing of losses.

But whereas the sharing of profit is an essential element of partnership, **the sharing of losses is not**. It is **open to one or more partners to bear all the losses** of the business.

it is open to the partners to agree to share the profits in **any way they like**. They may agree to share the profits either in **specific proportions** or in **specific sums**.

SHARING OF PROFITS IS NOT CONCLUSIVE TEST

Although sharing of profits is a prima facie evidence of the existence of partnership, this is not the conclusive test of the same.

A person *may have a share in the partnership profits, but still may not be a partner*. For instance, a **joint owner** of a property sharing its return or members of non-profit or non-trading associations will not be called partners.

ILLUSTRATION

A and B buy 100 bales of cotton agreeing to divide these between them. A and B are not partners.

(5) MUTUAL AGENCY- THE TRUE TEST

Mutual agency is the **foundation of partner’s liability**.

Each partner is **both an agent and principal** for himself and others; that is the significance of the phrase “*carried on by all or any of them acting for all*”.

Each partner is an agent binding the other partners who are his principal and **each partner is again a principal**, who in turn is *bound by* the acts of the other partners.

FORMATION OF PARTNERSHIP

According to the definition of partnership under the **Indian Partnership Act, 1932**, there **must be an agreement** between the partners of a partnership firm.

The partnership agreement must comply with **all the essentials of a valid contract**.

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There must be

free consent of the parties

who must be **competent to contract** and

the **object of partnership should not be forbidden by law** or immoral or opposed to public policy.

Two exceptions, however, may be noted:

(i) A minor may be admitted to the benefits of a partnership **with the consent of all other partners**.

(ii) As relations of partners **inter se are that of agency**, no consideration is required to create the partnership

PARTNERSHIP DEED

The agreement of partnership **may be oral** but to avoid future disputes it is always **advisable to have it in writing**.

The **mutual rights and obligations** of partners must be discussed in detail and should be put into writing in the shape of a '**Partnership Deed**', before the partnership is actually started.

Thus, the written document which contains the mutual rights and obligations of partners is known as partnership deed. (The partnership deed is also called as '**Partnership Agreement**', '**Constitution of Partnership**', '**Articles of Partnership**' etc.).

The deed must be **property drafted and stamped** according to the provisions of the Indian Stamp Act.

Each partner should be given a copy of the deed and if the firm is to be registered, a copy of the deed should be **filed with the Registrar of Firms** at the time of such legislation.

CONTENTS OF PARTNERSHIP DEED

The exact terms of the partnership deed (or agreement) **will depend upon the circumstances** but generally a partnership deed contains the following covenants:

(i) The **firm name** and **business** to be carried on under that name.

(ii) Names and addresses of **partners**.

(iii) **Nature and scope of business** and **address(s) of business place(s)**.

(iv) **Commencement and duration** of partnership.

(v) The **capital** and the **contribution** made by each partner.

(vi) Provision for **further capital and loans** by partners to the firm.

(vii) **Partner's drawings**.

(viii) **Interest on capital**, loans, drawings and current account.

(ix) **Salaries, commission** and remuneration to partners.

(x) **Profit (or loss) sharing ratio** of partners.

(xi) The **keeping of proper books** of accounts, inspection and audit, Bank Accounts and their operation.

(xii) The **accounting period** and the date on which that accounts are to be prepared.

(xiii) **Rights, powers and duties of the partners**.

(xiv) Whether and in what circumstances, **notice of retirement or dissolution** can be given by a partner.

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(xv)	Provision that death or retirement of a partner will not bring about dissolution of partnership,
(xvi)	Valuation of goodwill on retirement, death, dissolution etc.
(xvii)	The method of valuation of assets (and liabilities) on retirement or death of any partner.
(xviii)	Provision for expulsion of a partner .
(xix)	Provision regarding the allocation of business activities to be performed by individual partners .
(xx)	The arbitration clause for the settlement of disputes. [Section 11(1)]

CLASSIFICATION OF PARTNERSHIP

. From the duration point of view, a partnership may be classified into the following two categories

(i) PARTICULAR PARTNERSHIP (SECTION 8)

“A person may become a partner with another person in a particular adventure or undertaking”. When two or more persons agree to do business in a particular adventure or undertaking, such a partnership is called “**Particular Partnership**”. Thus, a particular partnership may even be for a **single adventure or undertaking**.

(ii) PARTNERSHIP AT WILL (SECTION 7)

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

A partnership is deemed to be a partnership at will when

(i) no fixed period has been agreed upon for the duration of partnership, and

(ii) there is no provision made as to the determination of partnership in any other way.

Section 43(1) provides that “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.

DIFFERENCE BETWEEN CO-OWNERSHIP AND PARTNERSHIP

There is a possibility that two co-owners may employ their property in a business and share the profits, and *still be not partners*.

Coownership is **not always the result of an agreement**: it may arise by the operation of law or from status, e.g., co-heirs of a property. *Partnership must arise from an agreement*.

A partner is the agent of the other partners, but a *co-owner is not the agent* of the other co-owner(s).

A co-owner can without the consent of the others transfer his rights and interests to strangers, a *partner cannot do so without the consent of all the other partners*.

Partnerships end at death or insolvency; *co-ownerships end at death*.

DIFFERENCE BETWEEN HINDU JOINT FAMILY FIRM AND PARTNERSHIP

A Hindu joint family firm differs from a partnership in the following ways:

A partnership comes into existence by **means of a contract** between the partners; a *Hindu joint family firm arises as a result of status, i.e., by birth in the family*.

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The **death** of a partner **dissolves the partnership**, *but the death of a co-parcener does not dissolve the family firm.*

In a joint family firm **only the Karta or manager (who is the head of the family) has implied authority** to borrow and bind other members; in a *partnership each partner is entitled to do so.*

Every **partner is personally liable** for the debts of the firm; in a joint family business ***only the Karta is personally liable.***

A **partner can demand the accounts of the firm**, a *co-parcener cannot ask for accounts*, his only remedy is to ask for partition of the assets of the family firm.

There is a **definite limit to the number of partners**, but there is *no such limit in the case of a Hindu joint family firm.*

A Hindu joint family business is governed by **Hindu Law**, while **Indian Partnership Act**, governs *partnerships*

DIFFERENCE BETWEEN COMPANY AND PARTNERSHIP

The **firm has no legal entity** and has **no rights and obligations separate from the partners**. A company, as soon as it is incorporated, say by registration under the Companies Act, *becomes a legal entity distinct from its members constituting it*

In a firm **every partner is an agent of the rest of the partners**, but a *member of a company is neither the agent of the company nor of other members.*

In a partnership, **there are rights and obligations as against individual partners**, but in the case of a company, *the rights and obligations are as against the fictitious entity of the whole of the company* and not the members composing it.

The **creditors of the partnership can call upon individual partners to pay** the firm's debt, but the *members of a company are not personally liable* for the company's debts.

In other words, a **partner's liability is unlimited** while the *liability of the members of a company is limited*

Partnership firm may **dissolve by the death or insolvency of a partner**, but a *company is not affected by the death or insolvency of a member.*

CHANGE IN A FIRM

The Indian Partnership Act, 1932, contemplates the following **changes in a partnership firm**:

(1) Changes in the **constitution** of a firm.

(2) Changes in the **nature of a business** or undertakings.

(3) Changes in the **duration** of a firm.

A change in the constitution of a firm takes place when:

(a) a **new partner is introduced** as a partner in a firm; (Section 31)

(b) a **partner retires** from a firm; (Section 32),

(c) a partner is **expelled** from a firm; (Section 33),

(d) a partner is adjudicated as **an insolvent**; (Section 34) and

(e) a partner **dies**. (Section 35)

A change in the nature of the business can only be brought about by **the consent of all the partners**.

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PARTNERSHIP PROPERTY

It is open to the partners to agree among themselves as to

what is to be treated as the **property of the firm**, and

what is to be **separate property of one or more partners**, although employed for the purposes of the firm.

In the absence of any such agreement, express or implied, *the property of the firm is deemed to include:*

(a) all property, rights and interests which have been brought **into the common stock** for the purposes of the partnership by individual partners, whether at the commencement of the business or subsequently added thereto;

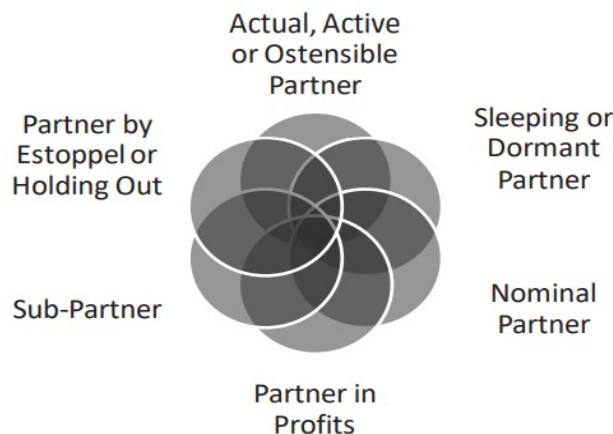
(b) those **acquired in the course of the business** with money belonging to the firm; and

(c) **the goodwill** of the business. (Section 14)

The property of the firm belongs to the firm and not to the individual partner or partners.

KINDS OF PARTNERS

The following kinds of partners generally exist in a partnership:



(i) ACTUAL, ACTIVE OR OSTENSIBLE PARTNER

These are the **ordinary types of partners** who invest money into the business of the firm, actively participate in the functioning and management of the business and share its profits or losses.

Such partner must give a public notice of his retirement from the firm in order to absolve (free) himself from liability for the acts of the other partners done after his retirement.

(ii) SLEEPING OR DORMANT PARTNER

These partners invest money in the firm's business and take their share of profits but **do not participate in the functioning and management of the business**. But even then their liability is unlimited.

A sleeping partner can retire from the firm without giving any public notice to this effect.

(iii) NOMINAL PARTNER

Some people **do not invest or participate** in the management of the firm but only give their name to the business or firm. They are nominal partners but are liable to third parties for all the acts of the firm.

Unlike a sleeping partner, they are known to the outsiders as partners in the firm, whereas actually they are not.

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(iv) **PARTNER IN PROFITS ONLY**

A partner who is entitled to **share in the profits of a partnership firm *without being liable to share the losses***, is called a partner in **profits only**. In spite of his specific position, **he continues to be liable to the third parties** for all acts of the firm, just like other parties.

(v) **SUB-PARTNER**

Where a **partner agrees to share his profits** in the firm with a third person, *that third person is called a subpartner*. Such a sub-partner has **no rights or duties towards the firm** and **does not carry any liability for the debts of the firm**.

(vi) **PARTNER BY ESTOPPEL OR HOLDING OUT**

Holding Out means **“to represent”**.

If the behaviour of a person arouses **misunderstanding that he is a partner in a firm** (when actually he is not), such a person is **estopped from later on denying the liabilities** for the acts of the firm. Such person is called partner by estoppel and is **liable to all third parties**.

The law relating to partners by holding out is contained in **Section 28** of the Act which lays down thus:

“Any one
who by words, spoken or written or by conduct
represents himself, or knowingly permits himself to be represented
to be a partner in a firm,
<i>is liable as a partner</i> in that firm to any one who has on the faith of any such representation <u>given credit to the firm,</u>
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 <i>the person so giving credit</i>”.

The rule as to holding out is based on the **doctrine of estoppel** as contained in **Section 115** of the Indian Evidence Act.

Exceptions to Holding Out

The doctrine of Holding Out is not applicable in the following cases:

1. It does not apply to cases of torts committed by partners . A person, therefore, cannot be held liable for the torts of another simply because that other person held himself to be his partner.
2. It does not extend to bind the estate of a deceased partner , where after a partner's death the business of the firm is continued in the old firm name . [Section 28(2)]
3. It also does not apply where the Holding Out partner has been adjudicated insolvent . (Section 45).

MINOR ADMITTED TO THE BENEFITS OF PARTNERSHIP

In view of **Section 11 of the Indian Contract Act, 1872**, and the decision of the Privy Council in ***Mohori Bibi v. Dharmo Das Ghose***, a minor's agreement is altogether void and unenforceable.

An agreement is an essential ingredient in a partnership, it follows that a ***minor cannot enter into an agreement of partnership***. On the same principle, a minor cannot be clothed with all the rights and obligations of a full-fledged partner through a guardian.

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Section 5 states “**The relation of partnership arises from a contract.**” The **minor is incompetent** to contract and, therefore, partnership cannot come into existence if the parties to a contract of partnership consist of one major and one minor.

EXCEPTION

The only provision that **Section 30** makes is that with the “**consent of all the partners** for the time being, a **minor can be admitted into the benefits of partnership** to which a minor is going to be admitted”.

A partnership firm cannot be formed with only minors as partners. There must be atleast **two major partners** before a minor is admitted into the benefits of partnership.

RIGHTS OF MINOR

He is entitled to his agreed share and

He can inspect books of account of the firm [Section 30(2)].

He can bring a suit for account and his share *when he intends to sever* his connections with the firm, *but not otherwise*. [Section 30(4)].

LIABILITIES OF MINOR

1. His Share in Liability

A minor partner’s liability is confined **only to the extent of his share** in the firm.

Section 30(3) provides that a minor’s share is liable for the acts of the firm. But a **minor is not personally liable** in any such act. Thus, he is *neither personally liable nor is his private estate liable* for the acts of the firm.

2. Personal Liabilities

Where a minor **on attaining majority**, elects to become a partner, he **becomes personally liable** as other partners to the third parties for **all the acts of the firm done since he was admitted to the benefits of partnership**.

ELECTION BY MINOR

A minor who was admitted to the benefits during his minority within six months

of his attaining the age of majority or

when he comes to know of his being so admitted

(whichever *date is later*),

he has to elect whether

he wants to become a partner, or

sever his connection with the firm.

If he becomes or elects to become a partner, his position will be as under:

1. His rights and liabilities will be **similar to those of a full-fledged partner**.

2. He will be **personally liable for all the acts of the firm**, done since he was first admitted to the **benefits of the partnership**.

3. His share of profits and property remains the **same as was before, unless altered by agreement**

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If he elects not to become a partner, then:

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| 1. His rights and liabilities shall continue to be those of a minor upto the date of his giving public notice . |
| 2. His share shall not be liable for any acts of the firm done after the date of the public notice . |
| 3. He is entitled to sue the partners for his share of the property and profits in the firm. [Section 30(8)] |

RELATION OF PARTNERS TO ONE ANOTHER

The relation of partnership arises **through an agreement** between the parties and such an agreement normally provides for **mutual rights and obligations**, or duties of the partners.

Where, however, partnership arises by implication, or wherever the articles of partnership are silent, or where they do not exist, the **rights and duties of partners are governed by the Act**.

RIGHTS OF PARTNERS

Unless otherwise agreed by the partners, the following rules apply:

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| (a) Every partner has a right to take part in the conduct and management of the business. [Section 12(a)] |
| (b) Every partner whether active or dormant, has a right of free access to all records, books and accounts of the business and also to examine and copy them. [Section 12(d)] |
| (c) Every partner is entitled to share in the profits equally , <i>unless different proportions are stipulated</i> . [Section 13(b)] |
| (d) A partner who has contributed more than the share of the capital for the purpose of the business is entitled to an interest at a rate agreed upon, and where no rate is stipulated for, at six per cent per annum . But a partner cannot claim interest on capital, unless there is an agreement to pay it. [Section 13(d)] |
| (e) A partner is entitled to be indemnified by the firm for all expenses incurred by him in the course of the business, |
| (f) Every partner is, as a rule, a joint owner of the partnership property , (Section 15) |
| (g) A partner has power to act in an emergency for protecting the firm from loss. (Section 21) |
| (h) Every partner is entitled to prevent the introduction of a new partner into the firm without his consent . (Section 31) |
| (i) Every partner has a right to retire by giving notice where the partnership is at will. [Section 32(1)(c)] |
| (j) Every partner has a right to continue in the partnership and not to be expelled from it. [Section 33(1)] |
| (k) An incoming partner will not be liable for any debts or liabilities of the firm before he becomes a partner . [Section 31(2)] (l) |

DUTIES OF PARTNERS

Apart from any **duties imposed by the partnership articles**, the following statutory duties are implied:

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| (a) Every partner is bound to carry on the business of the firm to the greatest common advantage. (Section 9) |
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(b) Every partner must be just and faithful to other partners. (Section 9)
(c) A partner is bound to keep and render true, proper and correct accounts of the partnership. (Section 9)
(d) Utmost good faith between the partners is the rule and one partner must not take advantage of the other. (Section 9)
(e) A partner must not make “ secret profits ”. [Section 16(a)]
(f) A partner must not compete with the firm , without the consent of the other partners.. [Section 16(b)]
(g) Every partner is bound to attend diligently to the business of the firm. [Section 12(b) and 13(a)]
(h) <i>In the absence of an agreement to the contrary</i> , every partner is bound to share losses equally with the others. [Section 13(b)]
(i) Every partner must hold and use the partnership property exclusively for the firm . (Section 15)
(j) Every partner is bound to indemnify the firm for any loss caused by fraud in the conduct of the business. (Section 10)

RELATION OF PARTNERS TO THIRD PARTIES

PARTNERS AS AGENTS

Every partner is an **agent of the firm and of other partners** for the purpose of the business of the firm (Section 18).

In the case of a partnership **each partner is a principal and each one is an agent** for the other partners. A partner is both a principal and an agent.

AUTHORITY OF A PARTNER

The authority of a partner means the capacity of a partner to bind the firm by his act. This authority may be express or implied.

(i) **EXPRESS AUTHORITY:-**

Authority is said to be express when it is **given by words, spoken or written**.

(ii) **IMPLIED AUTHORITY:-**

The implied authority of a partner is also known as **ostensible or apparent authority**, Sections 19 and 22 contain provisions regarding the scope of the implied authority of a partner.

The implied authority is subject to the **following conditions**:

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| (1) the act done must relate to the “ normal business ” of the firm; |
| (2) the act must be done in the usual way ; |
| (3) the act must be done in the name of the firm . |

IMPLIED AUTHORITY OF A PARTNER

Subject to the limitations mentioned above, **every partner has an implied authority to bind the firm** by the **following acts**:

- | |
|---|
| (i) By selling firm’s goods; |
| (ii) By purchasing goods for the firm; |
| (iii) By accepting any payment of debts due to the firm; and |
| (iv) By engaging and discharging employees . |

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ACTS BEYOND IMPLIED AUTHORITY

Section 19(2) states that *in the absence of any usage or custom or trade to the contrary*, the implied authority of a **partner does not empower him to:**

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

EXTENT OF PARTNERS' LIABILITY

It is, however, open to the partners by means of an EXPRESS contract to extend or limit the implied authority, but *third parties will be bound by such limitations only when they have notice* of such curtailment.

All partners are liable **jointly and severally** for all acts or omissions binding on the firm (Section 25).

This is known as the liability of partners for the acts of the firm.

LIABILITY OF THE FIRM FOR TORTS

Every partner is liable for the **negligence and fraud of the other partners** in the course of the management of business.

A partner charges the firm if he acts as an agent for it.

The firm is similarly liable where a partner commits a tort with the authority of his co-partners.(Section 26)

If a partner acting **within the scope** of his apparent authority **receives the property of a third person and misapplies it**, the firm is liable to make good the loss. (Section 27)

LIABILITY OF AN INCOMING PARTNER

As a general rule, an incoming partner **is not liable** for the debts incurred before he joined the firm as a partner [Section 31(2)].

The incoming partner may, however, assume liability for past debts by novation, i.e., by a **tripartite agreement** between

(i)	the creditor of the firm,
(ii)	the partners existing at the time the debt was incurred, and
(iii)	the incoming partner.

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LIABILITY OF AN OUTGOING OR RETIRING PARTNER

An outgoing partner **remains liable** for the partnership debts contracted **while he was** a partner.

He may, however, be **discharged by novation**, i.e., by an agreement **between**

himself,

the new firm and

the creditors.

He may also continue to be **liable after retirement if he allows himself to be held out as a partner**, e.g. by allowing his name to remain the firm name.

To protect himself from his liability, he should give express notice of his retirement

DEATH OR INSOLVENCY

The estate of a partner who dies, or who becomes insolvent, is **not liable** for partnership debts contracted **after the date of the death or insolvency**.

It will, **however, be liable** for debts incurred **before death or insolvency**. (Sections 34 and 35)

DISSOLUTION

According to Section 39 “

The dissolution of partnership

between all the partners of a firm”

is called the “**Dissolution of the Firm**”.

A dissolution does not necessarily follow because the **partnership has ceased to do business**, for the **partnership may continue for the purpose of realising the assets**.

DISTINCTION BETWEEN THE “DISSOLUTION OF PARTNERSHIP” AND “DISSOLUTION OF FIRM”.

Where there is dissolution of partnership between **all the partners** of a firm, **it is a dissolution of the firm** (Section 39).

Where there is an extinction of relationship between **some of the partners only**, **it is a dissolution of partnership ONLY**.

So the dissolution of a partnership **may or may not** include the dissolution of the firm,

but the dissolution of the firm necessarily means the dissolution of the partnership as well.

DISSOLUTION OF PARTNERSHIP

The **dissolution of partnership** takes place (even when there is no dissolution of the firm) **in the following circumstances**:

(a) By the expiry of the **fixed term** for which the partnership was formed.[Section 42(a)]

(b) By the **completion of the adventure**. [Section 42(b)]

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(c) By the death of a partner . [Section 42(c)]
(d) By the insolvency of a partner . [Section 42(d)]
(e) By the retirement of a partner . [Section 42(e)]

In all the above cases, the **remaining partners may continue the firm** in pursuance of an agreement to that effect. If **they do not continue then the dissolution of the firm** takes place automatically.

DISSOLUTION OF THE FIRM

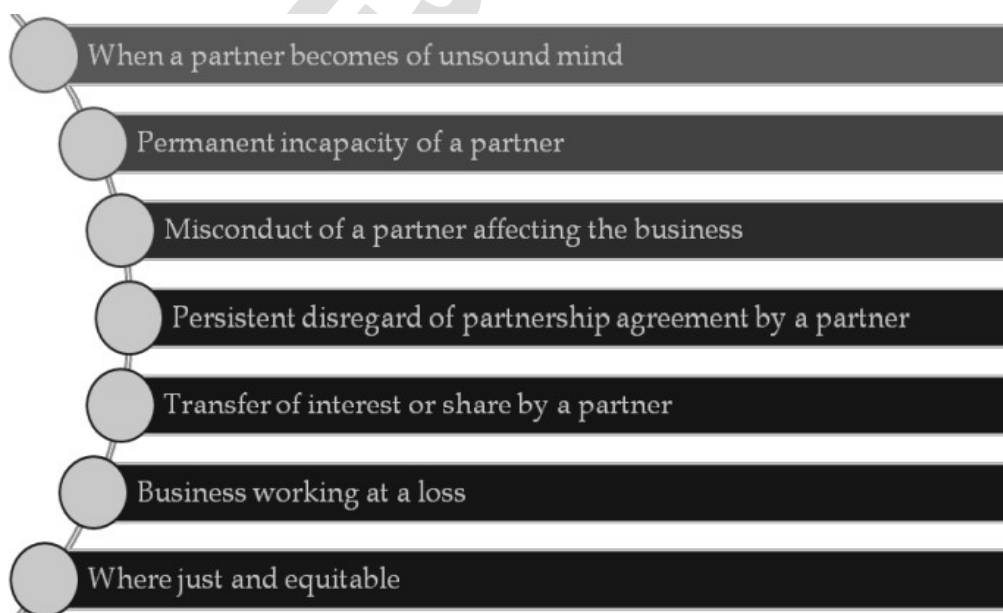
In the following cases there is necessarily a breaking up or extinction of the relationship **between all the partners of the firm, and closing up of the business**:

(a) By mutual agreement : A firm may be dissolved where all the partners agree that it shall be dissolved. (Section 40)
(b) By the insolvency of all the partners but one : If all the partners except one become insolvent, the firm must come to an end , as a partnership firm with one partner cannot continue. [Section 41(a)]
(c) By business becoming illegal : If the business of the firm becomes illegal because of some subsequent events, such as change of law , it is automatically or compulsorily dissolved by the operation of law. [Section 41(b)]
(d) By notice of dissolution : Where the partnership is at will, the firm may be dissolved at any time , by any partner giving notice in writing of his intention to dissolve the firm, to all the other partners. (Section 43)

DISSOLUTION OF THE FIRM THROUGH COURT

Unlike a partnership at will, the partnership for a fixed period cannot be dissolved by a notice. It could only be dissolved by Court in a suit by a partner.

As per **Section 44**, the Court may order dissolution of the firm **in the following circumstances**:



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EFFECT OF DISSOLUTION

1. CONTINUING AUTHORITY OF PARTNERS

The **authority of partners to bind the firm** continues so long as is necessary to wind up the business.

Also each partner has an **equitable lien over the firm's assets** entitling him to have them applied in **payment of the firm's debts**, and in **payment of whatever is due to partner**.

This lien can be enforced **by injunction** forbidding unfair distribution. (Section 46)

2. CONTINUING LIABILITY OF PARTNERS

The **partners continue to be liable to outsiders** for any act done by any of them which would have been an act of the firm **if done before the dissolution**, unless a public notice is given of the dissolution.

After dissolution, the rights and obligations of partners continue in **all things necessary for the winding up of the business**.

3. RIGHT TO RETURN OF PREMIUM

To buy entry into an existing firm, a **new partner sometimes has to pay a premium** to the existing partners in addition to any investment of capital. **On dissolution, he is entitled to demand the return** of a proportion of the premium if the partnership was for a fixed term

4. SETTLEMENT OF ACCOUNTS ON DISSOLUTION

Section 48 of the Act provides that **in settling accounts** between the partners after a dissolution of partnership, **the following rules shall, subject to any agreement, be observed:**

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| (a) Losses, including deficiencies of capital shall be paid
first out of undistributed profits ,
next out of capital , and
lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits | | | | |
| (b) The assets of the firm , including the sums, contributed by the partners to make up losses or deficiencies of capital shall be applied in the following manner and order: <table border="1"><tr><td>(i) in paying outside creditors;</td></tr><tr><td>(ii) in repaying advances made by partners (distinct from investment of capital);</td></tr><tr><td>(iii) in repaying capital to partners; and</td></tr><tr><td>(iv) the ultimate residue, if any, shall be divided among the partners in the proportions in which profits are divisible.</td></tr></table> | (i) in paying outside creditors ; | (ii) in repaying advances made by partners (distinct from investment of capital); | (iii) in repaying capital to partners ; and | (iv) the ultimate residue , if any, shall be divided among the partners in the proportions in which profits are divisible. |
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| (ii) in repaying advances made by partners (distinct from investment of capital); | | | | |
| (iii) in repaying capital to partners ; and | | | | |
| (iv) the ultimate residue , if any, shall be divided among the partners in the proportions in which profits are divisible. | | | | |

5. LOSS DUE TO INSOLVENCY OF PARTNERS

In case a partner is insolvent and is not able to contribute towards the deficiency, the principle laid down in the case of **Garner vs. Murray** will be applicable.

It holds that:

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| (a) The solvent partners will contribute only their share of deficiency in cash |
| (b) The available assets should be distributed among the solvent partners in proportion to their capital. |
| (c) Thus, the deficiency of capital of the insolvent partners will be distributed among the solvent partners in the ratio of their respective capitals. |

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GOODWILL

This is a **partnership asset** and means the benefit **arising from a firm's business connections or reputation**.

“It is the advantage which is acquired by a business, beyond the mere value of the capital, stock fund and properly employed therein, in consequence of the general public patronage and encouragement which it receives from constant or habitual customers”.

Though an intangible asset, it has value; and unless otherwise agreed in the partnership articles, upon dissolution it must be sold and the proceeds of sale distributed as capital.

SALE OF GOODWILL

Where goodwill is sold, *either to a partner or to an outsider*, the value is divisible among the partners in the same manner as they share profits and losses, unless otherwise agreed.

The rights of the **buyer and seller of the goodwill** are as follows:

(a) **Buyer's rights:** On the sale of goodwill the **buyer may**, unless the terms in the contract of sale provide otherwise:

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| (i) represent himself in continuing the business, |
| (ii) maintain his exclusive rights to the use of the firm name, and |
| (iii) solicit former customers of the business and restrain the seller of the goodwill from doing so. |

(b) **Seller's rights:** The vendors **may enter into competition** with the purchaser *unless he is prevented by a valid restraint clause in the contract of sale*.

REGISTRATION OF THE FIRM

Section 56-71 deal with the registration of a firm and consequences of non-registration.

REGISTRATION

The registration of a firm **may be** effected at any time by **sending by post or delivering to the Registrar** of the area in which any place of business of the firm is situated or proposed to be situated, a statement in the prescribed form and **accompanied by the prescribed fee, stating:**

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

The statement shall be **signed and verified by all the partners** or by their agents specially authorised in this behalf. (**Section 58**).

The Partnership Act, 1932, **does not make** registration of a firm **compulsory** *but it introduces certain disabilities, which makes registration necessary at one time or other*. An unregistered firm is not an illegal association.

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EFFECTS OF NON-REGISTRATION

The following are the effects of non-registration of a firm:

1. Sub-section (1) of Section 69 places a **bar on the right of the partners of a firm to sue each other or the firm** for enforcing any right arising from a contract or conferred by the Partnership Act,
2. Sub-section (2) of Section 69 places a **bar on the institution of a suit by or on behalf of a firm against a third-party**
3. There is **no bar** on the right of third-parties to sue the firm or any partner.

However, the Act allows the following suits:

- (a) A suit for the dissolution of a firm.
- (b) A suit for rendering of accounts of a dissolved firm.
- (c) A suit for realisation of the property of a dissolved firm.
- (d) A suit or claim of set-off, the value of **which does not exceed one hundred rupees**,
- (e) A suit by a firm which has **no place of business** in the territories to which the **Indian Partnership Act extends**.
- (f) A suit by a firm whose places of business are situated in areas which **are exempted from the application of Chapter VII of the Indian Partnership Act, 1932**.

SPECIFIC PERFORMANCE OF PARTNERSHIP AGREEMENT

It is not allowed. The working of a partnership depends upon the **personal inclination** of the partners, there can be **no specific performance** of a partnership agreement (*Scott v. Raymont, 1868, 7 Fq. 112*).

SUIT FOR LIBEL OR SLANDER

A firm is merely a collection of partners and **cannot bring a suit for libel or slander**.

Libel or slander against a **firm imply a libel or slander of its partners**.

Such partners themselves or any one may file the suit for libel or slander

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Answers to be analysed in Classroom

Q. 1.

Answer to Question No. 1:-

CS NITESH KR. JAISWAL



Answers to be analysed in Classroom

Q. 2.

Answer to Question No. 2:-

CS NITESH KR. JAISWAL