

Chapter 4- The Indian Partnership Act, 1932

Unit-1: General Nature of Partnership

Definition Of ‘Partnership’, ‘Partner’, ‘Firm’ And ‘Firm Name’ (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.

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’.

Elements Of Partnership

The definition of the partnership contains the following five elements which must co-exist before a partnership can come into existence.

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| 1. Association of Two Or More Persons: | <p><i>Partnership is an association of 2 or more persons. Again, only persons recognized by law can enter into an agreement of partnership. Therefore, a firm, since it is not a person recognized in the eyes of law cannot be a partner. Again, a minor cannot be a partner in a firm, but with the consent of all the partners, may be admitted to the benefits of partnership.</i></p> <p><i>The partnership Act is silent about the maximum number of partners but section 464 of the Companies Act, 2013 has now put a limit of 50 partners in any association/partnership firm.</i></p> |
| 2. Agreement: | <p><i>It may be observed that partnership must be the result of an agreement between two or more persons. There must be an agreement entered into by all the persons concerned. This element relates to voluntary contractual nature of partnership.</i></p> <p><i>Thus, the nature of the partnership is voluntary and contractual. An agreement from which relationship of Partnership arises may be express. It may also be implied from the act done by partners and from a consistent course of conduct being followed, showing mutual understanding between them. It may be oral or in writing.</i></p> |
| 3. Business: | <p><i>In this context, we will consider two propositions. First, there must exist a business.</i></p> |



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| | <p>For the purpose, the term 'Businesses include every trade, occupation and profession. The existence of business is essential. Secondly, the motive of the business is the "acquisition of gains" which leads to the formation of partnership. Therefore, there can be no partnership where there is no intention to carry on the business and to share the profit thereof.</p> |
| <p>4. Agreement to Share Profits:</p> | <p>The sharing of profits is an essential feature of partnership. There can be no partnership where only one of the partners is entitled to the whole of the profits of the business.</p> <p>Partners must agree to share the profits in any manner they choose. But an agreement to share losses is not an essential element. It is open to one or more partners to agree to share all the losses. However, in the event of losses, unless agreed otherwise, these must be borne in the profit-sharing ratio.</p> <p>Example: Co-owners who share amongst themselves the rent derived from a piece of land are not partners, because there does not exist any business.</p> <p>Example: No charitable institution or club may be floated in partnership [A joint stock company may, however, be floated for non-economic purposes].</p> <p>Example: X and Y buy certain bales of cotton which they agree to sell on their joint account and to share the profits equally. In these circumstances, X and Y are partners in respect of such cotton business</p> |
| <p>5. Business Carried on by All or Any of Them Acting for All:</p> | <p>The business must be carried on by all the partners or by anyone or more of the partners acting for all. This is the cardinal principle of the partnership Law. In other words, there should be a binding contract of mutual agency between the partners.</p> <p>An act of one partner in the course of the business of the firm is in fact an act of all partners. Each partner carrying on the business is the principal as well as the agent for all the other partners. He is an agent in so far as he can bind the other partners by his acts and he is a principal to the extent that he is bound by the act of other partners. It may be noted that the true test of partnership is mutual</p> |



agency rather than sharing of profits. If the element of mutual agency is absent, then there will be no partnership.

Example: A, B and C are partners in ABC Associates, a partnership firm. If A made certain purchases for the purpose of business from Mr. K, then Mr. K can recover the money from A, B or C as all partners are liable for any act done on behalf of firm.

In KD Kamath & Co.

The Supreme Court has held that the two essential conditions to be satisfied are that:

- (1) there should be an agreement to share the profits as well as the losses of business; and
- (2) the business must be carried on by all or any of them acting for all, within the meaning of the definition of 'partnership' under section 4.

The fact that the exclusive power and control, by agreement of the parties, is vested in one partner or the further circumstance that only one partner can operate the bank accounts or borrow on behalf of the firm are not destructive of the theory of partnership provided the two essential conditions, mentioned earlier, are satisfied.

Note: -The 'Partnership Agreement' is also known as 'Partnership Deed'.

True Test of Partnership

Mode of determining existence of partnership (Section 6): In determining whether a group of persons is or is not a firm, or whether a person is or not a partner in a firm, regard shall be had to the real relation between the parties, as shown by all relevant facts taken together.

For determining the existence of partnership, it must be proved.

1. There was an **agreement** between all the persons concerned;
2. The agreement was to **share the profits** of a business and
3. the business was **carried on by all or any of them** acting for all.

1. Agreement:

Partnership is created by agreement and not by status (Section 5). The relation of partnership arises from contract and not from status; and in particular, the members of a Hindu Undivided family carrying on a family business as such, or a Burmese Buddhist husband



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| | <p>and wife carrying on business as such are not partners in such business</p> |
| <p>2. Sharing of Profit:</p> | <p>The sharing of profits or of gross returns arising from property by persons holding a joint or common interest in that property does not of itself make such person's partners.</p> <p>The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business, does not of itself make him a partner with the persons carrying on the business; and in particular, the receipt of such share or payment-</p> <p>(a) by a lender of money to persons engaged or about to engage in any business,</p> <p>(b) by a servant or agent as remuneration,</p> <p>(c) by a widow or child of a deceased partner, as annuity, or</p> <p>(d) by a previous owner or part owner of the business, as consideration for the sale of the goodwill or share thereof, does not of itself make the receiver a partner with the persons carrying on the business.</p> <p>As discussed earlier, sharing of profit is an essential element to constitute a partnership. But it is only a prima facie evidence and not conclusive evidence, in that regard. The sharing of profits or of gross returns accruing from property by persons holding joint or common interest in the property would not by itself make such person's partners. Although the right to participate in profits is a strong test of partnership, and there may be cases where, upon a simple participation in profits, there is a partnership, yet whether the relation does or does not exist must depend upon the whole contract between the parties.</p> <p>Where there is an express agreement between partners to share the profit of a business and the business is being carried on by all or any of them acting for all, there will be no difficulty in the light of provisions of Section 4, in determining the existence or otherwise of partnership.</p> |



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| | <p><i>But the task becomes difficult when either there is no specific agreement or the agreement is such as does not specifically speak of partnership. In such a case for testing the existence or otherwise of partnership relation, Section 6 has to be referred.</i></p> <p><i>According to Section 6, regard must be had to the real relation between the parties as shown by all relevant facts taken together. The rule is easily stated and is clear but its application is difficult. Cumulative effect of all relevant facts such as written or verbal agreement, real intention and conduct of the parties, other surrounding circumstances etc., are to be considered while deciding the relationship between the parties and ascertaining the existence of partnership.</i></p> |
| <p>3. Agency:</p> | <p><i>Existence of Mutual Agency which is the cardinal principle of partnership law, is very much helpful in reaching a conclusion in this regard. Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners. If the elements of mutual agency relationship exist between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist.</i></p> <p><i>Existence of Mutual Agency which is the cardinal principle of partnership law, is very much helpful in reaching a conclusion in this regard. Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners. If the elements of mutual agency relationship exist between the parties constituting a group formed with a view to earn profits by running a business, a partnership may be deemed to exist.</i></p> |

Santiranjan Das Gupta Vs. Dasyran Murzamull (Supreme Court)

In Santiranjan Das Gupta Vs. Dasyran Murzamull, following factors weighed upon the Supreme Court to reach the conclusion that there is no partnership between the parties:



- (a) Parties have not retained any record of terms and conditions of partnership.
- (b) Partnership business has maintained no accounts of its own, which would be open to inspection by both parties.
- (c) No account of the partnership was opened with any bank.
- (d) No written intimation was conveyed to the Deput

Partnership Distinguished from Other Forms of Organisation

Partnership Vs. Joint Stock Company

| Basis | Partnership | Joint Stock Company |
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| Legal status | A firm is not legal entity i.e. it has no legal personality distinct from the personalities of its constituent members. | A company is a separate legal entity distinct from its members (Salomon v. Salomon). |
| Agency | In a firm, every partner is an agent of the other partners as well as of the firm. | In a company, a member is not an agent of the other members or of the company, his actions do not bind either. |
| Distribution of profits | The profits of the firm must be distributed among the partners according to the terms of the partnership deed. | There is no such compulsion to distribute its profits among its members. Some portion of the profits, but generally not the entire profit, become distributable among the shareholders only when dividends are declared. |
| Extent of liability | In a partnership, the liability of the partners is unlimited. This means that each partner is liable for debts of a firm incurred in the course of the business of the firm and these debts can be recovered from his private property, if the joint estate is insufficient to meet them wholly | In a company limited by shares, the liability of a shareholder is limited to the amount, if any, unpaid on his shares, but in the case of a guarantee company, the liability is limited to the amount for which he has agreed to be liable. However, there may be companies where the liability of members is unlimited. |



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| Property | <i>The firm's property is that which is the "joint estate" of all the partners as distinguished from the 'separate' estate of any of them and it does not belong to a body distinct in law from its members.</i> | <i>In a company, its property is separate from that of its members who can receive it back only in the form of dividends or refund of capital.</i> |
| Transfer of shares | <i>A share in a partnership cannot be transferred without the consent of all the partners.</i> | <i>In a company a shareholder may transfer his shares, subject to the provisions contained in its articles. In the case of public limited companies whose shares are quoted on the stock exchange, the transfer is usually unrestricted.</i> |
| Management | <i>In the absence of an express agreement to the contrary, all the partners are entitled to participate in the management.</i> | <i>Members of a company are not entitled to take part in the management unless they are appointed as directors, in which case they may participate. Members, however, enjoy the right of attending general meeting and voting where they can decide certain questions such as election of directors, appointment of auditors, etc.</i> |
| Registration | <i>Registration is not compulsory in the case of partnership.</i> | <i>A company cannot come into existence unless it is registered under the Companies Act, 2013.</i> |
| Winding up | <i>A partnership firm can be dissolved at any time if all the partners agree.</i> | <i>A company, being a legal person is either wind up by the National Company Law Tribunal or its name is struck off by the Registrar of Companies.</i> |
| Number of memberships | <i>According to section 464 of the Companies Act, 2013, the number of partners in any association shall not exceed 100.</i> | <i>A private company may have as many as 200 members but not less than two and a public company may have any number of members but not less</i> |



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| | | than seven. A private Company can also be formed by one person known as one person Company. |
| Duration of existence | However, the Rule given under the Companies (Miscellaneous) Rules, 2014 restrict the present limit to 50. | A company enjoys a perpetual succession. |

Partnership Vs. Club

| Basis of Difference | Partnership | Club |
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| Definition | It is an association of persons formed for earning profits from a business carried on by all or any one of them acting for all. | A club is an association of persons formed with the object not of earning profit, but of promoting some beneficial purposes such as improvement of health or providing recreation for the members, etc. |
| Relationship | Persons forming a partnership are called partners and a partner is an agent for other partners. | Persons forming a club are called members. A member of a club is not the agent of other members. |
| Interest in the property | Partner has interest in the property of the firm. | A member of a club has no interest in the property of the club. |
| Dissolution | A change in the partners of the firm affect its existence. | A change in the membership of a club does not affect its existence. |

Partnership vs. Hindu Undivided Family

| Basis of difference | Partnership | Joint Hindu Family |
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| Mode of creation | Partnership is created necessarily by an agreement. | The right in the joint family is created by status means its creation by birth in the family. |
| Death of a member | Death of a partner ordinarily leads to the dissolution of partnership. | The death of a member in the Hindu undivided family does not |



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| | | give rise to dissolution of the family business. |
| Management | All the partners are equally entitled to take part in the partnership business. | The right of management of joint family business generally vests in the Karta, the governing male member or female member of the family. ¹ |
| Authority to bind | Every partner can, by his act, bind the firm. | The Karta or the manager, has the authority to contract for the family business and the other members in the family. |
| Liability | In a partnership, the liability of a partner is unlimited. | In a Hindu undivided family, only the liability of the Karta is unlimited, and the other coparcener are liable only to the extent of their share in the profits of the family business. |
| Calling for accounts on closure | A partner can bring a suit against the firm for accounts, provided he also seeks the dissolution of the firm. | On the separation of the joint family, a member is not entitled to ask for account of the family business. |
| Governing Law | A partnership is governed by the Indian Partnership Act, 1932. | A Joint Hindu Family business is governed by the Hindu Law. |
| Minor's capacity | In a partnership, a minor cannot become a partner, though he can be admitted to the benefits of partnership, only with the consent of all the partners. | In Hindu undivided family business, a minor becomes a member of the ancestral business by the incidence of birth. He does not have to wait for attaining majority. |
| Continuity | A firm subject to a contract between the partners gets dissolved by death or insolvency of a partner. | A Joint Hindu family has the continuity till it is divided. The status of Joint Hindu family is not thereby affected by the death of a member. |



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| Number of Members | <i>In case of Partnership number of members should not exceed 50.</i> | <i>Members of HUF who carry on a business may be unlimited in number.</i> |
| Share business in the | <i>In a partnership, each partner has a defined share by virtue of an agreement between the partners.</i> | <i>In a HUF, no coparceners have a definite share. His interest is a fluctuating one. It is capable of being enlarged by deaths in the family diminished by births in the family.</i> |

Partnership Vs. Co-Ownership or joint ownership i.e. the relation which subsists between persons who own property jointly or in common.

| <i>Basis of difference</i> | <i>Partnership</i> | <i>Co-ownership</i> |
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| Formation | <i>Partnership always arises out of a contract, express or implied.</i> | <i>Co-ownership may arise either from agreement or by the operation of law, such as by inheritance.</i> |
| Implied agency | <i>A partner is the agent of the other partners.</i> | <i>A co-owner is not the agent of other co-owners.</i> |
| Nature of interest | <i>There is community of interest which means that profits and losses must have to be shared.</i> | <i>Co-ownership does not necessarily involve sharing of profits and losses.</i> |
| Transfer of interest | <i>A share in the partnership is transferred only by the consent of other partners.</i> | <i>A co-owner may transfer his interest or rights in the property without the consent of other co-owners.</i> |

Partnership vs. Association

| <i>Basis of difference</i> | <i>Partnership</i> | <i>Association</i> |
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| Meaning | <i>Partnership means and involves setting up relation of agency between two or more persons who</i> | <i>Association evolves out of social cause and there is no necessarily motive to</i> |



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| | <i>have entered into a business for gains, with the intention to share the profits of such a business.</i> | <i>earn and share profits. The intention is not to enter in a business for gains.</i> |
| Examples | <i>Partnership to run a business and earn profit thereon.</i> | <i>Members of charitable society or religious association or an improvement scheme or building corporation or a mutual insurance society or a trade protection association.</i> |

Kinds Of Partnerships

The following chart illustrates the various kinds of partnership:

1. Partnership at will according to Section 7 of the Act, partnership at will is a partnership when:

- 1. no fixed period has been agreed upon for the duration of the partnership; and*
- 2. there is no provision made as to the determination of the partnership.*

These two conditions must be satisfied before a partnership can be regarded as a partnership at will. But, where there is an agreement between the partners either for the duration of the partnership or for the determination of the partnership, the partnership is not partnership at will.

Where a partnership entered into for a fixed term is continued after the expiry of such term, it is to be treated as having become a partnership at will.

A partnership at will may be dissolved by any partner by giving notice in writing to all the other partners of his intention to dissolve the same.

2. Partnership for a fixed period: *Where a provision is made by a contract for the duration of the partnership, the partnership is called 'partnership for a fixed period'. It is a partnership created for a particular period of time. Such a partnership comes to an end on the expiry of the fixed period.*

3. Particular partnership: *A partnership may be organized for the prosecution of a single adventure as well as for the conduct of a continuous business. Where a person becomes a partner with another person in any particular adventure or undertaking the partnership is called 'particular partnership'. A partnership, constituted for a single adventure or undertaking is, subject to any agreement, dissolved by the completion of the adventure or undertaking.*



4. General partnership: Where a partnership is constituted with respect to the business in general, it is called a general partnership. A general partnership is different from a particular partnership. In the case of a particular partnership, the liability of the partners extends only to that particular adventure or undertaking, but it is not so in the case of general partnership. General partnership is different from limited liability partnership.

Partnership Deed

Partnership is the result of an agreement. No particular formalities are required for an agreement of partnership. It may be in writing or formed verbally. But it is desirable to have the partnership agreement in writing to avoid future disputes.

The document in writing containing the various terms and conditions as to the relationship of the partners to each other is called the 'partnership deed'. It should be drafted with care and be stamped according to the provisions of the Stamp Act, 1899. Where the partnership comprises immovable property, the instrument of partnership must be in writing, stamped and registered under the Registration Act.

Partnership deed may contain the following information: -

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| 1. Name of the partnership firm. |
| 2. Names of all the partners. |
| 3. Nature and place of the business of the firm. |
| 4. Date of commencement of partnership. |
| 5. Duration of the partnership firm. |
| 6. Capital contribution of each partner. |
| 7. Profit Sharing ratio of the partners. |
| 8. Admission and Retirement of a partner. |
| 9. Rates of interest on Capital, Drawings and loans. |
| 10. Provisions for settlement of accounts in the case of dissolution of the firm. |
| 11. Provisions for Salaries or commissions, payable to the partners, if any. |
| 12. Provisions for expulsion of a partner in case of gross breach of duty or fraud. |

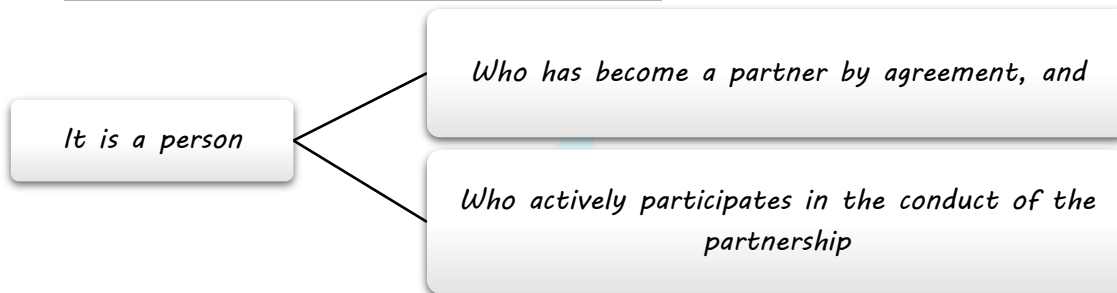


A partnership firm may add or delete any provision according to the needs of the firm.

Types Of Partners

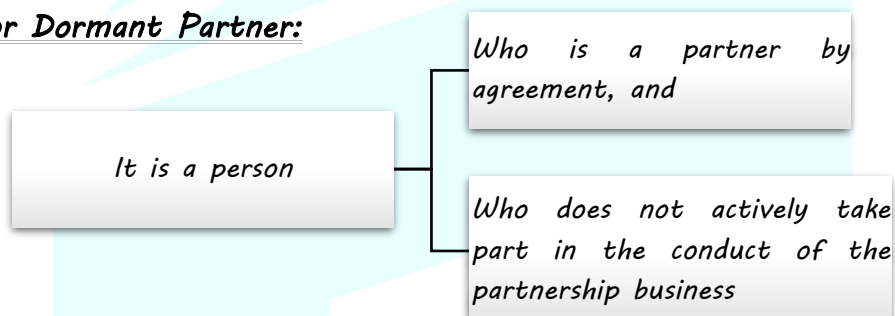
Based on the extent of liability, the different classes of partners are:

Active or Actual or Ostensible partner:



He acts as an agent of other partners for all acts done in the ordinary course of business. In the event of his retirement, he must give a public notice in order to absolve himself of liabilities for acts of other partners done after his retirement.

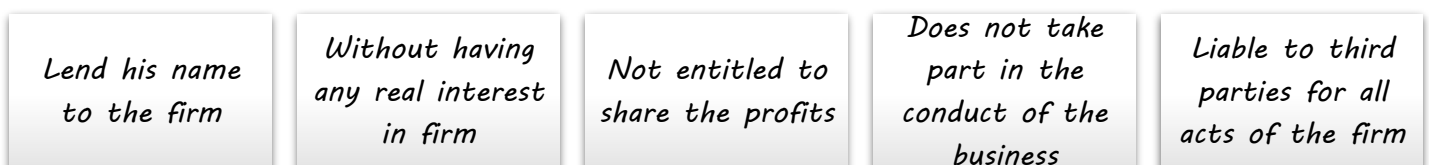
Sleeping or Dormant Partner:



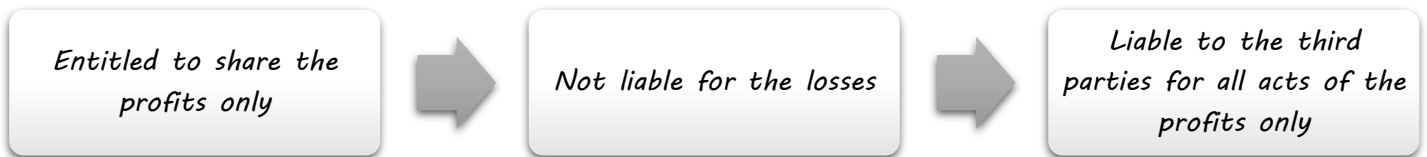
They are called as 'sleeping' or 'dormant' partners. They share profits and losses and are liable to the third parties for all acts of the firm. They are, however not required to give public notice of their retirement from the firm.

Nominal Partner: A person who lends his name to the firm, without having any real interest in it, is called a nominal partner.

He is not entitled to share the profits of the firm. Neither he invests in the firm nor takes part in the conduct of the business. He is, however liable to third parties for all acts of the firm.



Partner in profits only: A partner who is entitled to share the profits only without being liable for the losses is known as the partner for profits only and also liable to the third parties for all acts of the profits only.



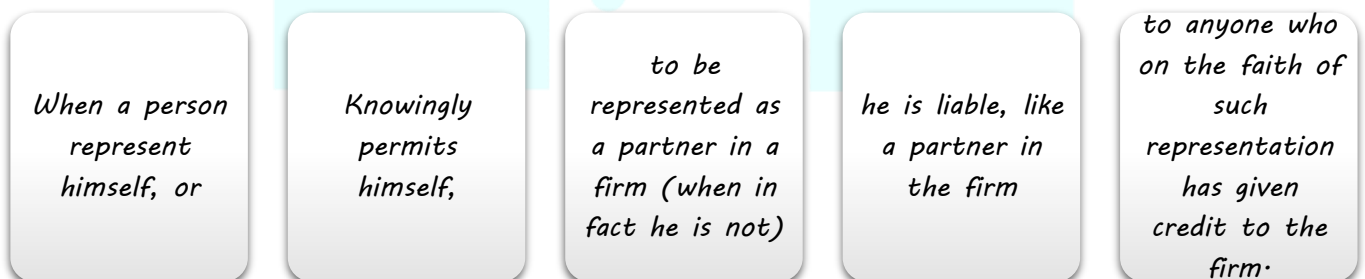
Incoming partners: A person who is admitted as a partner into an already existing firm with the consent of all the existing partners is called as “Incoming partner”.

Such a partner is not liable for any act of the firm done before his admission as a partner.

Example: Mr. A joined as a partner on 10th September, 2021 in a firm MNQ Associates which was existing from 10th July, 2017. Mr. A will not be liable for any acts of the firm done before his date of joining i.e. 10th September, 2021

Outgoing partner: A partner who leaves a firm in which the rest of the partners continue to carry on business is called a retiring or outgoing partner. Such a partner remains liable to third parties for all acts of the firm until public notice is given of his retirement.

Partner by holding out (Section 28): Partnership by holding out is also known as partnership by estoppel. Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.



A person may himself, by his words or conduct have induced others to believe that he is a partner or he may have allowed others to represent him as a partner. The result in both the cases is identical.



Example: X and Y are partners in a partnership firm. X introduced A, a manager, as his partner to Z. A remained silent. Z, a trader believing A as partner supplied 100 T.V sets to the firm on credit. After expiry of credit period, Z did not get amount of T.V sets sold to the partnership firm. Z filed a suit against X and A for the recovery of price. Here, in the given case, A, the Manager is also liable for the price because he becomes a partner by holding out (**Section 28, Indian Partnership Act, 1932**).

It is only the person to whom the representation has been made and who has acted thereon that has right to enforce liability arising out of 'holding out'. You must also note that for the purpose of fixing liability on a person who has, by representation, led another to act, it is not necessary to show that he was actuated by a fraudulent intention.

The rule given in **Section 28** is also applicable to a former partner who has retired from the firm without giving proper public notice of his retirement. In such cases a person who, even subsequent to the retirement, give credit to the firm on the belief that he was a partner, will be entitled to hold him liable.

Example: A partnership firm consisting of P, Q, R and S. S retires from the firm without giving public notice and his name continues to be used on letterheads. Here, S is liable as a partner by holding out to creditors who have lent on the faith of his being a partner.

