

## DUTIES OF PARTNERS

### 1. General Duties of Partners (Section 9)

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 representative.

### 2. Duty to indemnify for loss caused by fraud (Section 10)

Every partner shall indemnify the firm for any loss cause to it by his fraud in conduct of the business of the firm.

### 3. Duty not to carry on any other business (Section 11(2))

Notwithstanding anything contained in section 27 of the Indian Contract Act, the contract between the partners may provide that a partner shall not carry on business other than that of the firm while he is a partner.

### 4. Duty to work with due care and diligence (Section 12(b))

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

5. Application of the property of the firm (Section 15)  
subject to contract between the partners, the property of the firm shall be held and used by the partners exclusively for the purposes of the business. In partnership there is collective interest of all the partners in the property of the firm, but that does not mean that during the subsistence of the partnership a particular partner has any personal interest in the assets of the firm.

6. Duty to refund personal profit earned by partners (Section 16)

Subject to contract between partners:

→ 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 name, he shall repay it to firm.

→ If a partner carries on any business of the same nature as and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business.

Ex. A, B, C and D established partnership business for refining sugar. A, was himself a wholesaler grocer, was entrusted with the work of selection and purchase of sugar. As a wholesaler grocer, A was well aware of the variations in the sugar market and had the suitable sense of proprietary as regards purchase of sugar. He had already in stock

sugar purchased at low price which he sold to firm when it was in need of <sup>same</sup> some, without informing the partner that the sugar sold had belonged to him. It was held that A was bound to account to the firm for the profit so made by him.

Ex. A, B, C and D started a business in partnership for importing salt from foreign ports and selling it at Chittagong. A struck certain transactions in salt on his own account, which were found to be of the same nature as the business carried on by the partnership. It was held that A was liable to account to the firm for profits of the business so made by him. This rule is also subject to a contract between the partners.

### PARTNERSHIP PROPERTY (Section 14)

What constitutes a partnership property depends upon the agreement between the partners. 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.

They can convert by mutual agreement, partnership property into separate property of an individual partner and vice-versa. In the absence of any such agreement, the property of the firm according to section 14, means -

- (i) Property originally brought into the common stock of the firm by the partners.
- (ii) Property acquired <sup>in</sup> the course of the business with money belonging to the firm.
- (iii) The goodwill of the firm.

**NOTE:** Goodwill may be defined as the value of the reputation of a business house in respect of profits expected in future over and above the normal level of profits earned by undertaking belonging to the same class of business.

Property of a partner where the property is exclusively belonging to a person, it does not become a property of the partnership merely because it is used for the business of the partnership, such property will become property of the partnership if there is an agreement.

Application of the property of the firm (Section 15)  
 Subject to contract between the partners, the property of the firm shall be held and used by the partners exclusively for the purposes of the business. In partnership, there is collective interest of all the partners in the property of the firm, but that does not mean that during the subsistence of the partnership, a particular partner has any personal interest in the assets of the firm.

## PARTNERSHIP Vs CLUB

| BASIS               | PARTNERSHIP   | CLUB   |
|---------------------|---|--|
| 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 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 Partner | Has interest in the property of the firm.   | A member of a club has no interest in property of the club.  |
| Dissolution         | A change in the partners of the firm affects its existence.   | A change in the membership of a club does not affect its existence.  |

## PARTNERSHIP VS CO-OWNERSHIP

### Basic

### Partnership

### Co-ownership

#### Formation

Partnership always

Co-ownership may arise  
arises out of an agreement either from agreement or  
express or implied  
by the operation of law  
such as by inheritance.

#### Implied

A partner is the agent of the other partners. A co-owner is not  
an agency of other co-owners.

#### Nature of interest

There is collective interest which means that profits and losses must have to be shared.

#### Transfer of interest

A share in the partnership is transferred only by the consent of other partners.

A co-owner may transfer his interest or rights in the property without the consent of other co-owners.

## PARTNERSHIP Vs HUF (Hindu Undivided Family)

| Basis             | Partnership   | HUF  |
|-------------------|---|--|
| Mode of creation  | Partnership is created necessarily by an agreement.                             | The right in the joint family is created by birth 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 partner in HUF does not give rise to dissolution of 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 rests in the Karta, the governing male member or female member of the family.                       |
| Number of members | In case of partnership no. of members should not exceed 50.                     | Members of HUF who carry on a business may be unlimited in number.   |
| Persons called    | Persons forming a partnership are called partners.                              | Persons in HUF are called co-partners.   |
| Liability         | In a partnership, the liability of a partner is unlimited.                      | In a HUF, only the liability of the Karta is unlimited, & the other copartners are liable only to the extent of their share in profits of the family business. |

### Governing law

A partnership is governed by the Indian Partnership Act, 1932.

A HUF 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 HUF business, a minor becomes a member of the ancestral bus. by the incidence of birth. He does not have to wait for attaining majority.

### Share in

In a partnership, each partner has a definite share by virtue of an agreement between the partners.

In a HUF, no coparcener has 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.

## RIGHTS OF TRANSFEREE OF A PARTNER'S INTEREST (Sect 29&31)

A share in a partnership is transferable like any other property, but as the partnership relationship is based on mutual confidence, the assignee of a partner's interest by sale, mortgage or otherwise cannot enjoy the same rights & privileges as the original partner.

The rights of such a transferee are as follows:

During the continuance of partnership, such transferee is not entitled:

- to interfere with the conduct of the business.
- to require accounts, or
- to inspect books of the firm.

He is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e. he cannot challenge the accounts.

On the dissolution of the firm, <sup>or</sup> on the retirement of the transferring partner, the transferee will be entitled, against the remaining partners,

- to receive the share of the assets of the firm to which the transferring partner was entitled, and
- for the purpose of ascertaining the share, he is entitled to an account as from the date of the dissolution.

By virtue of section 31 - No person can be introduced as a partner in a firm without the consent of all the partners. A partner cannot by transferring his own interest, make anybody else a partner in his place, unless the other partners agree to accept that person as a partner.

DISSOLUTIONDissolution of Firms Section 39-47

| Basis                    | Dissolution of Firm  | Dissolution of Partnership  |
|--------------------------|--|---|
| Continuation of business | It involves discontinuation of business in partnership.        | It does not affect continuation of business.                        |
| Realisation/ Revaluation | It involves realisation of assets & settlement of liabilities. | It involves only revaluation of assets and liabilities of the firm. |
| Order of Court           | A firm may be dissolved by the order of the court.             | Dissolution of partnership is not ordered by the court.             |
| Scope                    | It necessarily involves dissolution of partnership.            | It may or may not involve dissolution of firm.                      |
| Final Closure of Books   | It involves final closure of books of the firm.                | It does not involve final closure of book of the firm.              |
| Example                  | Death, Business becomes unlawful etc.                          | Admission, change in PSR, Retirement, Death.                        |

According to section 39 of the Indian Partnership Act 1932, the dissolution of partnership between all partners of a firm is called the 'dissolution of the firm'.

MODES OF DISSOLUTION

1. without Court
2. By order of Court

## Dissolution of Firm

without the order  
of the Court (Sect. 40-43)

By order of the Court  
(Sect 44)

<sup>1</sup>Insanity <sup>2</sup>Misconduct <sup>3</sup>Permanent <sup>4</sup>Persistent <sup>5</sup>Transfer  
incapacity breach of of interest  
agreement

continuous just & loss equitable ground

By mutual agreement <sup>2</sup> Compulsory dissolution <sup>3</sup> On happening of certain event <sup>4</sup> By Notice (Sect. 43) (Sect 41) (Sect 42) (optional)

1. Without the order of the Court

## A. Dissolution by agreement (section 40)

Section 40 gives rights to the partners to dissolve the partnership by agreement with the consent of all the partners or in accordance with a contract between the partners.

## B Compulsory Dissolution (Section 41)

A firm is compulsorily dissolved by declaration.

- by the adjudication of all the partners or of all the partners ~~but~~<sup>except</sup> one as insolvent; or
  - by the happening of any event which makes it unlawful for the business of the firm to be carried on.

However, when more than one separate adventure or undertaking is carried on by the firm, the illegality of one or more shall not of itself cause the dissolution of the firm in respect of its lawful adventures and undertakings.

Example: A firm is carrying on the business of trading in chemical and a law is passed which bans on the trading of such chemical. The business of the firm becomes unlawful and so the firm will have to be compulsorily dissolved.

(C) Dissolution on happening of certain contingencies (Section 42)

Subject to contract between the partners, a firm can be dissolved on the happening of any of the following contingencies :

- (i) where the firm is constituted for a fixed term, on the expiry of that term.
- (ii) where the firm is constituted to carry out one or more adventures or undertaking, then by completion thereof.
- (iii) by the death of a partner, and
- (iv) by the adjudication of a partner as an insolvent.

D. Dissolution by notice of partnership at will (Sect. 43)

- (i) 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.

(ii) In case date is mentioned in the notice : The firm is dissolved as from the date mentioned in the notice as the date of dissolution, or in case no date is so mentioned, as from the date of the communication of the notice.

2. By order of the court (Section 44)  
Court may, at the suit of the partner, dissolve a firm on any of the following ground :

A. Insanity / unsound mind

Where a partner (not a sleeping partner) has become of unsound mind, the court may dissolve the firm on a suit of the other partners. Temporary sickness is no ground for dissolution of firm.

B. Permanent incapacity

When a partner, other than the partner suing, has become in any way permanently incapable of performing his duties as a partner, then the court may dissolve the firm. Such permanent incapacity may result from physical disability or illness etc.

C. Misconduct

Where a partner, other than the partner suing, is found guilty of misconduct. It is not necessary that misconduct must relate to the business. The important point is the adverse effect of misconduct on the business. In each case nature of business will decide whether an act is misconduct or not.

- D. Persistent breach of agreement  
 where a partner other than the suing wilfully or persistently commits breach of agreements relating to the management of the affairs of the firm or the conduct of its business.  
 Following comes into category of breach of contract:
- Holding more cash than allowed
  - Refusal to show accounts despite related request etc
  - Embezzlement (fraud)
  - Keeping erroneous accounts

Example If one of the partners keep erroneous accounts and omits to enter receipts or if there is continual quarrels between the partners, the court may order for dissolution of the firm.

- E. Transfer of interest  
 where a partner other than the partner suing, has transferred the whole of his interest in the firm to a third party, the court may dissolve the firm.  
 (By virtue of section 31) in such a way so as to constitute 3rd party as a partner in the firm

- F. Continuous/Repetual losses  
 where the business of the firm cannot be carried on except at a loss in future also, the court may order for its dissolution.

6. Just and equitable grounds  
Where the court considers any other ground to be just and equitable for the dissolution of the firm, it may dissolve a firm. The following are the cases for the just & equitable grounds:

- Deadlock in the management (Eg Retirement of another partner)
- Where the partners are not in talking terms between them. (Eg)
- Loss of substratum (Heavy losses will not affect the firm)
- Gambling by a partner on a stock exchange.

### ~~MINORS ADMITTED TO THE BENEFITS OF PARTNERSHIP~~

(Section 30)

|   |           |   |
|---|-----------|---|
| (Minor admitted in firm with the consent of all the partners) | 1 Jan, 15 | → Admitted for benefits of firm<br>→ Not as a partner in firm<br>→ Can claim his share in firm<br>→ Can file a suit on firm only when he serve his connections from firm. |
|---|-----------|---|

(Minor becomes major) 1 Jan, 22

2 options (6 Months)

- To opt as a partner
  - Profit same as minority
  - Liability - liable from 1 Jan 2015
- To quit the firm
  - Cancel all connections

1. A person who is minor cannot be a partner in a firm, but, with the consent of all the partners for the time being, he may be admitted to the benefits of partnership.

### 2. Rights

- (i) A minor partner has a right to his agreed share of the profits of the firm.
- (ii) He can have access to inspect & copy the accounts of the firm.
- (iii) He can sue the partners for accounts or for payment of his share but only when severing his connections with the firm, and not otherwise.
- (iv) On attaining majority he may within 6 months elect to become a partner or not to become a partner. If he elects to become a partner, then he is entitled to the share to which he was entitled as a minor. If he does not, then his share is not liable for any acts of the firm after the date of the public notice served to that effect.

### 3. Liabilities

- (i) Before attaining majority
  - a. The liability of a minor is confined only to the extent of his share in the profits and the property of the firm.
  - b. Minor has no personal liability for the debts of the firm incurred during his minority.

- C. Minor cannot be declared insolvent, but if the firm is declared insolvent his share in the firm vests in the Official Receiver / Assignee.
- (ii) After attaining Majority Within 6 months of his attaining majority the minor partner has to decide whether he shall remain a partner or leave the firm. Where he has elected not to become partner he may give public notice that he has elected not to become a partner and such notice shall determine his position as regards the firm. If he fails to give such notice he shall become a partner in the firm on the expiry of the said six months.
- (iii) Liabilities when he becomes a partner  
If the minor becomes a partner on his own willingness or by his failure to give the public notice within specified times, his rights & liabilities as given in Section 30(7) are as follows:
- He becomes personally liable to third parties for all acts of the firm done since he was admitted to benefits of partnership.
  - His share in the property and the profits of the firm remains the same to which he was entitled as a minor.

- (iv) When he elects not to become a partner
- His rights & liabilities continue to be those of a minor up to date of giving public notice.
  - His share shall not be liable for any acts of the firm done after the date of notice.
  - He shall be entitled to sue the partners for his share of the property & profits. It may be noted that such minor shall give notice to the Registrar that he has or has not become a partner.

### CONSEQUENCES OF DISSOLUTION (Section 45-49)

Consequent to the dissolution of a partnership firm, the partners have certain rights and liabilities, as are discussed :

- (I) Liability for acts of partners done after dissolution (Section 45)
- Notwithstanding the dissolution of a firm, the partners continue to be liable as such to third parties for any act done by any of them until public notice is given of the dissolution.
  - Provided that the estate of a partner who dies, or who is adjudicated an insolvent, or sleeping partner is not liable under this section for acts done after the date on which he ceases to be a partner.

Notices under sub-section (1) may be given by any partner.

Ex:

X and Y who carried on business in partnership for several years, executed on 1st December, a deed dissolving the partnership from the date, but failed to give a public notice of the dissolution. On 20th December X borrowed in the firm's name a certain sum of money from R, who was ignorant of the dissolution. In such case, Y also would be liable for the amount because no public notice was given.

However there are exceptions to the rule stated in above example i.e. even where notice of dissolution has not been given, there will be no liability for subsequent acts in the case of :

- the estate of a deceased partner
- an insolvent partner
- a dormant partner, i.e. a partner who was not known as a partner to the person dealing with the firm.

(II) Right of partners to have business wound up after dissolution (Section 46)

On the dissolution of a firm every partner or his representative is entitled, as against all the other partners or their representatives, to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners or their representatives according to their rights.

(III) Continuing authority of partners for purpose of winding up (Section 47)

After the dissolution of a firm the authority of each partner to bind the firm, and the other mutual rights and obligations of the partners, shall continue until winding up of the affairs of the firm in respect of transactions begun but unfinished at the time of the dissolution.

(IV) Mode of settlement of partnership accounts (Sect 48)

In settling the accounts of a firm after dissolution the following rules shall, subject to agreement by the partners, be observed:-

- Goodwill shall be included in the assets & it might be sold separately or along with other property of the firm.
- Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital and lastly if necessary, by the partners individually in the proportions in which they were entitled to share profits.
- The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, must be applied in the following manner & order:
  - in paying the debts of the firm to third parties
  - in paying to each partner what is due to him on account of capital and
  - the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits.

- (II) Payment of firm debts and of separate debts (Section 49)  
where there are joint debts due from the firm and also separate debts due from any partner:
- the property of the firm shall be applied in the first instance in payments of the debts of the firm, and if there is any surplus, then the share of each partner shall be applied to the payment of his separate debts or paid to him.
  - the separate property of any partner shall be applied first in the payment of his separate debts and surplus, if any, in the payment of debts of the firm.

#### EFFECT OF NOTICE TO ACTING PARTNER (Section 24)

According to Section 24 notice to a partner who habitually acts in the business of the firm of any matter relating to the affairs of the firm operates as notice to the firm, except in the case of a fraud on the firm committed by or with the consent of that partner.

Thus, the notice to one is equivalent to the notice to the rest of the partners of the firm, just as a notice to an agent is notice to his principal. It must be received by working partner & not by sleeping partner.

Date 1-1-

Eg. P, Q and R are partners in a business for purchase and sale of second hand goods. R purchases a second hand car on behalf of the firm from S. In the course of dealings with S, he comes to know that the car is a stolen one and it actually belongs to X. P & Q are ignorant about it. All the partners are liable to X, the real owner. (II)

### RIGHTS AND DUTIES OF PARTNER AFTER A CHANGE IN THE FIRM (Section 17)

It may occur in one of the four ways, namely

- where a new partner or partner comes in
- where some partner or partners go out i.e. by death or retirement
- where the partnership concerned carries on business other than the business for which it was originally formed.
- where the partnership business is carried on after the expiry of the term fixed for the purpose.

According to section 17, subject to contract between the partners:

After a change in the firm - where a change occurs in the constitution of a firm, the mutual rights & duties of the partners in the reconstituted firm remain the same as they were immediately before the change, as far as may be.

2. After the expiry of the term of the firm - where a firm constituted for a fixed term continues to carry on business after the expiry of that term, the mutual rights & duties of the partners remain the same as they were before the expiry.
3. Where additional undertakings are carried out - where a firm constituted to carry out one or more adventures or undertakings carries out other adventures or undertakings or are the same as those in respect of the original adventures or undertakings.
4. Section 22 mode of doing act to bind firm - In order to bind a firm, an act or instrument done or executed by a partner or other person on behalf of the firm shall be done or executed in the firm name.
5. Section 18 partner to be agent of the firm - Subject to the provisions of this Act a partner is the agent of the firm for the purpose of the business of the firm.
6. Section 19 Implied authority of partner as agent of the firm - Subject to the provisions of section 22, the acts of a partner which is done to carry on, usual business of the firm, binds the firm. The authority of a partner to bind the firm given under this section is called as "implied authority".  
The implied authority of a partner does not empower him to -

- (a) submit a dispute relating to the business of the firm to arbitration - (Panchayat)
- (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. (Compromise with creditors or debtors)
- (d) withdraw a suit or proceeding filed on behalf of the firm.
- (e) admit any liability in a suit or proceeding against the firm.
- (f) acquire immovable property on behalf of the firm.
- (g) transfer immovable property belonging to the firm.
- (h) enter into partnership on behalf of the firm.

Section 20 Extension & restriction of partners implied authority - The partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partner. Notwithstanding any such restriction, any act done by a partner on behalf of the firm which falls within his implied authority binds the firm, unless the person with whom he is dealing knows of the restriction or does not know or believe that partner to be a partner.

The act done must relate to the usual business of the firm, i.e., the act done by the partner must be within the scope of his authority & related to the normal business of the firm.

Eg. X, a partner in a firm of solicitors, borrows money and executes a promissory note in the name of firm without authority. The other partners are not liable on the note, as it is not part of ordinary business of a solicitor to draw, accept, or endorse negotiable instruments; however it may be usual for one partner of firm of bankers to draw, accept or endorse a bill of exchange on behalf of the firm.

### Section 21 Partner's authority in an emergency

A partner has authority, in an emergency, to do all such acts for the purpose of protecting the firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstances, & such acts binds the firm.

### LIABILITY TO THIRD PARTIES (Section 25-27)

It means every person who is partner at the time of contract is liable for such contract.

Eg. A, B & C were found to have been partners in a firm when the acts constituting an infringement of a trademark by the firm took place. Later on, C quit the firm. It was held that all partners (A, B, C) were liable for damages arising out of the alleged infringement.

Liability of a firm for wrongful acts of a partner (Section 26) - Where, by the wrongful act or omission of a partner in the ordinary course of the business of a firm, or with the authority of his partners, loss or injury is caused to any third party, or any penalty is incurred, the firm is liable therefore to the same extent as the partner.

Eg. ABC & co. is appointed as a manager of coal mines. He A during his visit at coal mine place his hand on trigger. As a result thereof, an injury was caused to a workman. The other partner was also held responsible for the same.

Liability of firm for misapplication by partners (Sect 27)

Where -

→ a partner acting within his apparent authority receives money or property from a third party and manipulates it, or

→ a firm in the course of its business receives money or property from a third party, and the money or property is misappropriated by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

Eg. A, B & C are partners of a place for car parking. P stands his car in the parking place but A sold out the car to a stranger. For this liability, the firm is liable for the acts of A. misappropriation