

BBA Semester IV

BBAHC-10

The Indian Partnership Act, 1932

1.1 The Indian Partnership Act 1932 defines a partnership as a relation between two or more persons who agree to share the profits of a business run by them all or by one or more persons acting for them all. As we go through the Act we will come across five essential elements that every partnership must contain. Let us have a look at Indian Partnership Act in detail.

1.2 True Test of Partnership

The Indian Partnership Act 1932 clearly defines a partnership. But how can we decide if a given association of persons is truly a partnership or not? So the Act has also given us a litmus test to determine if a firm is a partnership. This is known as the True Test of a Partnership. Let us study this.

True Test of a Partnership

The true test of a partnership is a way for us to determine whether a group or association of persons is a partnership firm or not. It also helps us recognize the partners of the firm and separate them from the third parties.

The idea behind such a true test is to examine the relevant facts and determine the real relations between parties and conclude about the presence of a partnership.

Let us take a look at the three important aspects of a true test of a partnership, namely agreement, profit sharing and mutual agency.

1] Agreement/Contract between Parties

For there to be a partnership between two or more persons there has to be an agreement of partnership between them. The partnership cannot arise family status or any operation of law. There has to be a specific agreement between the partners.

So if family members of a HUF are running a business together this is not a partnership. Because there is no agreement of partnership between them. The members of HUF are born into the HUF, so they cannot be partners.

2] Association of Two or More Persons

A partnership is an association between two or more persons. And persons by law only includes individuals, not other firms. The law also prohibits minors from being partners. But minors can be admitted to the benefits of a partnership.

The Act is actually silent on the maximum number of partners. But this has been covered under the Companies Act 2013. So a partnership can only have a maximum of 10 partners in a banking firm and 20 partners in all other kinds of firms.

3] Carrying on of Business

There are two aspects of this element. Firstly the firm must be carrying on some business. Here the business will include any trade, profession or occupation. Only that some business must exist and the partners must participate in the running of such business.

Also, the business must be run on a profit motive. The ultimate aim of the business should be to make gains, which are then distributed among the partners. So a firm carrying on charitable work will not be a partnership. If there is no intention to earn profits, there is no partnership.

4] Profit Sharing

The sharing of profits is one of the essential elements of a partnership. The profit sharing ratio or the manner of sharing profits is not important. But one partner cannot be entitled to the entire profits of the firm.

However, the sharing of losses is not of any essence. It is up to the partners whether the losses will be shared by all the partners. If nothing is said then the losses are also split in the profit sharing ratio.

Say for example two individuals are operating out of the same warehouse. So they agree to divide the rent amongst themselves. This is not a partnership since there is no profit sharing between the two.

5] Mutual Agency

The definition states that the business must be carried out by the partners, or any partner/s acting for all of them. This is a contract of mutual agency another one of the five elements of a partnership.

This means that every partner is both a principle as well as an agent for all the other partners of the firm. An act done by any of the partners is binding on all the other partners and the firm as well. And so every partner is bound by the acts of all the other partners. This is one of the most important aspects of a partnership. It is, in fact, the truest test of a partnership.

2.1 Kinds of Partnership

A partnership between two people is when they run a business together with the intention of sharing the profits amongst themselves. However, there can be various types of partnerships according to their duration or the intent of their creation. Let us take a look at the kinds of partnerships like a general partnership, partnership at will etc.

Kinds of Partnership

The distinction between partnerships can be done on the basis of two criteria. They are as follows

With Regard to the Duration of the partnership – either Partnership at Will or Partnership for Fixed Duration

With regards to the extent of the business carried by the partnership – either General Partnership or Particular Partnership

i] Partnership at Will

When forming a partnership if there is no clause about the expiration of such a partnership, we call it a partnership at will. According to Section 7 of the Indian Partnership Act 1932, there are two conditions to be fulfilled for a partnership to be a partnership at will. These are

There is no agreement about a fixed period for the existence of a partnership.

No provision with regards to the determination of a partnership

So if there is an agreement between the partners about the duration or the determination of the firm, this will not be a partnership at will. But if a partnership was entered into a fixed term and continues to operate beyond this term it will become a partnership at will from the expiration of this term.

ii] Partnership for a Fixed Term

Now during the creation of a partnership, the partners may agree on the duration of this arrangement. This would mean the partnership was created for a fixed duration of time.

Hence such a partnership will not be a partnership at will, it will be a partnership for a fixed term. After the expiration of such a duration, the partnership shall also end.

However, there may be cases when the partners continue their business even after the expiration of the duration. They continue to share profits and there is an element of mutual agency. Then in such a case, the partnership will now be a partnership at will.

ii] Particular Partnership

A partnership can be formed for carrying on continuous business, or it can be formed for one particular venture or undertaking. If the partnership is formed only to carry out one business venture or to complete one undertaking such a partnership is known as a particular partnership.

After the completion of the said venture or activity, the partnership will be dissolved. However, the partners can come to an agreement to continue the said partnership. But in the absence of this, the partnership ends when the task is complete.

iv] General Partnership

When the purpose for the formation of the partnership is to carry out the business, in general, it is said to be a general partnership.

Unlike a particular partnership in a general partnership the scope of the business to be carried out is not defined. So all the partners will be liable for all the actions of the partnership.

3.1 Partnership Firms registration procedure under Indian Partnership Act

According to the India Partnership Act 1932, there is no time limit as such for the registration of a firm. The firm can be registered on the date when it is incorporated or any such date after so. The requisite fees and fines must be paid. The procedure for such a registration is as follows,

a] Application to the Registrar of Firms in the prescribed form (Form A). Nowadays this facility is even available online. Such an application must contain certain basic details about the firm such as,

Name given to the Partnership firm

Any name can be given to a partnership firm as long as you fulfill the below-mentioned conditions:

The name shouldn't be too similar or identical to an existing firm doing the same business,

The name shouldn't contain words like emperor, crown, empress, empire or any other words which show sanction or approval of the government.

3.2 How should be the agreement between partners formed?

Partnership deed is an agreement between the partners in which rights, duties, profits shares and other obligations of each partner is mentioned.

Partnership deed can be written or oral, although it is always advisable to write a partnership deed to avoid any conflicts in the future.

Following details are required in a partnership deed:

3.2.1 A. General Details:

1. Name and address of the firm and all the partners
2. Nature of business
3. Date of starting of business Capital to be contributed by each partner
4. Capital to be contributed by each partner
5. Profit/loss sharing ratio among the partners

3.2.2 B. Specific Details:

Apart from these, certain specific clauses may also be mentioned to avoid any conflict at a later stage:

1. Interest on capital invested, drawings by partners or any loans provided by partners to firm
2. Salaries, commissions or any other amount to be payable to partners
3. Rights of each partner, including additional rights to be enjoyed by the active partners
4. Duties and obligations of all partners
5. Adjustments or processes to be followed on account of retirement or death of a partner or dissolution of firm.
6. Other clauses as partners may decide by mutual discussion

Is it necessary to register a partnership firm?

Indian Partnership Act, 1932 governs the partnerships. Registration of partnership firm is optional and at the discretion of the partners.

Registration of partnership firm may be done at any time – before starting a business or anytime during the continuation of partnership.

It is always advisable to register the firm since a registered firms enjoy special rights which aren't available to the unregistered firms.

4.How to register the partnership firm?

An application form along with fees is to be submitted to Registrar of Firms of the State in which firm is situated. The application has to be signed by all partners or their agents.

Documents to be submitted to Registrar are

Application for registration of partnership (Form 1)

Specimen of Affidavit

Certified original copy of Partnership Deed

Proof of principal place of business (ownership documents or rental/lease agreement)

If the registrar is satisfied with the documents, he will register the firm in Register of Firms and issue Certificate of Registration.

Register of Firms contains up-to-date information on all firms and can be viewed by anybody upon payment of certain fees.

5 Advantages of Registration:

The registration of a firm is not only advantageous for the firm but also for those who deal with it.

The following advantages are derived from the registration of a firm:

(i) Advantages to the Firm:

The firm gets a right to the third parties in civil suits for getting its rights enforced. In the absence of registration, the firm cannot sue outside partners in courts.

(ii) Advantages to Creditors:

A creditor can use any partner for recovering his money due from the firm. All partners whose names are given in the registration are personally responsible to the outsiders. So, creditors can recover their money from any partner of the firm.

(iii) Advantages to Partners:

The partners can approach a court of law against each other in case of dispute among partners. The partners can sue outside parties also for recovering their amounts, etc.

(iv) Advantages to Incoming Partners:

A new partner can fight for his rights in the firm if the firm is registered. If the firm is not registered then he will have to depend upon the honesty of other partners.

(v) Advantages of Outgoing Partners:

The registration of a firm benefits the outgoing partners in a number of ways.

6.1 Rights of Partners:

Broadly, the provisions of the Act regarding rights, duties and powers of partners are as under:

- (a) Every partner has a right to take part in the conduct and management of business.
- (b) Every partner has a right to be consulted and heard in all matters affecting the business of the partnership.
- (c) Every partner has a right of free access to all records, books and accounts of the business, and also to examine and copy them.
- (d) Every partner is entitled to share the profits equally.
- (e) A partner who has contributed more than the agreed share of capital is entitled to interest at the rate of 6 per cent per annum. But no interest can be claimed on capital.
- (f) A partner is entitled to be indemnified by the firm for all acts done by him in the course of the partnership business, for all payments made by him in respect of partnership debts or liabilities and for expenses and disbursements made in an emergency for protecting the firm from loss provided he acted as a person of ordinary prudence would have acted in similar circumstances for his own personal business.
- (g) Every partner is, as a rule, joint owner of the partnership property. He is entitled to have the partnership property used exclusively for the purposes of the partnership.
- (h) A partner has power to act in an emergency for protecting the firm from loss, but he must act reasonably.
- (i) Every partner is entitled to prevent the introduction of a new partner into the firm without his consent.
- (j) Every partner has a right to retire according to the Deed or with the consent of the other partners. If the partnership is at will, he can retire by giving notice to other partners.
- (k) Every partner has a right to continue in the partnership.
- (l) A retiring partner or the heirs of a deceased partner are entitled to have a share in the profits earned with the aid of the proportion of assets belonging to such outgoing partner or interest at six per cent per annum at the option of the outgoing partner (or his representative) until the accounts are finally settled.

6.2 Duties of Partners:

- (a) Every partner is bound to diligently carry on the business of the firm to the greatest common advantage. Unless the agreement provides, there is no salary.

- (b) Every partner must be just and faithful to the other partners.
- (c) A partner is bound to keep and render true, proper, and correct accounts of the partnership and must permit other partners to inspect and copy such accounts.
- (d) Every partner is bound to indemnify the firm for any loss caused by his willful neglect or fraud in the conduct of the business.
- (e) A partner must not carry on competing business, nor use the property of the firm for his private purposes. In both cases, he must hand over to the firm any profit or gain made by him but he must himself suffer any loss that might have occurred.
- (f) Every partner is bound to share the losses equally with the others.
- (g) A partner is bound to act within the scope of his authority.
- (h) No partner can assign or transfer his partnership interest to any other person so as to make him a partner in the business.

Dissolution of partnership firm is a process in which relationship between partners of firm is dissolved or terminated. If a relationship between all the partners of firm is dissolved then it is known as dissolution of firm. In case of dissolution of partnership of firm, the firm ceases to exist. This process includes the discarding and disposing of all the assets of firm or and settlements of accounts, assets, and liabilities. Learn more about Dissolution of partnership firm, legal provisions, and settlement of accounts.

7.1 Dissolution of Partnership Firm

As we know that after the dissolution of partnership firm the existing relationship between the partner's changes. But, the firm continues its activities. The dissolution of partnership takes place in any of the following ways:

Change in the existing profit sharing ratio.

Admission of a new partner

The retirement of an existing partner

Death of an existing partner

Insolvency of a partner as he becomes incompetent to contract. Thus, he can no longer be a partner in the firm.

On completion of a specific venture in case, the partnership was formed specifically for that particular venture.

On expiry of the period for which the partnership was formed.

7.2 Following are the ways in which dissolution of a partnership firm takes place:

1. Dissolution by Agreement

A firm may be dissolved if all the partners agree to the dissolution. Also, if there exists a contract between the partners regarding the dissolution, the dissolution may take place in accordance with it.

2. Compulsory Dissolution

In the following cases the dissolution of a firm takes place compulsorily:

Insolvency of all the partners or all but one partner as this makes them incompetent to enter into a contract.

When the business of the firm becomes illegal due to some reason.

When due to some event it becomes unlawful for the partnership firm to carry its business. For example, a partnership firm has a partner who is of another country and India declares war against that country, then he becomes an enemy. Thus, the business becomes unlawful.

3. When certain contingencies happen

The dissolution of the firm takes place subject to a contract among the partners, if:

The firm is formed for a fixed term, on the expiry of that term.

The firm is formed to carry out specific venture, on the completion of that venture.

A partner dies.

A partner becomes insolvent.

4. Dissolution by Notice

When the partnership is at will, the dissolution of a firm may take place if any one of the partners gives a notice in writing to the other partners stating his intention to dissolve the firm.

5. Dissolution by Court

When a partner files a suit in the court, the court may order the dissolution of the firm on the basis of the following grounds:

In the case where a partner becomes insane

In the case where a partner becomes permanently incapable of performing his duties.

When a partner becomes guilty of misconduct and it affects the firm's business adversely.

When a partner continuously commits a breach of the partnership agreement.

In a case where a partner transfers the whole of his interest in the partnership firm to a third party.

In a case where the business cannot be carried on except at a loss

When the court regards the dissolution of the firm to be just and equitable on any ground.