GOA

Judicial Services Exam

CIVIL JUDGE CADRE

High Court of Bombay

Volume - 3

GOA JUDICIAL SERVICES

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Indian Partnership Act

The Indian Partnership Act, 1932

Introduction

The Indian Partnership Act, 1932 is an act to define and amend the law relating to partnership. This act is based on the provisions of the English Partnership Act of 1890. This Act allows partnership between all kinds of people. A man may take his wife or daughter as a business partner.

The law relating to partnership was contained in Chapter XI (sections 239-266) of the Indian Contract Act, 1872. Those provisions were not found satisfactory, with the result that the said Chapter of the Indian Contract Act was repealed and the present Act was passed in the year 1932 with a view to make the law dearer and more satisfactory.

Extent:- The Indian Partnership Act, 1932 extends to the whole of India. The Act has been applied to Berar by the Berar Laws Act, 1941 (4 of 1941).

The Act has been extended to Dadra and Nagar Haveli by Reg. 6 of 1963, Sec. 2 and Sch. 1, to Pondicherry by Reg. 7 of 1963, Sec. 3 and Sch. 1, to Goa, Daman and Diu by Reg. 11 of 1963, Sec. 3 and Schedule and to Laccadive, Minicoy and Amindivi Islands by Reg. 8 of 1965, Sec.3 and Schedule.

The Preamble:- The preamble to the Act states as "an Act to define and amend the law relating to partnership",

The terms of the preamble to the Act cannot be serviced to qualify or cut down the language of some clause of the enacting provision to the Act which gives out the meaning of that clause clearly and unambiguously; In the matter of Ashraya, AIR 1991 Kant 10.

The Indian Partnership Act, 1932 is not exhaustive of all questions which can be raised in connection Act, with partnership, as it "defines and amends" and not codifies the law relating to partnership. This Act consolidates all the existing laws relating to partnership as it is clear from the preamble and sections 3 and 74 of the Act which expressly continue the un repealed law e.g., Contract Act, etc. in so far as they are inconsistent with the express provisions of this Act.

Partnership and Its Essential Elements

Section 4, Indian Partnership Act, 1932 provides "Definition of '*Partnership*'- 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".

Under the Partnership Act, three elements are necessary to constitute a Partnership

(1) There must be an agreement entered into by all the persons concerned:
(2) The agreement must be to share the profits of business, and
(3) The business must be carried on by all or any of the persons concerned acting for all.

These three elements relate to Firstly, the voluntary contractual nature of the partnership, Secondly, it gives the motive which leads to the formation of the firm. i.e. acquisition of gain Thirdly shows that the persons of the group who conduct the business do so as agents for all the persons in the group and are liable to account for all*; Raghunath Sahu v Trinath Das, AIR 1985 Ori 8(10)*

Further **section 6** of the Act provides that in determining whether a group of persons is or is not a firm, or whether a person is 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.

This section gives the main rule to be followed by the courts in determining the existence or non-existence of a partnership in a particular case.
The paramount rule is that regard must be had to the real intention of the parties as shown by all relevant facts taken together.

An agreement to share losses is not a necessary ingredient of partnership, *Mirza Mal Bhagwan Das v Ramesh*, AIR 1929. The mere fact that a person is to share profit only and not losses does not by itself militate against the presumption of partnership. Though sharing of losses of business may not be a fundamental condition of partnership, nevertheless it is a very important incident of relationship of partnership. Every man who has the share of profits of a trade ought also to bear his share of the loss in the same proportion as the profit in the absence of a contract to the contrary: *Pitchiah v. Subramanian AIR 1934 Mad 404.*

The Indian Partnership Act, 1932, does not make it essential that every partner must invest some capital in the shape of cash. It is open and lawful to the person entering into partnership to agree that one of them would devote himself entirely to the business of the firm and would not bring in any capital. Such an agreement is lawful*; Raghumal Khandelwal v. Offical Assignee of Calcutta, Al 1924 Cal 424.*

The following requirements have been summarized by the Supreme Court in *Dy. C.S.T. V. K. Kelukutty, (1915) 4 SCC 41* for a partnership firm.

(1) It is the result of an *agreement*.
(2) It is organised to carry on a *business.*
(3) The persons concerned agree to *share the profits* of the business.
(4) The business is to be carried *on by all or any of them* acting for all.

Partnership firm is not a legal entity, like a company. It is a group of individual partners, Comptroller and Auditor General v. Kamlesh, (2003) 2 5CC 349.

1. **Agreement**

   Section 5 declares that the relation of partnership arises from contract, not from status. It may be elementary in say that a partnership can arise only by an agreement between the parties concerned and in no other way, yet the point is important.

   It is one of those elements which clearly display the distinction between a partnership and other business relations like joint family carrying on business, which do arise by agreement, but are the result of statin, operation of law, succession or inheritance

Formal or Written Agreement-Not Necessary

It is, however, not necessary that there should be a very formal or written agreement.

An agreement to create a partnership may as well arise from the conduct of the parties concerned; Abdul v. Century Wood industry, AIR 1954 Mys 33

Deed of Partnership

When the partnership agreement is in writing, it is called the deed of partnership. Writing is not prescribed by the Partnership Act, not even for getting the firm registered under the Act with the Registrar of Firms.

But writing, known as "instrument of partnership" is necessary under the Income Tax Act, 1961 if the partners desire their firm to be assessed to income tax as such firm.

The stamp duty on the instrument would be in accordance with the Indian Stamp Act, 1899.

One of the chief advantages of getting the firm assessed is that working partners can be paid salary and thus the taxable income of the firm can be materially reduced.

However, the partners do not, by that reason alone, become employees or servants of the firm; *S Regional. Director, ESIC v. Ramanuja Match Industries, (1985) 1 SCC 218.*

Capital Contribution By Partners Not Necessary

The validity of a partnership firm does not depend upon capital contribution by partners. A person can become a partner without having to make any contribution towards the capital of the firm. A person may contribute his know-how, or intellectual property rights, or skill and experience or even sheer labour in consideration of becoming a partner; *Shivraj Reddy & Bras v. S. Raghu Rau Reddy, AIR 2002 NOC 120 (AP)* Contribution of tenanted premises may also be a good enough consideration. Such use of premises does not by itself amount to sub-letting; *Prakash Chand v. BhanChand, (1995) 2 Punj LR 147 (P&H).*

Devolution of Business

A partner died. The deed of partnership contained no clause to the effect that the surviving partners could carry on the business even after such eventuality. The firm inevitably became dissolved. The surviving partners continued the business. There was no proof of any fresh agreement of the business. It was held that the business so continued could not be regarded as the continuation of the earlier partnership; Shivraj Reddy & Bros. v. S. Raghu Rao Reddy, AIR 2002 NOC 120 (AP).

2. **Business**

   A partnership can exist in business and business alone. Section 2(b) only says that it "includes every trade, occupation and profession". This definition cannot be taken literally, because while every trade may be a business, every occupation or profession is not. Nor is there any judicial definition of the term.

   In Smith v. Anderson, (1880) 15 Ch D 247, JAMES LJ only said that the term business' must be taken in a practical sense, that is, in a sense in which men of business would use that term.

   Speaking broadly, it is taken to refer to any activity which if successful would result in profit. Where certain persons joined in the purchase of wheat (*Gibson v. Lupton, 9 Bing 297: (1832) 2 LJ CP 4*) and oil (*Coope v. Eyre, 1 B1 H 37: (1788) 2 RR 706*) with the intention of dividing and paying for it equally, it was held that, they being not interested in profit or loss, were not partners.

Where, on the other hand, two persons horsed a coach with their individual horses and shared the profits, this was held to be a business (Fremont v. Coupland, 2 Bing 170: (1824) 27 RR 575. The business must be of lawful nature. A partnership cannot be formed for an illegal purpose. An illegal purpose partnership becomes automatically dissolved under operation of law. No action lies between partners for dissolution or account, Foster v. Driscoll, (1929) 1 KB 470.

3. **Sharing of Profits**

   The word "partnership" is derived from the word "to part" which means "to divide". The division of profits is an essential condition of the existence of a partnership. There was a time when sharing of profits was considered to be the final word in the determination of the existence of a partnership.

   Every man who received any portion of the profits of a business had to incur therein the liability of a partner. This principle was laid down in *Grace v. Smith (1775) 2 Wm B1 997,* where the court said, "Every man who has a share of the profits of a trade, ought also to bear his share of the loss." This was approved in 1793 in Waugh v. Carter, (1793) 2 H Blacks 235; 1 Smith's LC.

   The section does not insist upon sharing of losses. Thus, a provision for loss sharing is not essential; *Walker West Development v. EJ, Emmett, (1978) 252 EG 1171 CA.*

4. **Mutual Agency**

   The definition of partnership **in Section 4** concludes with the words; "a business may be carried on by all or any of them acting for all". Thus, if the person carrying on the business acts not only for himself but for others also, so that they stand in the position of principals and agents, they are partners. This is the principle of Cox v. Hickman, (1860) 8 HLC 268.

Distinction Between Partnership and Joint Hindu Family Business

Definition:- Sir Frederick Pollock defines partnership as "the relation which subsists between persons who have agreed to share the profits of a business carried on by all, or any of them on behalf of all of them."

Section 4 of the Indian Partnership Act, 1932 states "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".

Joint Hindu Family Business

Before a business can be called a joint Hindu family business, three conditions must be satisfied i.e

(i) There must be a family within the meaning of Hindu law,
(ii) The business must be a family business meaning, one carried on for the benefit of all the members of the family to acquire profit,
(iii) The capital for the business must belong to the joint family, while such a family resembles a partnership in certain respects.

Section 5 lays down - Partnership not created by status-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 and wife carrying on business as such, are not partners in such business.

Thus, if the members of a joint Hindu family want to be governed by the provisions of the partnership act, they should enter into an agreement of partnership. Otherwise they will be simply governed by their personal law.

Partnership	Joint Hindu Family Business
1. An agreement is essential in the case of an ordinary partnership.	No agreement is necessary to constitute a joint family business.
2. In an ordinary partnership, the members have no interest by birth.	In an ancestral business, the members have an interest by birth.
3. Death of a partner has the effect of dissolving the partnership.	The death of any member of the joint Hindu family does not dissolve joint Hindu family business but his interest passes by survivorship and the business is carried on just as before.
4. In the ordinary partnership, each partner has to account to his co-partners for each and every paise he has spent over and above his legitimate share. A partner can ask for account of profit and loss.	There is no accounting between the members of a joint Hindu family firm and none of them can be made liable for the account of profit and loss.
5. Each partner is the agent of another partner so far as the dealings with third persons are concerned.	It is not so, in the case of joint family firms.
6. In an ordinary partnership, a partner can bind his co-partners by debts	The manager or karta of a joint Hindu family alone has implied authority to contract debts and pledge the credit and

borrowed by him in the ordinary course of business	the property of the family for the ordinary purposes of the family business. No other coparceners can do so. Such debts having been incurred in the course of a business are binding on the family property, including the interest of the minor coparceners therein.
7. In an ordinary partnership, the relation of partners arises out of a contract.	The coparceners are the joint owners of the family properly and their mutual rights are the result of survivorship.
8. Minors enjoy certain advantages under section 30 of the Indian Partnership Act.	The minor coparceners in the joint family trading firm can have no such advantages.

Distinction Between Partnership and Co-Ownership

Co-Ownership	Partnership
1. Co-ownership is not necessarily the result of an agreement.	Partnership is the result of an agreement.
2. There is no community of profit or losses in co-ownership.	In partnership, there is community of profits and losses.
3. A co-owner is never the agent, real or implied of the other co-owners.	A partner is the agent of the other partner.
4 A co-owner is at liberty to transfer his interest to a stranger against the wishes of the co-owners.	A partner is not entitled to transfer his interest to a third person so as to substitute him in his place.
5. A co-owner can have a partition of the property.	A partner has no right to get a partition of the partnership property in specie but on dissolution of the partnership, he can have it sold and the proceeds divided.
6. A co-owner has got no lien on the thing owned In common for outlay or expenses that may be due from others their share.	A partner has got such a lien.
7. Co-ownership does not necessarily exist for the sake of gain	Partnership exists for no other purpose but gain.

8. The remedies by way of account and otherwise, which one co-owner has against the other are in many important respects different from and less extensive than those, which one partner has against his co-partners.	A partner has more extensive remedies against his co-partners.

Distinction Between Partnership and Company

Partnership	Company
1. Partnership is a group of persons collectively called as partners and does not have a separate legal personality.	A company on the other hand, is a separate juristic entity and is distinct from its shareholders.
2 A partnership firm means all the partners put together. If the partners cease to be partners, the partnership firm gets dissolved.	A company being a person different from the members, the members may come and go but the company's life is not affected thereby.
3. A partner cannot substitute another person in his place unless all other partners agree to the same.	The shareholder of a company can transfer his share to anybody he likes.
4. On the death of a partner, his legal representatives do not get substituted in his place in partnership.	On the death of the member of the company, his legal representatives step into his shoes for the purpose of rights in the company,
5 The liability of the partners is unlimited.	The liability on the members of a company is limited.
6. The registration of a partnership is optional.	The registration of a company is compulsory.
7. Maximum number of partners can be 20 and 10, in the case of banking business.	There is no maximum limit for the number of members in a public limited company and in a private limited company the maximum limit is 50.
8. Decree against a firm can be executed against partners.	Decree against a company cannot be executed against share holders.

Partnership At Will

Section 7 of the Indian Partnership Act enumerates "Partnership at Will- Where provision is made by contract between the partners for the duration of their partnership, or for the determination of their partnership, the partnership is 'Partnership at will'."

Essentials of Partnership At Will:- A partnership is deemed to be a partnership at will if

(1) No period has been fixed by the partners for its duration, or
(2) There is no provision in the partnership agreement for its determination.

It is not necessary; however, that there should always be an express provision for the duration of the partnership or its determination and it is open to the court to decide whether any such stipulation could be inferred from an examination of the terms of the contract as a whole and the nature of the business to which it relates.

The conduct of the partners is also a relevant factor for consideration. The real test is the intention of the parties. The provisions relied on must be clearly inconsistent with the general right to dissolve a firm; *Karumuthu Thiagarajan Chettiar v. E. M. Muthappa Chettiar. AIR 1961 SC 1225.*

In a partnership-at-will the partnership-deed should not contain any provisions

(1) As to the duration of the partnership,
(2) For the determination of their partnership.

Where these provisions are absent or cannot be implied, then the partnership is at will; *Arunachalam & Co. v. M. Sadasivam, ATR 1985 Mad 354.*

A partnership-at-will can be dissolved by notice at any time. No notice by the retiring partner of his intention to retire is necessary. The intention to dissolve may be inferred from circumstances showing that the partner has in fact severed his interest from the concern; Amar Chand v. Jawahar Mal 32 IC 833.

The death of any partner operates to dissolve the partnership-at-will unless there is an agreement to for the contrary Tama Mal v Ganga Ram AIR 1925 Sind 103.

Implied Authority of A Partner and Its Limitations

Implied Authority of a Partner as Agent of The Firm

Section 19

Subject to the provisions of section 22, the act of a partner which is done to carry on, in the usual way, business of a kind carried on by the firm, binds the firm. The authority of a partner to bind the firm, conferred by this section, is called the implied authority.

Mode of Doing Act To Bind Firm

Section 22

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 or in any other manner expressing or implying an intention to bind the firm.

Section 19(1)

Read with section 22 provides that an act of a partner, done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm, provided the act is done in the firm's name, or in any manner expressing or implying an intention to bind the firm. Such an authority of a partner to bind the firm is called his implied authority.

A partner has, under the Act, authority to do certain acts in an emergency so as to bind the firm, but this arises from different considerations and cannot be said to form part of his implied authority.

Act Done, To Carry On, In The Usual Way

The question whether an act done by a partner is done to carry on, in the usual way, business of the kind carried on by the firm must evidently be determined by the nature of the business and by the practice of persons engaged in it. What is usual for one kind of business may be unusual for another. However, there are certain general rules which may be said to have been well established, vis-a-vis the implied authority of a partner to do certain acts.

A partner in a trading firm may thus be said to have implied authority to do the following acts on behalf of the firm:

(i) Every partner has implied authority to enter into all contracts usual in the ordinary course of business of the firm and to vary such contracts, if necessary. Thus, a partner may enter into contracts for the sale or purchase of goods in which the firm deals.

(ii) A partner can engage servants or agents or the services of any person, if necessary, for carrying on the business of the firm.
(iii) A partner can draw cheques in the name of the firm, but a partner in a non-trading firm cannot, in the exercise of his implied authority, bind his co-partners by giving a postdated cheque.
(iv) A partner has implied authority to adjust and settle accounts of partnership transactions with persons dealing with the firm. He cannot, however, release or compromise any claim or portion of a claim by the firm in the exercise of his implied authority. It is also not within the scope of a partner's implied authority to release or relinquish a debt due to the firm.
(v) Every partner has an implied authority to make a payment of a debt on behalf of the firm to any creditor of the firm.
(vi) A partner can accept a bill of exchange in respect of a debt due to the firm; he may, likewise, accept any security for a debt due to the firm.
(vii) A partner can assign a debt (actionable claim) due to the firm. He may also agree to the transfer of a debt due to the firm and agree to treat the transferee as a debtor to the firm
(viii) Partners in a trading firm have the power of borrowing money for the purposes of the firm, and bills or pro notes given by one of the partners of the firm for money borrowed will bind the firm. A partner in a non-trading firm has no implied authority to borrow money.
(ix) The implied authority of a partner in a trading firm to draw and accept bills of exchange is well recognized.

Some Examples of Implied Authority

The points concerning the scope of implied authority of a partner as established through cases may now be summarized: "If the partnership be of a general commercial nature, he may pledge or sell the partnership property; he may buy goods on account of the partnership; he may borrow money, contract debts, and pay debts; he may make, draw or accept cheques" (A passage in Story on agency, Section 124 as adopted by the Judicial Committee of the Privy Council in Bank of Australasia v. Berillal, (1847) 6 Moo PC 152 at 193) or otherwise deal with negotiable instruments on account of the firm. A partner of a trading or non-trading firm may buy or hire on credit the kind of goods that are used in the firm's business (Bond V. Gibson, (1808) 1 Camp 185: 10 RR 665). Thus, where a partner hired an elephant for the purpose of trapping wild elephants which was the business of the firm and the hired elephant died in the course of the operations, the firm was held liable. A partner may receive payments due to the firm and discharge the debtor even if the partner receiving payment misappropriates the money (Steady Salt, (1825) 3 Bing 101: 130 ER 453). A partner may engage servants for the purposes of business. A partner

may take a lease of premises on behalf of the firm or mortgage the assets of the firm, should that be necessary for purposes of business (JafferaliBhaloLakha v. Standard Bank of S. Africa, AIR 1928 PC 135: (1927) 107 IC 453) Where the nature of a firm's business did not warrant entering into a suretyship, the firm was held not liable for the act of a partner in giving a guarantee on behalf of the firm (Porbandar Commercial Coop Bank Ltd. v. BhanjLavji, (1985) 1 Guj LR 49).

In Banarseedas v. Ghulam Hussain, 13 MLJ 458, 463, the Judicial Committee of the Privy Council stated, "Every one of the partners in a mercantile firm of ordinary trading partnership is liable upon a bill drawn by a partner in the recognized trading name of the firm, for a transaction incidental to the business of the firm, although his name does not appear upon the face of the instrument, and although he be a sleeping and secret partner. The same rule applies to the making and endorsing of promissory notes by a partner."

Limitations of Implied Authority

Section 19(2) In the absence of any usage or custom of trade to the contrary, the implied authority of a partner does not empower him to firm 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 proceeding against the firm,
(f) Acquire immovable property on behalf of the firm,
(g) Transfer immovable property belonging to the firm, or
(h) Enter into partnership on behalf of the firm.

Extension and Restriction of Partner's Implied Authority [Section 20]

"The partners in the 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 section makes it clear that it is within the competence of partners to agree that a trusted partner should be authorized to do certain necessary acts in the conduct of the business of the firm, which would otherwise be in excess of the implied authority of a partner. Likewise, partners may agree to restrict the

activities of an inexperienced junior partner. For instance, partners may stipulate among themselves that only some of them shall enter into particular contracts or that as to certain contracts, none shall be liable except those by whom they are actually made.

Agreement between partners may also stipulate stringent terms which confer exclusive powers and control in favour of a financing managing partner, and with regard to the other partners as having been admitted as merely working partners'. However, third persons dealing with the firm without notice of such arrangements will not be affected in any way. On the other hand, a third party who deals with a partner knowing that his authority is restricted in respect of particular acts, cannot hold the firm liable in respect of those unauthorised acts.

So far as the restriction of authority of a partner is concerned, it does not affect the third parties dealing with the firm who have no knowledge of extension of authority; Cox v. Hickman, (1860) 8 HLC 268.

Statutory restrictions are imposed by Section 19(2). The sub-section lists a number of things that the implied authority of a partner does not empower him to do, without consulting the other partners. The section says that in the absence of any usage or custom of 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 (Luda Ram Ved Prakash v. Maharani of India, AIR 1989 Del 169),
(b) Open a banking account on behalf of the firm in his own name,
(c) Compromise or relinquish any claim or portion of claim by the firm (Chainraj v. Narayana swami, AIR 1982 Mad 326),
(d) Withdraw a suit or proceeding filed on behalf of the firm (Debt Dayal v. Baldeo Prasad, (1928) 50 All 982: AIR 1928 All 491),
(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 on behalf of the firm (Bina Murlidhar Hemdeo v. Kanhaiya Lokan Hemdev, (1999) 5 SCC 222: AIR 1999 SC 2171),
(h) Enter into partnership on behalf of the firm (But see Mann v. Darcy, [1968] 1 WLR 893),

These restrictions are effective against all the world, whether a particular person contracting with the firm has knowledge of them or not. The second kinds of restrictions are those that may be imposed by the partnership deed or any agreement between the partners.

Doctrine of Holding Out

Section 28 of the Indian Partnership Act, 1932 enumerates -

"Holding out-

1) Anyone 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, is liable as a partner in that firm to anyone who has on the faith of any such representation given credit to the firm, 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.
2) Where after a partner's death the business is continued in the old firm name, the continued use of that name or of the deceased partner's name as a part thereof shall not of itself make his legal representative or his estate liable for any act of the firm done after his death."

This section deals with the principle of holding out. In order to make a person liable as a partner under this section on the basis of the principle of holding out the following facts must be established

(1) That he by words spoken or written by conduct represented himself to be a partner or knowingly permitted himself to be represented as a partner, and
(2) That the person acting in the faith of such representation gave credit to the firm.

For the application of this rule it is not necessary that the person representing himself or represented to be a partner does not know that the representation has reached the person so given credit.

1. Representation

In order to make a person liable under the doctrine of holding out, it has to be proved that either he himself made a representation or knowingly permitted such a representation to be made by someone else. In other words, there has to be a representation by a person by words spoken or written or by his conduct that he is a partner in the firm.

Representation in any form indicating that a person is a partner in the firm will create the liability. Fraudulent intention to mislead another person is not required. Whether the liability for holding out exists or not depends not on the motive of the person making the representation but, on the fact, that a third party has given credit on the faith of the representation.