

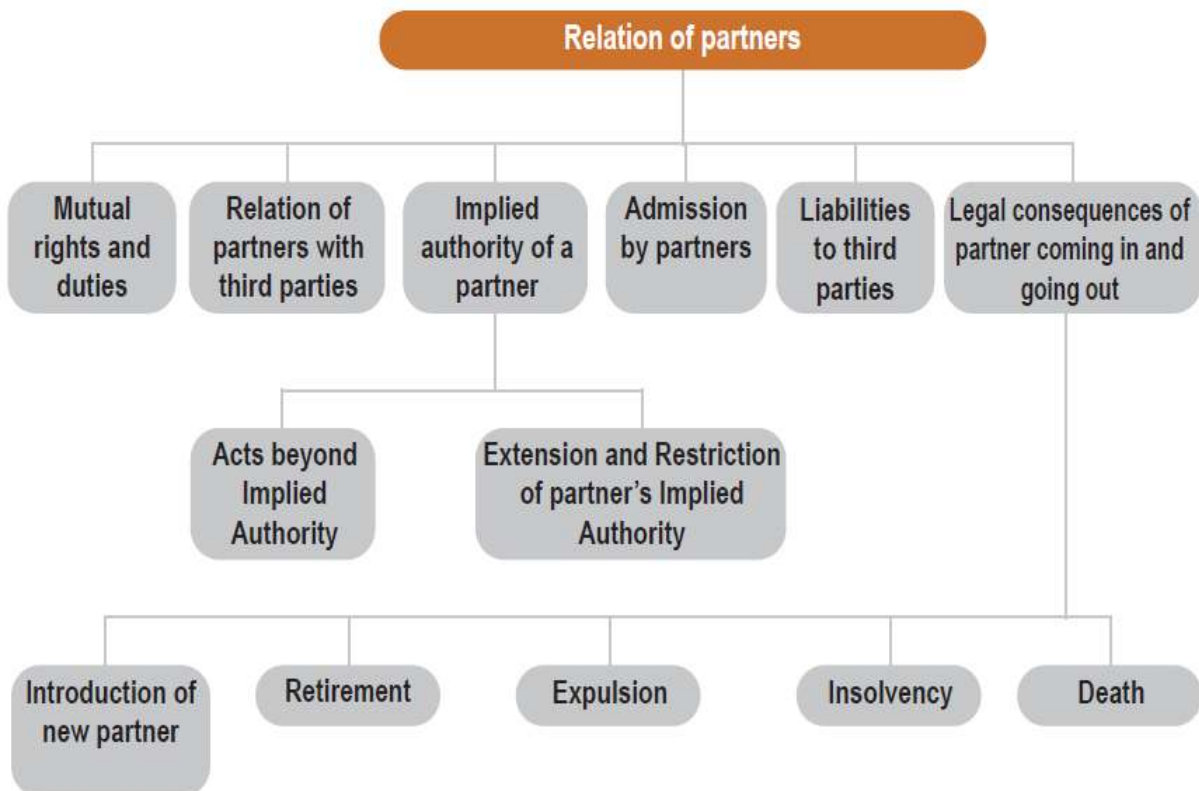
## UNIT – 2: RELATIONS OF PARTNERS

### LEARNING OUTCOMES

After studying this unit, you would be able to understand-

- ◆ Be familiar with the legal provisions regulating relation of partners' interest as well as relations with the third parties.
- ◆ Note the scope of implied authority of a partner to bind the partnership by his acts.
- ◆ Be aware of the various situations in which the constitution of a firm may change and its effect on the rights and duties of the partners.
- ◆ Learn how the share in a partnership is transferred and what shall be the rights and obligations of such transferee.

### UNIT OVERVIEW





## 2.1 RELATION OF PARTNERS TO ONE ANOTHER

The Partnership Act contains various provisions regulating the relationship between 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.

### Analysis of section 9:

The partners should carry business of the firm to the greatest common advantages and later, they should render to any partner or his legal representatives full information of all things affecting the firm. A partner must observe the utmost good faith in his dealings with the other partners.

All the partners are bound to render accounts to each other but where some of the accounts are kept by one of them, prima facie he would be the proper person to explain and give full information about them.

**Example 1:** In a transaction between partners for the sale and purchase of a share in the business, if one of them is better acquainted with the accounts than the other, it is his duty to disclose all material facts.

2. **DUTY TO INDEMNIFY FOR LOSS CAUSED BY FRAUD (SECTION 10):** Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

**Analysis of section 10:** The partner, committing fraud in the conduct of the business of the firm, must make good the loss sustained by the firm by his misconduct and the amount so brought in the partnership should be divided between the partners.

An act of a partner imputable to the firm or the principles of agency, which is a fraud on his co-partners, entitles the co-partners as between themselves, to throw the whole of the consequences upon him.

3. **DETERMINATION OF RIGHTS AND DUTIES OF PARTNERS BY CONTRACT BETWEEN THE PARTNERS (SECTION 11):**

- (1) Subject to the provisions of this Act, the mutual rights and duties of the partners of a firm may be determined by contract between the partners, and such contract may be express or may be implied by a course of dealing.

Such contract may be varied by consent of all the partners, and such consent may be express or may be implied by a course of dealing.

- (2) **Agreements in restraint of trade-** Notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such contracts may provide that a partner shall not carry on any business other than that of the firm while he is a partner.

### Analysis of section 11:

Section 11(1) provides that, subject of the provisions of the Act, the mutual rights and duties of the partners of a firm may be determined by contract between the partners and such contract may be express or may be implied by a course of dealing. It further provides that such contract may be varied by consent of all the partners.

Section 11(2) clearly provides that, 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 any business other than that of the firm while he is a partner.

Partnership is a relation eminently depending on the consent of the parties, not only for its existence, but for the terms of the agreement in all things consistent with its essential nature and purpose; and an agreement to become partners in the first instance, or to vary the terms at any time, need not be manifested in any particular form.

**4. THE CONDUCT OF THE BUSINESS (SECTION 12):** Subject to contract between the partners-

- (a) every partner has a right to take part in the conduct of the business;
- (b) every partner is bound to attend diligently to his duties in the conduct of the business;
- (c) any difference arising as to ordinary matters connected with the business may be decided by majority of the partners, and every partner shall have the right to express his opinion before the matter is decided, but no change may be made in the nature of the business without the consent of all partners; and
- (d) every partner has a right to have access to and to inspect and copy any of the books of the firm.
- (e) in the event of the death of a partner, his heirs or legal representatives or their duly authorised agents shall have a right of access to and to inspect and copy any of the books of the firm.

**Analysis of section 12**

- (i) **Right to take part in the conduct of the Business [Section 12(a)]:** Every partner has the right to take part in the business of the firm. This is because partnership business is a business of the partners and their management powers are generally co-extensive.

**Example 2:** Now suppose this management power of the particular partner is interfered with and he has been wrongfully precluded from participating therein. Can the Court interfere in these circumstances? The answer is in the affirmative. The Court can, and will, by injunction, restrain other partners from doing so. It may be noted in this connection that a partner who has been wrongfully deprived of the right of participation in the management has also other remedies, e.g., a suit for dissolution, a suit for accounts without seeking dissolution, etc.

The above mentioned provisions of law will be applicable only if there is no contract to the contrary between the partners. It is quite common to find a term in partnership agreements, which gives only limited power of management to a partner or a term that the management of the partnership will remain with one or more of the partners to the exclusion of others. In such a case, the Court will normally be unwilling to interpose with the management with such partner or partners, unless it is clearly made out that something was done illegally or in breach of the trust reposed in such partners.

- (ii) **Right to be consulted [section 12(c)]:** Where any difference arises between the partners with regard to the business of the firm, it shall be determined by the views of the majority of them, and every partner shall have the right to express his opinion before the matter is decided. But no change in the nature of the business of the firm can be made without the consent of all the partners. This means that in routine matters, the opinion of the majority of the partners will

prevail. Of course, the majority must act in good faith and every partner must be consulted as far as practicable.

It may be mentioned that the aforesaid majority rule will not apply where there is a change in the nature of the firm itself. In such a case, the unanimous consent of the partners is needed.

- (iii) **Right of access to books [Section 12 (d)]:** Every partner whether active or sleeping is entitled to have access to any of the books of the firm and to inspect and take out of copy thereof. The right must, however, be exercised *bona fide*.
- (iv) **Right of legal heirs/ representatives/ their duly authorised agents [Section 12(e)]:** In the event of the death of a partner, his heirs or legal representatives or their duly authorised agents shall have a right of access to and to inspect and copy any of the books of the firm.

**5. MUTUAL RIGHTS AND LIABILITIES (SECTION 13):** Subject to contract between the partners-

- (a) a partner is not entitled to receive remuneration for taking part in the conduct of the business;
- (b) the partners are entitled to share equally in the profits earned, and shall contribute equally to the losses sustained by the firm;
- (c) where a partner is entitled to interest on the capital subscribed by him such interest shall be payable only out of profits;
- (d) a partner making, for the purposes of the business, any payment or advance beyond the amount of capital he has agreed to subscribe, is entitled to interest thereon at the rate of six percent per annum;
- (e) the firm shall indemnify a partner in respect of payments made and liabilities incurred by him-
  - (i) in the ordinary and proper conduct of the business, and
  - (ii) in doing such act, in an emergency, for the purposes of protecting the firm from loss, as would be done by a person of ordinary prudence, in his own case, under similar circumstances;
- (f) a partner shall indemnify the firm for any loss caused to it by his wilful neglect in the conduct of business of the firm.

**Analysis of section 13**

- (i) **Right to remuneration [Section 13(a)]:** No partner is entitled to receive any remuneration in addition to his share in the profits of the firm for taking part in the business of the firm. But this rule can always be varied by an express agreement, or by a course of dealings, in which event the partner will be entitled to remuneration. Thus, a partner can claim remuneration even in the absence of a contract, when such remuneration is payable under the continued usage of the firm. In other words, where it is customary to pay remuneration to a partner for conducting the business of the firm he can claim it even in the absence of a contract for the payment of the same.
- (ii) **Right to share Profits [Section 13 (b)]:** Partners are entitled to share equally in the profits earned and so contribute equally to the losses sustained by the firm. The amount of a partner's share must be ascertained by enquiring whether there is any agreement in that behalf between

the partners. If there is no agreement then you should make a presumption of equality and the burden of proving that the shares are unequal, will lie on the party alleging the same.

There is no connection between the proportion in which the partners shall share the profits and the proportion in which they have contributed towards the capital of the firm.

- (iii) **Interest on Capital [Section 13 (c)]:** The following elements must be there before a partner can be entitled to interest on moneys brought by him in the partnership business: (i) an express agreement to that effect, or practice of the particular partnership or (ii) any trade custom to that effect; or (iii) a statutory provision which entitles him to such interest.
- (iv) **Interest on advances [Section 13 (d)]:** Suppose a partner makes an advance to the firm in addition to the amount of capital to be contributed by him, in such a case, the partner is entitled to claim interest thereon @ 6% per annum. While interest on capital account ceases to run on dissolution, the interest on advances keep running even after dissolution and up to the date of payment.
- (v) **Right to be indemnified [Section 13 (e)]:** Every partner has the right to be indemnified by the firm in respect of payments made and liabilities incurred by him in the ordinary and proper conduct of the business of the firm as well as in the performance of an act in an emergency for protecting the firm from any loss, if the payments, liability and act are such as a prudent man would make, incur or perform in his own case, under similar circumstances.
- (vi) **Right to indemnify the firm [Section 13 (f)]:** A partner must indemnify the firm for any loss caused to it by wilful neglect in the conduct of the business of the firm.



## 2.2 PARTNERSHIP PROPERTY (SECTION 14)

1. **THE PROPERTY OF THE FIRM (SECTION 14):** Subject to contract between the partners, the property of the firm includes all property and rights and interest in property originally brought into the stock of the firm, or acquired, by purchase or otherwise, by or for the firm, or for the purposes and in the course of the business of the firm, and includes also the goodwill of the business.

Unless the contrary intention appears, property and rights and interests in property acquired with money belonging to the firm are deemed to have been acquired for the firm.

### Analysis of section 14:

The expression 'property of the firm', also referred to as 'partnership property', 'partnership assets', 'joint stock', 'common stock' or 'joint estate', denotes all property, rights and interests to which the firm, that is, all partners collectively, may be entitled. The property which is deemed as belonging to the firm, in the absence of any agreement between the partners showing contrary intention, is comprised of the following items:

- (i) all property, rights and interests which partners may have brought into the common stock as their contribution to the common business;
- (ii) all the property, rights and interest acquired or purchased by or for the firm, or for the purposes and in the course of the business of the firm; and

(iii) Goodwill of the business.

The determination of the question whether a particular property is or is not 'property' of the firm ultimately depends on the real intention or agreement of the partners. Thus, the mere fact that the property of a partner is being used for the purposes of the firm shall not by itself make it partnership property, unless it is intended to be treated as such. Partners may, by an agreement at any time, convert the property of any partner or partners (and such conversion, if made in good faith, would be effectual between the partners and against the creditors of the firm) or the separate property of any partner into a partnership property.

**Goodwill:** Section 14 specifically lays down that the goodwill of a business is subject to a contract between the partners, to be regarded as 'property' of the 'firm'. But this Section does not define the term Goodwill.

'Goodwill' is a concept which is very easy to understand but difficult to define. 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.

When a partnership firm is dissolved every partner has a right, in the absence of any agreement to the contrary, to have the goodwill of business sold for the benefit of all the partners.

Goodwill is a part of the property of the firm. It can be sold separately or along with the other properties of the firm. Any partner may upon the sale of the goodwill of a firm, make an agreement with the buyer that such partner will not carry on any business similar to that of the firm within a specified period or within specified local limits and notwithstanding anything contained in Section 27 of the Indian Contract Act, 1872. Such agreement shall be valid if the restrictions imposed are reasonable.

**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.

2. **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.

**Analysis of section 15:**

Section 15 provides that the property of the firm shall be held and used exclusively for the purpose of the firm. In partnership, there is a community of interest which all the partners take in the property of the firm. But that does not mean that during the subsistence of the partnership, a particular partner has any proprietary interest in the assets of the firm. Every partner of the firm has a right to get his share of profits till the firm subsists and he has also a right to see that all the assets of the partnership are applied to and used for the purpose of partnership business.



## 2.3 PERSONAL PROFIT EARNED BY PARTNERS (SECTION 16)

**According to section 16,** subject to contract between the partners, -

- (a) 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 or the firm name, he shall account for that profit and pay it to the firm;

- (b) 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.

### Analysis of section 16

Where 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 or firm name, he must account for that profit and pay it to the firm.

**Example 3:** A, B, C & D established partnership business for refining sugar. A, who was himself a wholesale grocer, was entrusted with the work of selection and purchase of sugar. As a wholesale grocer, A was well aware of the variations in the sugar market and had the suitable sense of propriety as regards purchases of sugar. He had already in stock sugar purchased at a low price which he sold to the firm when it was in need of some, without informing the partners 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. This rule, however, is subject to a contract between partners.

Where a partner carries on a competing business, he must account for and pay to the firm all profits made by him in that business.

**Example 4:** 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.



## 2.4 RIGHTS AND DUTIES OF PARTNERS AFTER A CHANGE IN THE FIRM (SECTION 17)

Before going into rights and duties, we should first know how a change may take place in the constitution of the firm. It may occur in one of the four ways, namely,

<b>Where a new partner or partners come in</b>	
<b>Where some partner or partners go out, i.e., by death or retirement</b>	
<b>Where the partnership concerned carries on business other than the business for which it was originally formed</b>	
<b>Where the partnership business is carried on after the expiry of the term fixed for the purpose.</b>	

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

- (a) **after a change in the firm:** Where a change occurs in the constitution of a firm, the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change, as far as may be;
- (b) **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 and duties of the partners remain the same as

they were before the expiry, so far as they may be consistent with the incidents of partnership at will; and

- (c) **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 are the same as those in respect of the original adventures or undertakings.



## 2.5 RELATION OF PARTNERS TO THIRD PARTIES

1. **PARTNER TO BE AGENT OF THE FIRM (SECTION 18):** Subject to the provisions of this Act, a partner is the agent of the firm for the purposes of the business of the firm.

### Analysis of section 18:

You may recall that a partnership is the relationship between the partners who have agreed to share the profits of the business carried on by all or any of them acting for all (Section 4). This definition suggests that any of the partners can be the agent of the others.

**Section 18** clarifies this position by providing that, subject to the provisions of the Act, a partner is the agent of the firm for the purpose of the business of the firm. The partner indeed virtually embraces the character of both a principal and an agent. So far as he acts for himself and in his own interest in the common concern of the partnership, he may properly be deemed a principal and so far as he acts for his partners, he may properly be deemed as an agent.

The principal distinction between him and a mere agent is that he has a community of interest with other partners in the whole property and business and liabilities of partnership, whereas an agent as such has no interest in either.

The rule that a partner is the agent of the firm for the purpose of the business of the firm cannot be applied to all transactions and dealings between the partners themselves. It is applicable only to the act done by partners for the purpose of the business of the firm.

2. **IMPLIED AUTHORITY OF 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 the kind carried on by the firm, binds the firm.

The authority of a partner to bind the firm conferred by this section is called his “implied authority”.

- (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-
- (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 proceedings filed on behalf of the firm;
  - (e) admit any liability in a suit or proceedings against the firm;
  - (f) acquire immovable property on behalf of the firm;



- (g) transfer immovable property belonging to the firm; and
- (h) enter into partnership on behalf of the firm.

**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.

**Analysis of section 19 and 22:**

At the very outset, you should understand what is meant by “implied authority”. You have just read that every partner is an agent of the firm for the purpose of the business thereof. Consequently, as between the partners and the outside world (whatever may be their private arrangements between themselves), each partner is agent of every other in every matter connected with the partnership business; his acts bind the firm.

Sections 19(1) and 22 deal with the implied authority of a partner. The impact of these Sections is that the act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm binds the firm, provided that the act is done in the firm name, or 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. It is however subject to the following restrictions:

1. The act done must relate to the usual business of the firm, that is, the act done by the partner must be within the scope of his authority and related to the normal business of the firm.
2. The act is such as is done for normal conduct of business of the firm. The usual way of carrying on the business will depend on the nature and circumstances of each particular case [Section 19(1)].
3. The act to be done in the name of the firm or in any other manner expressing or implying an intention to bind the firm (Section 22).

Thus, a partner has implied authority to bind the firm by all acts done by him in all matters connected with the partnership business and which are done in the usual way and are not in their nature beyond the scope of partnership. You must remember that an implied authority of a partner may differ in different kinds of business.

**Example 5:** 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 the 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.

If partnership be of a general commercial nature,

- (i) he may pledge or sell the partnership property;
- (ii) he may buy goods on account of the partnership;
- (iii) he may borrow money, contract debts and pay debts on account of the partnership;

- (iv) he may draw, make, sign, endorse, transfer, negotiate and procure to be discounted, Promissory notes, bills of exchange, cheques and other negotiable papers in the name and on account of the partnership.

Section 19(2) contains the acts which are beyond the implied authority of the partners.

### 3. EXTENSION AND RESTRICTION OF PARTNERS' IMPLIED AUTHORITY (SECTION 20):

**According to Section 20**, the partners in a firm may, by contract between the partners, extend or restrict the implied authority of any partners.

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.

#### Analysis of section 20:

The implied authority of a partner may be extended or restricted by contract between the partners. Under the following conditions, the restrictions imposed on the implied authority of a partner by agreement shall be effective against a third party:

1. The third party knows about the restrictions, and
2. The third party does not know that he is dealing with a partner in a firm.

**Example 6:** A, a partner, borrows from B ₹ 1,000 in the name of the firm but in excess of his authority, and utilizes the same in paying off the debts of the firm. Here, the fact that the firm has contracted debts suggests that it is a trading firm, and as such it is within the implied authority of A to borrow money for the business of the firm. This implied authority, as you have noticed, may be restricted by an agreement between him and other partners. Now if B, the lender, is unaware of this restriction imposed on A, the firm will be liable to repay the money to B. On the contrary, B's awareness as to this restriction will absolve the firm of its liability to repay the amount to B.

It may be noted that the above-mentioned extension or restriction is only possible with the consent of all the partners. Any one partner, or even a majority of the partners, cannot restrict or extend the implied authority.

### 4. PARTNER'S AUTHORITY IN AN EMERGENCY (SECTION 21)

**According to section 21**, 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, and such acts bind the firm.



## 2.6 EFFECT OF ADMISSIONS BY A PARTNER (SECTION 23)

**According to Section 23**, an admission or representation made by a partner concerning the affairs of the firm is evidence against the firm, if it is made in the ordinary course of business.

#### Analysis of Section 23:

Partners, as agents of each other can make binding admissions but only in relation to partnership transaction and in the ordinary course of business. An admission or representation by a partner will not however, bind the

firm if his authority on the point is limited and the other party knows of the restriction. The section speaks of admissions and representations being evidenced against the firm. That is to say, they will affect the firm when tendered by third parties; they may not have the same effect in case of disputes between the partners themselves.

**Example 7:** X and Y are partners in a firm dealing in spare parts of different brands of motorcycle bikes. Z purchases a spare part for his Yamaha motorcycle after being told by X that the spare part is suitable for his motorcycle. Y is ignorant about this transaction. The spare part proves to be unsuitable for the motorcycle and it is damaged. X and Y both are responsible to Z for his loss.



## 2.7 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.

### Analysis of section 24:

The notice to a partner, who habitually acts in business of the firm, on matters relating to the affairs of the firm, operates as a 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. This notice must be actual and not constructive. It must be received by a working partner and not by a sleeping partner. It must further relate to the firm's business. Only then it would constitute a notice to the firm.

**Example 8:** 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 and Q are ignorant about it. All the partners are liable to X, the real owner.

The only exception would lie in the case of fraud, whether active or tacit.

**Example 9:** A, a partner who actively participates in the management of the business of the firm, bought for his firm, certain goods, while he knew of a particular defect in the goods. His knowledge as regards the defect, *ordinarily*, would be construed as the knowledge of the firm, though the other partners in fact were not aware of the defect. But because A had, in league with his seller, conspired to conceal the defect from the other partners, the rule would be inoperative and the other partners would be entitled to reject the goods, upon detection by them of the defect.



## 2.8 LIABILITY TO THIRD PARTIES (SECTION 25 TO 27)

The question of liability of partners to third parties may be considered under different heads. These are as follows:

1. **LIABILITY OF A PARTNER FOR ACTS OF THE FIRM (SECTION 25):** Every partner is liable, jointly with all the other partners and also severally, for all acts of the firm done while he is a partner.

**Analysis of section 25:**

The partners are jointly and severally responsible to third parties for all acts which come under the scope of their express or implied authority. This is because that all the acts done within the scope of authority are the acts done towards the business of the firm.

The expression 'act of firm' connotes any act or omission by all the partners or by any partner or agent of the firm, which gives rise to a right enforceable by or against the firm. Again in order to bring a case under Section 25, it is necessary that the act of the firm, in respect of which liability is brought to be enforced against a partner, must have been done while he was a partner.

**Example 10:** Certain persons were found to have been partners in a firm when the acts constituting an infringement of a trademark by the firm took place, it was held that they were liable for damages arising out of the alleged infringement, it being immaterial that the damages arose after the dissolution of the firm.

2. **LIABILITY OF THE 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 therefor to the same extent as the partner.

**Analysis of section 26:**

The firm is liable to the same extent as the partner for any loss or injury caused to a third party by the wrongful acts of a partner, if they are done by the partner while acting:

- (a) in the ordinary course of the business of the firm
- (b) with the authority of the partners.

If the act in question can be regarded as authorized and as falling within either of the categories mentioned in Section 26, the fact that the method employed by the partner in doing it was unauthorized or wrongful would not affect the question. Furthermore, all the partners in a firm are liable to a third party for loss or injury caused to him by the negligent act of a partner acting in the ordinary course of the business.

**Example 11:** One of the two partners in coal mine acted as a manager was guilty of personal negligence in omitting to have the shaft of the mine properly fenced. As a result thereof, an injury was caused to a workman. The other partner was also held responsible for the same.

3. **LIABILITY OF FIRM FOR MISAPPLICATION BY PARTNERS (SECTION 27):**

Where-

- (a) a partner acting within his apparent authority receives money or property from a third party and misapplies it, or
- (b) a firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss.

**Analysis of section 27:**

It may be observed that the workings of the two clauses of Section 27 is designed to bring out clearly an important point of distinction between the two categories of cases of misapplication of money by partners.

Clause (a) covers the case where a partner acts within his authority and due to his authority as partner, he receives money or property belonging to a third party and misapplies that money or property. For this provision to be attracted, it is not necessary that the money should have actually come into the custody of the firm.

On the other hand, the provision of clause (b) would be attracted when such money or property has come into the custody of the firm and it is misapplied by any of the partners.

The firm would be liable in both the cases.

If receipt of money by one partner is not within the scope of his apparent authority, his receipt cannot be regarded as a receipt by the firm and the other partners will not be liable, unless the money received comes into their possession or under their control.

**Example 12:** A, B, and 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.



## 2.9 RIGHTS OF TRANSFEREE OF A PARTNER'S INTEREST (SECTION 29)

- (1) A transfer by a partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee, during the continuance of the firm, to interfere in the conduct of business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.
- (2) If the firm is dissolved or if the transferring partner ceases to be a partner, the transferee is entitled as against the remaining partners to receive the share of the assets of the firm to which the transferring partner is entitled, and, for the purpose of ascertain that share, to an account as from the date of the dissolution.

**Analysis of section 29:**

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 and privileges as the original partner.

The rights of such a transferee are as follows:

- (I) During the continuance of partnership, such transferee is not entitled:
  - (a) to interfere with the conduct of the business,
  - (b) to require accounts, or
  - (c) 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.

- (II) On the dissolution of the firm or on the retirement of the transferring partner, the transferee will be entitled, against the remaining partners:
- (a) to receive the share of the assets of the firm to which the transferring partner was entitled, and
  - (b) 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, which we will discuss hereinafter, 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. At the same time, a partner is not debarred from transferring his interest. A partner's interest in the partnership can be regarded as an existing interest and tangible property which can be assigned.



## 2.10 MINORS ADMITTED TO THE BENEFITS OF PARTNERSHIP (SECTION 30)

- (1) A person who is a minor according to the law to which he is subject may not 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) Such minor has right to such share of the property and of the profits of the firm as may be agreed upon and he may have access to and inspect and copy any of the accounts of the firm.
- (3) Such minor's share is liable for the acts of the firm, but the minor is not personally liable for any such act.
- (4) Such minor may not sue the partners for an account or payment of his share of the property or profits of the firm, save when severing his connection with the firm, and in such case the amount of his share shall be determined by a valuation made as far as possible in accordance with the rules contained in Section 48:

Provided that all the partners acting together or any partner entitled to dissolve the firm upon notice to other partners may elect in such suit to dissolve the firm, and thereupon the Court shall proceed with the suit as one for dissolution and for settling accounts between the partners, and the amount of the share of the minor shall be determined along with the shares of the partners.

- (5) At any time within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, such person may give public notice that he has elected to become or that he has elected not to become a partner in the firm, and such notice shall determine his position as regards the firm.

Provided that, if he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months.

- (6) Where any person has been admitted as a minor to the benefits of partnership in a firm, the burden of proving the fact that such person had no knowledge of such admission until a particular date after the expiry of six months of his attaining majority shall lie on the persons asserting that fact.

- (7) Where such person becomes a partner,-
- (a) his right and liabilities as a minor continue up to the date on which he becomes a partner, but he also becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership, and
  - (b) his share in the property and profits of firm shall be the share to which he was entitled as a minor.
- (8) Where such person elects not to become a partner-
- (a) his rights and liabilities shall continue to be those of a minor under this section up to the date on which he gives public notice,
  - (b) his share shall not be liable for any acts of the firm done after the date of the notice, and
  - (c) he shall be entitled to sue the partners for his share of the property and profits in accordance with sub-section (4).
- (9) Nothing in sub-sections (7) and (8) shall affect the provisions of section 28.

#### Analysis of section 30:

You have observed that a minor cannot be bound by a contract because a minor's contract is void and not merely voidable. Therefore, a minor cannot become a partner in a firm because partnership is founded on a contract. Though a minor cannot be a partner in a firm, he can nonetheless be admitted to the benefits of partnership under Section 30 of the Act. In other words, he can be validly given a share in the partnership profits. When this has been done and it can be done with the consent of all the partners then the rights and liabilities of such a partner will be governed under Section 30 as follows:

#### (1) Rights:

- (i) A minor partner has a right to his agreed share of the profits and of the firm.
- (ii) He can have access to, inspect and 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 connection 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.

#### (2) Liabilities:

##### (i) Before attaining majority:

- (a) The liability of the 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 or on his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, 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 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.

- (a) **When he becomes partner:** If the minor becomes a partner on his own willingness or by his failure to give the public notice within specified time, his rights and liabilities as given in Section 30(7) are as follows:

- (i) He becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.
- (ii) His share in the property and the profits of the firm remains the same to which he was entitled as a minor.

(b) **When he elects not to become a partner:**

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



## 2.11 LEGAL CONSEQUENCES OF PARTNER COMING IN AND GOING OUT (SECTION 31 – 35)

Any change in the relation of partners will result in reconstitution of the partnership firm. Thus, on admission of a new partner or retirement of a partner or expulsion of the partner, or on insolvency of a partner etc. a firm will be reconstituted:

(i) **INTRODUCTION OF A PARTNER (SECTION 31):**

- (1) Subject to contract between the partners and to the provisions of section 30, no person shall be introduced as a partner into a firm without the consent of all the existing partners.
- (2) Subject to the provisions of section 30, a person who is introduced as a partner into a firm does not thereby become liable for any acts of the firm done before he became a partner.



**Analysis of section 31:**

As we have studied earlier, subject to a contract between partners and to the provisions regarding minors in a firm, no new partners can be introduced into a firm without the consent of all the existing partners.

**Rights and liabilities of new partner:** The liabilities of the new partner ordinarily commence from the date when he is admitted as a partner, unless he agrees to be liable for obligations incurred by the firm prior to the date. The new firm, including the new partner who joins it, may agree to assume liability for the existing debts of the old firm, and creditors may agree to accept the new firm as their debtor and discharge the old partners. The creditor's consent is necessary in every case to make the transaction operative. Novation is the technical term in a contract for substituted liability, of course, not confined only to case of partnership.

But a mere agreement amongst partners cannot operate as Novation. Thus, an agreement between the partners and the incoming partner that he shall be liable for existing debts will not ipso facto give creditors of the firm any right against him.

**In case of partnership of two partners:** This section does not apply to a partnership of two partners which is automatically dissolved by the death of one of them.

**(ii) RETIREMENT OF A PARTNER (SECTION 32):**

- (1) A partner may retire:
  - (a) with the consent of all the other partners;
  - (b) in accordance with an express agreement by the partners; or
  - (c) where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire.
- (2) A retiring partner may be discharged from any liability to any third party for acts of the firm done before his retirement by an agreement made by him with such third party and the partners of the reconstituted firm, and such agreement may be implied by a course of dealing between the third party and the reconstituted firm after he had knowledge of the retirement.
- (3) Notwithstanding the retirement of a partner from a firm, he and the partners continue to be liable as partners to third parties for any act done by any of them which would have been an act of the firm if done before the retirement, until public notice is given of the retirement:

Provided that a retired partner is not liable to any third party who deals with the firm without knowing that he was a partner.
- (4) Notices under sub-section (3) may be given by the retired partner or by any partner of the reconstituted firm.

**Analysis of section 32:**

A partner is said to retire when he ceases to be a member of the firm without bringing to an end the subsisting relations between the other members, or between the firm and third parties. The term does not cover the case where a partner withdraws from a firm by dissolving it, which should properly be referred as a dissolution and not as a retirement. Retirement of a partner from a firm does not dissolve it.

***Vishnu Chandra Vs. Chandrika Prasad [Supreme Court]***

The Supreme Court in *Vishnu Chandra Vs. Chandrika Prasad*, held that the expression 'if any partner wants to dissociate from the partnership business', in a clause of the partnership deed which was being construed, comprehends a situation where a partner wants to retire from the partnership. The expression clearly indicated that in the event of retirement, the partnership business will not come to an end.

**Example 13:** Mere retirement of a partner, who was the tenant of the premises in which the partnership business was carried out, would not result in assignment of the tenancy rights in favour of the remaining partners even though the retiring partner ceases to have any right, title or interest in the business as such.

**Liabilities of an outgoing partner:** As we have already stated earlier, a retiring partner continues to be liable to third party for acts of the firm after his retirement until public notice of his retirement has been given either by himself or by any other partner. But the retired partner will not be liable to any third party if the latter deals with the firm without knowing that the former was partner.

The liability of a retired partner to the third parties continues until a public notice of his retirement has been given. As regards the liability for acts of the firm done before his retirement, the retiring partner remains liable for the same, unless there is an agreement made by him with the third party concerned and the partners of the reconstituted firm. Such an agreement may be implied by a course of dealings between the third party and the reconstituted firm after he had knowledge of the retirement.

If the partnership is at will, the partner by giving notice in writing to all the other partners of his intention to retire will be deemed to be relieved as a partner without giving a public notice to this effect.

**(iii) EXPULSION OF A PARTNER (SECTION 33):**

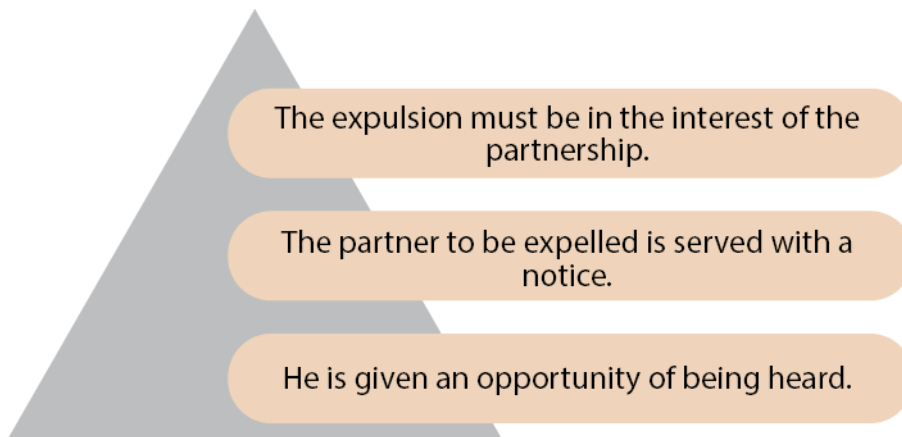
- (1) A partner may not be expelled from a firm by any majority of the partners, save in the exercise in good faith of powers conferred by contract between the partners.
- (2) The provisions of sub-section (2), (3) and (4) of section 32 shall apply to an expelled partner as if he were a retired partner.

**Analysis of section 33:**

- (i) the power of expulsion must have existed in a contract between the partners;
- (ii) the power has been exercised by a majority of the partners; and
- (iii) it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in bona fide interest of the business of the firm.

The test of good faith as required under Section 33(1) includes three things:



If a partner is otherwise expelled, the expulsion is null and void.

It may be noted that under the Act, the expulsion of partners does not necessarily result in dissolution of the firm. The invalid expulsion of a partner does not put an end to the partnership even if the partnership is at will and it will be deemed to continue as before.

**Example 14:** A, B and C are partners in a Partnership firm. They were carrying their business successfully for the past several years. Spouses of A and B fought in ladies club on their personal issue and A's wife was hurt badly. A got angry on the incident and he convinced C to expel B from their partnership firm. B was expelled from partnership without any notice from A and C. Considering the provisions of Indian Partnership Act, 1932 state whether they can expel a partner from the firm?

A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners. It is, thus, essential that:

- (i) the power of expulsion must have existed in a contract between the partners;
- (ii) the power has been exercised by a majority of the partners; and
- (iii) it has been exercised in good faith.

If all these conditions are not present, the expulsion is not deemed to be in bonafide interest of the business of the firm.

Thus, according to the test of good faith as required under Section 33(1), expulsion of Partner B is not valid.

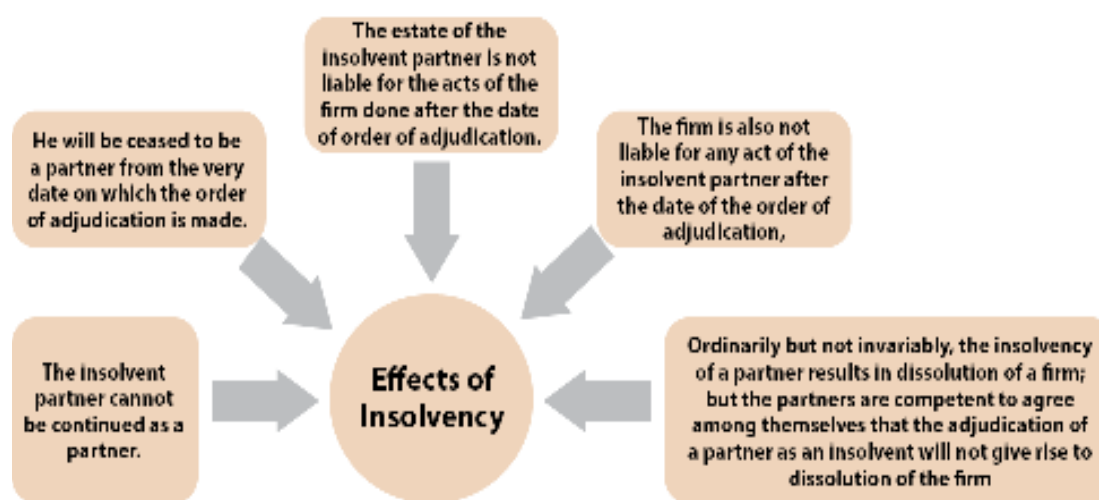
In this context, you should also remember that provisions of Sections 32 (2), (3) and (4) which we have just discussed, will be equally applicable to an expelled partner as if he was a retired partner.

**(iv) INSOLVENCY OF A PARTNER (SECTION 34):**

- (1) Where a partner in a firm is adjudicated as an insolvent he ceases to be a partner on the date on which the order of adjudication is made, whether or not the firm is hereby dissolved.
- (2) Where under a contract between the partners the firm is not dissolved by the adjudication of a partner as an insolvent, the estate of a partner so adjudicated is not liable for any act of the firm and the firm is not liable for any act of the insolvent, done after the date on which the order of adjudication is made.

**Analysis of section 34:**

When a partner in a firm is adjudicated an insolvent, he ceases to be a partner on the date of the order of adjudication whether or not the firm is thereby dissolved. His estate (which thereupon vests in the official assignee) ceases to be liable for any act of the firm done after the date of the order, and the firm also is not liable for any act of such a partner after such date (whether or not under a contract between the partners the firm is dissolved by such adjudication).



- (v) **LIABILITY OF ESTATE OF DECEASED PARTNER (SECTION 35):** Where under a contract between the partners, the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death.

**Analysis of section 35:**

Ordinarily, the effect of the death of a partner is the dissolution of the partnership, but the rule in regard to the dissolution of the partnership, by death of partner is subject to a contract between the parties and the partners are competent to agree that the death of one will not have the effect of dissolving the partnership as regards the surviving partners unless the firm consists of only two partners. In order that the estate of the deceased partner may be absolved from liability for the future obligations of the firm, it is not necessary to give any notice either to the public or the persons having dealings with the firm.

**Example 15:** X was a partner in a firm. The firm ordered goods in X's lifetime; but the delivery of the goods was made after X's death. In such a case, X's estate would not be liable for the debt; a creditor can have only a personal decree against the surviving partners and a decree against the partnership assets in the hands of those partners. A suit for goods sold and delivered would not lie against the representatives of the deceased partner. This is because there was no debt due in respect of the goods in X's lifetime.



## 2.12 RIGHTS OF OUTGOING PARTNER TO CARRY ON COMPETING BUSINESS (SECTION 36)

An outgoing partner may carry on business competing with that of the firm and he may advertise such business, but subject to contract to the contrary, he may not,-

- (a) use the firm name,
- (b) represent himself as carrying on the business of the firm or
- (c) solicit the custom of persons who were dealing with the firm before he ceased to be a partner.

**Agreement in restraint of trade-** (2) A partner may make an agreement with his partners that on ceasing to be a partner he will not carry on any business similar to that of the firm within a specified period or within specified local limits and, notwithstanding anything contained in section 27 of the Indian Contract Act, 1872, such agreement shall be valid if the restrictions imposed are reasonable.

### Analysis of section 36:

Although this provision has imposed some restrictions on an outgoing partner, it effectively permits him to carry on a business competing with that of the firm. However, the partner may agree with his partners that on his ceasing to be so, he will not carry on a business similar to that of the firm within a specified period or within specified local limits. Such an agreement will not be in restraint of trade if the restraint is reasonable [Section 36(2)]. A similar rule applies to such an agreement of sale of the firm's goodwill [Section 53(3)].



## 2.13 RIGHT OF OUTGOING PARTNER IN CERTAIN CASES TO SHARE SUBSEQUENT PROFITS (SECTION 37)

**According to section 37,** Where any member of a firm has died or otherwise ceased to be partner, and the surviving or continuing partners carry on the business of the firm with the property of the firm without any final settlement of accounts as between them and the outgoing partner or his estate, then, in the absence of a contract to the contrary, the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since he ceased to be a partner as may be attributable to the use of his share of the property of the firm or to interest at the rate of six per cent per annum on the amount of his share in the property of the firm:

**Provided that** whereby contract between the partners, an option is given to surviving or continuing partners to purchase the interest of a deceased or outgoing partner, and that option is duly exercised, the estate of the deceased partner, or the outgoing partner or his estate, as the case may be, is not entitled to any further or other share of profits; but if any partner assuming to act in exercise of the option does not in all material respects comply with the terms thereof, he is liable to account under the foregoing provisions of this section.

### Analysis of section 37:

Section 37 deals with rights of outgoing partners. It lays down a substantial law relating to a liability of the surviving or continuing partner, who without a settlement of accounts with legal representatives of the deceased partner utilizes the assets of partnership for continuing the business.

Although the principle applicable to such cases is clear but at times some complicated questions arise when disputes are raised between the outgoing partner or his estate on the one hand and the continuing or surviving partners on the other in respect of subsequent business. Such disputes are to be resolved keeping in view the facts of each case having regard to section 37.

**Example 16:** A, B and C are partners in a manufacture of machinery. A is entitled to three-eighths of the partnership property and profits. A becomes bankrupt whereas B and C continue the business without paying out A's share of the partnership assets or settling accounts with his estate. A's estate is entitled to three-eighths of the profits made in the business, from the date of his bankruptcy until the final liquidation of the partnership affairs.

**Example 17:** A, B and C are partners. C retires after selling his share in the partnership firm. A and B fail to pay the value of the share to C as agreed to. The value of the share of C on the date of his retirement from the firm would be pure debt from the date on which he ceased to be a partner as per the agreement entered between the parties. C is entitled to recover the same with interest.



## 2.14 REVOCATION OF CONTINUING GUARANTEE BY CHANGE IN FIRM (SECTION 38)

According to section 38, a continuing guarantee given to a firm or to third party in respect of the transaction of a firm is, in the absence of an agreement to the contrary, revoked as to future transactions from the date of any change in the constitution of the firm.

### Analysis of section 38:

Mere changes in the constitution of the firm operates to revoke the guarantee as to all future transactions. Such change may occur by the death, or retirement of a partner, or by introduction of a new partner.

## SUMMARY

The mutual rights and duties of partners are regulated by the contract between them. Such contract need not always be expressed, it may be implied from the course of dealing between the partners (Section 11). Section 12 gives rules regulating the conduct of the business by the partners and Section 13 lay down rules of mutual rights and liabilities. Sections 14 to 17 also contain particular rules which become useful and important while determining the relations of partners to one - another. What is essential to note, however, is that all these rules are subject to contract between the parties.

As regards third parties, a partner is the agent of the firm for all purposes within the scope of the partnership concern. His rights, powers, duties and obligations are in many respects governed by the same rules and principles which apply to the agent. Generally, he may pledge or sell the partnership property; he may buy goods on account of the firm; he may borrow money, contract debt and pay debts on account of the firm; he may draw, make, sign, endorse, accept, transfer, negotiate and get discounted promissory notes, bills of exchange, cheques and other negotiable papers in the name and account of the firm. The implied authority of the partner to bind the firm is restricted to acts usually done in the business of the kind carried on by the firm. He is also empowered under the Act to do certain acts in an emergency so as to bind the firm. The firm, however, is bound only by those acts of a partner which were done by him in his capacity as a partner.

A partner may in some circumstances become liable on equitable grounds for obligations incurred by a co-partner in doing acts in excess of his authority, real or implied. He may also become liable for an unauthorized act of his co-partner on the ground of estoppel.

## TEST YOUR KNOWLEDGE

### Multiple Choice Questions

1. A partner can be expelled if:
  - (a) Such expulsion is in good faith
  - (b) The majority of the partner does not agree on such expulsion
  - (c) The expelled partner is given an opportunity to start a business competing with that of the firm
  - (d) Compensation is paid
2. Which of the following is not the right of partner i.e., which he cannot claim as a matter of right?
  - (a) Right to take part in business
  - (b) Right to have access to account books
  - (c) Right to share profits
  - (d) Right to receive remuneration.
3. Which of the following acts are not included in the implied authority of a partner?
  - (a) To buy or sell goods on accounts of partners.
  - (b) To borrow money for the purpose of firm.
  - (c) To enter into partnership on behalf of firm.
  - (d) To engage a lawyer to defend actions against firm.
4. The reconstitution of the firm takes place in case of
  - (a) Admission of a partner
  - (b) Retirement of a partner
  - (c) Expulsion or death of a partner
  - (d) All of the above
5. A new partner can be admitted in the firm with the consent of
  - (a) All the partners
  - (b) Simple majority of partners
  - (c) Special majority of partners
  - (d) New partner only.
6. A partner may be expelled from the firm on the fulfilment of the conditions that the expulsion power is exercised.
  - (a) As given by express contract
  - (b) By majority of partners
  - (c) In absolute good faith
  - (d) All of the above

7. A minor is:
- (a) A partner of a firm
  - (b) Representative of the firm
  - (c) Entitled to carry on the business of the firm
  - (d) Entitled to the benefits of the firm
8. If a partner commits fraud in the conduct of the business of the firm:
- (a) He shall indemnify the firm for any loss caused to it by his fraud
  - (b) He is not liable to the firm.
  - (c) He is liable to the partners
  - (d) He is liable to the third parties
9. Partners are bound to carry on the business of the firm-
- (a) To the greatest common advantage
  - (b) For the welfare of the society
  - (c) For the advantage of the family members
  - (d) For earning personal profits
10. The liability of a minor partner is limited to the extent of:
- (a) His share in the firm
  - (b) His personal assets
  - (c) His share in the firm as well as his personal assets
  - (d) He is not liable
11. The authority of a partner to bind the firm for his acts as contained in section 19 of the Partnership Act is known as:
- (a) Express authority
  - (b) Legal authority
  - (c) Implied authority
  - (d) Managerial authority
12. Which are the matters that require unanimous consent of all the partners:
- (a) Admission of a partner
  - (b) Transfer by a partner of his interest in the firm
  - (c) Fundamental change in the nature of the business
  - (d) All of the above
13. For admitting a minor into the benefits of the partnership, which of the following is required?
- (a) Consent of the minor's guardian
  - (b) Consent of the Registrar of firms
  - (c) Consent of all the partners of the firm
  - (d) All of the above
14. The implied authority of a partner of the firm does empower him to:
- (a) Open a bank account on behalf of the firm in his own name.
  - (b) Enter into partnership on behalf of the firm.



- (c) Acquire immovable property on behalf of the firm.
- (d) Act expressing or implying an intention to bind the firm.
15. In case of transfer of share in a partnership firm by one partner to any third party give such third party entitlement:
- (a) to interfere with the conduct of the business.
- (b) to require accounts.
- (c) to receive the share of the profits of the transferring partner as agreed by the partners.
- (d) to receive the share of the profits of the transferring partner whether or not agreed by the partners.

### Answers to MCQs

1.	(a)	2.	(d)	3.	(c)	4.	(d)	5.	(a)
6.	(d)	7.	(d)	8.	(a)	9.	(a)	10.	(a)
11.	(c)	12.	(d)	13.	(c)	14.	(d)	15.	(c)

### Descriptive Questions

- State the modes by which a partner may transfer his interest in the firm in favour of another person under the Indian Partnership Act, 1932. What are the rights of such a transferee?
- Whether a minor may be admitted in the business of a partnership firm? Explain the rights of a minor in the partnership firm.
- M/s XYZ & Associates, a partnership firm with X, Y, Z as senior partners were engaged in the business of carpet manufacturing and exporting to foreign countries. On 25th August, 2018, they inducted Mr. G, an expert in the field of carpet manufacturing as their partner. On 10th January 2020, Mr. G was blamed for unauthorized activities and thus expelled from the partnership by united approval of rest of the partners.
  - Examine whether action by the partners was justified or not?
  - What should have the factors to be kept in mind prior expelling a partner from the firm by other partners according to the provisions of the Indian Partnership Act, 1932?
- A, B and C are partners in a firm. As per terms of the partnership deed, A is entitled to 20 percent of the partnership property and profits. A retires from the firm and dies after 15 days. B and C continue business of the firm without settling accounts. Explain the rights of A's legal representatives against the firm under the Indian Partnership Act, 1932?
- Master X was introduced to the benefits of partnership of M/s ABC & Co. with the consent of all partners. After attaining majority, more than six months elapsed and he failed to give a public notice as to whether he elected to become or not to become a partner in the firm. Later on, Mr. L, a supplier of material to M/s ABC & Co., filed a suit against M/s ABC & Co. for recovery of the debt due.

In the light of the Indian Partnership Act, 1932, explain:

- (i) To what extent X will be liable if he failed to give public notice after attaining majority?
  - (ii) Can Mr. L recover his debt from X?
6. Mr. A (transferor) transfer his share in a partnership firm to Mr. B (transferee). Mr. B is not entitled for few rights and privileges as Mr. A (transferor) is entitled therefor. Discuss in brief the points for which Mr. B is not entitled during continuance of partnership?

### Answers to the Descriptive Questions

1. Section 29 of the Indian Partnership Act, 1932 provides that 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 and privileges as the original partner.

The rights of such a transferee are as follows:

- (1) During the continuance of partnership, such transferee is not entitled
  - (a) to interfere with the conduct of the business,
  - (b) to require accounts, or
  - (c) 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.

- (2) On the dissolution of the firm or on the retirement of the transferring partner, the transferee will be entitled, against the remaining partners:
  - (a) to receive the share of the assets of the firm to which the transferring partner was entitled, and
  - (b) 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. At the same time, a partner is not debarred from transferring his interest. A partner's interest in the partnership can be regarded as an existing interest and tangible property which can be assigned.

2. A minor cannot be bound by a contract because a minor's contract is void and not merely voidable. Therefore, a minor cannot become a partner in a firm because partnership is founded on a contract. Though a minor cannot be a partner in a firm, he can nonetheless be admitted to the benefits of partnership under Section 30 of the Act. In other words, he can be validly given a share in the partnership profits. When this has been done and it can be done with the consent of all the partners then the rights and liabilities of such a partner will be governed under Section 30 as follows:

**Rights:**

- (i) A minor partner has a right to his agreed share of the profits and of the firm.
- (ii) He can have access to, inspect and 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 connection 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. Expulsion of a Partner (Section 33 of the Indian Partnership Act, 1932):**

A partner may not be expelled from a firm by a majority of partners except in exercise, in good faith, of powers conferred by contract between the partners.

The test of good faith as required under Section 33(1) includes three things:

- The expulsion must be in the interest of the partnership.
- The partner to be expelled is served with a notice.
- He is given an opportunity of being heard.

If a partner is otherwise expelled, the expulsion is null and void.

- (i) Action by the partners of M/s XYZ & Associates, a partnership firm to expel Mr. G from the partnership was justified as he was expelled by united approval of the partners exercised in good faith to protect the interest of the partnership against the unauthorized activities charged against Mr. G. A proper notice and opportunity of being heard has to be given to Mr. G.
- (ii) The following are the factors to be kept in mind prior expelling a partner from the firm by other partners:
  - (a) the power of expulsion must have existed in a contract between the partners;
  - (b) the power has been exercised by a majority of the partners; and
  - (c) it has been exercised in good faith.

**4. Section 37 of the Indian Partnership Act, 1932 provides that where a partner dies or otherwise ceases to be a partner and there is no final settlement of account between the legal representatives of the deceased partner or the firms with the property of the firm, then, in the absence of a contract to the contrary, the legal representatives of the deceased partner or the retired partner are entitled to claim either.**

- (1) Such shares of the profits earned after the death or retirement of the partner which is attributable to the use of his share in the property of the firm; or
- (2) Interest at the rate of 6 per cent annum on the amount of his share in the property.

Based on the aforesaid provisions of Section 37 of the Indian Partnership Act, 1932, in the given problem, A's Legal representatives shall be entitled, at their option to:

- (a) the 20% shares of profits (as per the partnership deed); or
  - (b) interest at the rate of 6 per cent per annum on the amount of A's share in the property.
5. As per the provisions of Section 30(5) of the Indian Partnership Act, 1932, at any time within six months of his attaining majority, or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, such person may give public notice that he has elected to become or that he has elected not to become a partner in the firm, and such notice shall determine his position as regards the firm.

However, if he fails to give such notice, he shall become a partner in the firm on the expiry of the said six months.

If the minor becomes a partner by his failure to give the public notice within specified time, his rights and liabilities as given in Section 30(7) are as follows:

- (A) He becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of partnership.
  - (B) His share in the property and the profits of the firm remains the same to which he was entitled as a minor.
    - (i) In the instant case, since, X has failed to give a public notice, he shall become a partner in the M/s ABC & Co. and becomes personally liable to Mr. L, a third party.
    - (ii) In the light of the provisions of Section 30(7) read with Section 30(5) of the Indian Partnership Act, 1932, since X has failed to give public notice that he has not elected to not to become a partner within six months, he will be deemed to be a partner after the period of the above six months and therefore, Mr. L can recover his debt from him also in the same way as he can recover from any other partner.
6. As per Section 29 of Indian Partnership Act, 1932, a transfer by a partner of his interest in the firm, either absolute or by mortgage, or by the creation by him of a charge on such interest, does not entitle the transferee, during the continuance of the firm, to interfere in the conduct of business, or to require accounts, or to inspect the books of the firm, but entitles the transferee only to receive the share of profits of the transferring partner, and the transferee shall accept the account of profits agreed to by the partners.

In the given case during the continuance of partnership, such transferee Mr. B is not entitled:

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

However, Mr. B 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.