Unit- 4

Nature of Partnership: Definition

Chapter II(Ss 4-8) , Partnership Act, 1932

Partnership is an aspect of right of association guaranteed under article 19(1) (c)of the Constitution of India, which right is always subject to reasonable restrictions imposed by law from time to time. The rights and obligations of a partnership firm which has no distinct legal existence but only a compendious name for the partners are regulated by the provisions of the Indian Partnership Act. Legislative competence under the Constitution of India emanates from article 245. Various subjects under which the Parliament or the State Legislature can legislate has been provided in schedule VII. It contains three lists- Union List, State List and Concurrent List. Subjects enumerated in List III (the Concurrent List) can be legislated upon by both the Parliament and the State Legislature subject to the restrictions provided in article 246. The subject of partnership falls in Entry 7 of List III and reads: 'Contracts, including partnership, agency, contracts of carriage, and other special form of contracts, but not including contracts relating to agricultural land.' The Act, though a pre-Constitutional enactment, continued to be in force in view of article 372 (1) of the Constitution of India. However, both the Parliament and the state legislatures have the power to amend the Act subject however to the provisions contained in ch 1 of Part XI of the Constitution. It is pursuant to this amending power that the states have made amendments to the provisions of the Act.

The task of consolidating the many Common Law rules largely formulated in the eighteenth and nineteenth centuries was performed by Sir Frederick Pollock who first drafted the Partnership Bill in 1879 and having amended it several times, saw it enacted as the Partnership Act 1890 which has proved to be one of the most successful pieces of legislation in English Law. The Indian Partnership Act has drawn its luminosity from the English Act by enacting similar substantive provisions. The Law Commission of India in its Seventh Report on Partnership Act 1932, Part I traces the history of the Indian Partnership Act in the following words:

> Prior to 1932, Chapter XI (Sections 239 to 266)[1] of the Indian Contract Act, 1872 (Act IX of 1872) contained the law relating to partnership in India. As these provisions were not exhaustive, it was considered expedient and necessary to separate the law relating to partnership and to embody it in a separate enactment; hence, the Indian Partnership Act, 1932 (Act IX of 1932). The Act is based mainly on the English Partnership Act 1890[2] (53 and 54 Vict, C39) which codified the common law relating to partnership. The English Partnership Act 1890 has been the basis of the law of partnership in all countries which have adopted the English common law as the basis of their law, for example, some of the countries constituting the Commonwealth and the United States of America.
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> 2. Before the enactment of the Indian Partnership Act 1932, the whole subject was carefully examined by a Special Committee which scrutinised the English Partnership Act and the judicial decisions in England and in India with a view to adapting the English provisions to the needs and conditions of India. Apart from minor differences necessitated by the peculiar conditions of India, the basic principles embodied in the Indian Partnership Act 1932 are the same as

[1] Report of the Select Committee on the Indian Contract Bill, dated 22 February 1870.
[2] For a history of the English codification, Pollock, *Digest of the Law of Partnership*, Prefaces, fifteenth edn, 1952, can be referred to.

those contained in the English Partnership Act 1890 and in the Uniform Partnership Act prepared by the United States of America. The difficulties felt and the defects disclosed in the working of the English Partnership Act from 1890 to 1931 were considered by the Special Committee which drafted the Indian Partnership Bill and provisions were made in the Act so as to avoid these difficulties and defects.

Nature of Partnership

Partnership is a form of business organisation where two or more persons join together for jointly carrying on some business. It is an improvement over the 'Sole-trade business', where one single individual or proprietor with his own resources, skill and effort carries on his own business. Due to the limitations of the resources of only a single person being involved in the sole-trade business, a larger business requiring more investment and resources available to a sole-trader, cannot be thought of in such a form of business organisation. In a Partnership, on the other hand, a number of persons could pool their resources and efforts and could start a much larger business than could be afforded by any of these partners individually. In case of loss also the burden gets divided amongst various partners in a Partnership.

Any two or more persons can join together for creating partnership. The new Companies Act has prescribed the maximum number of members in case of a partnership firm not to be more than 100. As per the previous Companies Act, 1956, the maximum limit in case of partnerships was 10 and 20 for banking business and other businesses respectively. The minimum number of partners is 2. In case of private companies, the maximum limit has been increased by the new Companies Act, 2013 from 50 to 200. There is however no maximum limit on the number of members in a public company and, therefore, any number of persons can hold shares in a public company. The minimum number of members in case of a public company is seven and in case of a private company is 2. In case the parties intend to opt for a much larger business, they can go for the company form of business organisation. For example, there could be a public company having 1,00,000 members, each one of them having contributed just Rs. 10 and thus having a capital of Rs. 10,00,000 for its business. A Company, as a form of business organisation may be better than a partnership in another way also. It is an artificial person, distinct from its members and has much longer life than that of a partnership, whereas the partnership being nothing but an aggregate of all the partners, partnership has a much smaller span of life than a company. In the case of a company, the liability of a member (shareholder) is limited to the extent of the amount of shares purchased by him, whereas in case of partnership, the liability of every partner is unlimited, and this factor is of great advantage in the case of a company, from the point of view of risk of investors in the business.

In certain respects, a partnership is a more suitable form of business organisation than a Company. For the creation of partnership, just an agreement between various persons is all what is required, whereas in the case of a company, there are a lot of procedural formalities which have to be gone through before a Company is created. For the day to day running of the business, maintenance of the accounts, holding of meetings, distribution of profits and numerous other things a company is subject to a lot of statutory control, whereas the partners are their own masters for regulating their affairs. Even for the dissolution of partnership, a

mere agreement between the partners is enough, but that is not so in the case of a company, which can be wound up only after a certain set procedure is followed.

Because of distinct advantages of a partnership over a sole-trade business and certain advantages even over a company, it is a very popular form of business organisation.

Definition of 'partnership', 'partner', 'firm' and 'firm name'.-

'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'.[3]

Partnership

Historical Background

This clause contains the difficult definition of 'partnership' and the simple ones of 'partner', 'firm' and 'firm name'.[4] Lindley[5] gives nineteen definitions of partnership in four languages. Those in French, German and Latin are consistent in defining partnership as a contract or agreement; but the definitions of the English and American writers show the confusion in the use of the term which has been carried into the English Act.[6] The definitions given by the Indian Contract Act and by Pollock regard 'partnership' as a relation between persons; the New York Civil Code speaks of it as an association between two or more persons for certain purpose; Kent, Story and Watson see it as a contract between persons; Dixon regards it as a group of persons between whom a certain relation exists. For a proposed scheme of statutory contract law, of which the present Bill is to form a part to be administered by courts of all grades of experience, it is most desirable to have this confusion removed and to give to 'firm' an 'partnership' meanings which will be distinct from one another, and can be consistently used throughout the statute. Unfortunately, the confusion has already gone so far that this difficulty cannot be entirely avoided, for the word 'partnership', which ought to have been restricted to its obvious meaning of a relationship, is both in legal writings and in popular usage, employed sometimes to denote a group of persons. This difficulty, it is submitted, should be faced and the words restored to their proper meanings.[7] Throughout the Bill, therefore, the word 'partnership' is used in the defined sense of a relationship, and in no other. Where the partners are referred to collectively the word 'firm' is invariably used.

[3] Section 4.
[4] Statement of Objects and Reasons, which is a part of the Report of the Special Committee appointed by the Government of India to examine and report on the provisions of the Bill which became this Act. The Chairman of the Committee was Sir Brojendra Lal Mitra, and Sir Dinshah Mulla was a member.
[5] *Lindley on Partnership*, ninth edn, pp 12-13.
[6] UK Partnership Act, 1860.
[7] Pollock & Mulla, *The Indian Partnership Act*, 7th Edn. Lexis Nexis Butterworths.

The definition of 'partnership' in the Indian Contract Act, s 239, was based upon Kent's definition. Pollock proposes an improvement upon the present Indian definition in order to meet the criticisms of Jessel MR in Pooley v Driver[8] who points out that certain elements in Kent's definition are subsidiary and superfluous. The form adopted in the bill is that of Pollock, with one small change only. Pollock's definition speaks of the business as being 'carried on by all or any of them on behalf of all', whereas the definition proposed by the Special Committee speaks of it as 'carried on by all or any of them acting for all'. The difference lies in the use of the phrase 'acting for' instead of 'on behalf of'. The intention is to bring out more clearly the fundamental principle that the partners when carrying on the business of the firm are agents as well as principals. Further, the use of the words 'on behalf of' seems to give justification to the wrong view that a person who merely shares the profits of the business is a partner, for inasmuch as such a person derives benefit from the business it may be said to be carried on his behalf.

It is claimed that the definition includes all the essential elements contained in all the definitions quoted by Lindley, the only exception being the element of the sharing of losses. This element may be regarded as consequential upon the sharing of profits, as a firm may be created in which losses are not contemplated or provided for by the sanguine partners. The Bill, therefore, does not seek to make agreement to share losses a test of the existence of partnership, but takes the course of treating the sharing of losses as a legal consequence arising out of the relation of partnership, which is established otherwise.

Elements of 'Partnership'

The definition of 'partnership' contains three elements:

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

All these elements must be present before a group of associates can be held to be partners. These three elements may appear to overlap but they are nevertheless distinct. The first element relates to the voluntary contractual nature of partnership; the second gives the motive which leads to the formation of firms, i.e., the acquisition of gain; and the third shows that the persons of the group who conduct the business do so as agents for all the persons in the group, and are therefore liable to account for all. Elaborating the third essential element, the Supreme Court has held that the position of a partner qua the firm is thus not that of a master and a servant or employer and employee which concept involves an element of subordination, but that of equality. The status of a partner qua the firm is different from employees working under the firm. It may be that the partner is being paid some remuneration for any special attention which he devotes but that would not involve any change of status and bring him within the definition of employee.[9] In KD Kamath & Co v CIT,[10] the Supreme Court has held that the two essential conditions to be satisfied are that: (1) there should be an agreement to

[8] 5 Ch D 472.
[9] Regional Director, Employees' State Insurance Corporation v Ramanuja Match Industries (1985) 1 SCC 218, paras 4 and 9.
[10] (1971) 2 SCC 873, para 28.

share the profits as well as the losses of business; and (2) the business must be carried on by all or any of them acting for all, within the meaning of the definition of 'partnership' under s 4.

1. An Agreement

Partnership arises from an agreement between two or more persons for the creation of this relation. If the basis of the relationship between certain persons is not an agreement, the association would not be a partnership. Some associations may be created without an agreement e.g., the association between certain persons may arise from status as in the case of members of a Joint Hindu Family, the main reason being that their association is not the result of an agreement between those persons. To make the things further clear, s 5 expressly provides that 'the relation of partnership arises from contract and not from status.' Thus, it is the element of agreement which distinguishes a partnership from various other relationships like members of a Joint Hindu Family, joint owners or joint heirs.

> The Supreme Court has, construing the provisions of s 4, observed that a partnership agreement is the source of partnership, and it also gives expression to the other ingredients defining the partnership, specifying the business to be carried on, the persons who will actually carry on the business, the shares in which the profits will be divided, and several other considerations which constitute such an organic relationship.[11]

Partnership Agreement - Oral, Written or By Conduct

An agreement of partnership need not be express, but can be inferred from the course of conduct of the parties to the agreement. The Supreme Court in Tarsem Singh v Sukhminder Singh,[12] has held that it is not necessary under the law that every contract must be in writing. There can be an equally binding contract between the parties on the basis of oral agreement, unless there is a law which requires the agreement to be in writing.

Persons capable of becoming partners

The agreement to form partnership has to be between two or more persons. Since the creation of partnership itself requires a contract between persons, such persons, therefore, must be competent to contract. A minor or a person of unsound mind, who are not competent to contract, cannot become partners.

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[11] Deputy Commr of Sales Tax (Law) Board of Revenue (Taxes) v K Kelukutty AIR 1985 SC 1143.
[12] (1998) 3 SCC 471, para 13.

A minor has been permitted to be admitted to the benefits of partnership.[13] Such minor has a right to such share of property and profits as may be agreed upon.[14] Moreover, such minor's share is liable for the act of the firm, but the minor is not personally liable for any such act.[15]

The word 'person' in s 4 which has been replaced by s 239 of the Indian Contract Act contemplates only natural or artificial, i.e., legal persons and a firm is not a 'person' and as such is not entitled to enter into a partnership with another firm or Hindu undivided family or individual.

The Partnership Act permits partnership between any two or more persons. Such persons may be either natural or artificial. Thus, a partnership could be formed between a number of companies. Although formation of a partnership with a company being a partner is a possibility under the Partnership Act, but there would be practical difficulties in the working of such partnership from the point of view of the provisions of the Companies Act. In Ganga Metal Refining Company v Commr of Income Tax, West Bengal,[16] the Calcutta High Court has expressed the view that though there is a possibility of an incorporated Company forming partnership with another incorporated Company in the loose sense of the term for the purpose of income-tax, the regular concept of partnership cannot really be applied to say that an incorporated company under the Companies Act can enter into a partnership with another incorporated Company in the regular and technical sense. In this context, P.B. Mukherji, J. observed that:

> 'Notionally and juristically if two incorporated Companies under the Indian Companies Act enter into a partnership, then each Company becomes the agent for the other and agrees to share the profits. This will create many problems for the two incorporated Companies. The two Companies will have to be, therefore, agents for each other in a manner which may not be permissible at all by their own charters, articles and memorandum. It would be difficult to apply the very specific rights and obligations as between partners in the case of Companies as partners such as in Chapter III, Chapter IV and Chapter VI of the Partnership Act. Then there is need also for the registration of firms and the companies as such partners in a partnership will have therefore to obey two masters, the Registrar of Firms and the Registrar of Companies. The access of each partner to the other partner's books of accounts will mean that one incorporated Company would be entitled to go into the fields of accounts of other incorporated Company which is its partner. This will make nonsense of the Companies Act. Strangers then will have access to the books, accounts and papers of the Companies where under the Companies Act, they are only limited to their own members and shareholders.'

Though s 3 (42) of the General Clauses Act provides that 'person shall include any company or association or body of individuals whether incorporated or not', the Supreme Court has

[13] S. 30 (1).
[14] S. 30 (2).
[15] S. 30 (3).
[16] AIR 1967 Cal. 429.

held that to import the definition of the word 'person' occurring in s 3 (42) of the General Clauses Act 1897 into s 4 will be totally repugnant to the subject of partnership law.[17]

It is more usual, however, for companies to work together by means of joint boards or committees without any formal combination. Railway Companies in England have done this in the past on a large scale, and similar arrangements are well-known in the banking business also.

Partnership between a corporation and an individual does not seem to be convenient as a business arrangement, nor does it often occur in practice.

The Partnership Act does not directly mention that only a solvent person can become a partner but s 34, however, states that when a partner is adjudicated insolvent, he ceases to be a partner. In view of this provision, only such person who is not insolvent can become a partner. The reason for such a provision is that the interests of the third parties do not suffer when they want to enforce their rights against various partners. Hence, a person who has been adjudicated insolvent cannot become a partner, and if he is solvent when he becomes a partner, he ceases to be a partner, if and when he is adjudicated insolvent.

2. Sharing of profits

The object of every partnership must be to carry on business for the sake of profits and to share the same. Therefore, clubs or societies which do not aim at making profits are not partnerships. The term 'profits' has not been defined in the Act. The profits contemplated by the Act and by the common law of partnership sometimes called 'net profits', are the excess of returns over advances, the excess of what is obtained over the cost of obtaining it. It was formerly common to speak of the total receipts or gross returns of a business as 'gross profits'. This is objectionable, and should be avoided.[18] Obviously, there may be very large gross returns and yet little or no real profit. Sharing gross returns will not create a partnership, as the English Act [s 2, sub-s (2)], affirming the general law, has expressly declared. The Supreme Court discussed in Narayanappa v Bhaskara Krishnappa,[19] :

> The whole concept of partnership is to embark upon a joint venture and for that purpose to bring in capital money or even property including immovable property. Once that is done, whatever is brought in would be thee trading asset of the partnership.

The person who brought it in would not be able to claim or exercise any exclusive right.

Although sharing of profits is one of the essential elements of every partnership, every person who shares the profits need not always be a partner. For example, I may pay a share of profits to the manager of my business instead of paying him fixed salary so that he takes more interest in the progress of the business, such person sharing the profits is simply my servant or agent but not my partner. Similarly, a share of profits may be paid by a business man to a money-lender by way of payment towards the return of his loan and interest thereon, such a

[17] CIT v AW Figgis & Co AIR 1953 SC 455.
[18] *Lindley on Partnership*, fifteenth edn, p 85.
[19] AIR 1966 SC 1300.

money-lender does not thereby become a partner. Similarly, the author of a book receiving a royalty on copies sold is not a partner with the publisher.

At one time it was thought that a person who shared the profits must incur the liability also as he was deemed to be a partner. This rule was laid down in Grace v Smith,[20] in 1775 and it was stated by Grey C.J. that 'every man who has the share of the profits of a trade ought also to bear his share of the loss.' This principle was confirmed in 1793 in Waugh v Carver.[21] In 1860this question came for consideration before the House of Lords in Cox v Hickman.[22] In that case it was laid down that the persons sharing the profits of a business do not always incur the liability of partners unless the real intention between them is that of partners. The principle laid down in Cox v Hickman forms the basis of the provisions of s 6 of the Indian Partnership Act, which gives a caution that the presence of only some of the essentials of partnership does not necessarily result in partnership. For determining the existence of partnership regard must be had to the real relation between the parties after taking all the relevant facts into account. The provision contained in s 6 is as follows:

> **6. Mode of determining existence of partnership.-** In determining whether a group of persons is or is not a firm, or whether a person is or 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.
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> *Explanation 1*.- The sharing of profits or of gross returns arising from property by persons holding a joint or common interest in that property does not of itself make such persons partners.
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> *Explanation 2*.- The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business, does not of itself make him a partner with the persons carrying on the business; and in particular, the receipt of such share or payment-
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> a) By a lender of money to persons engaged or about to engage in any business,
> b) By a servant or agent as remuneration,
> c) By the widow or child of a deceased partner, as annuity, or
> d) By a previous owner or part owner of the business, as consideration for the sale of the goodwill or share thereof,
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> does not of itself make the receiver a partner with the persons carrying on the business.

Section 6 gives a caution that for determining whether there is partnership between certain persons or not, regard is to be had to the real relation between the parties as shown by all relevant facts taken together. The note of the Special Committee says that cl 5, as this section was numbered in the draft, is a comprehensive statement of the rule in Cox v Hickman[23] and adds that it has not been incorporated in the English Partnership Act. What Cox v Hickman did was to deny the erroneous but then common opinion that sharing the profits of a business

[20] (1775) 2 Wm. Blacks. 998.
[21] (1793) 2 H. Blacks 235.
[22] (1860) 8 H.L.C. 268.
[23] (1860) 8 HLC 268.

was not only evidence but conclusive evidence of partnership, and thus to make the courts free to arrive at the real intention of the parties by considering all relevant documents and facts. The facts of the case are as under:

> Smith and Son carried on business as iron merchants. They got into financial difficulties as a consequence of which they executed a deed of arrangement with the creditors. According to the arrangement, five reprsentatives of the creditors were appointed as five trustees. They included Cox and Wheatcroft. The business of Smith and Son was to be managed by the five trustees. The net income of the business was to be distributed by these trustees amongst the general creditors of Smith & Son. After all the creditors had been paid off the business was to be returned to Smith & Son. While the business was being managed by the trustees, the plaintiff, Hickman, supplied goods to the firm. One of the trustees accepted bills of exchange drawn by Hickman undertaking to pay the price of those goods. Hickman sued Cox and Wheatcroft to recover the price of the goods supplied by him. It was held that although the creditors were sharing the profits and the business was being managed by the trustees, still the relationship between Smith and Son on the one hand and the creditors (including trustees) on the other was that of debtor and creditor and not that of partners and, therefore, Cox and Wheatcroft could not be made liable.
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> Discussing the position of a person sharing the profits Lord Cranworth observed:[24]
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> > "It is not strictly correct to say that his right to share in the profits makes him liable to the debts of the trade. The correct mode of stating the proposition is to say that the same thing which entitles him to the one makes him liable to the other, namely, the fact that the trade has been carried on, on his behalf, i.e., that he stood in the relation of a principle towards the persons acting ostensibly as the traders, by whom the liabilities have been incurred, and under whose management the profits have been made.
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> > Taking this to be the ground of liability as a partner, it seems to me to follow that the mere concurrence of creditors in an arrangement under which they permit their debtor, or trustees for their debtor, to continue his trade, applying the profits in discharge of their demands does not make them partners with their debtors, or the trustees. The debtor is still the person solely interested in the profits, save only that he has mortgaged them to his creditors. He receives the benefit of the profits as they accrue, though he has preclude himself from applying them to any other purpose than the discharge of his debts. The trade is not carried on by or on account of the creditors; though their consent is necessary in such a case, for without it all the property might be seized by them in execution. But the trade still remains the trade of the debtor."

The position may also be explained by the decision of the Privy Council in Mallwo, March & Co v Court of Wards.[25] In this case, a Hindu Raja advanced large sums of money to a firm. The Raja was given extensive powers of control over the business and he was to get commission on profits until the repayment of his loan with 12 percent interest thereon. It was held that the Raja could not be made liable for the debts contracted by the firm while the said

[24] *Ibid*, at 306.
[25] (1872) LR 4 PC 419.

agreement was in force, because the intention in the agreement was not to create partnership but simply to provide security to Raja, who had lent money to the firm. This was decided to be a contract not of partnership, but of loan and security between a debtor and a creditor. Similarly, an agreement by A to pay Z, in consideration of his guaranteeing A in his underwriting business, a certain proportion of A's profits in that business, does not make Z a partner with A.[26]

Sometimes a share in the profits may be given to a servant or agent in the business so that hecan take more interest in the business. Such a person sharing the profits does not thereby become a partner. In McLaren v Verschoyle,[27] an assistant in a firm of brokers was paid a share in the profits over and above his salary. It was held that such a servant only acted as an agent for the firm and the mere fact that he shared the profits did not make him a partner in the firm. In Walker v Hirsch,[28] the plaintiff, who was a clerk in the defendant's firm, was to be paid fixed salary and also 1/8th of the profits. He agreed to advance 1500 ponds to the firm's business. By an agreement this relationship could be terminated by 4 months' notice from either side. He performed the duties of a clerk only and had no say in the conduct of the business. He was given notice by the defendants terminating his services. He contended that he was a partner and claimed dissolution of the firm and accounts. It was held that though he shared the profits, he was having the capacity of a servant only. He was not a partner and could not seek dissolution of the firm.

Sometimes on the death of a partner, the widow or the child of the deceased partner may be given a share of profits in accordance with an agreement which may have been entered into between the partners. Such widow or child does not become partner merely because he or she is sharing the profits in the business. In Holme v Hammond,[29] 5 persons entered into partnership for 7 years and agreed to share the profits and losses equally. They further agreed that if any one of them died before the expiry of the said period of 7 years, the others would continue the business and pay the share of the profits of the deceased to the executors. On the death of one of the partners the survivors continued the business. The executors of the deceased who did not actually take any part in the management of the business, were paid 1/5th share of profits made since the death of the deceased. The plaintiff sued the executors of the deceased to make them liable in respect of a contract entered into by the surviving partners after the death of the deceased partner. It was held that the executors, though sharing the profits, had not become partners and therefore, they could not be made liable.

A person selling the goodwill of his business may be entitled to share the profits of a business in consideration for the sale of goodwill, such a person will not become a partner merely because he is sharing the profits with the person carrying on such business. In Pratt v Strick,[30] a doctor sold the goodwill of medical practice and entered into an agreement with the buyer of the goodwill that he would help such buyer to introduce patients for 3 months and he would be entitled to half the share of profits and incur half the expenses. It was held that the doctor had not become a partner with the person to whom the goodwill was sold.

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[26] Ex p Tennant (1877) 6 Ch D 303.
[27] (1901) 6 CWN 429.
[28] (1884) 27 Ch. D. 460.
[29] L.R. 7 Ex. 218.
[30] (1932) 7 Tax Cas. 459.

Salaried Partners

Sometimes, it is not easy to draw the line between a partnership and a payment of salary by a share of profits. It seems impossible to say that a salaried person is, or is not, a partner in the true sense of the term. He may or may not be a partner depending on the facts. In Stekel v Ellice, Megarry J summarised the position thus:

> It seems impossible to say that as a matter of law a salaried partner is or is not a partner in the true sense. He may or may not be a partner, depending on the facts, what must be done, I think, is to look at the substance of the relationship between the parties; and there is ample authority for saying that the question whether or not there is a partnership depends on what the true relationship is, and not on any mere label attached to that relationship.[31]

The owner of a ship, who has been paying the master fixed wages, hands over the management of the ship to the master on the terms of receiving a fixed share of profits from him. It is a question as to what status does this provide to the master- the owner's servant, though a servant with large discretion, or make him a partner with the owner in the venture. Probably it grants partner status but either opinion is plausible.[32]

A carries on in his own name the business of loading and unloading wagons for a limited company. A appoints B to manage the business. It is agreed between them that B shall get a 12 annas share out of the net profits as remuneration, and that A shall get a 4 annas share but shall not be liable for any loss. Upon these facts, it was held by the High Court of Calcutta that the relation between A and B was not that of partners but of principal and agent.[33]

In R.N. Kothare v Hormasjee,[34] there was an agreement between two partners that one of them was to get a salary of Rs. 500/- pm in lieu of profits, and moreover, he was not responsible for any loss or liability of the firm. It was held that there was a valid partnership in which one of the partners was a 'salaried partner.' In Stekel v Ellice,[35] it has been held that when a person joining a firm of chartered accountants as a partner is to get fixed salary in lieu of profits, he is no doubt a partner and there is valid partnership.

3. Carrying on of Business

The object of every partnership must be carrying on a business and sharing its profits. It may be any business which is not unlawful. The Act defines business as including 'every trade, occupation or profession.'[36] The definition is not exhaustive and is capable of including any kind of commercial activity aimed at earning profits. The business, for instance, may be of working as tailors, engaging in legal profession, rendering medical services, producing a film, running a banking business, or purchasing and selling of goods.

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[31] (1973) 1 All ER 465, p 473.
[32] Steel v Lester (1878) 3 CPD 121.
[33] Munshi Abdul Latiff v Gopeswar Chattoraj (1932) 56 Cal L.J 172.
[34] AIR 1927 Bom. 187.
[35] (1973) 1 All ER 465.
[36] S. 2 (b).

The business which the partners agree to carry on must not be unlawful or opposed to public policy. Thus, where a partnership between two persons to carry on business of transport service by obtaining permit in the name of one of them only involved the contravention of the provisions of sections 42 (1) and 59 (1), Motor Vehicles Act, the partnership is illegal and opposed to public policy. A claim on the basis of the settlement of accounts of such partnership is also illegal and the same, therefore, cannot be enforced.[37]

It is further necessary that the business must be carried on by all the partners or any of them acting for all of them. Carrying on of a business involves a series of transactions. Merely a single isolated transaction of purchases and sale by a number of persons does not mean carrying on of the business. For example, A and B jointly purchase a building for a sum of Rs. 2,00,000 and after sometime they sell the building for Rs. 3,00,000 and share the gain of Rs. 1,00,000 equally. This transaction is not the carrying on of the business between A and B and, therefore, they are not partners. There is, however, a possibility that the partners may engage in a single adventure or a single undertaking and that may involve the carrying on of a business.

According to s 8, there can be 'Particular partnership' between partners whereby they engage in particular adventures or undertaking. Thus, persons can be partners in the working out of a coal-mine or the production of a film because although that may be a single adventure but the same requires a series of transactions and continuous relationship.

Illustration of a firm constituted for carrying out a particular venture is furnished in the case of Karimuthu Thyagarajan Chettiar v Muthappa Chettiar.[38]

The decision of the A.P. High Court in K. Jaggaiah v Kokumanu,[39] illustrates a single venture amounting to the carrying on of business. In this case, the plaintiff and the two defendants joined together and obtained a contract for the maintenance of a road. There was held to be partnership in the road building activity. Such activity though arising out of a single contract was spread over a particular period and the firm had to employ certain workers, supervise the work, prepare the bills and finalise the work and get the approval from the Government and finally receive the bills, and all that meant carrying on of business. A firm constituted for managing the agency of a company would come to an end when the managing agency is terminated. Another instance of a firm constituted for carrying out a particular adventure is Deoki Prasad Rajgarhiah v Anari Dai Poddar.[40]

'Business must be carried on by all or any of them acting for all.'[41] This implies that in order to constitute 'partnership', there must be existence of mutual agency. The words 'acting for all' implies that any partner can carry on the business on behalf of others. Every partner, therefore, can bind other partners by his act done on behalf of the firm. Every partner can be the agent of any other partner and the relationship is that of mutual agency. For example, a partnership consists of A and B. A may enter into a contract on behalf of the firm and thereby make B bound by the agreement. In this transaction A is the agent and B the principal. Similarly, B may borrow money for the firm and A would be bound thereby. In this transaction B acts as agent and A is bound as principal. Thus, every partner occupies the dual

[37] Kanniappa Nadar v Karuppiah Nadar AIR 1962 Mad. 240.
[38] AIR 1961 SC 1225.
[39] AIR 1984 AP 149.
[40] (1998) 3 BLTR 1836.
[41] S 4.

position, that of the principal and agent. He is agent in so far as others are bound by his acts and he is also the principal in so far as he is bound by what is done by others. As already noted in the case of Cox v Hickman,[42] although the trustees were managing the business of Smith and Son, they did not thereby become partners. The reason is that the trustees were merely agents of Smith & Son but they were not the principals and thus there was no mutual agency. Similarly, if the servant of agent is paid remuneration out of profits, such a person constitutes merely an agent of the person with whom he is sharing the profits. Since such a servant or agent does not occupy the position of a principal, there is no mutual agency and thus the servant or agent sharing the profits cannot be termed as a partner.

Partnership Firm- Not a separate legal entity

Partnership is a relation between persons who have agreed to share the profits of a business carried on by all or any of them for the benefit of all. The section further makes it clear that a firm or partnership is not a legal entity separate and distinct from the partners. Firm is only a compendious description of the individuals who compose the firm.

The law, English as well as Indian, has relaxed its rigid notions and extended a limited personality to a firm.[43] Nevertheless, the general concept of partnership, firmly established in both systems of law, still is that a firm is not an entity or 'person' in law but is merely an association of individuals and a firm name is only a collective name of those individuals who constitute the firm. In other words, a firm name is merely an expression, a compendious mode of designating the persons who have agreed to carry on business in partnership. For this reason, the past experience of one of the partners can be counted towards experience of the firm. This gains importance especially in matters pertaining to award of contracts through tenders.

A firm as such is not entitled to enter into partnership with another firm or individuals.[44] As a firm is not a legal entity, there cannot be a partnership of firms, but when two firms combine, the legal effect is that the individuals in the two firms become partners.[45]

For purposes of income tax, a firm can be assessed as an entity distinct and separate from its members.[46] Notwithstanding the fact that a firm like an association of persons is for the purpose of assessment treated as a separate entity, it is not a legal person having a corporate character distinct from that of its members.[47]

Where a suit is filed in the name of a firm, it is still a suit by all the partners of the firm unless it is proved that all the partners had not authorized the suit. A firm may not be a legal entity in the sense of a corporation or a company incorporated under the Companies Act, 2013, but it is still an existing concern where business is done by a number of persons in partnership.[48]

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[42] (1860) 8 HLC 268.
[43] Pollock & Mulla, *The Indian Partnership Act*, 7th Edn. Lexis Nexis Butterworths.
[44] CIT v Jadavji Narsidas and Co AIR 1963 SC 1497, para 12.
[45] Malabar Fisheries Co v CIT AIR 1980 SC 176, p 182.
[46] Nandlal Sohanlal v CIT AIR 1977 Punj 320, p 325.
[47] Chidambaram v CIT AIR 1970 Mad 497, pp 500,501.
[48] Purushottam Umedbhai and Co v Manilal and Sons AIR 1961 SC 325, para 8.

The position on this point, which is the same under both Indian and English law, was explained by the Supreme Court in Dulichand Laxminarayan v Commr of Income-tax[49] as under:

> "The general concept of partnership, firmly established in both systems of law, still is that a firm is not an entity or 'person' in law but is merely an association of individuals who constitute the firm. In other words, a firm name is merely an expression, only a compendious mode of designating the persons who have agreed to carry on business in partnership… In these circumstances to import the definition of the word 'person' occurring in s 3 (42) of the General Clauses Act, 1897 into s 4 of the Indian Partnership Act will, according to lawyers, English and Indian, be totally repugnant to the subject of partnership law as they know and understand it to be."

Experience of the Firm

A firm, as already noted, is merely the association of individual partners who constitute it. Therefore, the experience of the partners can be treated as experience of the firm.[50] In view of the above stated position if the partners of the firm submitting the tender hold adequate experience required for submitting the tender, the tender submitted by the firm is valid because the firm in such a case happens to be a qualified tenderer.

Firm's personality for Tax purposes

For the purposes of tax laws a firm is a taxable unit or a person different from the partners, and in that sense it has personality of its own. To the extent a partnership firm is recognised as a person under different tax laws, the provisions of the Partnership Act do not apply to such situations.

According to s 2 (31) of the Income Tax Act, the term 'person' includes a firm and six other categories of assesses or the units of assessment. Thus, under the Income Tax Act, unlike the Partnership Act, a firm is a separate and distinct legal entity or a separate unit of assessment.

In view of the fact that under the Income Tax Act, a firm is a separate person or taxable unit distinct from its members, there is a possibility of there being two separate firms though they consist of the same partners. In Income Tax Commissioner v G.P. Naidu & Sons,[51] on 1st October 1968 a partnership firm consisting of G.P Naidu and his 3 major sons was constituted under the name and style of M/s G.P. Naidu & Sons to deal in pulses. On November 26, 1968 another partnership, which also consisted of the same partners, i.e., G.P. Naidu and his 3 sons was constituted in the name and style of M/s Sri Lakshmi Oil and Flour Mills for the purpose of erecting an oil mill and for carrying on oil business. For the assessment year 1971-72 the assesse firm, G.P. Naidu & Sons filed a return admitting a total income of Rs. 57, 340 from its business. Another return declaring a total income of Rs. 35,000 was filed in the name of M/s Sri Lakshmi Oil & Flour Mills. The Income Tax Officer

[49] (1956) 29 TLR 535.
[50] Aula Constructions Pvt. Ltd. V Sr. Div. Electrical Engineer AIR 1999 AP 312, p. 321.
[51] AIR 1980 .P. 158 (F.B.).

clubbed the income of the two firms and assessed the assessee firm accordingly on the ground that the constitution and ownership of the two businesses was one and the same. The contention of the assessee that there were two different firms independent of each other and there was no inter-lacing or inter-mixing between the two firms and hence the profits of the two firms were not to be clubbed but taxed separately, was accepted by the Income Tax Appellate Tribunal. On appeal, the Full Bench of A.P. High Court agreed with the view taken by the Income Tax Appellate Tribunal and held that under the Income Tax Law a firm is an independent and distinct juristic person for the purpose of assessment as well as for recovery of tax as it is a 'person' within the meaning of s 2 (31) of the Income Tax Act, and therefore, the two firms had to be treated as separate entities for the purpose of assessment.

A similar approach has been adopted by the Bombay,[52] Punjab & Haryana[53] and Madras[54] High Courts, and approved by the Supreme Court in Deputy Commissioner, Sales Tax v M/s K. Kelukutty.[55] The Supreme Court visualised the creation of separate and distinct partnership firms with the same partners under the Partnership Act, when it observed[56]:

> "It is permissible to say that a partnership agreement creates and defines the relation of partnership and therefore identifies the firm. If that conclusion be right, it is only a further step to hold that each partnership agreement may constitute a distinct and separate partnership and therefore distinct and separate firms. That is not to say that a firm is a corporate entity or enjoys a juristic personality in that sense. The firm name is only a collective name for the individual partners. But each partnership is a distinct relationship."

In Kelukutty's case, the respondent M/s K. Kelukutty was a partnership firm consisting of six partners and carrying on timber business. Those partners also constituted another partnership firm in the name of M/s K.K.K. Sons Saw Mills, and owned a saw mill. It was held that for the purposes of Sales Tax, the two firms were distinct units and the turnover of one firm could not be included in the turnover of the other.

Duration of partnership

Partners are free to decide as to how long partnership between them shall continue. It may be partnership for a fixed term, say for 2 years or 5 years, or it may be until the completion of certain adventures or undertakings, for instance, until the production of a film. Sometimes the agreement may stipulate about the determination (end) of partnership on the happening of certain events, e.g., if the business runs into loss for consecutively five years. When the partners have not decided about the duration of partnership, such a partnership is known as partnership at will.

Partnership at will

[52] Jesingbhai v CIT Bombay (1955) 28 ITR 454.
[53] Oswal Hosiery and Mahavir Woolen Mills v CIT, Punjab AIR 1969 Punj. 8.
[54] Mahendra Kumar v State of Madras AIR 1968 Mad. 241.
[55] AIR 1985 SC 1143.
[56] Ibid at 1147.

S 7 says where no 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'.

The essence of partnership at will is that it is open to either partner to dissolve the partnership by giving notice. Section 7 contemplates two exceptions to a partnership at will. The first exception is where there is a provision in the contract for the duration of the partnership; the second exception is where there is provision for the determination of the partnership. In either of these cases, the partnership is not at will. The duration of a partnership may be expressly provided for in the contract; but even where there is no express provision, the partnership will not be at will if the duration can be implied.

Since in a partnership at will, duration of partnership is not fixed, nor is there any provision as regards its determination, the partners are not legally bound to continue in partnership for any specified period, etc., and the partnership can be ended at the sweet will of any of the partner. The following provisions of the Partnership Act in this regard may be noted:

a) Where a partnership is at will, a partner may retire by giving a notice to all the other partners of his intention to retire.[57]
b) Where the partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partners of his intention to dissolve the firm.[58] The firm is dissolved as from the date mentioned in the notice as to the date of dissolution or, if no date is so mentioned, as from the date of the communication of the notice.[59]

Although a partnership at will could be dissolved by a mere notice but that does not debar a partner from filing a suit for dissolution. In such a case the service of the summons will be deemed to be the communication of notice for dissolution and the firm shall stand dissolved when the summons are served. The following observations of the Supreme Court in Banarsi Das v Kanshi Ram,[60] may be noted:

> "Even assuming, however, that the term 'notice' in the provision (s 43) is wide enough to include within it a plaint filed in a suit for dissolution of partnership, the sub-section itself provides that the firm will be deemed to be dissolved as from the date of communication of notice. It would follow, therefore, that a partnership would be deemed to be dissolved when the summons accompanied by a copy of the plaint is served on the defendant, where there is only one defendant, and on all defendants, when there are several defendants. Since a partnership will be deemed to be dissolved only from one date, the date of dissolution would have to be regarded to be the one on which the last summon was served."

In Moss v Elphick,[61] an agreement between the two partners provided that the partnership shall be terminated by mutual arrangement only. One of the partners sought the dissolution of

[57] S 32 (1) (c).
[58] S 43(1).
[59] S 43 (2).
[60] AIR 1963 SC 1165 at pp. 1169-70.
[61] (1910) 1 K.B. 486.

the firm by a notice to the other partner contending that it was a partnership at will. It was held that the partnership was not at will and the same could not, therefore, be terminated by notice. It was observed by Fletcher J. that in this case in effect the partnership was "for the joint lives of the parties, unless terminated by mutual agreement. There is, therefore, a specific provision as to the duration of the partnership in the partnership agreement, and it is in that sense a partnership for a fixed, i.e., defined term." The question of the construction of the contract also arose before the Supreme Court in K.T. Chettiar v EMI Muthappa.[62] In this case, an agreement between two partners concerning the business of managing agencies of mills, inter alia provided for carrying on the management in rotation once in four years by the two partners. It further provided that the partners and their heirs and those getting their rights should carry on the management in rotation. It was held by the Supreme Court that the intention of the partners could not be to create a partnership at will, but to have a partnership of some duration, though the duration was not expressly fixed in the agreement. The decision of the Delhi High Court in Suresh Kumar v Amrit Kumar,[63] also explains the position in this regard. In this case, the terms of the partnership agreement included stipulations (a) that any partner desirous of retiring from the partnership shall give 6 calendar months' notice of his intention to retire and on the expiry of the notice he shall be deemed to have ceased to be a partner, and (b) that on the death or retirement of a partner, the firm shall be continued with respect to the other partners and the nominee or legal heirs of the retiring or deceased partner, as the case may be. One of the partners contended that it was a partnership at will and sought the dissolution of the firm but it was held that the parties never intended that the partnership be dissolved at the sweet will of any of the partners, rather their intention was that business of the partnership should continue as long as possible, notwithstanding death or retirement of any partner. This being not a partnership at will could not be dissolved by a notice by a partner.

Distinction between Partnership and Joint Family

a) The basis of partnership is a contract between persons. No partnership can arise without a contract. The relation of members of Joint Hindu Family is based on the status of persons, i.e., a person becomes its member by virtue of his being born in the particular family. Reference here may be made to s 5. It says that 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.
b) When a new partner has to be introduced into a partnership firm, consent of all the partners is needed for the same. No such consent is needed for the addition of a member into the joint Hindu family. A person becomes the member of the family on being born in that family.
c) There is mutual agency between the partners of a partnership firm and the act done by any of the partners binds the firm, whereas there is no such mutual agency between

[62] AIR 1961 SC 1225.
[63] AIR 1982 Delhi 131.

the members of a joint Hindu family. The Karta of the joint Hindu family has all the powers to act on behalf of the family and he is the only person who can represent the family.

d) The liability of a partner is not only joint liability or limited to his share in the partnership business, the liability is several liability also. Such liability is unlimited and even a partner's personal property can be attached for the partnership debts. The liability of the coparceners, on the other hand, is limited only to the extent of their shares in the family business.
e) A partnership is dissolved by the death of a partner but that is not so in the case of a joint Hindu family.

Distinction between Partnership and Company

a) In a partnership, the persons who have entered into partnership are individually called partners and collectively a firm. A partnership firm, therefore, is merely a collective name of all the partners. A partnership firm does not have a separate legal personality. A company is a legal entity distinct from its members.
b) A partnership firm means all the partners put together, if all the partners cease to be partners, e.g., all of them die or become insolvent, 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.
c) The shareholder of a company can transfer his share to anybody he likes but a partner cannot substitute another person in his place unless all the other partners agree to the same. Similarly, on the death of the member of a company his legal representatives will step into his shoes for the purpose of the rights in the company, but on the death of a partner his legal representatives do not get substituted in his place in partnership.
d) The new Companies Act has prescribed the maximum number of members in case of a partnership firm not to be more than 100. As per the previous Companies Act, 1956, the maximum limit in case of partnerships was 10 and 20 for banking business and other businesses respectively. The minimum number of partners is 2. In case of private companies, the maximum limit has been increased by the new Companies Act, 2013 from 50 to 200. There is however no maximum limit on the number of members in a public company and, therefore, any number of persons can hold shares in a public company.The minimum number of members in case of a public company is seven and in case of a private company is 2.
e) The liability of the members of a company is limited but the liability of the partners is unlimited.

Distinction between Partnership and Co-ownership

a) A partnership arises from an agreement between certain persons, but persons may become co-owners or joint owners of some property even without an agreement. For instance, on the death of A, his property may devolve to B and C and thus make B and C as the co-owners of the property.

b) The purpose of a partnership is the carrying on of business and sharing the profits, whereas persons may become co-owners of the property without engaging themselves in any business.
c) In the partnership business there is mutual agency between the partners and the act done by any of the partners binds the others. There may be no mutual agency between the co-owners, and the act of one co-owner does not bind the others.
d) A partner cannot transfer or sell the whole of his share to an outsider so as to substitute an outsider in his place. A co-owner, on the other hand, has a right to transfer his part of the share to anybody he likes.

DEED OF PARTNERSHIP

THIS DEED OF PARTNERSHIP made at _____ on the _____ day of _____20____
BETWEEN (1) SRT of _____, Indian Inhabitant, having address at _____

(which expression shall unless repugnant to the context or meaning thereof, include his heirs, executors, administrators, legal representatives and assigns) hereinafter called the Party of the FIRST PART; (2) SMG of _____, Indian Inhabitant, having address at_____

(which expression shall unless it be repugnant to the context or meaning thereof, include his heirs, executors, administrators, legal representatives and assigns) hereinafter called the Party of the SECOND PART

WHEREAS

The parties hereto are desirous of carrying on business of_____ in partnership upon the terms and conditions recorded hereinafter.

IT IS HEREBY AGREED BY AND BETWEEN THE PARTIES AS UNDER:

1. The Partnership shall commence on the _____day of_____20____.
2. The name of the firm shall be "Messrs_____".
3. The Partnership shall be "at Will".
4. The business of the Partnership shall be carried on at_____ or at such other place or places as the partners may agree upon.
5. The business of the partnership shall be of_____ _____and/or such other business as the partners may decide.
6. The accounting year of the partnership shall be from 1st April to 31st March of the next year.
7. The Bankers of the Partnership shall be such bank or banks as the partners may from time to time agree upon and such bank account or accounts shall be operated by such partners or partner as the parties hereto may from time to time agree upon.
8. The capital of the partnership shall be the sum of Rs._____/- and shall be provided by the partners in their profit and loss sharing ratio. If at any time hereafter any further capital is required for the purpose of the partnership the same shall, unless otherwise agreed, be contributed by the partners in the same ratio. The partners shall be entitled to interest on the capital brought in by them.
9. Simple interest at the rate of 12% per annum shall be payable on the amounts standing to the credit of Accounts of the Partners, from time to time.
10. The share of the Partners in the profit and loss of the partnership, after payment of interest on Partners' account and remuneration to the Partner, shall be as follows:

    NAMES PERCENTAGE
    (1) SRT
    (2) SMG

11. Proper books of account shall be maintained and be properly posted up and kept at the principal place of business of the partnership or such other place/s as may be agreed upon.

12. Each partner shall:
    a) Devote his whole time and attention to the Partnership business;
    b) Punctually pay and discharge his separate debts and engagements and indemnify the other partners and the partnership assets against the same and all proceedings cost, claims or demands in respect thereof;
    c) Be just and faithful to the other partners in all transactions relating to the partnership business and at all times give to the others a true account of all such dealings.
13. None of the partners shall without the consent of the other Partners:
    a) engage or be concerned or interested either directly or indirectly in any other similar business or occupation;
    b) make any contract with or dismiss any employee;
    c) forgo the whole or any part of any debt or sum due to the partners;
    d) except in the ordinary course of trade dispose of by loan pledge, sale or otherwise of any part of the partnership property;
    e) assign or charge their interest in the firm or;
    f) draw or accept or endorse any bill of exchange or promissory note on account of the partnership.
14. Death of any of the partners hereto shall not dissolve the partnership but the legal representatives of the deceased partner shall be taken up as a partner in place and stead of the deceased partner.
15. The rights, powers, duties and obligations of the parties (partners) hereto shall be governed by The Indian Partnership Act, 1932 or such other statutory modifications or re-enactment thereof.
16. If any dispute arises between the parties hereto in respect of the partnership, the same shall be referred to The Arbitration and Conciliation Act, 1996 or the Arbitration Act as may be in force.

IN WITNESS WHEREOF the parties hereto have hereunto set and subscribed their respective hands the day and year first hereinabove written.

SIGNED AND DELIVERED by the)

withinnamed, SRT the Party of the First Part,)

in the presence of. ..)

SIGNED AND DELIVERED by the)

withinnamed, SMG the Party of the Second)

Part, in the presence of. ..)