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# Relations Of Partners To One Another In A Partnership

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## Introduction

### Partnership:

An association of two or more persons engaged in a business enterprise in which the profits and losses are shared proportionally.

According to section 4 of the Partnership Act of 1932, "*Partnership is defined as the relation between two or more persons who have agreed to share the profits according to their ratio of business run by all or any one of them acting for all*".

The Common law definition of a partnership is generally stated as "*an association of two or more persons to carry on as co-owners a business for profit*".

A partnership firm is not a legal entity apart from the partners constituting it. It has limited identity for the purpose of tax law as per section 4 of the Partnership Act of 1932.

The formation of a partnership requires a voluntary "association" of persons who "co-own" the business and intend to conduct the business for profit. Persons can form a partnership by written or oral agreement, and a partnership agreement often governs the partners' relations to each other and to the partnership. The term *person* generally includes individuals, corporations, and other partnerships and business associations. Accordingly, some partnerships may contain individuals as well as large corporations. Family members may also form and operate a partnership, but courts generally look closely at the structure of a family business before recognizing it as a partnership for the benefit of the firm's creditors.

Certain conduct may lead to the creation of an implied partnership. Generally, if a person receives a portion of the profits from a business enterprise, the receipt of the profits is evidence of a partnership. If, however, a person receives a share of profits as repayment of a debt, wages, rent, or an annuity, such transactions are considered "protected relationships" and do not lead to a legal inference that a partnership exists.

## **Rights Of Partners:**

Two fundamental principles govern relations of partners to one another. The first principle gives the partners the freedom to settle their mutual rights and duties by their own voluntary agreement. The statement of duties and rights should be prefaced with the contents of Section 11 which gives freedom to partners, subject, of course, to the provisions of the Act, to determine their mutual rights and duties by their own agreement. Certain duties, as stated in the chapter, are of compulsory nature and, therefore, cannot be altered by an agreement to the contrary. But, subject to that, the partners can settle their rights and obligations inter se by their own contract.

The second principle of high importance is that relations of partners to one another are based upon the fundamental principle of absolute good faith. Every partner is an unlimited agent of his co-partners for all matters connected with the business and, therefore, has the power to bind them into any amount of liability. Mutual trust and confidence among the partners, therefore, becomes a necessary condition of their relations. Section 9 gives statutory recognition to this principle by providing that "partners are bound to be just and faithful to each other" . . . . This duty cannot be excluded by any agreement to the contrary. Commenting upon his fiduciary obligation Bacon VC observed in *Helmores v Smith*:

If fiduciary relationship means anything I cannot conceive a stronger case of fiduciary relations than that which exists between partners. Their mutual confidence is the life blood of the concern. It is because they trust one another that they are partners in the first place; it is because they continue to trust one another that the business goes on.

The statutory rights of partners can be enumerated as under:

1. Right to take part in business [S. 12(a)]
2. Majority rights [S.13(c)]
3. Access to books [S. 12(d)]
4. Right to indemnity [S.13(e)]
5. Right to profits [S. 13(b)]
6. Right to interest on capital [S. 13(c) and (d)]
7. Right to remuneration [S. 13(a)].

In Short, the Partnership Deed contains the mutual rights, duties and obligations of the partners, in certain cases, the Partnership Act also makes a mandatory provision as regards to the rights and obligations of partners. When there is no Deed or the Deed is silent on any point, rights and

obligations as provided in the Partnership Act shall apply.

### **1. Right to take part in business [S. 12(a)]:**

According to Section 12(a), every partner has a right to take part in the conduct of the business. Since the business of partnership belongs to all the partners, every partner is entitled to take part in the conduct of the business. The partners are free to provide in their agreement that only some of them will take part in the conduct of the business and certain other partners will not. If such a right is wrongfully denied to a partner, he can seek the enforcement of the right through a court of law. If the right to manage the business has been conferred on only some of the partners, they alone will be entitled to this right.

In *Suresh Kumar v Amrit Kumar*, The Delhi High Court issued an injunction against a partner who, in order only to undermine the position of the managing partner, wrote to the principals of the firm not to supply motor vehicles and to the bankers not to honour the firm's cheques.

**2. Majority rights or Right to express opinion [S. 13(c)]:** Section 13(c) contains the following provision with regard to the right of a partner to express the opinion in the partnership matters:

(c) any difference arising as to ordinary matters connected with the business may be decided by a 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 the partners.

According to the above stated provision, when there is difference of opinion between the partners, majority of the partners cannot ignore the minority and take decisions without consulting them. The difference of opinion may be either (i) as to ordinary matters connected with the business, or (ii) matters of fundamental importance.

When the difference of opinion pertains to an ordinary or routine matter connected with the business, the same may be resolved by a decision of the majority of the partners. But before the matter is decided every partner must be provided with an opportunity to express his opinion.

In *Highley v Walker* the partners were divided over the question of the introduction of a partner's son into the business with a view to his learning the business, it was held that the difference related to an ordinary matter of business and, therefore, majority opinion should prevail.

In this connection Lord Eldon observed, "I call that the act of all, which is the act of the majority, provided all are consulted, and the majority are acting bona fide, meeting not for the purpose of

negating, what anyone have to offer, but for the purpose of negating, what, when they met together, they may, after due consideration, think proper to negative: For a majority of the partners to say, 'We do not care what one partner may say, we, being the majority, will do what we please, is, I apprehended, what this Court will not allow.' The power of the majority has to be exercised in good faith. If, for instance, the majority of the partners decide to expel a partner without sufficient cause, the expulsion would be set aside."

When the matter is not an ordinary or a routine matter but is of fundamental importance, consent of all the partners is needed. Admission of a new partner to the firm or a change in the nature of the business are the matters of this nature. The partnership deed may, however, provide that in all matters majority opinion shall prevail. The manner in which majority powers should be exercised was explained in *Blisset v Daniel*:

The plaintiff was working in partnership with certain persons. It was proposed to appoint one of the partner's son as a co- manager of the firm. The plaintiff objected. The aggrieved father complained to his partners behind the back of the plaintiff and persuaded them to sign and serve upon the plaintiff a notice of expulsion. This was done in the exercise of a power which authorised a majority to expel any partner without giving any reason.

The plaintiff contested the validity of the expulsion and it was set aside. The court pointed out that powers are given to the majority so that in case of need they may be exercised in good faith for the benefit of the firm. It is no doubt for the partners to decide what is in the interest of the firm but they must do so in good faith. Majority powers should not be used for base or unworthy purposes or merely to injure a co-partner.

### **3. Right To Have Access To Books Of The Firm. [Section 12(D)]**

According to Sec. 12(d), every partner has a right to have access to and to inspect and copy any books of the firm. This right is available to both active and dormant partners. This right is not only in respect of books of accounts but in respect of any books of the firm.

A partner may exercise this right himself or by agent, but either can be restrained from making use of the knowledge thus gained against the interest of the firm. A partner can have the accounts inspected through an agent and need not do it personally. For example, where a sleeping partner wanted to sell his interest to the other partners and authorised an expert valuer to inspect accounts to ascertain the value of his interest, it was held that the other partners could not object to it, unless they could show some reasonable grounds for their objection such as for example,

protection of trade secrets (*Bevan v Webb*). The right to inspect papers, however, does not include the right to carry them, without the consent of the other partners, to any other place than the registered office of the company (*Floydd v Cheney*).

#### **4. Right To Share Profits [Section 13(B)]**

Every partner has a right to share the profits. Generally, the partners provide in their agreement as to what will be the proportion in which they will share the profits. For example, in a firm of three partners, it may be agreed that the profit sharing

Proportion will be 2/4:1/4:1/4. According to Section 13(b), in the absence of any such agreement, the partners are to share the profits equally and also to contribute equally to the losses sustained by the firm and not in the proportion in which various partners contribute capital (*Mansha Ram v Tej Bhan*).

In *Robinson v Anderson*, two solicitors were jointly retained to defend certain actions and there was no satisfactory evidence to show in what proportion they were to divide their remuneration. It was held that they were entitled to share it equally although they had been paid separately and had done unequal amount of work.

If any partner alleges that their shares are unequal, he has to prove an agreement to that effect. Since every partner is entitled to share the profits, no other remuneration, as a general rule, is to be paid to a partner for the management of the firm's business. The rule contained in this regard in Section 13(a) is that a partner is not entitled to receive remuneration for taking part in the conduct of the business, unless otherwise agreed. Thus, it is only if the partners so agree a partner may be entitled to additional salary, commission, etc. for the efforts made by him in running the business of the firm.

#### **5. Right To Interest On Capital And Advances [Section 13(C) & (D)]**

Generally, no interest on capital subscribed by the partners is to be given because the partners share the profits of the business of the firm. In case the partners agree that interest on capital is to be given, according to Sec. 13(c), such interest shall be payable only out of profits (*Keshavji Ravji & Co v CIT*).

Sometimes over and above the capital subscribed by the partners, the firm may need extra money. In case a partner makes any payment or advance beyond the amount of capital he has agreed to subscribe, he is entitled to interest thereon at the rate of six per cent per annum, according to Sec. 13(d).

So far as interest on capital contribution is concerned, it ceases to run from the date of dissolution

*(Somasundaran v S. Chettiar).*

## **6. Right To Indemnity [Section 13(E)]**

A partner while acting on behalf of the firm may make certain payments and also incur some liabilities. According to Sec. 13(e), he is entitled to claim indemnity for the same. The indemnity can be claimed for the acts done by a partner in the ordinary and proper conduct of the business and also for doing some act in an emergency for the purpose of protecting the firm from the loss.

Thus the Act provides for two kinds of indemnity. In the first place, a partner is entitled to recover from the firm any expenses incurred by him "in the ordinary and proper conduct of the business". These words constitute an important condition of this right and were explained in *Thomas v Atherton*:

T, the managing partner of a colliery, received notice from L, an adjoining owner that the workings were being carried on beyond the boundary. T insisted that he was entitled to the disputed ground, and carried on his working. The matter, having been referred to arbitration, he was held liable to pay £6000 as damages for the trespass. His claim for contributions from his co-partners failed as the loss was not suffered in the ordinary and proper conduct of the business.

He worked beyond the limits of the partnership colliery without proper inquiry as to limits and had acted with gross negligence and recklessness in continuing his working after notice and without consulting his partner, when it was evident that his right to work in the disputed area was extremely doubtful.

The second kind of indemnity is recoverable when a partner has done an act involving expenditure in order to protect the property of the firm from a loss threatened by an emergency. It is necessary that the partner concerned should have acted as a reasonable person would have acted in his own case.

Proof of actual loss attributable to the conduct of a partner is necessary and not merely one which is imagined or notional (*T.B. Mody v Ghanshyam J. Sanghrajka*).

The right to indemnity is not lost by the dissolution of the firm and it also does not matter that there is or has been no settlement of accounts (*Sadhu Narayana Aiyangar v Ramaswami*).

## **7. Right To Remuneration [S. 13(A)]**

Unless otherwise agreed, partners are not entitled to receive salary or remuneration for taking part in the conduct of the business. Section 13(a) so provides:

*A partner is not entitled to receive remuneration for taking part in the conduct of the business.*

The partnership agreement may, however, provide for the payment of remuneration to the working partners (*Garwood's Trusts, re*). But even so a firm cannot be regarded as an employer of a partner. A contract of service stipulates two different persons whereas a firm and its partners are one and the same thing. The so-called remuneration paid to the partners is in reality a distribution of profits (*C. V. Mulik v CIT (Ag)*). It has been observed that in the United States, Great Britain and Australia, a partner is not treated as an employee of his firm because he receives a wage or remuneration for work done for the firm. Even where a partner renders extraordinary services, in the absence of an agreement, he cannot claim remuneration for such services (*Shelat Bros v Nanalal Harilal Shelat*). The Sind High Court acted upon the same principle in a case where a licensed business was being managed by an agent under the supervision of the licensed partner and the other unqualified partner was doing nothing. Even so no remuneration was allowed to the qualified partner (*Hassanand Jethanand v Bassarmal*). Aston JC captured points from different cases:

It is well known principle that under ordinary circumstances the contract of partnership excludes any implied contract for payment for services (*Thompson v Williamson*). In the absence of an agreement one partner cannot charge his co-partners with any sum for compensation in the form of salary or otherwise (*Whittle v M'Farlane*), even where the services rendered by the partners were exceedingly unequal (*Webster v Bray*).

### **Duties of a Partner:**

The duties of partners which emerge from the provisions of the chapter can be briefly enumerated thus:

1. Duty of absolute good faith [S. 9]
2. Duty not to compete [S. 16(b)]
3. Duty of due diligence [Ss. 12(b) and 13(/)]
4. Duty to indemnify for fraud [S. 10]
5. Duty to render true accounts [S. 9]
6. Proper use of property [S. 15 and S. 16(a)]
7. Duty to account for personal profits [S. 16]

The duties of a partner are as follows:

**i. To carry on the business to the greatest common advantage:** Every partner is bound to carry on the business of the firm to the greatest common advantage. In other words, the partner must use his knowledge and skill in the conduct of business to secure maximum benefits for the firm.

**ii. To be just and faithful to each other:**

Every partner must be just and faithful to other partners of the firm. Every partner must observe utmost good faith and fairness towards other partners in business activity.

**iii. To render true accounts:**

Every partner must render true and proper accounts to his co-partners. Each and every entry in the books must be supported by vouchers and explanations if demanded by other partners.

**iv. To provide full information:**

Every partner must provide full information of all activities affecting the firm to the other co-partners. No information should be concealed, kept secret.

**v. To attend diligently to his duties:**

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

**vi. To work without remuneration:**

A partner is not entitled to receive any kind of remuneration for taking part in the conduct of the business. But in practice, the working partners are generally paid remuneration as per agreement, so also commission in some cases.

**vii. To indemnify for loss caused by fraud or wilful neglect:**

If any loss is caused to the firm because of a partner's willful neglect in the conduct of the business or fraud committed by him against a third party then such partner must indemnify the firm for the loss.

**viii. To hold and use partnership property exclusively for the firm:** The partners must hold and use the partnership property exclusively for the purpose of business of the firm not for their personal benefit.

**ix. To account for personal profits:**

If a partner derives any personal profit from partnership transactions or from the use of the property of the firm or business connection of the firm or the firm's name, he must account for such profit and pay it to the firm.

**X. Not to carry on any competing business:**

A partner must not carry on competing business to that of the firm. If he carries on and earns any profit then he must account for the profit made and pay it to the firm.

**Xi. To share losses:**

It is the duty of the partners to bear the losses of the firm. ' partners share the losses equally when there is no agreement or as per their profit share ratio.

**Xii. To act within authority:**

Every partner is bound to act within the scope of authority. If he exceeds his authority and the firm suffers from any loss, he shall have compensate the firm for such loss.

**Xiii. Duty to be liable jointly and severally:**

Every partner is jointly and individual liable to the third parties for all acts of the firm done while he is a partner.

**Xiv. Duty not to assign his interest:**

A partner cannot assign or transfer his partner interest to an outsider so as to make him the partner of the firm without the consent of other partners. However, he can assign his share of the profit and his share in the assets the firm where the assignee shall not be entitled to interfere in the conduct of the business.

### **3. Liabilities Of A Partner To Third Parties:**

The following are the liabilities of a partner to third parties:

**i. Liability of a partner for acts of the firm:**

Every partner is jointly and severally liable for all acts of the firm done while he is a partner. Because of this liability, the creditor of the firm can sue all the partners jointly or individually.

**ii. Liability of the firm for wrongful act of a partner:**

If any loss or injury is caused to any third party or any penalty is imposed because of wrongful act or omission of a partner, the firm is liable to the same extent as the partner. However, the partner must act in the ordinary course of business of the firm or with authority of his partners.

**iii. Liability of the firm for misutilisation by partners:**

Where a partner acting within his apparent authority receives money or property from a third party and misutilises it or a firm receives money or property from a third party in the course of its business and any of the partners misutilises such money or property, then the firm is liable to make

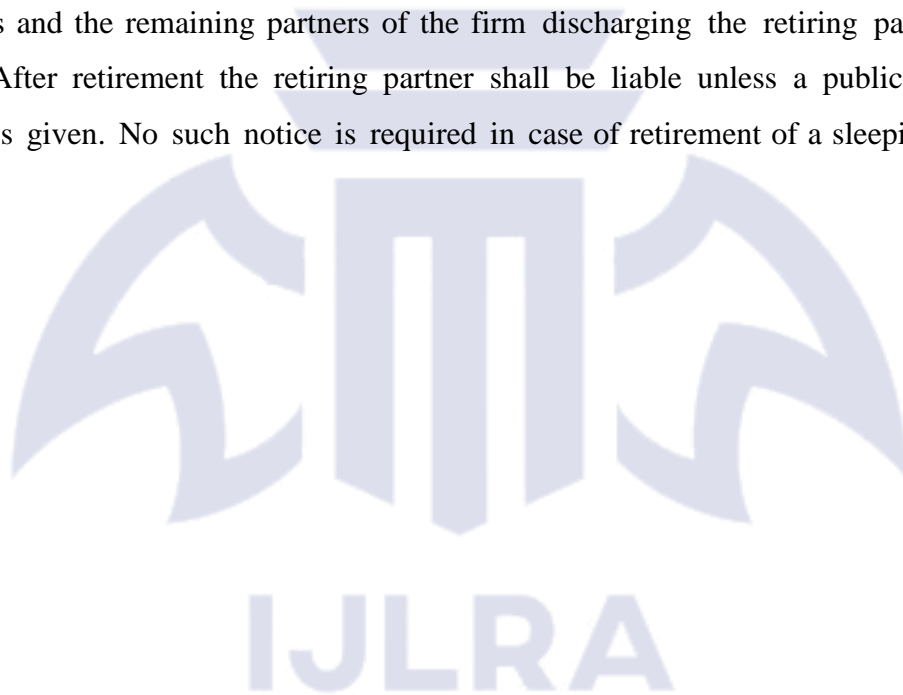
good the loss.

**IV. Liability of an incoming partner:**

An incoming partner is liable for the debts and acts of the firm from the date of his admission into the firm. However, the incoming partner may agree to be liable for debts prior to his admission. Such agreeing will not empower the prior creditor to sue the incoming partner. He will be liable only to the other co- partners.

**V. Liability of a retiring partner:**

A retiring partner is liable for the acts of the firm done before his retirement. But a retiring partner may not be liable for the debts incurred before his retirement if an agreement is reached between the third parties and the remaining partners of the firm discharging the retiring partner from all liabilities. After retirement the retiring partner shall be liable unless a public notice of his retirement is given. No such notice is required in case of retirement of a sleeping or dormant partner.



## **Conclusion:-**

In a partnership, The partners are free to outline an agreement and decide the mutual rights and duties. Relation of partners in the partnership is of paramount good faith; hence, it is the duty of every partner to work for the furthestmost common advantage of the firm and to work diligently in order to stay away from any loses to the firm. While deciding the shares of the partners in a firm it becomes very important to determine the partnership property.

Theoretically speaking, the partnership property is not anything but the joint property of every partner.

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