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CS LLM Arjun Chhabra 9552 52 143 8  
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## Chapter – 3 The Indian Partnership Act, 1932

### Unit- 1: General Nature of a Partnership

#### Definition of Partnership & its essentials

1. 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.
2. Persons competent to be Partners -
  - (a) Persons competent to enter into a Valid Contract can become Partners,
  - (b) A Minor cannot be a Partner,
  - (c) Company can be a Partner,
  - (d) Partnership between Indian Nationals and Alien Friends is possible, and
  - (e) Two Partnership Firms cannot enter into Partnership.
3. Relation of Partnership arises from an agreement and not from status.
4. Essentials of Partnership
  - 1) Association of two or more person
  - 2) Agreement between person
  - 3) Business: Business includes trade, occupation and profession. Association created for charitable, religious and social purposes are not Partnership.
  - 4) Sharing of profit: Sharing cannot be conclusive proof. It is only an evidence.
  - 5) A business carried on by all or any of them acting for all (Mutual Agency): Test of Partnership. Capacity of a Partner to bind other Partners by his acts done in Firm's name and be bound by the acts of the other Partners.

#### Specific Exclusions from Partnership:

- (a) Joint owners sharing Gross Returns arising from property held by them are not Partners.
- (b) A Partnership is NOT created when share or payment is received by -
  - a lender of money - to any persons engaged or about to engage in any business,
  - a servant or agent - as remuneration,
  - a widow or child of a deceased Partner - as annuity.
  - a previous owner or part owner of the business, as consideration for sale of G/W or share thereof.

#### Kinds of partnership

- (a) Particular Partnership - For a particular adventure or undertaking.

(b) **Partnership at Will** - Duration of Partnership is not fixed. No provision is made as to how the Partnership will come to an end.

(c) **Partnership for a Fixed Term**: Partnership entered for a Fixed Period, after the expiry of which it comes to an end.

### Kinds of partner

(a) **Actual Partner** - Partner by agreement,

(b) **Nominal Partner** - Partner only by name. He is not entitled to share the profits of the firm but is liable for all acts of the firm as if he were a real partner.

A nominal partner must give public notice of his retirement and his insanity is not a ground for dissolving the firm.

(c) **Sleeping Partner** - One who contributes to capital, no active participation in the business,

(d) **Sub-Partner** - A third party with whom the Partner shares his profits,

(e) **Minor** - can be admitted only for benefits,

(f) **Incoming Partner** - admitted to a Firm already in existence; not liable for the Firm's act done before his admission,

(g) **Outgoing Partner** - Partner who leave the Firm due to retirement, death, insolvency or expulsion,

(h) **Partner by Holding Out**: Partnership by holding out is also known as partnership by estoppel. Where a man holds himself out as a partner, or allows others to do it, he is then stopped from denying the character he has assumed and upon the faith of which creditors may be presumed to have acted.

The rule given in Section 28 is also applicable to a former partner who has retired from the firm without giving proper public notice of his retirement. In such cases, a person who, even subsequent to the retirement, give credit to the firm on the belief that he was a partner, will be entitled to hold him liable.

(i) **Partner in profits only** - Partner shall get a share only in the Profits and shall not be liable to contribute towards losses.

## Unit- 2 Relations of partners - Very Important unit

### Reconstitution of firm

#### Expulsion of a Partner [Sec. 33]

- (a) **Expulsion of a Partner [Sec. 33]:** A Partner cannot be expelled from a Firm by a **majority of Partners** except in the exercise in good faith of powers conferred by the contract between the Partners.
- (b) **Good Faith:** Hence, for any expulsion by majority, it is necessary that -
- The **power of expulsion** must have existed in the contract between Partners,
  - Such power has been exercised by a **majority of the Partners**, and
  - Such power has been exercised in **good faith** for the interest of the Firm and not used as vengeance against a Partner.
- (c) **What constitutes Good Faith?** An expulsion is said to be in good faith if -
- Such expulsion is done to **protect the interests** of Partnership and of the Firm,
  - The Partner who is to be expelled had been **served with a Notice**,
  - Such Partner has given an **opportunity of being heard**.
- (d) **Expulsion Void:** When a Partner is otherwise expelled than in good faith, it is null and void. He continues to be a Partner, and can (a) claim reinstatement or (b) sue for the refund of his share of Capital and profits in the Firm.
- (e) **Position of Expelled Partner:** The provisions of Sec. 32 regarding liability of a Retired Partner to Third parties and giving of public notices apply to an expelled Partner as well, as if he was a retired Partner.

Partner may be expelled by **majority rule**, where the contract provides for it and such right is exercised in **good faith** and for **Firm's benefit**. Partner expelled otherwise than in good faith is null and void.

#### Death [Sec. 35]

##### Liability of estate of deceased partner [Sec. 35]:

The Firm is generally dissolved on the death of a Partner. If it is not dissolved, the estate of the deceased Partner is not liable for the Firm's act after the death of the Partner.

## Transfer of interest [Sec. 29]

### Rights of transferee or a partner's interest [Section 29 of The Indian Partnership Act, 1932]

A share in a partnership is transferable like any other property, but as the partnership is based on a mutual agency, the transferee of a partner's interest by sale, mortgage or otherwise, cannot enjoy the same rights and privileges as the original partner.

In the light of the above provision and facts of the case Mr. M can validly transfer his interest in the firm by way of sale.

### The rights of a transferee (Mr. Z) are as follows:

1. During the continuation of the partnership, such transferee is not entitled
  - a) to interfere with the conduct of the business,
  - b) to require accounts, or
  - c) to inspect the 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 dissolution of the firm or on the retirement of the transferring partner, the transferee partner is entitled [Section 29(2)]

- a) to receive the share of 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 from the date of the dissolution.

## Insolvency [Sec. 34]

### Insolvency [Sec. 34]:

- (a) When a Partner in a Firm is adjudicated insolvent, he **ceases** to be a Partner on the **date of the order**, irrespective of whether the Firm is dissolved or not.
- (b) When under a contract between the Partners, the Firm is **not dissolved** by the insolvency of a Partner, the estate of such Partner is **NOT liable** for any act of the Firm.
- (c) Also, further the Firm is **NOT liable** for any act of the insolvent, done after the date on which the order or adjudication is made.

## Retirement [Sec. 32]

### Retirement [Sec. 32]:

Partner may retire -

- (a) with other Partner's Consent,
- (b) in accordance with express agreement,
- (c) by giving written notice of his intention to retire.

Public Notice has to be given on retirement either by Retiring Partner or any Partner of Reconstituted Firm.

## Authority of Partner [Sec 19-22]

### Implied authority of partner [Section 19 & 22]

**Implied Authority:** 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.

**Conditions -**

- (i) act must relate to normal business,
- (ii) done in the usual way of carrying on the Firm's business, and
- (iii) done in the name of the Firm.

### Acts outside Implied Authority [Sec. 19(2)]

In the absence of any usage or custom of trade to the contrary, implied authority of a Partner does not enable him to

- (a) Submit to arbitration, a dispute relating to the business of the Firm,
- (b) Open a bank account on behalf of the Firm in Partner's own name,
- (c) Compromise or relinquish any claim or portion of claim by the Firm,
- (d) Withdraw any suit or proceeding filed on behalf of the Firm,
- (e) Admit any liability in a suit or proceeding against the Firm,
- (f) Acquire immovable property on behalf of the Firm,
- (g) Transfer immovable property belonging to the Firm,
- (h) Enter into Partnership on behalf of the Firm.

## Extension and restriction of partner's implied authority - Section - 20

### Section - 20 Extension and restriction of partner's implied authority

- (a) The Partners, by mutual agreement, can restrict or extend the Implied Authority of any Partner.
- (b) Notwithstanding any 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
  - So, a third party is not affected by limitation of implied authority unless he has actual notice of it.

## Partner's authority in an emergency - Section 21

### Partner's authority in an emergency [Sec. 21]

In case of an emergency, a Partner has the authority to do all such acts so as to protect the Firm from loss, as would be done by a man of ordinary prudence under similar conditions. These acts bind the Firm even though they do not form part of the Partner's implied authority.

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

- 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.
- 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.
- 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.

## Minors admitted to the benefits of partnership - Section 30

**Position of Minor on attaining majority:** The Minor Partner has to decide whether he shall remain a Partner or leave the Firm, within 6 months of his attaining majority, or his obtaining knowledge that



he had been admitted to the benefits of the Firm. He shall give Public Notice of his intention. Where he fails to give notice, he becomes a Partner in the Firm on the expiry of such period.

### Personal profits earned by partners - Section 16

Subject to the contract between the partners, -

(a) if a partner derives any profits 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.

### Effect of notice to acting partner - Section 24

According to Section 24 of the Indian Partnership Act, 1932, 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.

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.

### Remuneration to partners - Section 13(a)

By virtue of provisions of Section 13(a) of the Indian Partnership Act, 1932 a partner is not entitled to receive remuneration for taking part in the conduct of the business. 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.

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.

### Right of outgoing partner in certain cases to share subsequent profits - Section 37

**Retirement / Death of Partner:** 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.

- (i) 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
- (ii) 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 shall be entitled, at his option to:

- (i) the 20% shares of profits (as per the partnership deed); or
- (ii) interest at the rate of 6 per cent per annum on the amount of A's share in the property.

### Rights of outgoing Partner to Carry on competing business - Section 36

Every outgoing partner has a right to carry on a competing business and to advertise such business. But, he cannot

- (i) use the firm's name,
- (ii) represent the firm, or
- (iii) solicit the firm's customers.

He may sometimes agree with his Partners that on his cessation, he will not carry on a business similar to that of Firm within - (a) a specified period or (b) 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.

### Continuing guarantee & Goodwill [Section 38 & 14]

**Revocation of continuing guarantee (Section 38 of the Indian Partnership Act, 1932)**

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. Such change may occur by the death, or retirement of a partner, or by introduction of a new partner.

OR

**Goodwill:** The term "Goodwill" has not been defined under the Indian Partnership Act, 1932. Section 14 of the Act lays down that goodwill of a business is to be regarded as a property of the firm.

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.

Difference between		
Basis of difference	Partnership	Co-ownership
1. Formation	Partnership always arises out of a contract, express or implied.	Co-ownership may arise either from agreement or by the operation of law, such as by inheritance.
2. Implied agency	A partner is the agent of the other partners.	A co-owner is not the agent of other co-owners.
3. Nature of interest	There is community of interest which means that profits and losses must have to be shared.	Co-ownership does not necessarily involve sharing of profits and losses.
4. Transfer of interest	A share in the partnership is transferred only by the consent of other partners.	A co-owner may transfer his interest or rights in the property without the consent of other co-owners.

CS LLB LLM Arjun Chhabra 9552 52 143 8

CS LLB LLM ARJUN CHHABRA

## Unit 3 - Registration and dissolution of a firm

### Registration of firm

1. Registration of the Firm is **not mandatory** under the Act.
2. **Registration does not create Partnership**, but it is **only the evidence** of existence of a Partnership.
3. Registration is **effective from the date** when the **Registrar** files the statement and **makes entries in the Register of Firms** and not from the date of presentation of the Statement to him.
4. Disabilities of Unregistered Firms -
  - (a) **Cannot sue the Firm or any other Partner/ Aggrieved partner cannot bring legal action against other partner or the firm** unless the firm is registered and the persons suing are or have been shown in the register of firms as partners in the firm.
  - (b) **cannot file a suit against third party/ No suit in a civil court by firm or other co-partners against third party, and**
  - (c) **cannot claim a set off.**
5. Non Registration of Firm does not affect -
  - (a) **Right of third parties to sue the Firm**
  - (b) **The right of partners to sue for**  
the **dissolution** of the firm or for  
the **settlement of the accounts** of a dissolved firm, or  
for **realization of the property** of a dissolved firm.
  - (c) **Power of Official Assignee to bring a suit on behalf of the Insolvent Partner**
  - (d) **Right of the Firm to institute a suit or claim of set-off not exceeding 100**
  - (e) **The right to suit and proceeding instituted by legal representatives or heirs of the deceased partner of a firm for accounts of the firm or to realise the property of the firm.**

### Dissolution of firm

S. NO.	BASIS OF DIFFERENCE	DISSOLUTION OF FIRM	DISSOLUTION OF PARTNERSHIP
1.	Continuation of business	It involves <b>discontinuation</b> of Business in partnership.	It does not affect continuation of business. It involves only <b>reconstitution</b> of the firm.
2.	Winding up	It involves <b>winding up</b> of the firm and requires realization of assets and settlement of liabilities.	It involves only <b>reconstitution</b> and requires only <b>revaluation</b> of assets and liabilities of the firm.

3.	Order of court	A firm may be dissolved by the order of the court.	Dissolution of partnership is not ordered by the court.
4.	Scope	It necessarily involves dissolution of partnership.	It may or may not involve dissolution of firm.
5.	Final closure of books	It involves final closure of books of the firm.	It does not involve final closure of the books.

