

## General Nature of Partnership

### Definition:-

Section 4 - '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'.

Partnership Deed - The document in writing containing various terms and conditions as to the relationship of the partners to each other is called the 'partnership deed'. It contains -

1. NAME - firm, partners, 2. Nature and place of the business of the firm, 3. Date - Commencement & Duration, 4. Partners - Capital Contribution, PSR, Admission & Retirement, Rate of Interest on capital, Drawings. 5. Provision- settlement of accounts, Salaries or commissions, expulsion, etc.

### True test of Partnership - Must be proved that -

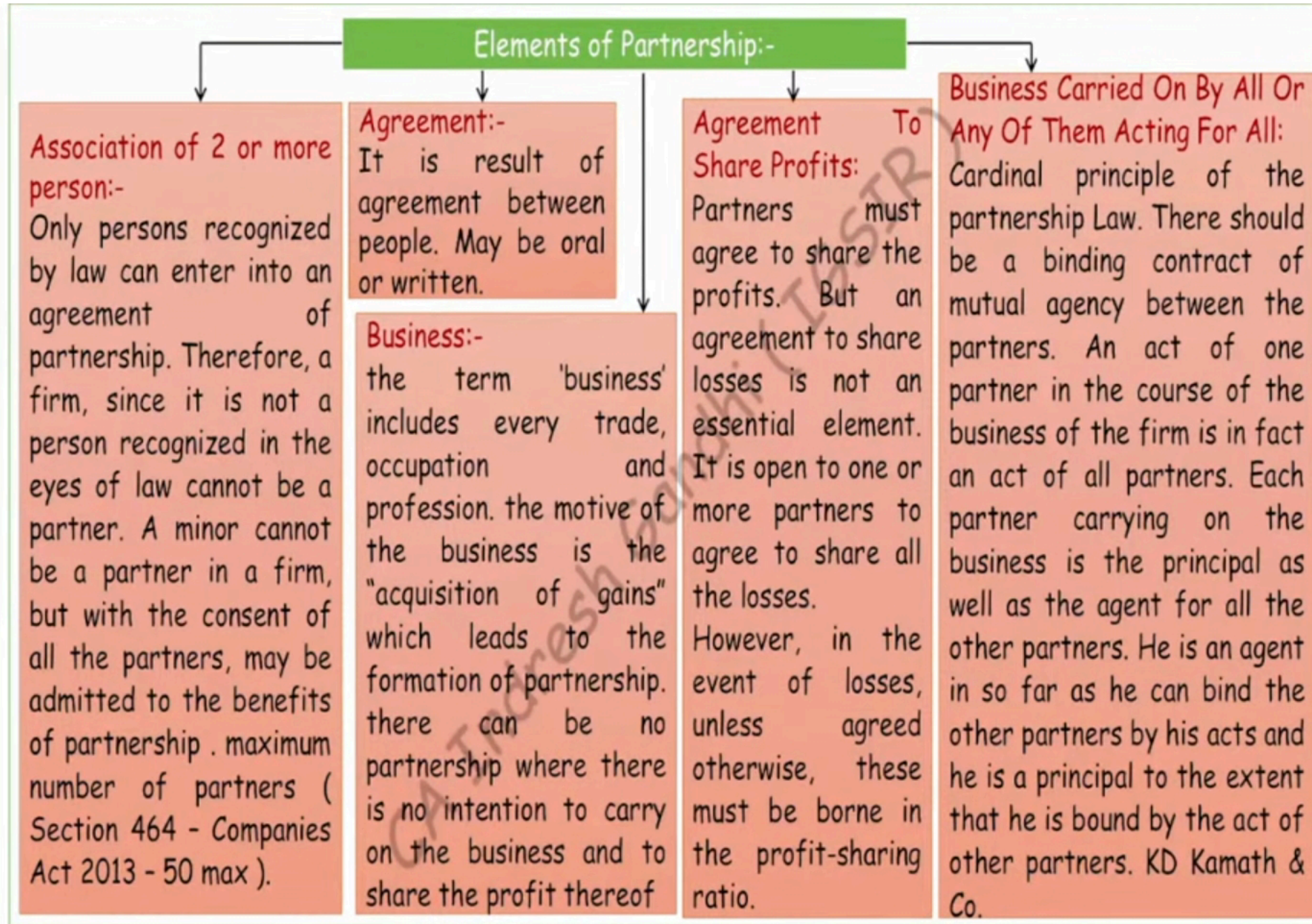
1. Agreement: Partnership is created by agreement and not by status

2. Sharing of Profit: 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. It is only a prima facie evidence and not conclusive evidence. Cumulative effect of all relevant facts such as written or verbal agreement, real intention and conduct of the parties, other surrounding circumstances etc., are to be considered while deciding the relationship between the parties and ascertaining the existence of partnership.

3. Agency : Each partner carrying on the business is the principal as well as an agent of other partners. So, the act of one partner done on behalf of firm, binds all the partners. Santiranjana Das Gupta Vs. Dasyran Murzammul (Supreme Court).







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### Difference between Partnership and Joint Stock Company:-

- ✓ **Legal Status** - firm is not legal entity whereas joint stock is separate legal entity.
- ✓ **Agency** - Every partner is agent of other partners as well as of firm whereas member is not agent of other member or of company.
- ✓ **Distribution of profits** - profits are distributed among the partners according to the deed whereas there is no compulsion to distribute its profit.
- ✓ **Extent of liability** - partners have unlimited liability whereas liability of member depends on the type of company.
- ✓ **Transfer of shares** - Share in firm cannot be transferred without consent of all partners whereas transfer of shares in company are subject to article.
- ✓ **Management** - Partners are entitled to take part in management whereas members are not.
- ✓ **Registration** - Not compulsory for firm but compulsory for company.
- ✓ **Max. No.** - firm: 50, company - Pvt co. - Min 2, max 200; Public co. - Min -2, Max - no limit.

### Difference between partnership and club:-

- ✓ **Relationship** :- persons forming firm are called partners whereas persons forming club are called members.
- ✓ Partner have **interest in property** of firm whereas members of club don't.
- ✓ **Dissolution**:- Change in partners affect the existence of firm whereas change in member of club doesn't.

### Difference between Partnership and HUF :-

- ✓ Partnership is **created by** agreement whereas HUF is created by birth in family.
- ✓ **Death of member** :- Firm - leads to dissolution, HUF - no dissolution
- ✓ **Management** :- Firm - all partners, HUF - karta
- ✓ Every partner has **authority to bind** the firm whereas HUF only karta has authority.
- ✓ **Liability**:- Partner - unlimited; karta - unlimited and co parcener - liable only to extent of share.
- ✓ Firm is **governed by** Partnership act; HUF by hindu law.

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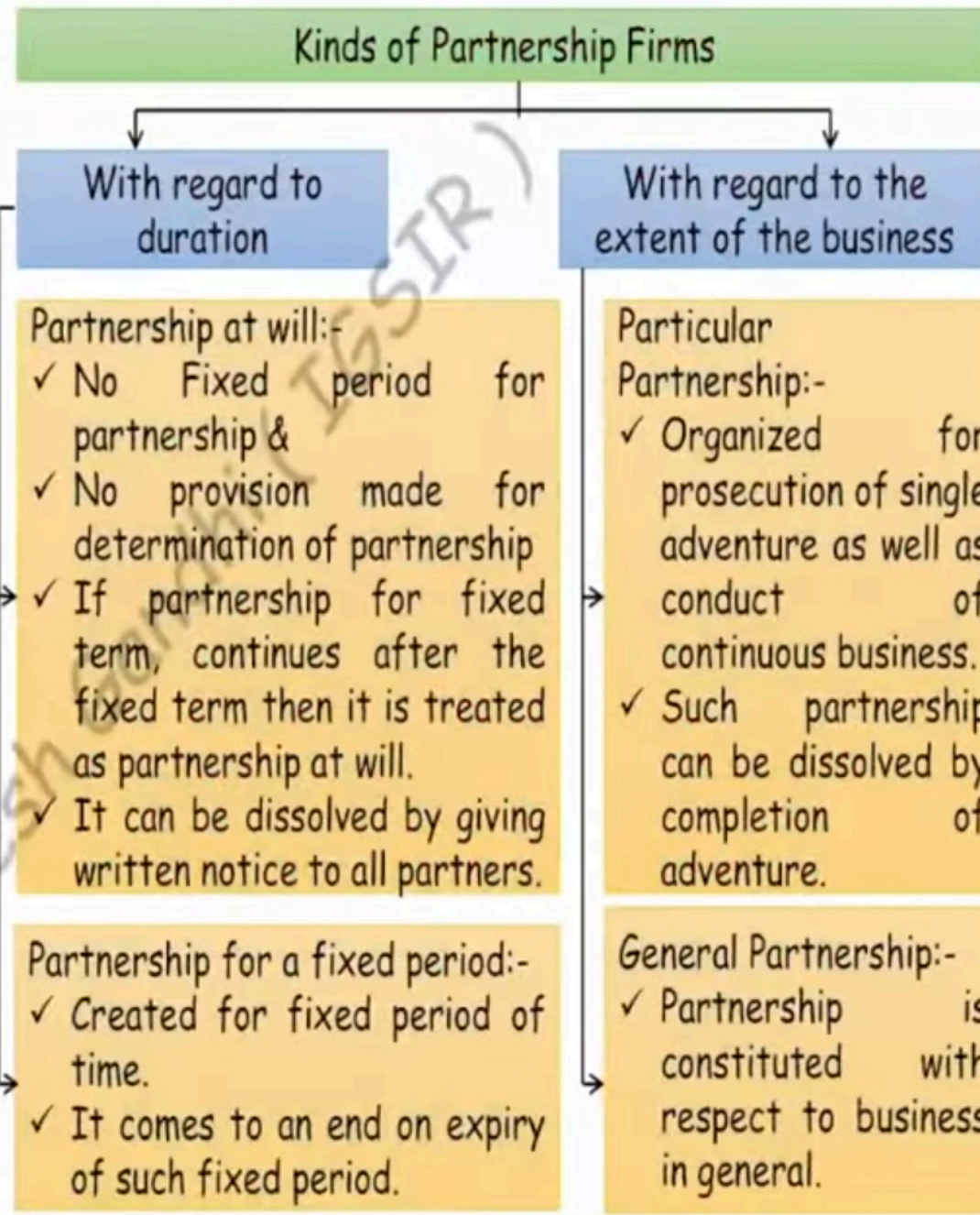


### Difference between Partnership and Co ownership -

- ✓ Partnership arises out of a contract whereas co ownership can arise out of agreement/operation of law
- ✓ Partner is agent of other partners whereas co owner is not agent of other.
- ✓ Profits and losses needs to be shared whereas co owner cannot be shared.
- ✓ Share in partnership is transferable on consent of all the partners whereas transfer of share of co owner can be made without any consent.

### Difference between Partnership and Association -

- ✓ Partnership evolves out of setting up a relation of agency between two or more persons who have entered into a business for gains. Whereas Association evolves out of social cause where there is no motive to earn and share profits.



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**Active Partner:-** 1. Becomes a partner by agreement. 2. Actively participates in business. 3. Acts as an agent of other partners. 4. Public notice for his retirement.

**Partner by holding out**  
1. When a person represents himself or knowingly permits himself, 2. To be represented as a partner in a firm (when in fact he is not) 3. He is liable, like a partner in the firm.

**Sleeping Partner:-**  
1. Not active part in business. 2. Liable like any other partner. 3. No public notice of retirement. 3. His insanity doesn't dissolve firm.

**Partner in Profit Only:-** 1. Entitled to share profits only. 2. Not liable for the losses. 3. Liable to third parties for all acts of profits only.

## Types of Partners

**Incoming Partner:-** 1. Person who comes into a partnership firm already in existence with the consent of all existing partners. 2. No liability for any acts of the firm done before his admission as a partner.

**Nominal Partner:-** 1. Partner only in name. 2. Not entitled to share the profits. 3. Liable as a real partner. 4. Public notice of his retirement. 5. His insanity does not dissolve firm.

**Sub Partner:-** 1. Partner agrees to share his share of profits in a partnership firm with an outsider; such an outsider is called a sub-partner. 2. Neither has rights against the firm nor is he liable for the debts of firm.

**Outgoing / Retiring Partners:-** 1. Retirement, expulsion, insolvency or death. 2. Rest of the partners continues to carry on business. 3. Remains liable to third parties for all acts of the firm until public notice of retirement is given.

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## Relations of Partners to One Another

### 1. General Duties of Partner:-

Partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner or his legal representative.

### 2. Duty To Indemnify For Loss Caused By Fraud:

Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm.

### 3. Determination Of Rights And Duties Of Partners By Contract Between The Partners:

The mutual rights and duties of the partners of a firm may be determined by contract between the partners, and such contract may be express or may be implied by a course of dealing. Such contract may be varied by consent of all the partners, and such consent may be express or may be implied by a course of dealing. Agreements in restraint of trade - Sec 27 shall be applied.

### 4. The Conduct Of The Business (Section 12):

- every partner has a right to take part in the conduct of the business. If there is an agreement with respect to this then that prevails unless there illegal act or breach of trust.
- every partner is bound to attend diligently to his duties in the conduct of the business.
- Right to be consulted - Difference arising in matters:- Ordinary matters- Decided by majority. Change in nature of business - Consent of all.
- every partner (active or sleeping) has a right to have access to and to inspect and copy any of the books of the firm.
- in the event of the death of a partner, his heirs or legal representatives or their duly authorised agents shall have a right of access to and to inspect and copy any of firm's books.

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### 5. Mutual Rights and Liabilities:- Subject to a contract between the partners -

<u>Right to remuneration</u> No additional remuneration in addition to his share in the profits unless express or customary.	<u>Right to share Profits</u> - Share Equally profits & losses	<u>Interest on Capital:</u> express agreement + trade custom + statutory provision which entitles him to such interest.	<u>Interest on advances:</u> - Int @ 6%p.a., While interest on capital account ceases to run on dissolution, the interest on advances keep running even after dissolution and up to the date of payment.	<u>Right to be indemnified:</u> If partner makes payment in the ordinary and proper conduct of the business of the firm as well as in the performance of an act in an emergency for protecting the firm - Payments which prudent man would make.	<u>Right to indemnify the firm:</u> A partner must indemnify the firm for any loss caused to it by wilful neglect in the conduct of the business of the firm.
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### RIGHTS AND DUTIES OF PARTNERS AFTER A CHANGE IN THE FIRM

- after a change in the firm
- after the expiry of the term of the firm
- where additional undertakings are carried out

Same as those in previous operation

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### PARTNERSHIP PROPERTY

1. **THE PROPERTY OF THE FIRM:** Includes property originally brought into the stock of the firm, or acquired, by purchase or otherwise, by or for the firm, or for the purposes and in the course of the business of the firm, and includes also the goodwill of the business.
2. **Property of a partner:** Where the property is exclusively belonging to a person, it does not become a property of the partnership merely because it is used for the business of the partnership, such property will become property of the partnership if there is an agreement.
3. **APPLICATION OF THE PROPERTY OF THE FIRM:** Subject to contract between the partners, the property of the firm shall be held and used by the partners exclusively for the purposes of the business

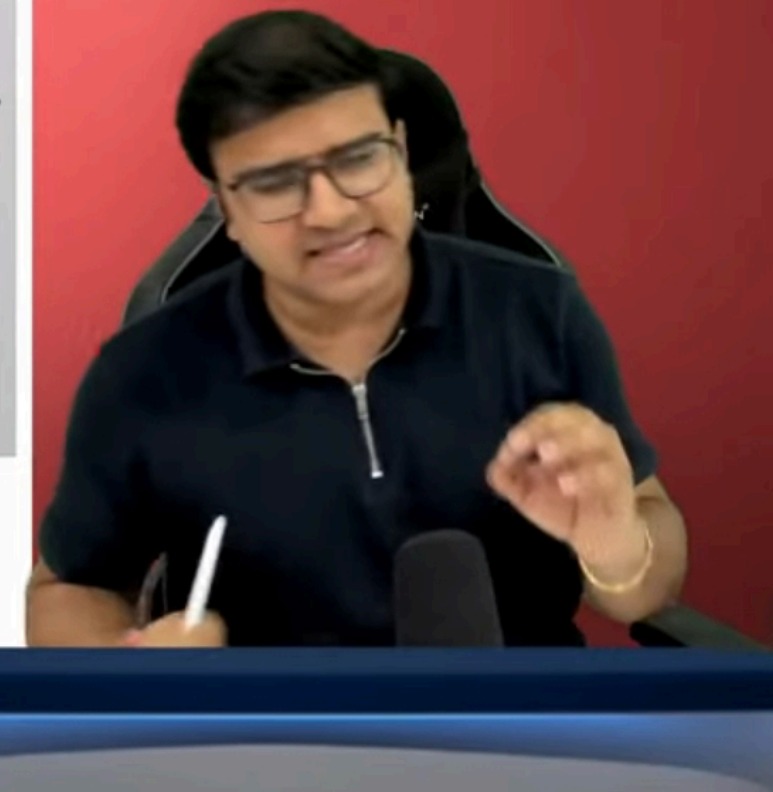
### Personal Profit Earned By Partners (Section 16) - subject to contract between the partners,-

1. If a partner derives any profit for himself from any transaction of the firm, or from the use of the property or business connection of the firm or the firm name, he shall account for that profit and pay it to the firm;
2. 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.

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## Relation of Partners to third parties.

### Partner to be Agent Of Firm -

a partner is agent of the firm for the purpose of the business of the firm. Embraces the character of both a principal and an agent.

**Implied Authority of Partner as Agent of Firm -**  
The act of a partner which is done to carry on, in the usual way, business of the kind carried on by the firm, binds the firm.

#### Include -

1. Purchase goods. 2. Sell the goods. 3. Settle accounts. 4. Receive payment of firm. 5. Engage servants for firm. 6. Engage a lawyer to defend an action brought against the firm. 7. Borrow money for firm's business. 8. Pledge the goods of the firm as security for the repayment of borrowings made for firm's business. 9. Draw, accept, and endorse bill of exchange and other negotiable instruments in the name of the firm.

#### Does not Include -

1. Submit a dispute to arbitration. 2. Opening a bank account. 3. Compromising or relinquishing any claim. 4. Withdrawal a suit or proceeding. 5. Admit any liability in a suit or proceeding. 6. Acquire immovable property. 7. Transfer immovable property. 8. Enter into partnership on behalf of the firm.

### Extension & Restriction Of Partners' Implied Authority

(consent of all the partners necessary): It may be extended/restricted by contract between partners. Restriction imposed on implied authority of partner shall be effective -  
The third party knows about the restrictions, and the third party does not know that he is dealing with a partner in a firm.

### Partner's Authority In Emergency-

to do all such acts for the purpose of protecting firm from loss as would be done by a person of ordinary prudence, in his own case, acting under similar circumstance, and such acts bind the firm.

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### MODE OF DOING ACT TO BIND FIRM:

In order to bind a firm - shall be done or executed in the firm name, or in any other manner expressing or implying an intention to bind the firm.

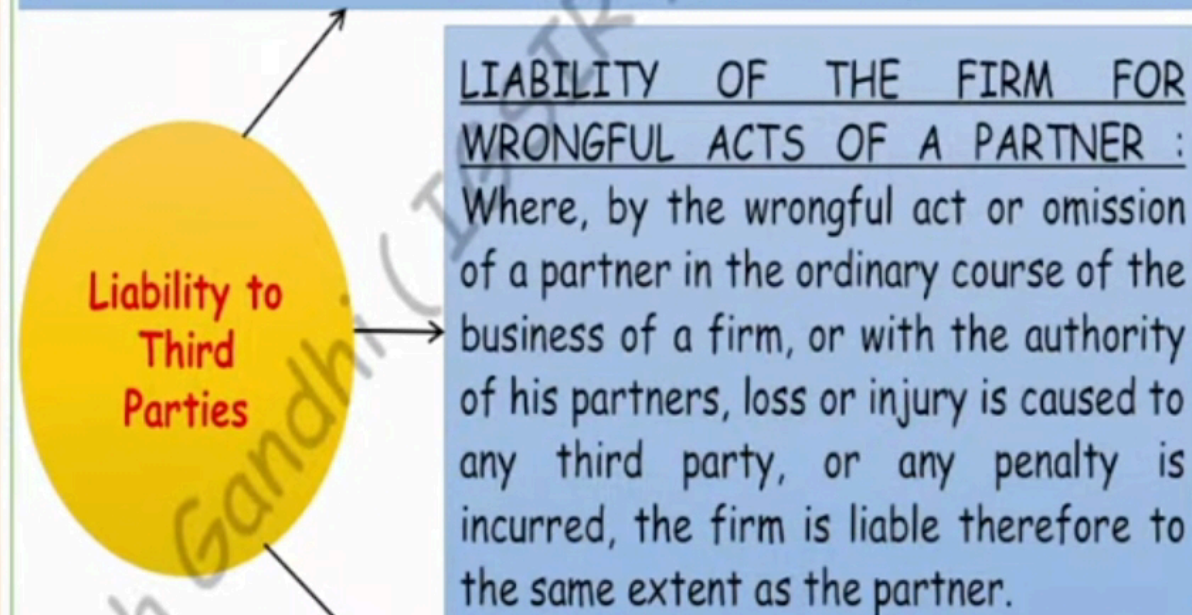
### EFFECT OF ADMISSIONS BY A PARTNER

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

### EFFECT OF NOTICE TO ACTING PARTNER

- 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. It must be received by a working partner and not by a sleeping partner.

LIABILITY OF PARTNER FOR ACTS OF THE FIRM : partners are jointly and severally responsible to third parties for all acts which come under the scope of their express or implied authority.



### LIABILITY OF THE FIRM FOR WRONGFUL ACTS OF A PARTNER :

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 therefore to the same extent as the partner.

### LIABILITY OF FIRM FOR MISAPPLICATION BY PARTNERS:

Firm is Liable in both cases -

1. where a partner acts within his authority and due to his authority as partner, he receives money or property belonging to a third party and misapplies that money or property.
2. when such money or property has come into the custody of the firm and it is misapplied by any of the partners.

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### Rights Of Transferee Of A Partner's Interest

A share in a partnership is transferable like any other property, but as the partnership relationship is based on mutual confidence, the assignee of a partner's interest by sale, mortgage or otherwise cannot enjoy the same rights and privileges as the original partner. Other partners should agree to transfer interest.

During the continuance of partnership, such transferee is not entitled:

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

He is only entitled to receive the share of the profits of the transferring partner and he is bound to accept the profits as agreed to by the partners, i.e., he cannot challenge the accounts.

On the dissolution of the firm or on the retirement of transferring partner, transferee will be entitled, against the remaining partners:

- to receive the share of the assets of the firm
- for the purpose of ascertaining the share he is entitled to an account as from the date of the dissolution.

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### Rights of Minors Admitted To The Benefits Of Partnership

1. Right to his agreed share of the profits
2. Access to, inspect and copy the accounts of the firm
3. Sue the partners for accounts or for payment of his share but **only when severing** his connection with the firm, and not otherwise.
4. On attaining majority he may within 6 months elect to become a partner or not to become a partner. If he elects to become a partner, then he is entitled to the share to which he was entitled as a minor. If he does not, then his share is not liable for any acts of the firm after the date of the public notice served to that effect

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## Liabilities of Minors Admitted To The Benefits Of Partnership

### Before attaining majority:

- a) confined only to the extent of his share in the profits and the property of the firm.
- b) no personal liability for the debts of the firm incurred during his minority
- c) cannot be declared insolvent, but if the firm is declared insolvent his share in the firm vests in Official Receiver.

### After attaining majority:

Within 6 months of his attaining majority or on his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, the minor partner has to decide whether he shall remain a partner or leave the firm. Where he has elected not to become partner he may give public notice that he has elected not to become partner and such notice shall determine his position as regards the firm. If he fails to give such notice he shall become a partner in the firm on the expiry of the said six months.

When he becomes partner: If the minor becomes a partner on his own willingness or by his failure to give the public notice within specified time -

- a) He becomes personally liable - since he was admitted to the benefits of partnership
- b) His share in the property and the profits of the firm remains the same to which he was entitled as a minor.

When he elects not to become a partner:

- a) His rights and liabilities continue to be those of a minor up to the date of giving public notice.
- b) His share shall not be liable for any acts of the firm done after the date of the notice
- c) entitled to sue the partners for his share of the property and profits

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## LEGAL CONSEQUENCES OF PARTNER GOING OUT

### RETIREMENT OF A PARTNER:

- ✓ A partner may retire: with consent of all or as per deed or if partnership is at will, by giving notice in writing to all the other partners.
- ✓ Discharge of retiring partner for acts of the firm done before his retirement 1.By an agreement b/w third party and remaining partners. 2.By an implied agreement to above effect. (E.g. Dealing between such third party and the reconstituted firm, after he (the third party) had the knowledge of the retirement.)
- ✓ A retiring partner continues to be liable as partner after the retirement until public notice is given of the retirement.

### DEATH OF A PARTNER:

- 1.The firm is dissolved unless otherwise specifically provided in deed.
- 2.The estate of the deceased partner is not liable for any act of the firm done after his death.
- 3.No public notice is required of the death of a partner.

### EXPULSION OF A PARTNER:

Three conditions: (a) As per contract between the partners & (b) Majority of the partners & (c) In good faith. If condition not fulfilled - Partner may claim re-instatement as a partner, or may sue for the refund of his share of capital and profits in the firm. (Good faith includes -interest of the firm +served with notice + oppo to be heard)

### INSOLVENCY OF A PARTNER:

- 1.The insolvent partner ceases to be a partner on the date on which the order of adjudication is made.
- 2.The firm is dissolved unless otherwise specifically provided in deed.
- 3.The estate of the insolvent is not liable for the acts of the firm done after the date of the order of adjudication.
- 4.The firm is not liable for any act of the insolvent partner after the date of the order of adjudication.
- 5.No public notice is required for insolvency.

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## LEGAL CONSEQUENCES OF PARTNER COMING IN:-

### INTRODUCTION OF PARTNER :

- ✓ No person shall be introduced as a partner into a firm without the consent of all the existing partners or as per deed.
- ✓ Admitted partner not liable for any acts of the firm done before he became a partner unless he agrees.
- ✓ Liability for the acts of the old firm only if: 1. the new firm assumes the liabilities of the old firm, and 2. the creditors accept the new firm as their debtor

### RIGHTS OF OUTGOING PARTNER:-

To carry on competing business:- but he may not- (i) use the firm name; (ii) represent himself as carrying on the business of firm, or (iii) solicit the customers who were dealing with the firm before he ceased to be a partner.

To Subsequent profits :- If final settlement is pending, legal representatives of the deceased partner or the retiring partner are entitled to any of the following two options: (a) Share of the profit earned after the death or retirement. (b) Claim interest at the rate of 6% per annum on the amount of his share in the property.

### REVOCATION OF CONTINUING GUARANTEE BY CHANGE IN FIRM

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

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## REGISTRATION OF FIRMS



**REGISTRATION OF FIRMS** -ROF may be effected at any time by sending by post or delivering to the Registrar of the area in which any place of business of the firm is situated or proposed to be situated - Statement of Fees + Fees , stating -

1. **Name** - Firm , other places where firm carries on business , partner address in full
2. place or principal place of business of the firm,
3. Date - Partner joined , Duration of firm

The statement shall be signed by all the partners, or by their agents specially authorised in this behalf.

1. Each person signing the statement shall also verify it in the manner prescribed.
2. A firm name shall not contain any of the following words, namely: 'Crown', 'Emperor', 'Empress', 'Empire', 'Imperial', 'King', 'Queen', 'Royal', or words expressing or implying the sanction, approval or patronage of Government except when the State Government signifies its consent to the use of such words as part of the firm-name by order in writing.



**REGISTRATION (SECTION 59):** Registrar is satisfied + he shall record an entry of the statement in a register called the Register of Firms, and shall file the statement.

**LATE REGISTRATION ON PAYMENT OF PENALTY (SECTION 59A-1):** 100/year + Penalty of ROF

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## CONSEQUENCES OF NON - REGISTRATION

### RIGHTS AFFECTED BY NON REGISTRATION:

1. **No suit in a civil court by firm or other co-partners against third party :** A registered firm can only file a suit against a third party and the persons suing have been in the register of firms as partners in the firm.
2. **No relief to partners for set-off of claim:** If value is more than 100 then firm or partner cant claim set off.
3. **Aggrieved partner cannot bring legal action against other partner or the firm:** A partner of an unregistered firm (or any other person on his behalf) is precluded from bringing legal action against the firm or any person alleged to be or to have been a partner in the firm. But, such a person may sue for dissolution of the firm or for accounts and realization of his share in the firm's property where the firm is dissolved.
4. **Third party can sue the firm:** In case of an unregistered firm, an action can be brought against the firm by a third party.

### RIGHTS **NOT** AFFECTED BY NON REGISTRATION :-

1. Right of third parties to sue the firm or any partner.
2. Power of an Official Assignee or Receiver or the Court.
3. Right of the partners to sue for the dissolution of the firm or for the accounts of a dissolved firm or for the realization of the property of a dissolved firm.
4. Rights of the firm or partners of firm having no place of business in India.
5. Right to sue or claim a set-off if the value of the suit upto Rs. 100.
6. Rights of partners to sue for the criminal proceedings against the other partners of the firm and against the third parties.

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**Dissolution of firm :-** means the discontinuation of the legal relation existing between all the partners of the firm

**Dissolution of Partnership :-** when only one or more partners retires or becomes incapacitated from acting as a partner due to death, insolvency or insanity, the partnership is dissolved, but the rest may decide to continue.

**Difference between dissolution of firm and partnership:-**

Basis	Dissolution of Firm	Dissolution of Partnership
Continuance of business	involve discontinuation of business.	does not affect continuation of business
Winding Up	involves winding up	Involves only reconstitution
Order of Court	May be by order of court.	Cannot be ordered by court.
Scope	involves dissolution of partnership	May or not involve dissolution of firm.
Final Closure of books	involves final closure.	Does not involve final closure.

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## **MODES OF DISSOLUTION OF FIRM** **Without order of Court or Voluntary Dissolution:-**

a. **Dissolution by Agreement (Section 40):** with the consent of all the partners or as per the contract between the partners.

b. **Compulsory dissolution:-** It happens when - 1.All but one of the partners are adjudicated as insolvent. 2.By the happening of an event which makes partnership unlawful.

c. **Dissolution on the happening of certain contingencies:-** 1.Where Firm is constituted for fixed term/particular adventure, such term/adventure is completed. 2.By death of partner, 3.By adjudication of partner as insolvent

d. **Dissolution by notice of partnership at will :** Can be dissolved when one of partners gives written notice to all the other partners. Date of dissolution shall be date mentioned in notice as such, if not mentioned then date of communication of notice.

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## DISSOLUTION BY COURT

### Transfer of interest:

Where a partner has transferred the whole of his interest in the firm to a third party or has allowed his share to be charged or sold by the court, in the recovery of arrears of land revenue due by the partner, the court may dissolve the firm at the instance of any other partner.

### Permanent incapacity:

When a partner has become in any way permanently incapable of performing his duties as partner, then the court may dissolve the firm. Such permanent incapacity may result from physical disability or illness etc.

### Misconduct:

Where a partner is guilty of conduct which is likely to affect prejudicially the carrying on of business, the court may order for dissolution of the firm. Not necessary that it must relate to the conduct of business.

### Insanity/unsound mind:

Where a partner (not a sleeping partner) has become of unsound mind, the court may dissolve the firm on a suit of the other partners or by the next friend of the insane partner. Temporary sickness is no ground for dissolution of firm.

**Just and equitable grounds** - As per court. Cases involve - Deadlock in management, partners are not on talking terms, loss of substratum, gambling on stock exchange.

**Continuous/Perpetual losses**

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**Persistent breach of agreement:** wilfully persistently commits breach of agreements relating to the management of the affairs of the firm or the conduct of business, or otherwise conduct himself in matter relating to the business that is not reasonably practicable for other partners to carry the business in partnership with him, then the court may dissolve the firm at the instance of any of the partners. Following comes in category of breach of contract: Embezzlement, Keeping erroneous accounts, Holding more cash than allowed, Refusal to show accounts etc.



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Liability for acts of partners done after dissolution:

Section 45 has two fold objectives: 1. To protect third parties dealing with the firm who had no notice of prior dissolution and 2. To protect partners of a dissolved firm from liability towards third parties.

However, there are exceptions to the rule there will be no liability for subsequent acts in the case of: the estate of a deceased partner, an insolvent partner, or a dormant partner.

## CONSEQUENCES OF DISSOLUTION

**Right** of partners to have business wound up after dissolution: partners have right to have the **property** of the firm **applied** in **payment** of the **debts** and liabilities of the firm, and to have the surplus distributed among themselves according to their rights.

Continuing authority of partners for **purposes** of **winding up** :

After dissolution, the partner's act bind the firm and other mutual rights continue as is for the purpose of winding up and completing the unfinished transaction.

However, firm is in no case bound by the **acts** of a partner who has been **adjudicated insolvent**; but this proviso does not affect the liability of any person who has after the adjudication represented himself or knowingly permitted himself to be represented as a partner of the insolvent.

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Mode of Settlement of partnership accounts : Rules for settlement:-

1. Losses, including deficiencies of capital SHALL be paid first out of profits, Capital lastly partner: PSR  
2. The assets of the firm must be applied in the following manner and order: a. debts of the firm to third parties, b. paying to each partner rateably what is due to him from capital, c. paying to each partner rateably what is due to him on account of capital, d. the residue shall be divided among the partners in PSR.

**Payment of firm debts and separate partner debts -**

Property of firm first applied to debt of firm then to separate debts. Separate partner property first applied to separate debts.

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