**MODULE II**

**PARTNERSHIP**

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# ESSENTIAL FEATURES OF PARTNERSHIP

The essential features of partnership as per the definition of partnership are listed below:

1) Association of two or more people

2) Valid Agreement

3) Created for the purpose of carrying on business

4) Sharing of Profits

5) Mutual Agency

***1) Association of two or more people:***

Minimum two people are needed to create a partnership. The Indian Partnership Act, 1932 does not prescribe any upper limit on the number of people who can be partners. However, Section 11 of the Companies Act, 1956 provides that number of partners cannot exceed 10 persons in case of banking business and 20 in other businesses. If the number of partners exceeds the limit, the partnership becomes an illegal association. Similarly, if the number falls below two, the partnership is deemed dissolved.

The people who are partners in a firm must be competent to contract. If all partners are minors or if there is only one adult partner, it is not a partnership at all.

***2) Valid Agreement***

The foundation of partnership is an agreement. Section 5 clearly states that partnership is not created by status – the relationship of partnership can arise only out of a contract. Thus, if a Hindu Undivided Family is carrying on a family business, it is not a partnership. Similarly, a Burmese Buddhist husband and wife carrying business are not partners in such business.

The partnership agreement must fulfil all the requirements of a valid contract. There should be free consent, competency of the parties, lawful consideration and object. The agreement to create partnership may be express or implied. The agreement can also be inferred from the conduct of the parties. The agreement need not be in writing except where required under the Income Tax Act or if the partners wish to get the firm registered.

Partnership does not arise by mere joint acquisition of property like in the case of co-ownership. If a wife entrusts her stridhan to her husband, it is not an agreement of partnership even if the husband uses the property for business.

***3) Created for the purpose of carrying on business:***

The partnership must have been created to carry on business. It is not necessary that all the partners actively participate in the conduct of the business. For example, one partner may contribute skill or experience while another may contribute capital for the firm. The business may be permanent or temporary, trading or non-trading.

Services rendered jointly also constitute a partnership. For example, if two advocates may agree to jointly plead a case and divide the fees, they are partners in respect to that case. But an agreement to carry on business in the future is not a partnership.

***4) Sharing of Profits:***

The purpose of a partnership is to carry on business. Thus, it is obvious that the partners have an interest in sharing the profits so earned from the business of the firm. Here, profits include losses as well. Division of profits is an important element in a partnership. There was a time when sharing of profits was used as a test to determine whether a partnership existed or not. If a person shared the profits and incurred liabilities too, he was deemed a partner as held in ***Grace vs. Smith [[1]](#footnote-1)***

However, in the present day, a person does not become a partner merely because he shares the profits of the business. Similarly, sharing of losses is not a must for a partnership. Sharing profits and contributing to losses are indications or prima facie evidence of a partnership but not the conclusive test of partnership. It is possible that a partner may be paid salary or a fixed sum periodically in lieu of profits.

In ***Cox vs. Hickman[[2]](#footnote-2)***, it was held that the conclusive test for partnership is mutual agency (*Right of all partners in a partnership to act as agents for the normal business operations of the partnership, and their responsibility for their partners' business related (but not personal) actions)* because it is possible that every man who gets a share in the profits might not be liable for the losses of the firm or might not be a partner.

For example, a servant or agent may receive a share of profits instead of his salary or as a bonus. Similarly, a person who sells his business and goodwill may be given a share of profits as consideration for sale. An employee of the firm may loan some money to the firm. But these persons do not ipso facto become partners in the firm due to such participation.

In the case of ***Mollow vs. Court of Wards*** [[3]](#footnote-3), a Hindu Raja loaned some money to a company. In return, he was given a certain percentage of profit and also allowed to exercise control on some aspects of the business. But the Raja was not empowered to direct the transactions of the company. It was held that although sharing of profits is a very strong test, the relationship of partnership depends on the real intention and conduct of the parties.

The partners can decide the ratio or proportion of share in profits and losses through an agreement between them. A partner may get more percentage of the profits than the other(s) based on factors like contribution of capital, special skills or taking a more active part in the daily functioning of the firm.

***5) Mutual Agency:***

Section 4 of the Act states that the business of the partnership must be carried on by all or any of them acting for all. Thus, there must be a relationship of mutual agency amongst all the partners.

*Mutual agency means that every partner has a dual role – that of a principal and of an agent. Every partner is an agent of the other partners and can bind other partners by his acts done on behalf of the firm in all matters that are within the scope and object of the partnership. Similarly, every agent is also the principal for the other partners in the firm and in turn, is bound by their acts.* Section 18 stresses the necessity of mutual agency again and states that a partner is an agent of the firm. The act of the partner is binding on the firm just like an act of an agent is binding upon the principal.

The foundation or basis of the law of partnership is agency. The law of partnership is undoubtedly, a branch of the law of the principal and agent. Every partner is both – an agent and principal for the other partners. For example, a notice to partner serves as a notice to the firm. The acts of a partner during the ordinary course of business bind the other partners and they are liable for the same.

Subject to limitations under Section 20 of the Act, one partner can always bind the other partner(s) in any matter that falls within the scope of partnership. Partners are not agents for each other outside of the firm or for other purposes.

In the above case, House of Lords clarified that the sharing of profits only created a rebuttable presumption of partnership. Lord Cranworth elaborated further “Where two or more persons are engaged as partners in any ordinary trade, each of them has an implied authority from the other to bind all by contracts entered into according to the usual course of business in that trade. The public have a right to assume that every partner has authority from his co-partner to bind the whole firm in contracts made according to the ordinary usages of trade.”

Whether there was a partnership or not is a mixed question of fact and law, depending upon the varying circumstances in different cases.

**Explanation:**

Partnership is an intangible relationship between two or more people. It arises only out of a contract which may be express or implied. If two or more persons work in the same business and agree to share profits and losses, it is still not a partnership unless there is mutual agency. A partner plays the role of an agent as well as that of a principal with respect to the other partners in the firm.

1. [1775 2 WM Blacks 998] [↑](#footnote-ref-1)
2. [1860 8 HL Cas 268] [↑](#footnote-ref-2)
3. [1872 LR 4 PC 419] [↑](#footnote-ref-3)