

TOPICS
Indian Partnership Act – 1932

- Partnership – Concept, Essentials, True Test of Partnership, Partnership Deed, Types of Partnership, Rights and Duties of Partners, Distinguish between Partnership & Hindu Undivided Family (HUF).
- Dissolution – Concept, Modes of Dissolution, Consequences of Dissolution.
- Limited Liability Partnership (LLP) 2008 – Concept, Characteristics, Advantages & Disadvantages, Procedure for Incorporation.
- Extent of L.L.P.- Conversion of LLP, Mutual rights & duties of partners, Winding up of LLP, Distinction between LLP and Partnership.

Partnership

Concept -

When the relation between all the partners of the firm comes to an end, this is called dissolution of the firm. Section 39 of the Indian Partnership Act, provides that “the dissolution of the partnership between all the partners of a firm is called the dissolution of a firm.” It implies the complete break down of the relation of partnership between all the partners.

Dissolution of partnership is different from the dissolution of firm.

Dissolution of a partnership firm merely involves a change in the relation of partners; whereas the dissolution of firm amounts to a complete closure of the business. When any of the partners dies, retires or become insolvent but if the remaining partners still agree to continue the business of the partnership firm, then it is dissolution of partnership not the dissolution of firm. Dissolution of partnership changes the mutual relations of the partners. But in case of dissolution of firm, all the relations and the business of the firm comes to an end. On dissolution of the firm, the business of the firm ceases to exist since its affairs are wound up by selling the assets and by paying the liabilities and discharging the claims of the partners. The dissolution of partnership among all partners of a firm is called dissolution of the firm.

Essentials of Partnership

1. Two or more persons:

There must be at least two persons to form a partnership. A person cannot enter into partnership with himself. The maximum number of persons in a partnership should not exceed 10 in case of banking business and 20 in other types of business.

If the number of partners exceeds the prescribed maximum, it would become an illegal association of persons. A firm cannot become a partner of another firm though its partners can join any other firm as partners.

2. Agreement:

Partnership is the outcome of an agreement between persons. The relation of partnership arises from the formation of a contract and not from status or birth.

If a proprietor gives a share in profits to his employee it will not be called a partnership unless there is an agreement of partnership between the two. The agreement may be oral or in writing but it must satisfy all the essentials of a valid contract.

3. Lawful business:

A partnership can be formed only for the purpose of carrying on a business. An association of persons who jointly own a house without carrying on a business is not partnership.

Moreover, the business carried on by the partners must be lawful. Illegal acts such as theft, dacoity, smuggling, etc., cannot be called partnership.

4. Sharing of profits:

The agreement between the partners must be to share the profits of business. There can be no partnership without the intention of mutual gain. The profits must be distributed among the partners in an agreed ratio.

Similarly, losses should be shared among the partners. However, sharing of profits is not a conclusive proof of partnership. For example, a manager may be given a share in profits of the firm.

5. Mutual agency:

Partnership business can be carried on by all the partners or by any of them acting on behalf of the others. In other words, every partner is an implied agent of the other partners and of the firm. Each partner is liable for acts performed by other partners on behalf of the firm.

The above mentioned features are the real tests of partnership. In addition, partnership has the following characteristics:

6. Utmost good faith:

The relations between partners are based upon mutual trust and confidence. Every partner is expected to act in the best interests of other partners and of the firm as a whole.

He must observe utmost good faith in all the dealings with his co-partners. He must render true accounts and make no secret profits from the business.

7. Unlimited liability:

Every partner is jointly and severally liable to an unlimited extent for the debts of the partnership firm. In case the assets of the firm are insufficient to pay the debts in full, the personal property of each partner can be attached to pay the creditors of the firm.

8. Restriction on transfer of interest:

No partner can transfer his share in the partnership without the prior consent of all other partners.

Partnership Deed

Partnership deed generally contains the following:

1. Name of the firm.
2. Nature of the business.
3. Names of partners.
4. Place of the business.
5. Amount of capital to be contributed by each partner.
6. Profit sharing ratio between the partners.
7. Loans and advances from the partners and the rate of interest thereon.
8. Drawings allowed to the partners and the rate of interest thereon.
9. Amount of salary and commission, if any, payable to the partners.
10. Duties, powers and obligations of partners.
11. Maintenance of accounts and arrangement for their audit.
12. Mode of valuation of goodwill in the event of admission, retirement and death of a partner.
13. Settlement of accounts in the case of dissolution of the firm.
14. Arbitration in case of disputes among the partners.

Types of Partners

- **Active Partner-** who takes active part in business. He shares the profits. He must give public notice on retirement.
- **Sleeping Partner-** A Sleeping Partner is one who contributes only capital to the business, but does not take part in its management. He is also called dormant partner or financing partner. He shares profits. He is unknown to outsiders.
- **Nominal partner-** A Nominal Partner does not contribute capital. Neither does he take active part in the management. His contribution in a partnership is limited to allowing the other partners to make use of his name. He is a person who lends his name to the firm without having any real interest in it. He does not share the profits.
- **Partner by Estoppel**
Partner by Estoppel is not a partner of the firm but by his words and conduct he leads the outsiders to believe that he is also a partner of the firm. Usually this arises, when the outgoing partner fails to give notice about his retirement.
- **Sub – Partner**
A Sub-Partner has no direct contact with the firm. He is only next to a partner. The sub-partner cannot represent the firm nor he is liable to the acts of the firm.
- **Limited Partner:** A limited partner is a partner whose liability is limited to his invested capital only. Such partner cannot take part in the management of the business but he can inspect the accounts and receive profit from the business. Moreover, a partnership cannot be established only with limited partners.
- **Minor as a partner:**
A partnership is created by an agreement. And if a partner is incapable of entering into a contract, he cannot become a partner. Thus, at the time of creation of a firm a minor (i.e., a person who has not attained the age of 18 years) cannot be one of the

parties to the contract. But under section 30 of the Indian Partnership Act, 1932, a minor 'can be admitted to the benefits of partnership', with the consent of all partners.

Types of Partnership

1. Partnership for a fixed term - Time period is fixed. Partnership gets dissolved at the expiry of the time period. Before the fixed period, it may be dissolved by mutual consent. However, if it continues after the fixed period, it becomes partnership at will.
2. Partnership at will- It is a partnership in which duration is not fixed and can be dissolved by any partner by giving a notice.
3. Particular Partnership –It is a partnership which is formed for a purpose of carrying on the particular venture. Such particular partnership comes to an end on the completion of the venture. Again if it continues after completion of the venture, it becomes partnership at will.

Rights and Duties of Partners

Rights:

1. Every partner has a right to take part in the conduct of business of the firm.
2. Every partner has a right to have an access to the books of the firm. He can examine and copy such accounts.
3. Every partner has the right to share the profits in the agreed proportion or equally if no agreement to that effect is there.
4. Subject to the contract between the partners, every partner has right to be consulted in all matters of the firm. However with regard to ordinary matters, majority rule will prevail.
5. Every partner has a right to be indemnified for the expenses incurred in the ordinary course of business and for the expenses incurred in an emergency.
6. Generally no person can be admitted as a partner without the consent of all partner. In other words, every partner has the right to be consulted for admission of new partner.
7. A partner has a right to retire with the consent of all partners or in case of partnership at will.

Duties and Liabilities of Partners

1. All partners are bound to carry on business of the firm to the greatest common benefit, and be just and faithful to each other in their mutual dealings
2. All partners are bound to render true accounts and full information of all things, affecting the firm to any partner or to his legal representative.
3. Every partner shall indemnify the loss, caused to it by his fraud in the conduct of the business of the firm.
4. Every partner is bound to attend diligently to his duties in the conduct of the business. He must use his knowledge and skill and take care to the common advantage of all partners of the firm.
5. Every partner shall indemnify the firm for any loss, caused to it by his wilful neglect in the conduct of the business of the firm.
6. A partner is liable to account to the firm, regarding the private profits earned by him.
7. Every partner is duty bound not to carry on business in competition with the firm.
8. It is the duty of every partner not to transfer his rights and interest in the firm to outsiders.

Distinguish between Partnership & Hindu Undivided Family (HUF).**1. Basis of formation**

A partnership arises out of a contract between partners. Whereas an HUF arises by the operation of Hindu Law. It is created by status or birth in the family, no agreement is needed for it.

2. Regulating law

A partnership is governed by the provisions of the Indian Partnership Act, 1932. An HUF business is governed by Hindu Law Succession Act.

3. Number of members

In a partnership business, the number of members cannot exceed 20 in case of non-banking business and 10 in case of banking business. But there is no such ceiling on the number of members (coparceners) in HUF.

4. Admission of new members

No new partner can be admitted to the existing partnership without the consent of all the other partners. In case of HUF firm, a person becomes a member (coparcener) merely by his birth.

5. Minor member

A minor cannot become a full-fledged partner in a firm; he can be admitted only to the benefits of partnership. In an HUF, a male child becomes a full-fledged member by birth.

6. Rights of females

In a partnership, women can become partners and they enjoy the same rights and privileges, as do male partners. In case of an HUF business, on the other hand, the membership is restricted to male members only. However, as per Hindu Law Succession Act, 1956, a female relative of a deceased male member gets a coparcenary interest in the event of his death.

7. Implied agency

In a partnership, every partner has implied authority to represent the firm and bind the other partners by his acts. In HUF this right rests with the Karta only, other members may be allowed by Karta expressly or impliedly to contract debts on behalf of the firm.

8. Liability of members

In a partnership, the liability of all the partners is unlimited. Every partner is jointly and severally liable to third parties for the full debts of the firm. Whereas in case of HUF, liability of each member, except the Karta, is limited to the extent of his share in the property of the family.

9. Right to accounts

Each partner not only enjoys a right to inspect the books of account of the firm and demand a copy thereof, he can even demand the accounts of the past dealings. But a coparcener has no right to ask for the accounts of past dealings. He can ask for the position of the existing assets only.

10. Mode of dissolution

A partnership firm is dissolved on the insolvency or death of a partner. But the death, lunacy or insolvency of a coparcener does not affect an HUF. It continues to operate even after the death of a coparcener.

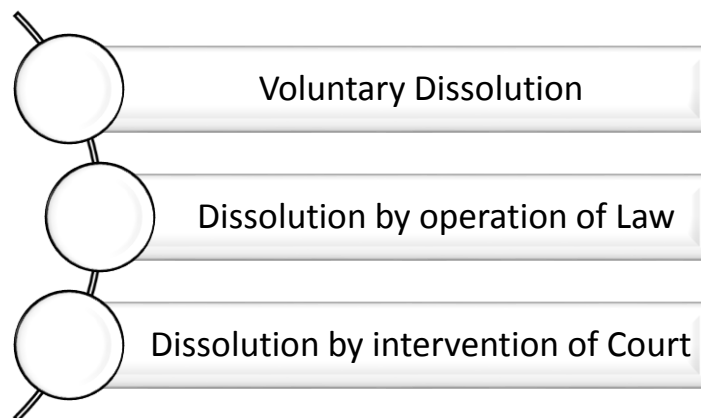
11. Management of the Business

In a partnership firm, every partner has a right to take part in the conduct and management of the firm's business, whereas in a Joint Hindu Family Firm, the members have no such rights. The head of the family exercises full control over the affairs of the business. The other members cannot interfere into the affairs of the business.

Dissolution

Meaning - When the relation between all the partners of the firm comes to an end, this is called dissolution of the firm. Section 39 of the Indian Partnership Act, provides that "the dissolution of the partnership between all the partners of a firm is called the dissolution of a firm." It implies the complete break down of the relation of partnership between all the partners.

Modes of Dissolution



A) Voluntary Dissolution

- 1) **By Consent:** All partners may consent for the dissolution of the firm. This can happen whether the firm is for a fixed duration or not.
- 2) **By Agreement:** A partnership can be dissolved in accordance with the terms of the Partnership Deed or of the separate agreement. E.g Partnership for a fixed term.
- 3) **By Notice:** Whenever a partnership is at will any partner can give a notice for dissolution, and dissolve the firm. A notice once given cannot be withdrawn without the consent of other partners.

B) Dissolution by Operation of Law This can be divided into –

- a) **Compulsory Dissolution (Sec.41):-** In case, any of the following events take place then it becomes compulsory for the firm to dissolve:

- i) **Insolvency of Partners:-** In case all the partners or all the partners except one become insolvent.
- ii) **Unlawful Business:-** In case the firm's business become unlawful on the happening of a subsequent event. e.g. trading with alien country

b) Dissolution on the happening of contingent event (S.42) A firm may be dissolved on the happening of any of the following contingent event:-

- (i) **Expiry of Fixed Period:-** If the firm is constituted for fixed period, then the firm is dissolves automatically.
- (ii) **On achievement of specific task:-** If the firm has been constituted for the achievement of specific task, on achievement of that task, firm ceases to exist, unless there is an agreement to the contrary.
- (iii) **Death of Partner:-** Death of any of the partner dissolves the partnership.
- (iv) **Insolvency of Partner:- in the absence of a contract to the contrary,** the insolvency of any of the partner may dissolve the firm.the rule shall apply even though the partnership has been constituted for a fixed term and the term has not yet expired or has been constituted for particular ventureand the same has yet not been completed.
- (v) **Resignation of Partner:-** Resignation by any of the partners dissolves the partnership

(C) Dissolution by Court:-

The court may order for the dissolution of the firm on the following grounds:-

- (i) **Insanity of Partner:-** On the application of any of the partner, court may order for the dissolution of the firm if a partner has become of an unsound mind. Lunacy of a partner does not itself dissolve the partnership but it will be a ground for dissolution at the instance of other partners. It is not necessary that the lunacy should be permanent. In the case of a dormant partner the court may not order dissolution even on the ground of permanent insanity, except in special circumstances.
- (ii) **Incapacity of Partner:-** If a partner has become permanent in capable of discharging his duties and obligations then court may order for the dissolution of firm on the application of any of the partner. Where a partner is imprisoned for a long period of time the court may dissolve the partnership.
- (iii) **Misconduct of Partner:-** If any partner other than partner suing is responsible for any loss to the firm, which amounts to misconduct and prejudicially affects the carrying on of business then the court may order for the dissolution of the firm.

(iv) **Constant breach of agreement by partner:-** The court may order for the dissolution of the firm if the partner other than the suing partner is found guilty for constant breach of agreement regarding the conduct of business or the management of the affairs of the firm and it becomes impossible to continue the business with such partner.

(v) **Transfer of Interest:-** When any of the partner other than the suing partner transfers whole of its share to the third party for permanently.

(vi) **Continuous Losses:-** The court may order for dissolution if the firm is continuously suffering losses and there is no more capital available for the future growth of the firm.

(vii) **Just and Equitable:-** The court may order for dissolution on any other ground which court think is just, fair and equitable. e.g. loss of total confidence between the partners.

Limited Liability Partnership (LLP) 2008

Limited Liability Partnership enterprise, the world wide recognized form of business organization, has now been introduced in India by enacting the Limited Liability Partnership Act, 2008. LLP Act was notified on 31.03.2009.

A Limited Liability Partnership, popularly known as LLP combines the advantages of both the Company and Partnership into a single form of organization. Limited Liability Partnership (LLP) is a new corporate form that enables professional knowledge and entrepreneurial skill to combine, organize and operate in an innovative and proficient manner.

It provides an alternative to the traditional partnership firm with unlimited liability. By incorporating an LLP, its members can avail the benefit of limited liability and the flexibility of organizing their internal management on the basis of a mutually-arrived agreement, as is the case in a partnership firm.

Characteristics of an LLP:

1. LLP is governed by the Limited Liability Partnership Act 2008, which has come into force with effect from April 1, 2009. The Indian Partnership Act, 1932 is not applicable to LLP.
2. LLP is a body incorporate and a legal entity separate from its partners having perpetual succession, can own assets in its name, sue and be sued.
3. The partners have the right to manage the business directly, unlike corporate shareholders.
4. One partner is not responsible or liable for another partner's, misconduct or negligence.
5. Minimum of 2 partners and no maximum limit.
6. Should be 'for profit' business.
7. The rights and duties of partners in an LLP, will be governed by the agreement between partners and the partners have the flexibility to devise the agreement as per their choice. The duties and obligations of Designated Partners shall be as provided in the law.

8. Limited liability of the partners to the extent of their contributions in the LLP. No exposure of personal assets of the partner, except in cases of fraud.
9. LLP shall maintain annual accounts. However, audit of the accounts is required only if the contribution exceeds Rs. 25 lakh or annual turnover exceeds Rs. 40 lakh. A statement of accounts and solvency shall be filed by every LLP with the Registrar of Companies (ROC) every year.

Advantages of LLP:

1. Separate legal entity
2. Easy to establish
3. Flexibility without imposing detailed legal and procedural requirements
4. Perpetual existence irrespective of changes in partners
5. Internationally renowned form of business in comparison to Company.
6. No requirement of minimum capital contribution.
7. No restriction as to maximum number of partners
8. LLP and its partners are distinct from each other.
9. Partners are not liable for act of other partners.
10. Personal assets of the partners are not exposed in case of fraud.
11. Easy to dissolve or wind-up.
12. Professionals like CS/CA/CWA/Lawyers can form Multi-disciplinary Professional LLP.
13. Less cost of formation(compared to a Company)

Disadvantages of LLP

1. LLP cannot raise funds from public.
2. Any act of the partner without the other may bind the LLP
3. Under some cases, liability may extend to personal assets of partners.
4. No separation of Management from owners.

Process for the Incorporation of an LLP**REQUIREMENTS FOR INCORPORATION OF LLP:****PARTNER:**

1. A minimum of two partners will be required for formation of an LLP. There will not be any limit to the maximum number of partners.
2. A body corporate can also be Partner of LLP.

DESIGNATED PARTNER:

1. Every LLP shall be required to have at least TWO DESIGNATED PARTNERS.
2. Designated Partners shall be Individuals
3. At least one of the Designated Partner shall be a resident of India.
4. In case of a LLP in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, {At least two individuals who are partners of such LLP or nominees of such bodies corporate shall act as designated partners}.

REGISTERED OFFICE:

1. Every LLP shall have a registered office to which all Communications and Notices may be addressed and where they shall be received. (Section- 13)

PROCESS FOR INCORPORATION OF COMPANY: Below Given are Seven Simple**Process for Incorporation of LLP.****STEP WISE PROCESS FOR INCORPORATION OF LIMITED LIABILITY PARTNERSHIP “LLP”****Step-I- Obtain DIN**

Every individual intending to be appointed as designated partner of a limited liability partnership has to make an application for allotment of Director Identification Number. MCA has vide its notification amended the limited liability partnership rules, 2009. Now instead of DPIN, every partner who will be appointed as designated Partner , will need to apply for DIN and not DPIN.

Step-II- Obtain Digital Signature Certificate (DSC)

Designated partner of LLP/proposed LLP, whose signatures are to be affixed on the e-forms has to obtain class 2 Digital Signature Certificate (DSC) from any authorized certifying agency. Register Digital Signature of Designated Partner on the website of Ministry of Corporate Affairs. Fill in the registration form. Fields marked * in the form are to be mandatorily filled.

Upload digital signature certificate. On successful registration, system will give a message that you have been registered successfully.

Step-III- search for name availability

Selection of business name is crucial for the image of your venture. You select a name which reflects the business you plan. Ensure selected name satisfy LLP Name Guidelines of Ministry of Corporate Affairs.

Free name search facility (of existing companies / LLPs) is available on MCA portal. The system will provide the list of similar/closely resembling names of existing companies/LLPs based on the search criteria filled up . Link given below:

<http://www.mca.gov.in/DCAPortalWeb/dca/MyMCALogin.do?method=setDefaultProperty&mode=16>

Step-IV- filling of form llp-1 (name approval)- Section-16

After Search of Name approval, if name is available according to your search. Then Download Form LLP-1 from the below given

Link: http://www.mca.gov.in/MinistryV2/Download_eForm_LLP.html

Step-V- Drafting of LLP agreement Section- 23(3)

Section 23(3) of the LLP Act provides that an agreement in writing made before the incorporation of a LLP Between the persons who have subscribed their names to the incorporation document. The LLP agreement is very lengthy document and should be on Stamp paper.

Step-VI Filing of (Form 2) for Incorporation and Subscription Document

After receiving of Name approval Letter from ROC within 90 days there is need to prepare and get sign all the documents required to be attached in Form-2 and file Form-2 with ROC.

Step-VII- Filling of LLP agreement (form- 3)

It is not mandatory to file LLP agreement at the time of registration and same can be file in form LLP-3 within 30 days of Incorporation of LLP. Designated partners are responsible for doing all acts, matters and things that are required to be done for complying with the provisions of the LLP act. They are liable to all penalties imposed on the LLP. So it is very important to draft LLP agreement with professional help.

The LLP agreement has to be uploaded. Once it gets approved all the formalities for registration gets completed. The LLP can start its business now onwards.