

1. Details of Module and its structure

Module Detail	
Subject Name	Business Studies
Course Name	Business Studies 01 (Class XI, Part- 1)
Module Name/Title	Forms of Business Organisation/ Partnership – Part 4
Module Id	kebs_10204
Pre-requisites	Basic knowledge about partnership form of organisation
Objectives	After going through this lesson, the learners will be able to understand the following: <ul style="list-style-type: none">• Types of Partners• Types of Partnership• Partnership Deed• Registration of Partnership Firms
Keywords	Partnership, Sleeping Partner, Limited Liability, Active partner, Partnership at will, Agreement, Profit sharing Ratio

2. Development Team

Role	Name	Affiliation
National MOOC Coordinator	Prof. Amarendra P. Behera	CIET, NCERT, New Delhi
Program Coordinator	Dr. Rejaul Karim Barbhuiya	CIET, NCERT, New Delhi
Course Coordinator (CC) / PI	Dr. Punnam Veeraiah	CIVE, RIE Campus, Bhopal
Course Co-Coordinator / Co-PI	Dr. Nidhi Gusain	CIET, NCERT, New Delhi
Subject Matter Expert (SME)	Mrs. Madhu Vaswani	Delhi Public School, Mathura Road, New Delhi
Review Team	Dr. Munipalle Usha	UPGC, Osmania University, Hyderabad
Technical Team	Mr. Shobit Saxena Ms. Khushboo Sharma	CIET, NCERT, New Delhi CIET, NCERT, New Delhi

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A partnership is when two or more people work together and share the profits from the business or profession. However, one must not always assume that all partners participate in the work or profits or even liabilities of the firm equally. In fact,

There are various types of partners based on:

- the extent of their liability, or
- their participation in the firm with different roles and liabilities

– like an active partner or dormant partner etc.

An understanding of these types is important for a clear understanding of their rights and responsibilities. These are described as follows:

Here we will look at **six types of partners** we come across on a regular basis. This list is not exhaustive; the **Partnership Act** does not restrict any unique kind of partnership that the partners want to define for themselves.

Let us take a look at some of the important **Types of partners**:

i) Active Partner/Managing Partner: An active partner is one who contributes capital, participates in the management of the firm, shares its profits and losses, and is liable to an unlimited extent to the creditors of the firm. These partners take actual part in carrying out business of the firm on behalf of other partners. An active partner is also known as Ostensible Partner. As the name suggests he takes active participation in the firm and the running of the business. He carries on the daily business on behalf of all the partners. This means he acts as an agent of all the other partners on a day to day basis and with regards to all ordinary business of the firm. Hence when an active partner wishes to retire from the firm he must give a public notice about the same. This will absolve him of the acts done by other partners after his retirement. Unless he gives a public notice he will be liable for all acts even after his retirement.

ii) Sleeping or dormant partner: Partners who do not take part in the day to day activities of the business are called sleeping partners. A sleeping partner, however, contributes capital to

the firm, shares its profits and losses, and has unlimited liability. If such a dormant partner retires, he need not give a public notice of the same.

iii) Secret partner: A secret partner is one whose association with the firm is unknown to the general public. Other than this distinct feature, in all other aspects he is like the rest of the partners. He contributes to the capital of the firm, takes part in the management, shares its profits and losses, and has unlimited liability towards the creditors.

iv) Nominal partner: A nominal partner is one who allows the use of his/her name by a firm, but does not contribute to its capital. He/she does not take active part in managing the firm, does not share its profit or losses but is liable, like other partners, to the third parties, for the repayments of the firm's debts. This is a partner that does not have any real or significant interest in the partnership. So, in essence, he is only lending his name to the partnership. He will not make any capital contributions to the firm, and so he will not have a share in the profits either. But the nominal partner will be liable to outsiders and third parties for acts done by any other partners.

v) Partner by estoppel: A person is considered a partner by estoppel if, through his/her own initiative, conduct or behaviour, he/she gives an impression to others that he/she is a partner of the firm. Such partners are held liable for the debts of the firm because in the eyes of the third party they are considered partners, even though they do not contribute capital or take part in its management. In other words, if a person holds out to another that he is a partner of the firm, either by his words, actions or conduct then such a partner cannot deny that he is not a partner. This basically means that even though such a person is not a partner he has represented himself as such, and so he becomes partner by estoppel or partner by holding out.

Suppose Rani is a friend of Seema who is a partner in a software firm — Simplex Solutions. On Seema's request, Rani accompanies her to a business meeting with Mohan Software's and actively participates in the negotiation process for a business deal and gives the impression that she is also a partner in Simplex Solutions. If credit is extended to Simplex Solutions on the basis of these negotiations, Rani would also be liable for repayment of such debt, as if she is a partner of the firm.

vi) Partner by holding out: A partner by 'holding out' is a person who though is not a partner in a firm but knowingly allows him/her to be represented as a partner in a firm. Such a person becomes liable to outside creditors for repayment of any debts which have been extended to the firm on the basis of such representation. In case he is not really a partner and wants to save

himself from such a liability, he should immediately issue a denial, clarifying his position that he is not a partner in the firm. If he does not do so, he will be responsible to the third party for any such debts.

Minor Partner: A minor cannot be a partner of a firm. However, a minor can be admitted to the benefits of a partnership if all partners give their consent for the same. Partnership is based on legal contract between two persons who agree to share the profits or losses of a business carried on by them. As such a minor is incompetent to enter into a valid contract with others, he cannot become a partner in any firm. However, a minor can be admitted to the benefits of a partnership firm with the mutual consent of all other partners.

- He will share profits of the firm,
- His liability for the losses will be limited to his share in the firm.
- He will not be eligible to take an active part in the management of the firm.
- Thus, a minor can share only the profits and cannot be asked to bear the losses.
- However, he can if he wishes, inspect the accounts of the firm.

The status of minor changes when he attains majority.

In fact, on attaining majority, the minor has to decide whether he would like to become a partner in the firm. He has to give a public notice of his decision within six months of attaining majority.

If he fails to do so, within the stipulated time, he will be treated as a full-fledged partner and will become liable to the debts of the firm to an unlimited extent, in the same way as other active partners are.

Types of Partnerships:

Partnerships can be classified on the basis of two factors, viz.,

- Duration and
- Liability.

On the basis of **duration**, there can be two types of partnerships:

- ‘partnership at will’ and
- ‘particular partnership’

On the basis of **liability**, the two types of partnership include:

- ‘with limited liability’ and
- ‘with unlimited liability’

These types are described in the following sections.

Classification of the types of Partnership on the **basis of duration**:

i) Partnership at will: This type of partnership exists at the will of the partners. It can continue as long as the partners want and is terminated when any partner gives a notice of withdrawal from partnership to the firm.

ii) Particular partnership: Partnership formed for the accomplishment of a particular project say construction of a building or an activity to be carried on for a specified time period is called particular partnership. It dissolves automatically when the purpose for which it was formed is fulfilled or when the time duration expires.

Classification of the types of partnership on the **basis of liability**:

In a partnership, each person contributes something to the business -- such as ideas, money, property, or some combination of these. Management rights, profit share, and personal liability will vary depending on which of the three modern partnership forms the business takes: general partnership, limited partnership. Following are basic summaries of the main types of business partnerships.

i) General Partnership: In general partnership, the liability of partners is unlimited and joint. The partners enjoy the right to participate in the management of the firm and their acts are binding on each other as well as on the firm. Registration of the firm is optional. The existence of the firm is affected by the death, lunacy, insolvency or retirement of the partners.

A general partnership involves two or more owners carrying out a business purpose. General partners share equal rights and responsibilities in connection with management of the business, and any individual partner can bind the entire group to a legal obligation. Each individual partner assumes full responsibility for all of the business's debts and obligations.

ii) Limited Partnership: A limited partnership allows each partner to restrict his or her personal liability to the amount of his or her business investment. In limited partnership, the liability of at least one partner is unlimited whereas the rest may have limited liability. Such a

Partnership does not get terminated with the death, lunacy or insolvency of the limited partners. The limited partners do not enjoy the right of management and their acts do not bind the firm or the other partners. Registration of such partnership is compulsory. This form of partnership was not permitted in India earlier. The permission to form partnership firms with limited liability has been granted after introduction of New Small Enterprise Policy in 1991. The idea behind such a move has been to enable the partnership firms to attract equity capital from friends and relatives of small scale entrepreneurs who were earlier reluctant to help, due to the existence of unlimited liability clause in the partnership form of business

Not every partner can benefit from this limitation -- at least one participant must accept general partnership status, exposing him or herself to full personal liability for the business's debts and obligations. The general partner retains the right to control the business, while the limited partner(s) do(es) not participate in management decisions. Both general and limited partners benefit from business profits.

Partnership Deed

A partnership is a kind of business where a formal agreement between two or more people is made and agreed to be the co-owners, distribute responsibilities for running an organization and share the income or losses that the business generates. These features of partnerships are documented in a document which is known as partnership deed so that there is no misunderstanding later among the partners.

It is advisable to have a written agreement as it constitutes an evidence of the conditions agreed upon. The written agreement which specifies the terms and conditions that govern the partnership is called the partnership deed.

The Indian Partnership Act, 1932 governs partnership forms of businesses in India. This law contains several provisions defining rights, duties, liabilities, and powers of partners. These provisions, however, are not always binding on them. Partners are free to bind themselves with contrary provisions.

Most provisions of the Partnership Act are subject to a contract to the contrary. This means that if partners have agreed to contrary understandings, they will prevail over the Act. For example, although payment of salary to partners is prohibited by the Act, partners can still draw a salary if they mutually agree.

The Partnership comes into the limelight when:

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- There is an outcome of agreement among the partners.
 - The agreement can be either in written or oral form

The Partnership Act does not demand that the agreement has to be in writing. Wherever it is in the form of writing, the document, which comprises terms of the agreement, is called **‘Partnership Deed’**

It normally comprises the attributes about all the characteristics influencing the association between the partners counting the aim of trade, contribution of capital by each of the partner, the ratio in which the gains and losses will be divided by the partners and privilege and entitlement of partners to interest on loan, interest on capital, etc.,

The sections of partnership deed can be modified with the accord of all the partners. The deed must be appropriately drafted and outlined as per the provisions of the ‘Stamp Act’ and ideally registered with the Registrar of Firms.

The partnership deed generally includes the following **contents/aspects**:

- Name of firm
- Nature of business and location of business
- Duration of business
- Investment made by each partner
- Distribution of profits and losses
- Duties and obligations of the partners
- Salaries and withdrawals of the partners
- Terms governing admission, retirement and expulsion of a partner
- Interest on capital and interest on drawings
- Procedure for dissolution of the firm
- Preparation of accounts and their auditing
- Method of solving disputes

Importance of partnership deed:

- It controls and monitors the rights, responsibilities, and liabilities of all the partners
- Avoids dispute between the partners
- Avoids confusion on profit and loss distribution ratio among the partners
- Individual partner’s responsibilities are mentioned clearly
- Partnership deed also defines a remuneration or salary of the partners and working partners. But, interest is paid to each partner who has invested capital in the business.

Registration of Partnership Firms:

Registration of a partnership firm means the entering of the firm's name, along with the relevant prescribed particulars, in the Register of firms kept with the Registrar of Firms. It provides conclusive proof of the existence of a partnership firm.

It is optional for a partnership firm to get registered. In case a firm does not get registered, it is deprived of many benefits.

The consequences of non-registration of a firm are as follows:

- (a) A partner of an unregistered firm cannot file a suit against the firm or other partners,
- (b) The firm cannot file a suit against third parties, and
- (c) The firm cannot file a case against the partners.

In view of these consequences, it is therefore advisable to get the firm registered.

According to the India Partnership Act 1932, the partners may get the firm registered with the Registrar of firms of the state in which the firm is situated. The registration can be at the time of formation or at any time during its existence.

The procedure for getting a firm registered is as follows:

1. Submission of application in the prescribed form to the Registrar of firms. The application should contain the following particulars:

- Name of the firm
- Location of the firm
- Names of other places where the firm carries on business
- The date when each partner joined the firm
- Names and addresses of the partners
- Duration of partnership

This application should be signed by all the partners.

2. Deposit of required fees with the Registrar of Firms.

3. The Registrar after approval will make an entry in the register of firms and will subsequently issue a certificate of registration.

Summary:

Types of partners:

- i) Active Partner/Managing Partner
- ii) Sleeping or dormant partner
- iii) Secret partner
- iv) Nominal partner
- v) Partner by estoppels
- vi) Partner by holding out

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