1961 *Present :* Gunasekara, J., and Sinnetamby, J.

R. W. PATHIRANE, Appellant, *and* A. PATHIRANE, Respondent

S. C. 351/85—D. C. Kurunegala, 5810/M

Partnership—Dissolution—Action for accounts—Correct procedure—Effect of non-production of accounts—Distribution of assets—Division of profits—Partnership Act, ss. 29, 42—Civil Procedure Code, ss. 202, 430, 431, 508, 511, 513, 515.

Plaintiff and defendant carried on a business as partners. The defendant was the managing partner. The plaintiff instituted the present action averring the dissolution of the partnership and asking that the accounts of the partnership be taken. He also asked for distribution of the assets and for division of profits.

Held, (i) that, when a partner states that accounts have not been rendered and asks for the taking of accounts, the Court should first make an order directing accounts to be rendered from the date from which it finds that they have not been rendered. In such cases the procedure prescribed by sections 202, 430, 431, 508, 511, 513 and 515 should be followed.

(ii) that if a partner has books or accounts in his possession and fails to submit any accounts to the Court, the Court is entitled to draw inferences adverse to the accounting party.

(iii) that the defendant was liable to share with the plaintiff the profits he made by fraudulently obtaining a renewal in his own name of certain agreements which the partnership had with a third party.

(iv) that, in the present case, as assets had not been distributed at the time of the action, the plaintiff was entitled to recover profits up to the date of the decree and, thereafter, legal interest on the aggregate sum found due to him.

APPEAL from a judgment of the District Court, Kurunegala.

H. W. Jayewardene, Q.C., with *N. R. M. Daluwatte*, for the defendant-appellant.

E. B. Wikramanayake, Q.C., with *T. W. Rajaratnam*, for the plaintiff-respondent.

Cur. adv. vult.

July 25, 1961. SINNETAMBY, J.—

The plaintiff and defendant were partners and carried on a business under a partnership agreement marked P1 bearing No. 285 dated 30th December, 1942. The nature of their business involved the sale of petrol and other products of Caltex (CEYLON) Ltd. in premises belonging to the Caltex Company. They were permitted to use the equipment provided by the company on payment of a nominal hire and were subject to the conditions set out in the agreements entered into between the partnership and Caltex (CEYLON) Ltd. embodied in the documents D1, D3 and D14. The partners were, for the purpose of this business regarded as the business agents of the Caltex company, though in point of fact, they were not agents in the lega sense. Differences appear to have arisen between the partners and the plaintiff had instituted an action against the defendant in the District Court of Kurunegala on 18th August, 1948, claiming profits for the three years ended 31st March, 1948. He obtained a decree in November, 1954, in a sum of Rs. 10,550 on account of his share of the profits. In the meant me, on 10th September, 1948, the defendant gave the plaintiff, in terms of the partnership agreement P1, three months notice terminating the partnership as from 10th December, 1948.

The present action was instituted prior to the decree in that case on 25th August, 1949, averring the dissolution of the partnership and asking that the accounts of the partnership be taken. The plaintiff also asked for distribution of the assets and for division of profits.

The defendant, according to the partnership agreement, was the managing partner and it is not denied that he kept books ; indeed, in the earlier action he produced his books to a firm of chartered accountants who reported on them to the court. Even in the present action he called as a witness a gentleman employed in a firm of accountants and submitted a statement prepared by him. The plaintiff averred that the defendant had failed to render a true and correct account of the partnership from 1st April, 1945. Article 7 of the partnership agreement P1 requires that on the 31st of March each year a balance sheet should be prepared showing the assets and liabilities and each partner's share of the capital and profits. Article 9 provides that these accounts should be audited by a recognised auditor. Article 11 further provides that neither partner shall draw a sum exceeding Rs. 150 per month except with the consent of the other partner. The need for an annual balance sheet and a profit and loss account was thus imperative. Each partner contributed a sum of Rs. 2,000 to the business as capital. They also appear to have borrowed money from the bank to finance the business and this had been subsequently liquidated. Although the defendant said he had liquidated this loan out of his personal funds he has not established it by satisfactory evidence and the learned Judge has, in my view, rightly rejected his contention.

The plaintiff also averred that prior to the notice of termination of the partnership the defendant fraudulently obtained from the Caltex company an agreement for the sale of their products in the same premises in his own name after inducing them to cancel the agreement with the partnership. This, under the agreements, they could have done at short notice. The plaintiff claimed the profits made by the defendant in conducting the business in his own name from the date of the cancellation of the agreement with the Caltex company up to the date on which assets are distributed. The defendant, in his answer denied that he failed to render accounts from 1st April, 1945, and stated that only a sum of Rs. 280 was due as plaintiff's share of the profits. On the trial date, several issues were framed but there was no issue suggested or adopted in regard to whether the defendant had in terms of the partnership agreement submitted accounts to the plaintiff after March, 1945. The consequence was that the learned trial Judge permitted evidence to be led on various matters which need not have been gone into if the correct procedure had been followed.

Sitting in appeal, I have noticed that in several partnership cases in which the plaintiff has asked for the dissolution of partnership and for an order directing accounts to be taken, some trial courts have not followed the correct procedure and do not appear to have a proper appreciation of the steps that should be taken in the course of such proceedings. Where the plaintiff states that accounts have not been rendered and asks for the taking of accounts, the court should first consider what defence the defendant has put up in regard to that claim. If his defence is that accounts have been rendered, then the first question the court must decide on is whether in fact accounts had been rendered and if so up to what date. It should then make an order directing accounts to be rendered from the date from which it finds they have not been rendered. Section 508 of the Civil Procedure Code expressly provides that in actions of accounts, the court may adjudicate piece meal upon the matters in issue and in such adjudications make interlocutory orders of a final character. Having decided this issue the court should then call upon the defendant if he is the accounting party to file a statement of accounts for such period as it considers necessary. In rendering his accounts the accounting party must comply with the provisions of Section 511 : it should be verified on oath or affirmation. Thereafter, a date should be fixed for the opposite party to falsify and surcharge. When that has been done, the trial should be confined only to those items in the accounts in respect of which there are disputes. Section 513 provides for the procedure to be followed when the accounting party makes default. The hearing of the main issues in the case should be adjourned until after the accounts are taken in terms of Section 515. There are, of course, several other defences also open to the accounting party when the plaintiff asks the court for an order calling on the defendant to file accounts. If such defences are taken they should first be adjudicated upon before an order is made. In the case of partnerships Section 202 expressly provides that accounts shall be taken before a decree for dissolution is made. Ordinarily, in partnership cases, an action for accounting is never instituted except when it is associated with a prayer for an order of dissolution unless in point of fact there has already been a dissolution. If after accounts are filed the court thinks it requires the services of an accountant, it may issue a commission in terms of Section 430 and 431 of the Civil Procedure Code to an accountant to examine and report on the account. This should only be done if the court considers such a reference necessary and should not be done solely on the initiative of either or both parties—*Seneviratne v. Kariawasan*[1]. If courts of first instance would only follow these provisions of the Civil Procedure Code in taking partnership accounts much time would be saved and the issue narrowed to a smaller compass.

[1] *(1949) 51 N. L. R. 206 ; 42 C. L. W. 20.*

In the present case, the defendant was not called upon to submit an account and, indeed, he did not submit one which was supported by books, but several issues were framed and the main ones with which the appeal was concerned and in respect of which argument was addressed to us were issues 1, 2, 3 (1), 3 (2), 4, 5 and 6. After trial the learned Judge entered judgment for the plaintiff for profits at the rate of Rs. 2,000 per year from 31st March, 1948, up to the date of payment of his " capital and costs ". There was no express direction in the judgment or in the decree specifying what amount had to be paid on account of capital, but, in answer to issue 2, the learned Judge fixed the amount due to the plaintiff on account of his share of the assets and goodwill at Rs. 2,300. Against the judgment of the learned District Judge, the defendant preferred the present appeal.

The defendant, as stated earlier, failed to submit any accounts to the court ; he only called an accountant who submitted a statement unsupported by any books. The court was accordingly entitled to draw inferences adverse to the accounting party. Lindley in his book on Partnership refers to the effect of non-production of books in the following terms :—

> " If a partner has books or accounts in his possession, and he will not produce them, an account may, nevertheless, be arrived at by presuming everything against him. Thus in a case where an account was directed at the suit of the representatives of a deceased partner against the surviving partner, and the latter would not produce the books necessary to enable the Master to take the accounts, the Master estimated the nett profits at £10 per cent. on the capital employed, and the Court, on exception to his report, confirmed it, adding that if he had set the nett profits down at £20 per cent. his report would have been equally confirmed."

In the present case, therefore, the failure of the defendant to produce the account books entitles the court to draw every adverse inference against him but the court had material upon which it could have proceeded. In the earlier action to which I have referred, a firm of chartered accountants audited the books and prepared and submitted a statement of the profits disclosed up to the end of March, 1948. They were fixed at Rs. 10,550 after deduction of drawings. The learned Judge assessed the profits for the subsequent period on that basis, and it was not argued in appeal that his method of assessment was wrong. I think it was perfectly open to him to proceed on that basis. Indeed, the learned Judge has been very considerate to the defendant for on that basis he should have allowed profits to be fixed at about Rs. 3,000 per annum but having regard

to the fact that it was the defendant who managed the business the learned Judge has allowed Rs. 1,000 per year to be deducted on that account and assessed the profits at Rs. 2,000 per year, despite the fact that the remuneration allowed for his services in the partnership agreement was only Rs. 50 per month. The plaintiff did not in appeal contest the correctness of this award. It is not clear how the learned Judge arrived at the value of the capital contributed and the assets and goodwill at Rs. 2,300 but this figure too was not seriously contested. What the defendant did contest, however, was that the plaintiff was not entitled to claim any profits after the Caltex company had terminated its agreement with the partnership. This was done by letter D9 addressed by the Caltex company to the partners dated 23rd September, 1948, terminating the petrol agreement by giving a month's notice. In regard to kerosene, a new agreement with the defendant was entered into as from 1st October, 1948.

The notice of termination by the Caltex company was, as would appear from D8, made in consequence of a letter written by the defendant to the Caltex company dated 21st September, 1948, which has been produced marked D13. Obviously, in D13, there are misrepresentations upon which the company appears to have acted. For instance, in it the defendant says that the plaintiff had withdrawn his capital of Rs. 2,000. This was in September, 1948, and is totally inconsistent with the decree entered in the earlier case No. D. C. 5029 in which judgment was only for the profits and the assets fixed at Rs. 3,232·84 were directed to be carried forward to the next account. The defendant's accountant produced statements of account D15 and D16 which the Judge has quite rightly rejected. In regard to profits not included in the partnership accounts made by a partner by utilising partnership assets before the termination of the partnership, Section 29 of the Partnership Act would apply. In my view it clearly applies to the profits made by the defendant after he secretly wrote letter D13 to the Caltex company and thereby induced them to cancel the original agreement with the partners and to enter into a new agreement with him personally. This was done without the knowledge of and without notice to the plaintiff, and at a time when the partnership had not been terminated. Lindley refers to several cases where a partner who, on the termination of the partnership, obtains renewal of a lease in his own name, was ordered to account to the partnership for the profits he thereby made. In my opinion, the defendant was liable to share with the plaintiff the profits he made by obtaining a renewal in his own name of the several agreements the partnership had made with the Caltex company.

The learned Judge in his judgment has ordered that the defendant should pay the plaintiff profits as decreed till the date on which the payment is made of the capital and costs. The only question that now

remains for decision is whether this order is right. The learned counsel who appeared for the respondent conceded that he was not entitled to ask for profits until the date of payment of capital and costs. This question is not easy to determine and would depend in each case upon the facts and circumstances established therein. The accounts of a partnership must be kept open even after the date of dissolution for the purpose of debiting and crediting the parties with monies payable by them and monies they are entitled to receive both in respect of new transactions as well as old transactions. The same will be the case with partnerships which continue to do business in the partnership name after dissolution. The main question to be taken into account is whether the business is being conducted with property belonging to the partnership and not to the individual partner who continues to trade in the partnership business without the consent of his co-partner. The general rule in such a case, as stated by Lindley, is for the continuing partner to be condemned to pay either a share in the profits till final distribution of the assets or, in the alternative, interest on the capital at the usual rate, whichever is higher.

In the present case, the partnership agreement expressly provides that fresh capital brought in should carry interest at 6 per cent. but the profits were definitely larger. The plaintiff should, therefore, be entitled to recover profits so long as the business of the partnership continues. This is provided for by Section 42 of the Partnership Act, which, however, restricts the right of interest to 5 per cent. on the outgoing partner's share of the partnership assets. In this case, as assets had not been distributed at the time of the action, it seems to me that the plaintiff is entitled to recover profits on the basis of the Judge's order up to the date of the decree for by its decree the court has in effect distributed the assets and, therefore, it cannot be said that the defendant was still carrying on the business utilising partnership assets. The plaintiff's rights in short have been merged in the decree and, as learned counsel for the plaintiff-respondent conceded, the order as to profits must come to an end on the date of the decree. Thereafter, the plaintiff would only be entitled to legal interest on the aggregate sum found due to him.

I would accordingly vary the decree by directing that the defendant do pay to the plaintiff profits at the rate of Rs. 2,000 per year from 31st March, 1948, up to the date of the decree and his share of the assets and goodwill amounting to Rs. 2,300/- and that thereafter, he should pay legal interest on the aggregate amount till payment in full with costs of action. Subject to this variation, I would dismiss the appeal with costs.

GUNASEKARA, J.—I agree.

Appeal mainly dismissed.