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UNREGISTERED PARTNERSHIP: BOON OR BANE

A. Understanding Unregistered Partnership in India

Section 58 of the Indian Partnership Act of 1932 (“the Act”) specifies the incorporation process for a partnership. The opposite of registration, known as non-registration, is when a business does not go through the formation procedure or operates without being registered. In India, it is not necessary to register a partnership deed. However, there are some significant ramifications which the partners should take into account as an unregistered partnership. In India, a partnership can be established orally or in writing, and an unregistered partnership deed is nevertheless regarded as a legally binding contract between the partners.

B. Filing a suit by an Unregistered Partnership Firm

If we consider Section 69(2) of the Act, it eliminates the unregistered partnership firms from filing a suit. As a result, a partnership firm that is not registered cannot sue a third party for any disagreement unless it is registered. In addition, Section 69 of the Act bars the unregistered partnership firms from filing lawsuits against their partners for any contractual rights or rights derived from the Act, as well as from claiming set-off or taking any other legal action to enforce their contractual rights.

C. Other Consequences

- The Unregistered Partnership Firm Cannot be Estopped from Being Sued by Third Parties:** Although an unregistered partnership firm is not permitted to sue a third party, the Act does not bar the opposite. As a result, a third party may still bring a lawsuit against the unregistered partnership firm. The firm is not immune to the suit brought by other parties simply because it lacks the power to sue.
- Cannot Assert a Set-Off Claim Against Third Parties:** Section 69(3) of the Act explains the concept of set-off claims. The debtor adjusts the

mutual obligations with the creditor and might present reciprocal claims in a set-off claim. However, this cannot be done by a partnership firm which is not registered.

- Cannot Convert to Another Entity:** A registered partnership firm has the option of converting to any other corporate entity, such as an LLP. Partnership firms that are not registered are ineligible to do the same.

The following rights, however, are unaffected if the firm is unregistered:

- The ability of a partner to bring a lawsuit for the firm's dissolution, for the firm's accounts, or to enforce any right or authority to recover the assets of a disbanded firm.
- The ability of a formal assignee or receiver to seize an insolvent partner's assets.
- The company's or its partners' rights if they do not have a place of business in India.
- The capability of the unregistered business or its partners to be sued by a third party.
- The ability to file a lawsuit against a third party for violating a patent right.

D. Judicial Interpretation

The Hon'ble NCLT, New Delhi in the case of **Preet Shuttering Store v. M.I. Buildtech Private Limited [CP (IB)-300/ND]** admitted an application submitted by an unregistered partnership firm despite the bar under section 69(2) of the Act, based on the interpretation that the provision only applies to "suits" and not to proceedings under the IBC placing reliance upon **Shree Dev Chemicals Corporation vs. Gammon India Ltd.**

The Hon'ble Supreme Court in the case of **Sunilbhai Somabhai Ajmeri v. Aksharay Developers & Ors, [(2022) SCC OnLine SC 114]** clarified the kind of lawsuits that will not be precluded by Section 69(2) of the Act when filed by an unregistered partnership. The



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Supreme Court reviewed the principles pertaining to Section 69(2) of the Act, and noted that the provision's objective was for a third-party doing business with a firm to be aware of the names of the people they are dealing with, which is not the case when a right is being sought to be enforced. The Court emphasized that because the current case involved the sale of the firm's share in a property, and transaction which was disputed did not relate to the firm's business. The lawsuit was brought to seek remedies under the Specific Relief Act of 1963 and the Transfer of Property Act of 1882 rather than to enforce a contractual right.

The Hon'ble Court referred to its earlier judgments in **Haldiram Bhujiawala and Anr.v. Anand Kumar Deepak Kumar & Anr, [(2000) 3 SCC 250]** and **Raptakos Brett & Co. Ltd. v. Ganesh Property [(1998) 7 SCC 184]** interpreted Section 69(2) of the Act and held that it would be applicable only when:

- a. the contract in question is entered into by the firm with a third party;
- b. the contract is entered into by the firm in the course of its business dealings and
- c. the contract is entered into for the enforcement of a statutory right or a common law right.

The Hon'ble Court further stated that the unregistered partnership's lawsuit cannot be dismissed under the terms of Section 69(2) because it did not assert any contractual claims against third parties during the business transaction, but rather relied on the applicability of common law principle to assert its statutory rights.

It can be safely drawn that the prohibition under section 69(2) of the Act is not absolute and instead has its own peculiarities, namely that an unregistered partnership firm may file any lawsuit other than one arising from contractual rights in the ordinary course of business.

E. Conclusion

The main reason that many firms choose a partnership firm is because it is simple to set up and does not need to be registered. However, the partners may have to pay a steep price if they decide to ignore it and do nothing about it. Unregistered partnership firms are nonetheless legitimate in the eyes of the law and are still able to conduct business as usual, but they come with drawbacks. A partnership cannot operate in an ideal environment for very long since it is prone to disputes/ conflicts. In order to resolve these disputes/ conflicts, the firm and its partners will need to take legal action, which they would be unable to do without the registration of the firm. As a result, the partners must exercise caution while choosing whether to register the partnership firm or not.