

# Dispute Resolution Hotline

April 02, 2009

## SUPREME COURT GIVES RELIEF TO PARTNERS OF UNREGISTERED PARTNERSHIP FIRM

The Hon'ble Supreme Court of India ("Court") has held that a partner of an unregistered partnership firm under the Indian Partnership Act, 1932, ("the Act") in the state of Maharashtra, can file a suit for dissolution of the firm<sup>1</sup>. The Court declared sub-section 2A of Section 69<sup>2</sup> of the Act (incorporated by the Maharashtra Act No. 29 of 1984 ("State Amendment"), as unconstitutional and invalid. In doing so, the Court has provided an effective remedy to partners in an unregistered partnership firm, in the State of Maharashtra, who were earlier deprived of their rights to their investment and properties in the firm and the right to dissolve the firm and ask for accounts due to the restrictions under the State Amendment. Significantly, due to the Court now declaring Section 69(2-A) as unconstitutional and invalid, the position of law has been returned to as it was as far back as 1984 when the State Amendment was introduced!

### THE LAW:

Though modeled as per the English Law on Partnerships under which registration of a partnership firm is compulsory and a penalty is imposed for non registration of the firm, the Act does not make registration of a firm compulsory. This was because making registration compulsory was considered too drastic a measure that would lead to complexities. However, the Act did follow the consequences of non registration as laid down in under English Law. Thus, under the Act, non-registration of the firm would lead to a disability whereby the firm or its partner (as the case may be) could not file suits for enforcing certain claims against other parties or the firm (as the case may be). Section 69 of Act deals with the effects of non-registration of the partnership. Section 69 (2-A) of the Act, as incorporated by the State Amendment, reads as under:

*"69 (2-A) No suit to enforce any right for the dissolution of a firm or for accounts of a dissolved firm or any right or power to realise the property of a dissolved firm shall be instituted in any Court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm, unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.*

*Provided that the requirement of registration of firm under this sub-section shall not apply to the suits or proceedings instituted by the heirs or legal representatives of the deceased partner of a firm for accounts of a dissolved firm or to realise the property of a dissolved firm."*

Thus, once the State Amendment came into force on January 01, 1985, a partner in an unregistered partnership firm in the State of Maharashtra could not file a suit for (1) dissolution or (2) accounts of a dissolved firm or (3) realize properties of a dissolved firm, unless the duration of the firm was only six months or its capital was up to Rs. 2,000 only.

The effects of non registration of a partnership firm are provided under Section 69<sup>2</sup> of the Act, whereby a partner of an unregistered firm cannot sue the firm or other partners enforce a right arising from a contract. Further, the partners were restricted from suing third parties on behalf of the unregistered firm to enforce a right arising from a contract. The Court further observed that one of the objects of registration of a firm was protection to third parties trying to enforce their rights against partners of a firm. Registration provided protection to such third parties from hardships and false denials of partnership and evasion of liability. Since the names of partners would be submitted at the time of registration, the partners so sued would not be able to deny their liabilities thus saving time and costs in the enforcement of a decree.

### BACKGROUND:

The Appellant had filed a suit before the Bombay City Civil Court ("City Civil Court") for inter alia, dissolution of an unregistered partnership firm between the appellant and the respondent. The respondent submitted that the suit was not maintainable in view of Section 69(2-A), as incorporated by the State Amendment.

The City Civil Court was of the view that this provision was unconstitutional being violative of Articles 14<sup>3</sup> and 19(1) (g)<sup>4</sup> of the Constitution of India and proceeded to make a reference<sup>5</sup> to the High Court of Bombay.

The High Court of Bombay held that the provision was not unconstitutional and therefore, the aggrieved Appellant filed an appeal in the Court.

### JUDGMENT:

Whilst noting that the State Amendment virtually deprived a partner in an unregistered firm from recovery of his share in the property of the firm without any compensation and prohibits a partner from seeking dissolution of the firm, the Court stated that in its opinion, the State Amendment effected stringent disabilities of a crippling nature on a partnership firm.

The Court observed that unlike a company, a firm does not have a distinct legal entity under the Indian laws and is

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only a compendium of its partners and registration did turn the firm into a distinct legal entity. Hence the partners are co-owners of the property of the firm, unlike shareholders in a company who are not co-owners of the property of the company. The State Amendment virtually deprived a partner from his share in the property without any compensation and prohibited him from seeking its dissolution.

The Court noted that the effect of the State Amendment was that an unregistered partnership firm was allowed to come into existence and function but it could not go out of existence (subject to certain exceptions). Consequently, in a case of disputes between partners, the relationship of partnership cannot be put to an end by approaching a court of law thus resulting into extreme hardship and injustice.

The Court further held that the restrictions placed by the State Amendment were arbitrary and were of an excessive nature and went beyond what was in the public interest and could not, therefore, be considered as reasonable.

The Court thereafter held that State Amendment violated Articles 14, 19(1)(g) and 300A<sup>6</sup> of the Constitution and was unconstitutional and was declared as invalid.

#### ANALYSIS AND IMPLICATIONS:

By striking down Section 69(2-A), as incorporated by the State Amendment and declaring it as unconstitutional and invalid, the Court has effectively granted a remedy to partners in unregistered partnership firms in the State of Maharashtra. Going forward, any such partner would be able to file a suit for (1) dissolution of the partnership or (2) accounts of a dissolved firm or (3) realize properties of a dissolved firm, which was done for about 53 years before the State Amendment was introduced.

#### - Sahil Kanuga & Shafaq Uraizee-Sapre

1. In V. Subramaniam Vs Rajesh Raghuvendra Rao - Civil Appeal No. 7438 of 2000.

2. **69. Effect of non-registration.**—(1) No suit to enforce a right arising from a contract or conferred by this Act shall be instituted in any Court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm.

(2) No suits to enforce a right arising from a contract shall be instituted in any Court by or on behalf of a firm against any third party unless the firm is registered and the persons suing are or have been shown in the Register of Firms as partners in the firm.

(3) The provisions of sub-sections (1) and (2) shall apply also to a claim of set-off or other proceeding to enforce a right arising from a contract, but shall not affect—

(a) the enforcement of any right to sue for the dissolution of a firm or for accounts of a dissolved firm, or any right or power to realise the property of a dissolved firm; or

(b) the powers of an official assignee, receiver or Court under the Presidency-towns Insolvency Act, 1909 (3 of 1909), or the Provincial Insolvency Act, 1920 (5 of 1920), to realise the property of an insolvent partner.

(4) This section shall not apply—

(a) to firms or to partners in firms which have no place of business in 1[the territories to which this Act extends], or whose places of business in 2[the said territories] are situated in areas to which, by notification under 3[Section 56], the CHAPTER does not apply, or

(b) to any suit or claim or set-off not exceeding one hundred rupees in value which, in the Presidency-towns, is not of a kind specified in Section 19 of the Presidency Small Cause Courts Act, 1882 (15 of 1882), to outside the Presidency-towns, is not of a kind specified in the Second Schedule to the Provincial Small Cause Courts Act, 1887 (9 of 1887), or to any proceeding in execution or other proceeding incidental to or arising from any such suit or claim.

#### STATE AMENDMENTS

MAHARASHTRA.—In Section 69 of the principal Act,—

(a) to sub-section (1), the following proviso shall be added, namely:—

“Provided that the requirement of registration of firm under this sub-section shall not apply to the suits or proceedings instituted by the heirs or legal representatives of the deceased partner of a firm for accounts of the firm or to realise the property of the firm.”;

(b) after sub-section (2), the following sub-section shall be inserted, namely:—

“(2-A) No suit to enforce any right for the dissolution of a firm or for accounts of a dissolved firm or any right or power to realise the property of a dissolved firm shall be instituted in any Court by or on behalf of any person suing as a partner in a firm against the firm or any person alleged to be or to have been a partner in the firm, unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner in the firm:

Provided that the requirement of registration of firm under this sub-section shall not apply to the suits or proceedings instituted by the heirs or legal representatives of the deceased partner of a firm for accounts of a dissolved firm or to realise the property of a dissolved firm.”;

(c) in sub-section (3),—

(i) for the words, bracket and figures “sub-sections (1) and (2)” the words, brackets, figures and letter “sub-sections (1), (2) and (2-A)” shall be substituted;

(ii) for clause (a), the following clause shall be substituted, namely:—

“(a) the firms constituted for a duration upto six months or with a capital upto two thousand rupees; or”.—Mah. Act 29 of 1984, S. 13 (w.e.f. 1-1-1985).

Section 69-A

MAHARASHTRA.—After Section 69 of the principal Act, the following section shall be inserted, namely:—

“69-A. Penalty for contravention of Section 60, 61, 62 or 63.—If any statement, intimation or notice under Sections 60, 61, 62 or 63 in respect of any registered firm is not sent or given to the Registrar, within the period specified in that section, the Registrar may, after giving notice to the partners of the firm and after giving them a reasonable

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opportunity of being heard, refuse to make the suitable amendments in the records relating to the firm, until the partners of the firm pay such penalty, not exceeding ten rupees per day, as the Registrar may determine in respect of the period between the date of expiry of the period specified in Sections 60, 61, 62, or as the case may be, 63 and the date of making the amendments in the entries relating to the firm.”—Mah. Act 29 of 1984, S. 14 (w.e.f. 1-1-1985).

3. 14. Equality before law.—The State shall not deny to any person equality before the law or the equal protection of the laws within the territory of India.

4. 19. (1) All citizens shall have the right—

(g) to practise any profession, or to carry on any occupation, trade or business.

5. Under Section 113 of the Code of Civil Procedure, 1908.

6. 300-A. Persons not to be deprived of property save by authority of law.—No person shall be deprived of his property save by authority of law.

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