

COMPANY LAW

UNIT 5 : Dividends, Audit and Winding Up

TOPIC- WINDING UP OF COMPANIES

Winding up of Companies

A company is an artificial person created by law through the process of incorporation. So, its life can be brought to an end ,through a legal process only called winding up or liquidation. The process of winding up involves **realisation of assets, payment of liabilities and distribution of surplus, if any, amongst the members of the company.** Winding is not same as dissolution.

WINDING UP	DISSOLUTION
Winding up involves realisation of assets, payment of liabilities and distribution of surplus amongst the members of the co.	Dissolution involves striking off the name of company from the Register of Companies by the Registrar and notifying this fact in the Official Gazette.
Winding up precedes dissolution	Dissolution follows winding up .
Winding up is a process	Dissolution is its end result
Legal entity of the company remains at the time of commencement of winding up	The company loses its legal entity after dissolution
The company maybe allowed to do business so far as its required for beneficial winding up	The company is no more in existence so there is no question of doing any business

MODES OF WINDING UP THE COMPANIES -

- I. **Compulsory winding up** by the Tribunal u\s 270 of the Companies Act, 2013 –
- II. **Insolvency Resolution and Liquidation** under Insolvency and Bankruptcy Code, 2016.
- III. **Voluntary Liquidation** u\s 59 of Insolvency and Bankruptcy Code, 2016

Compulsory Winding up by Tribunal under Companies Act, 2013

Grounds for winding up by the Tribunal (Sec.271)

- **Special Resolution**- The company can , by special resolution, decide that it be wound up by the Tribunal. However, the power of Tribunal in this case is discretionary and may not be exercised if the Tribunal finds that the winding up would be opposed to public interest or company's interest.
- **Acting against national interest**- A company may be ordered to be wound up if it had acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality.
- **Fraudulent Conduct** - The Tribunal may order winding up of a company if it is of the opinion that
 - ✓ its affairs have been conducted in a fraudulent manner
 - ✓ the company was formed for fraudulent and unlawful purpose
 - ✓ persons concerned in its formation \ management are guilty of fraud, misfeasance or misconduct and it is better that company be wound up
- **Default in filing financial statements**- If the company defaulted in filing with ROC its financial statements or annual returns for immediately preceding 5 consecutive financial years, it can be wound up by the Tribunal
- **Just and Equitable**- The Tribunal may order for winding up of a company if it is of the opinion that it is just and equitable . The Tribunal enjoys wide discretionary power under this clause and gives due weightage to the interest of the company, its employees, creditors, shareholders ,public etc while considering this ground. On the basis of earlier judicial pronouncements, the following are few examples in this head -

Just and Equitable (Examples)

- **Loss of substratum**- when the main object has failed and its impossible to carry on .eg
 - ✓ patent ,under which the company proposed to manufacture, could not be granted
 - ✓ company proposed to acquire some running business, but vendor refused to sell the business
- **Deadlock in management**
 - ✓ applicable in closely held companies where directors only are shareholders & so reconstitution of BOD is not possible & directors not on speaking terms/ bitterly hostile to each other
- **Oppression of minority**-when majority follows oppressive policy towards the minority.eg.
 - ✓ forcing an unjust scheme on minority against their wishes
 - ✓ disregarding the minority interest while taking any decision
- **Fraudulent object** - when co. was conceived to carryout illegal \ fraudulent business
 - ✓ If main object of company is to conduct lottery
 - ✓ a co. professing to be in real estate business of developing and selling plots, without actually having any title to the land thus deceiving innocent buyers
- **Losses** -eg. where business cannot be carried except at a loss/ no reasonable hope of trading at a profit in the business
- **Bubble Company**-eg company which does not carry any business/ company not owning any assets or property

Petition for Winding up(Sec.272)

The application to the Tribunal for winding up is called a petition. Whenever any petition to Tribunal is made, a copy of it must also be filed with the Registrar who shall submit his views within 60 days .As per Sec.272 , this petition can be made by any of the following-

Petition by the Company- Here petition is made by directors after co. passes special resolution for winding up. Petition must be accompanied by Statement of Affairs in prescribed form

Contributory's Petition- *Contributories are present or past members (who left company within 1 year preceding the commencement of winding up)who are liable to contribute to the assets of the company in winding up and also entitled to share in the surplus , left after liabilities are paid off.)*

Joint Petition-The company and any contributory can jointly also present petition for winding up

Petition by Central\ State government-This petition is made if company had acted against national interest \ sovereignty\ integrity \ security of India \against public order\ decency.

Petition by any person authorised by Central Government- The CG may authorise a person to file a petition for winding up on its behalf incase it finds that company has acted fraudulently .

Registrar's Petition-He can file petition only after obtaining prior approval of CG . Before giving approval CG must give opportunity to the concerned co. to make its representation. Grounds for petition could be - company working against national interest or fraudulent conduct of the co., default in filing financial statements, returns etc.

Powers of the Tribunal (Sec.273)

After receiving the petition for winding up, the Tribunal will fix a **date for hearing of petition**. It will issue notice to the company to enable it appear before it on that day and present its case. It shall also issue public notice of winding up petition so that all creditors and contributories come to know about it and may put their objections, if any, on the date of hearing. On the day of hearing, it hears the concerns of all the concerned parties and considering all the factors, the Tribunal may, within 90 days from the date of presentment of petition, pass any of the following orders:

- **dismiss the petition**
- **make any interim order it thinks fit**
- **appoint a provisional liquidator of the company till the making of a winding up order**
- **make an order for winding up of the company**
- **make any other order it thinks fit**

Company Liquidators and their appointment

- The company liquidator is a person who helps in completing the liquidation proceedings of the company i.e. in realising the assets and distributing them among the creditors and contributories in a fair manner.
- In case the Tribunal decides to make a winding up order, it shall appoint a Company Liquidator who could be an Official Liquidator or a liquidator appointed by it from amongst the Insolvency Professionals registered under Insolvency and Bankruptcy Code, 2016
- It also specifies the powers, duties, and remuneration of the Company Liquidator.

Consequences of winding up order

Winding up commences not from the date of winding up order of the Tribunal but it shall be deemed to commence at the time of presentment of petition. The consequences of winding up order are-

- Within 7 days of winding up order, the Tribunal shall send its intimation to the Co. Liquidator and the Registrar
- The Registrar shall then notify this information of winding up order in the Official Gazette. Incase of listed companies, the Registrar shall intimate the Stock Exchanges also where securities of the co. are listed
- The powers of the Board of Directors are terminated and the same to be exercised by Company Liquidator
- The winding up order shall be deemed to be notice of discharge to officers and employees of the company
- Any debts payable at a future date, becomes immediately payable
- The winding up order shall operate in favour of all the creditors and contributories
- Within 3 weeks of the date of winding up order, the Company Liquidator shall apply to Tribunal for the constitution of 'winding up committee' (comprising of him, nominee of secured creditors and a professional nominated by Tribunal) which shall assist and monitor the progress of liquidation proceedings.
- No suit or legal proceeding can be commenced against the company without the permission of the Tribunal. Similarly, the Tribunal shall have full powers to entertain or dispose of any new or pending suit by or against the company. Any suit \ proceeding pending in any other court shall also be transferred to the Tribunal.
- The Company Liquidator shall prepare and place before the Tribunal, periodical reports till the final report for dissolution of the company is submitted to the Tribunal
- The final report , after approval of winding up committee, shall be submitted by Company Liquidator to the Tribunal for passing of a ' dissolution order'

Consequences of winding up order

Advisory Committee - As per Sec.287, the Tribunal may ,at the time of making a winding up order or any time later, direct that Advisory Committee be appointed to advice company liquidator and to report to the Tribunal on specific matters. It shall consist of creditors and contributories in such proportion as may be agreed amongst them. The advisory committee shall have the right to inspect books of account , other documents, assets, properties etc at reasonable time. The meetings of Advisory Committee be chaired by company liquidator and be held frequently

Dissolution of Company

- When the affairs of a company have been completely wound up, the Company Liquidator shall make an application to the Tribunal for its dissolution.
- The Tribunal , then makes an order for dissolution of the company and the company stands **dissolved from the date of such order**.
- A copy of the dissolution order shall be filed by the Company Liquidator with the Registrar within 30 days of receiving it
- The Registrar will then record the same in his records and registers.

Insolvency Resolution and Liquidation under Insolvency and Bankruptcy Code ,2016

- **Insolvency and Bankruptcy Code(IBC),2016-** came into operation from 2016 and seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy in India. The Code focusses on a creditor - driven insolvency process and marks a paradigm shift from the regime of *Debtor - in- Possession* to *Creditor- in- Control*. The Code has been designed to explore revival opportunities for an ailing corporate entity. Only when the entity cannot be revived or its insolvency cannot be resolved, that an entity is liquidated.
- **Insolvency and Bankruptcy Board of India(IBBI)-** to act as a regulator of Insolvency Professionals (IPs)and Insolvency Professional Agencies(IPAs) and to oversee the insolvency proceedings in India .Its a 10 member Board and includes representatives from Ministry of Finance, Ministry of Law , Ministry of Corporate Affairs, RBI etc.
- **Insolvency Professionals (IPs)-** play a key role in the insolvency process and manage and control the assets of the debtor during the insolvency process .**Professionals(** like Advocates, CAs, Company Secretaries, Cost Accountants **having experience ≥ 10 years)** or **Graduates(** having **managerial experience ≥ 15 years)** + **having passed the Insolvency Examination + registered with Insolvency Professional Agencies(IPAs),** can serve as IPs. These IPs act as IRPs(Interim Resolution Professionals) , RPs (Resolution Professionals)or Liquidators.
- **Insolvency Professional Agencies(IPAs)-**agency to enroll and regulate members practicing as IP. IPA is also responsible for capacity building of IPs to ensure that they remain updated with knowledge and market requirements. IBBI has given registration to ICAI, ICSI, and Institute of Cost accountants to function as IPAs
- **National Company Law Tribunal (NCLT)-** Benches of NCLT are the Adjudicating Authority for corporate insolvency i.e. insolvency of Companies and LLP . Appeals against the order of NCLT are to be made to NCLAT (National Company Law Appellate Tribunal). AA for individuals or partnerships is DRT (Debt recovery Tribunal)
- **Information Utility-** It is a professional organization registered with IBBI which specializes in procuring, maintaining and providing financial information to businesses, adjudicating authority, insolvency professionals and relevant stake holders. It also carries out the function of authentication and verification of financial information. 1st IU in India is **NeSL** i.e. National E-Governance Services Limited .

Insolvency Resolution Process as per IBC,2016

- **Initiation of the Process-** When any company commits a default in payment of a financial debt \ operational debt of **₹1 crore** or more, a financial creditor \operational creditor or the company itself may initiate corporate insolvency resolution process by filing an application in prescribed Form with the Tribunal along with prescribed fees and names of Interim Resolution Professionals. The date of filing the application with Tribunal is known as *Initiation Date*.
 - ✓ *financial creditor are those to whom co. owes financial debt eg. Banks, FIs*
 - ✓ *operational creditors are those whom co. owes operational debt eg. workers,suppliers*
- **Determination of default by Tribunal-** Having received the application , the Tribunal shall, ascertain the existence of default by the co. by confirming it from-
 - ✓ Records of Information Utility (IU)(data banks which collect, collate and disseminate financial information & so play key role in insolvency resolution process) .
 - ✓ Evidences and records furnished by financial\ operational creditor
- **Initiation of Insolvency Process-**The NCLT shall, within 14 days of filing of application, may either accept it or reject it. If the Tribunal is satisfied that a default has occurred and the application is complete , it shall , accept it and initiate corporate insolvency resolution process.
 - ✓ The corporate insolvency resolution process shall be completed within 180 days (extendable by maximum 90 days). (Maximum 330 days in any case-inserted by IBC(Amendment) Act,2019.)
 - ✓ Moratorium is declared which implies initiation\continuation of legal proceedings against the company are stalled, creditors' claims are freezed and the company is prohibited from selling, alienating or creating any encumbrance without approval from relevant authority.

Insolvency Resolution Process as per IBC, 2016

- **Appointment of Interim Resolution Professional (IRPs)** - The Tribunal shall also appoint an interim resolution professional who is generally named in the application filed with the Tribunal. Otherwise, the Tribunal shall make a reference to IBBI for recommending person for the same. Once interim resolution professional is appointed-
 - ✓ Public announcement is made to inform public about the initiation of insolvency process and for providing details such as last date for submission of claims, penalties for false claims, date of closure of this resolution process, details of IRPs etc.
 - ✓ Powers of the BOD stand suspended and are to be exercised by him. The management of affairs of co. shall also vest in him.
- **Formation of Committee of Creditors (CoC)**- The IRPs shall, after collation of all the claims received against the company, constitute a Committee of Creditors. This committee makes all important decisions in corporate insolvency resolution process
 - ✓ This committee shall comprise all the financial creditors of the company. The voting power of each creditor would be on the basis of financial debts owed by the co. to such creditor.
 - ✓ All decisions pertaining to revival and implementation of effective resolution plan are required to be taken by the Committee of Creditors by majority vote of not less than 66%.
- **Appointment of Resolution Professional-**
 - ✓ The Committee of Creditors, in its first meeting (which must be held within 7 days of its constitution), may either resolve to appoint the Interim Resolution Professional as Resolution Professional (RP) or appoint someone else. The Committee is empowered to replace Resolution Professional at any point of time. Decisions on appointment or replacement of Resolution Professional require consent of 66% majority.
 - ✓ The Resolution Professional, takes custody and control of all assets and business records of the company immediately after appointment, maintains updated list of claims, convenes and attends all meetings of CoC, prepares Information Memorandum, invites prospective resolution applicants, presents all resolution plans at the CoC meetings etc.
- **Information Memorandum-**
 - ✓ Information Memorandum is prepared by RP and contains information that may be required by resolution applicant to make the resolution plan for the company eg. financial position of the company, disputes by or against the company etc.
 - ✓ The resolution applicant must be provided access to all relevant information in physical and electronic form

Insolvency Resolution Process as per IBC, 2016

- **Submission of Resolution Plan**
 - ✓ The resolution applicant prepares the Resolution Plan on the basis of Information Memorandum and submits it to the RP. The Resolution Professional examines each resolution plan received by him.
 - ✓ The resolution plan, which meets the prescribed criteria and conditions of the Code, is then presented to the Committee of Creditors for approval. The plan needs to be approved by at least 66% majority and if approved, it is submitted to the Tribunal.
- **Approval of Resolution Plan by Tribunal**
 - ✓ If NCLT is satisfied that it meets the prescribed criteria, it shall by order approve the resolution plan which will be binding on the company and its employees, members, creditors, and other stakeholders.
 - ✓ The company will be restructured and revived as per the approved resolution plan.
- **Liquidation Process-** Liquidation proceedings against the company will be initiated by the Tribunal if
 - ✓ **If NCLT is not satisfied with the resolution plan and rejects it on technical grounds**
 - ✓ **Tribunal doesn't receive a resolution plan within the prescribed maximum period**
 - ✓ **If CoC does not approve resolution plan**
 - ✓ **If approved resolution plan is contravened by the co. and any person aggrieved by the contravention applies to the Tribunal for liquidation.**

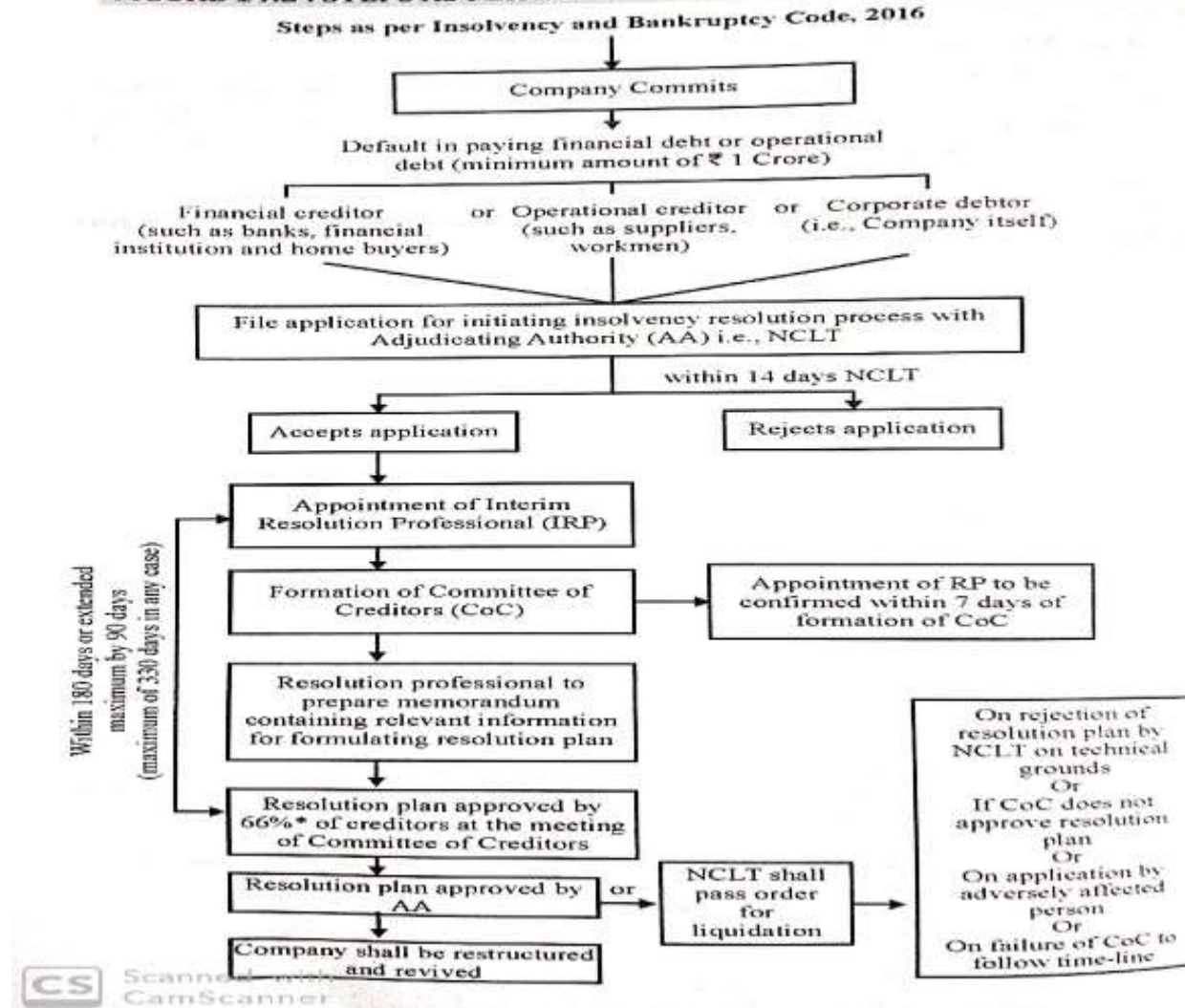
Once the liquidation order is passed, the Tribunal may appoint RP as liquidator of the co. who shall then take control \ custody of all assets, realise assets, determine the claims of all creditors, pay all liabilities and distribute the surplus if any, amongst the members of the company. Then, he shall apply to NCLT for obtaining 'Dissolution Order'. A copy of it shall be forwarded to the Registrar within 7 days for his information and record.

Flow chart taken from Rajni Jagota's company law

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UNIT V : DIVIDENDS, AUDIT AND WINDING UP

FIGURE 14.2 : STEPS AS PER INSOLVENCY AND BANKRUPTCY CODE, 2016



Voluntary Liquidation of Company Under IBC, 2016

Chapter V of The Insolvency and Bankruptcy Code, 2016 deals with voluntary liquidation of Companies. As per sec.59(1) of the Code, a company intending to liquidate itself voluntarily must follow the conditions u/s 59(3) and meet procedural requirements of IBBI. Following is the process of voluntary liquidation-

- **Initiation of liquidation proceedings-** A voluntary winding up is possible only when company had not defaulted i.e. it is fully solvent and its purpose is not to defraud any person. Such a company must file with the Registrar a '**Declaration of Solvency**' from majority of directors **verified by an affidavit** assuring that the company will be able to pay its debts in full & that liquidation is not to defraud anyone. This declaration must be accompanied with
 - ✓ **Audited financial statements** and records of last two years
 - ✓ **Valuation report of its assets** prepared by Registered Valuer
- **Contributories Resolution-** Within 4 weeks of Declaration of Solvency, special resolution of the contributories - requiring the co. to be liquidated voluntarily and appointing insolvency professionals to act as liquidators - should be obtained. However, if company needs to be liquidated voluntarily as a result of expiry of the period of its duration as fixed by Articles or on occurrence of any event provided in the Articles to trigger liquidation, then ordinary resolution is sufficient.
- **Creditors Approval** - In case the company owes any debt to any person then, **approval of winding up by creditors** representing at least two-thirds in value should also be obtained within 7 days of Contributories' Resolution.
- **Information to ROC and IBBI-** The company shall notify the Registrar of Companies and the IBBI about its resolution to liquidate within 7 days of Contributories' Resolution (or the subsequent Creditors Resolution, where company owes debt)
- **Liquidation Commencement Date** - The liquidation proceedings shall be deemed to have commenced from the date of passing of the contributories resolution (or the date of creditors approval, as the case may be). The co. shall from this date cease to carry-on its business except as far as is necessary for beneficial winding up. The legal entity however, shall continue to exist until it is dissolved.

Voluntary Liquidation of Company Under IBC, 2016

- **Public Announcement and Collation of Claims** -Within 5 days of his appointment, the liquidator shall make a public announcement (in an English newspaper, regional newspaper, and on website of the company) calling upon all stakeholders like creditors, employees, etc. to submit their claims within 30 days of liquidation commencement date.
- **Preparation of Preliminary Report**-The liquidator shall prepare Preliminary Report about the capital structure, estimates of assets and liabilities, proposed plan of action etc. and submit it to the company within 45 days of Contributories' Resolution
- **Verification of claims**-The liquidator shall verify the claims within 30 days of the last date of the receipt of claims and on the basis of claims admitted, prepare a list of stake holders within 45 days from the last date of receipt of claims.
- **Opening of bank account** -The liquidator should open a bank account in the name of company followed by words "in voluntary liquidation" in a scheduled bank for receipt of all moneys due to the company.
- **Realisation of Assets and Distribution of Proceeds**-The liquidator shall sell, recover and realize all assets\ moneys due to the company in a time bound manner. He should distribute the proceeds to the stakeholders within 6 months of receipt of proceeds .
- **Completion of Liquidation**-The liquidator shall endeavor to complete the liquidation process within 12 months from the liquidation commencement date. When the liquidation process gets fully completed, the liquidator should prepare a Final Report and submit it to the Registrar, IBBI and NCLT . He shall make an application to NCLT for the dissolution of the company
- **Dissolution of the company**-Based on Final Report and the application for dissolution from the liquidator, the NCLT shall pass an order of dissolution and the company shall stand dissolved from the date of NCLT's order. A copy of the Dissolution Order shall , within 14 days, be forwarded to the Registrar for his information and record.

Pre- Packaged Insolvency Resolution Plan for MSMEs

- Micro, Small and Medium Enterprises (MSMEs) are the backbone of the Indian Economy . In the wake of Covid pandemic, which badly hit these companies, a prepackaged insolvency resolution process was introduced in April 2021 via Insolvency and Bankruptcy Code (Amendment) Act, 2021 as an alternate, cost -effective and speedier resolution mechanism for MSMEs in financial distress.
- Corporate debtor classified as MSME can make an application to NCLT for Pre-packaged insolvency resolution if its default ranges between Rs.10 lakhs to Rs. 1 crore.
- The application shall contain
 - Names of insolvency professional
 - Declaration by majority of directors that necessary provisions have been complied with
 - Special resolution by the members of the corporate debtor approving the filing of application
 - Base resolution plan prepared by it
 - Such other documents as may be provided.
- The NCLT shall within 14 days of application, admit it or reject it. If the application is accepted, the process shall be completed within 120 days from the pre-packaged commencement date.
- The resolution plan is required to be approved by the Committee of Creditors (CoC). If it is so approved, the NCLT shall approve it within 30 days. If it is not so approved with CoC, within 90 days, application for termination of the pre-packaged insolvency resolution plan shall be filed by the MSME.