

Winding-Up (Liquidation)

Chartered Accountancy
Corporate Level
Corporate Law (LAW)

Mohomed Jesmin
LL.B, Attorney at Law

WINDING-UP (LIQUIDATION)

If a company is in financial difficulties, it has two options

1. Winding up (Liquidation)-this is done to close down the company
2. Administration-this is done to rescue the company so that it may continue its business without winding up

WINDING UP (LIQUIDATION)

The **winding up** of a company is the process by which the operations of a company are formerly brought to an end. In a winding-up a **liquidator** is appointed and he will dispose the assets of the company; settle the debts and distribute any remaining surplus among shareholders.

Modes (Types) of Winding Up (Section - 267)

The winding up of a company may be either –

- (a) **By the court** (i.e. Compulsory)
- (b) **Voluntary**; (without going to court) or
- (c) **Subject to the supervision of the court**

WINDING-UP BY THE COURT

To windup a company an application should be presented to the **Commercial High Court situated in Colombo** by way of a petition.

The procedure for the winding up of a company is set out in the **Company Winding Up Rules of 1939**. Therefore, the provisions of the Companies Act 2007 and the Winding Up Rules are applicable to liquidate a company through the court.

Circumstances under which a company may be wound up by the Court (Grounds for compulsory winding-up) - Sec.270

- (a) The company has by **special resolution** resolved that the company should be wound up by the court;
- (b) The company does not commence its business within **a year** from its incorporation or **suspends its business** for **one year**;
- (c) The number of the members **falls below** the statutory **minimum number**;
- (d) The company has **no directors**;
- (e) The company is **unable to pay its debts**; or
- (f) The court is of opinion that it is **just and equitable** that the company should be wound up.

What is the meant by **Inability to Pay Debts?**

As per Sec.271, A company shall be **deemed** to be unable to pay its debts –

- (a) If the company is indebted to a creditor in a sum **exceeding Rupees Fifty Thousand (Rs.50,000/-)** and even after that creditor **demand**s the payment if the company has for **three weeks** from the date of such demand, neglects to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor;
- (b) If execution or other process issued on a judgment, decree or order of **any court** in favour of a creditor of the company, **is returned unsatisfied** in whole or in part; or
- (c) If it is proved to the satisfaction of the court that the company is unable to pay its debts, and in determining whether a company is unable to pay its debts, the court shall take into account the **contingent and prospective liabilities** of the company.

Who may Petition to wind up a Company by the Court?

1. By the company itself.
2. By any creditor or creditors.
3. By any contributory or contributories.

Contributory means every **shareholder** and every other person liable to contribute to the assets of a company in the event of its being wound up.

Winding up Order

After hearing the winding up petition, the court may order the company to be wound up. After the winding-up order is made the **official receiver** will take charge of the company and its properties, he will call a meeting of shareholders and creditors to appoint a liquidator, after the liquidator is appointed, the liquidator will take steps to liquidate (wind up / close down) the company.

PARTIES TO A WINDING UP

- Official Receiver
- Committee of Inspection
- Liquidator

Official Receiver and his duties

The official receiver is an officer attached to the court for insolvency purposes. The court may appoint the Official Receiver as the provisional (temporary) liquidator until he or another becomes liquidator. Therefore, an official receiver is an individual appointed to manage a company for a short period of time.

The official receiver's main duty is to **summon separate meetings of creditors and contributories** for the purpose of determining a **liquidator** and for the appointment of a **committee of inspection** to **act with** the liquidator.

Committee of Inspection (Section - 299)

The committee consists of a small number of creditors and contributories. Its function is **to assist the liquidator** and **to inspect and certify the accounts**. In certain matters the **liquidator must obtain their consent**. If there is no committee of inspection, the court will exercise the powers of the committee.

LIQUIDATOR

Appointment

As per sec.285, it is the **court that has the power to appoint a liquidator**. The court may appoint a liquidator based on the nominations made after the meetings of the creditors and contributories. If the two meetings do not agree on the person to be appointed, the court will decide the difference and make such order as it thinks fit. If a liquidator is not appointed by the court, the official receiver will act as the liquidator.

A person other than the official receiver who is appointed as a liquidator cannot act until he has given notice of his appointment to the Registrar of Companies and given security in the prescribed manner to the satisfaction of the Registrar.

POWERS OF THE LIQUIDATOR

S.292 provides that the liquidator in a winding-up by the court has two types of powers,

- (1) **The powers which he has to exercise with the sanction of the court** or of the committee of inspection
 - a) Bring and defend cases in the name and on behalf of the company.
 - b) Carry on company's business so far as may be **beneficial for winding-up**.
 - c) Appoint an Attorney-at-Law to assist him in his duties.
 - d) Pay any classes of creditors in full.
 - e) Make a compromise or arrangement with creditors.
 - f) Compromise, secure and discharge all calls, claims, debts and liabilities of the company.

- (2) The powers that can be exercised on his own responsibility
- a) Sell the property of the company.
 - b) Do all acts and execute, in the name and on behalf of the company, all deeds and documents, and use the company's seal there for.
 - c) In the insolvency or death of a contributory, to claim any amount due from him.
 - d) Draw, accept, make and endorse bills of exchange in the name of the company.
 - e) Raise money on the security of the company's assets.
 - f) Appoint an agent to do business which he cannot do himself.
 - g) Do all such other things as are necessary for winding up the affairs of the company and distributing its assets.

Vacation of Office of Liquidator

The liquidator vacates his office,

- (a) When he resigns
- (b) When he is removed by the court
- (c) When he is released by the court - A release may be granted when he has realized all the property of the company or so much thereof as can be realized.

A vacancy in the office of the liquidator is filled up by the court.

Sec.383 Qualifications of Liquidator.

Dissolution Order

When the affairs of the company have been completely wound up, the court shall on the application of the liquidator make a DISSOLUTION ORDER. The company is dissolved from the date of the order. Within 15 days of making of the Order the liquidator must notify the Registrar of Companies and the Registrar should make in his books a minute of the dissolution of the company: S. 316.

VOLUNTARY WINDING - UP

Closing a company without going to Court

When may a Company be wound Up Voluntarily? (Section - 319)

- (1) If the articles provide for the dissolving of the company after a specified period or on the occurrence of a specified event, and when such period expires or when such an event occurs, the company may pass an ordinary resolution to wind up the company.
- (2) If the company resolves by special resolution that the company should be wound up voluntarily.
- (3) Where the company resolves by special resolution to the effect that it cannot by reason of its liabilities continue its business and that it is advisable to wind up. (Creditors voluntary Winding-Up)

Notice of winding-up resolution must be given in the Gazette within 14 days of passing of the resolution: S - 320.

COMMENCEMENT

A voluntary winding-up is deemed to commence at the time of passing of the resolution for voluntary winding - up: s.321.

Effects of Voluntary Winding-Up

On the commencement of the winding-up:

- (1) The company should cease to carry on its business.
- (2) All transfers of shares are void unless sanctioned by the liquidator:
- (3) Any alteration in the status of the shareholders is void:

Even though the winding up commences the corporate state (separate legal personality) and corporate powers of the company will continue until the company is dissolved.

Appointment of liquidators in a voluntary winding up (section - 326)

As per sec.326, the company at a general meeting shall appoint one or more liquidators for the purpose of winding up the affairs and distributing the assets of the company and may fix the remuneration to be paid to each such liquidator. On

the appointment of a liquidator, all the powers of the directors shall cease, except so far as the company in general meeting or the liquidator sanctions the continuance thereof.

TYPES OF VOLUNTARY WINDING-UP

Voluntary winding-up may be

- 1) a shareholders' voluntary winding-up or
- 2) a creditors' voluntary winding-up.

A voluntary winding-up becomes a shareholders' voluntary winding-up when a declaration of solvency is made, and a creditors' voluntary winding-up when such a declaration is not made.

Declaration of Solvency (Section - 324)

Such a declaration is made by the directors or a majority of them at a meeting of directors. The statutory declaration must state to the effect that the directors having made a full inquiry into the affairs of the company are of the opinion that the company will be able to pay its debts in full within a period not exceeding 12 months from the commencement of the winding-up.

The declaration takes effect only on registration with the Registrar of Companies. The statutory declaration must be made and filed within 5 weeks preceding the date on which the winding-up resolution is passed and must embody a statement of the assets and liabilities. (Declaration of solvency is attached for the reference)

Final meeting and dissolution under winding up by creditors

- (i) As soon as the affairs of the company are fully wound up, the liquidator shall make up an account and shall call a general meeting of the company and a meeting of the creditors, for the purpose of laying the accounts and giving an explanation thereof.

(ii) Within one week from the date of these meetings, the liquidator shall send to the Registrar a copy of the account and shall make a return to him of the holding of the meetings and of their dates.

(iii) The Registrar on receiving the account in respect of each of these meetings shall forthwith register them and on the expiration of **three (3) months** from the date of registration thereof, the company shall be deemed to be dissolved:

WINDING-UP SUBJECT TO SUPERVISION OF COURT (SECTION - 351)

This is a voluntary winding up done under the supervision of the court. When a company has passed a resolution for voluntary winding-up, the court may order that the voluntary winding-up shall continue subject to such supervision of the court, and with such liberty for creditors, contributories or others to apply to the court, and generally on such terms and conditions as the court thinks just. The main advantage of the supervision order is that no proceedings can be commenced or continued against the company without leave of the court. Another advantage is that where such an order is made, the court may appoint additional liquidator, the liquidator so appointed is in the same position as if he had been appointed in a voluntary winding-up:

QUALIFICATIONS OF LIQUIDATORS SEC.383

(1) None of the following persons may be appointed or act as a liquidator of a company: —

- (a) a person **below eighteen years of age**;
- (b) a **creditor** of the company in liquidation;
- (c) a person who has **within the two years immediately preceding** the commencement of the winding up, been a **shareholder, director, auditor, or receiver** of the company or of a related company;
- (d) an undischarged bankrupt;
- (e) a person who has been adjudged to be of **unsound mind** under the provision of the Mental Diseases Ordinance;

- (f) a person in respect of whom an order has been made under section 468;
 - (g) a person who is prohibited from being a director or promoter of or being concerned or taking part in the management of a company under section 186 of the Companies Act, No. 17 of 1982, or who would be so prohibited, but for the repeal of that Act; or
 - (h) a person who is prohibited from being a director or promoter of or being concerned or taking part in the management of a company under section 213 or 214.
- (2) **A body corporate** shall not be appointed or act as a liquidator.

ADMINISTRATORS

Power of board to appoint Administrator - Sec.401(1)

The board may resolve to appoint an administrator of a company, where the board considers that the company is unable to pay its debts as they fall due and it is **necessary to recover the company** from the loss.

An administrator shall not be appointed in the following circumstances-

Sec.401(4)

- (a) if an order has been made for the winding up of the company;
- (b) if a receiver has been appointed, unless that receiver consents to the making of the order; or
- (c) if an administrator has been appointed by the company on a previous occasion, unless the leave of the court to make the further appointment is first obtained.

If a resolution is passed in contravention of Sec.401(4) such a resolution shall be void (invalid) and of no effect - Sec.401(5).

Effect of appointment of administrator- Sec. 403

Generally, the period of administration will be one year, during the period of administration—

- (a) no resolution may be passed or order made for the liquidation of the company;
- (b) no steps be taken to enforce any security over any property of the company or to repossess any goods in the company's use or possession under any hire-purchase agreement, except with the consent of the administrator or with the leave of the court;
- (c) no other proceedings and no execution or other legal process may be commenced except with the consent of the administrator or with the leave of the court.

Powers of administrators-Sec.416

An administrator—

- (a) shall manage the affairs, business and property of the company;
- (b) may do all such things as may be necessary or desirable for the management of the affairs, business and property of the company;
- (c) shall have all the powers that could be exercised by a receiver of the whole of the property and undertaking of the company

DECLARATION OF SOLVENCY

Sections 324(1) (2) of the Companies Act No. 7 of 2007

No. of Company [] [] [] [] []

Name of Company []

We
.....
.....of
.....

..... being all the/ the majority of the* Directors of and being assembled, on at a meeting of Directors of the Company for the purposes of section 324, state that we have made a full inquiry into the affairs of this Company, and that, having so done, we have formed the opinion that this Company will be able to pay its debts in full within a period, not exceeding twelve months, from the commencement of the winding up.

Date [] [] [] [] [] []
Day Month Year

Signatures
1. []
2. []
3. []

Presented by []

Email (Optional) []
Telephone: []
Facsimile : []

Note : This declaration should be delivered to the Registrar of Companies, within 5 weeks immediately preceding the date of the passing of the resolution of winding up .

* Delete what is not applicable