

Ch. Liquidation of Companies

Meaning of Liquidation:

Liquidation is the process a debt-laden company initiates to wind up its operations and sell its assets in order to repay said liabilities and other obligations. A company is liquidated when it is ascertained that the business is not in any state to continue. This may be due to various reasons such as insolvency (usually the main reason), unwillingness to carry on with the operations, etc.

If the enterprise is bankrupt, the liquidator sells the company's assets to repay all liabilities. The positive balance after repaying the creditors is then distributed among the company's shareholders.

The word 'Liquidation' has not been used anywhere in the Companies Act, 1956. It is the word 'winding up' which has been used in this Act. By winding up of a Company, we mean, "Winding up of a Company is the process whereby its life is ended and its property is administered for the benefit of its creditors and members. And an administrator, called a Liquidator, is appointed and he takes control of the Company, collects its assets, pays its debts and finally distributes any surplus among the members in accordance with their rights."

Consequences of Winding Up:

The consequences of winding up may be discussed under the following heads:

1. An official designated as liquidator will take over the administration of the Company. In case of compulsory winding up, the official liquidator, attached to the High Court, functions as liquidator of the Company. In case of voluntary winding up, such an official is appointed by the members or the creditors depending upon members, or creditor's voluntary winding up.
2. The powers of the Board of Directors will terminate and will now vest in the liquidator.
3. No suit or other legal proceedings can be proceeded with against the Company except with permission of the court.
4. The order for winding up has the effect of a notice of discharge to the employees of the company, except where the business of the company is continued by the order of the court.
5. A shareholder is liable to pay the full amount up to the face value of the shares held by him. Not only the present members but past members are also liable in the event of winding up of the company.

The liabilities of present member is the amount remaining unpaid on the shares held by him while a past member can be called upon to pay if the contributions made by the present members are not adequate.

6. A Company, whether solvent or insolvent, can be wound up under the Act. In case of solvent company, all claims of its creditors when proved are fully met. In case of insolvent company, the rules under the Law of Insolvency shall apply.

‘Winding up’ and ‘Dissolution’.

Winding up is the first stage in the process whereby assets are released, liabilities are paid off and the surplus, if any distributed among its members. **Winding up the affairs represents another step after the dissolution process starts**

Dissolution is the final stage whereby the existence of the company is withdrawn by the law. Dissolution is an act which puts an end to the life of the company. **Dissolution is the procedure that ends a company’s existence as a legal entity**

The Important differences between Dissolution and Winding Up are listed below:

Dissolution:

1. The dissolution of a company is recorded and registered by the Registrar of Companies.
2. The process of dissolution is purely administrative function i.e. Order for dissolution is given by court only.
3. The Liquidator does have any important role in the dissolution.
4. The dissolution must take place after winding up.

Winding Up:

1. The winding up of a company is heard and judged by the Tribunal.
2. The process of winding up is purely judicial function.
3. Winding up is carried on by liquidator appointed by company/court The Liquidator has important role in the winding up.
4. After winding up, dissolution takes place.
5. Winding up always don't lead to dissolution

Liquidation is the process of ending a company's existence and redistributing company's assets to creditors and owners

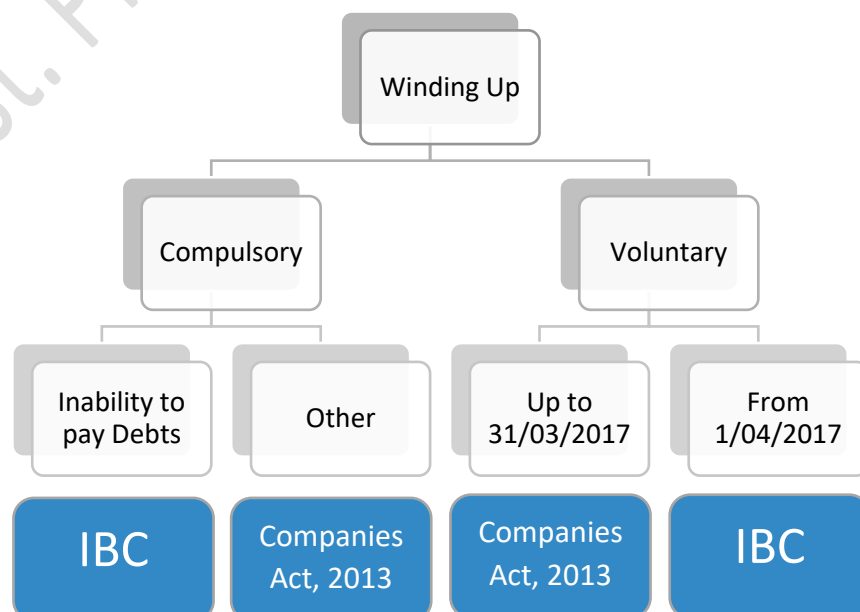
Liquidation is also referred to as dissolution and the terms are used interchangeably, but technically they describe different actions and their meaning is not the same. In other words, liquidation is seen as a last legal resort for a stressed company, while dissolution is the first step in closing a business.

Based on the availability of funds, the sale proceeds are distributed in the following order: **creditors, debt security owners, preferred shareholders and lastly common shareholders.**

In the case of dissolution, shareholders or owners do not receive any proceeds, whereas in case of liquidation, the shareholders or owners receive proceeds from the company if there are enough assets, after paying the debts owed to the creditors of the company.

There is difference between Winding Up & Liquidation, that Winding Up is a process of ending all business affairs of the company and Liquidation refers to selling off assets of the company.

Modes of Winding Up



Winding Up by Tribunal (S. 271)

- Special Resolution
- Against National Interest
- Fraud
- Default in FS or Annual reports

Petitions (S. 272) by

By Contributory

By Registrar

By Company

Submit copy of Petition to Registrar and Registrar submit to Tribunal within 60 days of receipts of such petition

Statement of Affairs

➤ **Assets**

List A: Full Description of property not specifically pledge

List B: Assets Specifically Pledge

➤ **Liabilities**

List C: Preferential Creditors (Taxes, Salaries, Wages)

List D: List of Debenture holders Secured

List E: Unsecured Creditors

➤ **Share Capital**

List F: List of Preference Share holders

List G: List of Equity share holders

➤ **Deficiency/Surplus**

List H: Deficiency or Surplus account.

Liquidator's Final Statement of A/c : It is a statement showing Receipts and Payments for Liquidation it is prepare by Liquidator.

Liquidator's Final Statement of Accounts

Receipts	Payments
To Assets	By Liquidation Expenses
To Call Money	By Liquidation Remuneration
To Surplus from Securities (left after paying liability)	By Secured Creditors
	By Preferential Creditors
	By Unsecured Creditors
	By Preference Dividend
	By Preference Shareholders
	By Equity Shareholders

► 1. Liquidation Expenses

All the costs, charges and expenses incurred in winding up, including remuneration of liquidator are paid in priority to all other claims.

► 2. Liquidator's Remuneration

Liquidator's Remuneration is based on

Realisation of Assets and on **Payment made to Unsecured creditors**

- $\text{Remuneration} = \text{Amount} \times \text{Rate of Commission}$
(Funds are sufficient)
- $\text{Remuneration} = \frac{\text{Amount available} \times \text{Rate of commission}}{100 + \text{Rate of Comm.}}$
(Funds are Not sufficient)

► 3. Secured Creditors : Are those having pledge of any assets or property, their funds are secured against some assets , Like Debentures , Bank loans etc.

- ▶ 4. Preferential Creditors : Preferential Creditors should be paid in priority to all other debts eg.

Government taxes,

Salary and Wages,

Contribution under ESI Act,

Compensation, PF, Pension fund, Gratuity

- ▶ 5. Unsecured Creditors : They are specified by Co. and even unsatisfied portion of Secured creditors due to Preferential Creditors are also treated as unsecured creditors

- ▶ After Making payment of all the creditors i.e. External Liabilities Amount is used for

1st Arrears of Preference Dividend

2nd Preference Share Capital

Finally to Equity shareholders any left with liquidator