

**LIQUIDATION OF COMPANIES UNDER THE COMPANIES ACT, 2013 VIS-À-VIS THE INSOLVENCY AND BANKRUPTCY CODE, 2016**

*This article is divided into two parts covering the provisions relating to the winding up of the companies by the Tribunal under the Companies Act, 2013 and the Insolvency and Bankruptcy Code, 2016 in Part I and Voluntary Liquidation in Part II.*

**Part - I - Winding up of Companies by the Tribunal**

**Winding up under the Companies Act, 2013**

Prior to the enforcement of the Insolvency and Bankruptcy Code, 2016 (“Code”), winding-up of the companies was largely dealt under Chapter XX of the Companies Act, 2013, which included winding up of the companies by the ‘Tribunal’ or ‘Voluntary’. With the Code coming into effect, Chapter XX of the Companies Act, 2013 underwent substantial modifications to amend the provisions pertaining to winding up of companies by the Tribunal (*in particular Section 271 and the company’s inability to pay its debts*) and further to exclude the provisions of voluntary liquidation from the ambit of the Companies Act, 2013<sup>1</sup>. Therefore, all proceedings of voluntary winding up of a company is now governed by the Code.

Post the notification dated 31<sup>st</sup> March 2017, the Tribunal is empowered to wind up a company under Section 271 of the Companies’ Act 2013 only in circumstances such as:

- i. When the company passes a special resolution that the company may be wound up by the Tribunal;
- ii. If the company acts 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;
- iii. if any application is made by the registrar of companies or any other person authorized by the Central Government and the Tribunal is satisfied that there is fraudulent conduct in managing the affairs of the company;
- iv. if the company has defaulted in filing the its financial statements and annual returns for immediately preceding five consecutive financial years; or
- v. if the Tribunal is of the opinion that it is just and equitable that the company should be wound up.

The Ministry of Corporate Affairs vide its notification dated 24<sup>th</sup> January 2020<sup>2</sup>, has notified the Companies (Winding Up) Rules, 2020 that are applicable to companies undergoing liquidation under section 271 of the Companies’ Act, 2013 as well as to the summary procedure for liquidation under section 361 of Companies’ Act, 2013.

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<sup>1</sup> Notification No. IBBI/2016-17/GN/REG010 dated March 31, 2017 has substituted the provision for voluntary winding up with Section 59 of Code

<sup>2</sup> The Ministry of Corporate Affairs vide its notification dated 24<sup>th</sup> January 2020 has introduced Companies (Winding Up) Rules, 2020.

### ***Resolution process leading to liquidation under the Code***

As regards, the circumstances wherein the company was unable to pay its debts, the same came to be covered under the newly introduced provisions, Section 7, 9 and 10 of the Code. Under these provisions, either company itself, or any other creditor (operational or financial) could initiate corporate resolution insolvency process (“CIRP”) against the company for being in default and for not being able to pay the debt owed by the company to such operational or financial creditor.

The CIRP against the company has to mandatorily be completed within 330 days from the date of commencement of insolvency i.e. appointment of an insolvency resolution professional (“IRP”) as per the amendments in Section 12 of the Code by the Central Government vide its notification dated 16<sup>th</sup> August 2019<sup>3</sup> including any extension and the time taken in legal proceedings in relation to such resolution process of the corporate debtor, without any further extension. Pursuant to the Hon’ble Supreme Court judgement dated 15<sup>th</sup> November 2019 in case of *Essar Steel India Limited*<sup>4</sup>, it has been held that “*in certain cases it may be open for the Adjudicating Authority and/or Appellate Tribunal to extend time beyond 330 days*”.

On the commencement of the CIRP, the corporate entity undergoes moratorium and claims pending against such corporate entity are then invited by way of a public announcement. Subsequently, a committee of creditors is formed comprising of financial creditors. At the first meeting of the committee of creditors, either the appointment of the IRP is confirmed as the Resolution Professional or the IRP is replaced by another resolution professional on a majority vote of not less than 66% of voting share of the committee of creditor. The Resolution professional will then issue an information memorandum for formulating a resolution plan and inviting the resolution applicants to submit their resolution plans based on all the required information provided by the Resolution professional. If the committee of creditors approve the resolution plan and if the NCLT is satisfied that the resolution plan so approved meets the requirements under the Code, the NCLT can pass an order of approval of the resolution plan thus completing the CIRP for the effective implementation of the same. In the circumstances, the resolution plan is either rejected by the NCLT or the committee of creditors, the Corporate Debtor goes into liquidation. On liquidation, a Waterfall Mechanism (order of priority in which the proceeds from the sale of liquidation assets are distributed) will have to be followed. Under this, secured creditors have to be paid before any payments can be made to unsecured financial creditors who in turn have priority over operational creditors. Hence, under the Code, every attempt is made to rehabilitate the company, failing which, the company is liquidated.

### ***Part - II - Voluntary Liquidation under Section 59 of the Code***

Moving on to the provisions relating to voluntary liquidation of the companies under the Code, with effect from 1<sup>st</sup> April 2017 the procedure for voluntary winding-up of companies has been shifted from

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<sup>3</sup> The Ministry of Corporate Affairs vide its notification dated 16<sup>th</sup> August 2019 has amended section 12 of the Code by increasing the time line for completion of CIRP mandatorily with maximum of 330 days.

<sup>4</sup> *Committee of Creditors of Essar Steel India Limited v. Satish Kumar Gupta & Ors. (Civil Appeal No. 8766-67 Of 2019)*

the Companies Act, 2013, and is now contemplated as 'voluntary liquidation' proceedings, which are covered under Section 59 of the Code read with Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulation 2017 (**"the Regulation"**) and the adjudicating authority for the same is the National Company Law Tribunal (**"NCLT"**).<sup>5</sup>

The key differences as between the old and new provision are as follows:

- Shift of jurisdiction from the High Court to the NCLT;
- Shift of powers from the Official Liquidator to the Insolvency Professional (**"IP"**);
- The timeline for carrying out voluntary dissolution is 12 months.

The idea was that the shifting of the jurisdiction to the NCLT would result in faster execution and settlement of cases, since IPs are to themselves oversee the liquidation process and simply report on compliance to the NCLT, who will thereafter, pass the order of liquidation.

***Who can initiate voluntary liquidation proceedings?***

A corporate person<sup>6</sup> who intends to liquidate itself voluntarily and has not committed any default may initiate voluntary liquidation proceedings.

"Default" here means non-payment of debt when whole or any part or installment of the amount of the debt has become due and payable and is not repaid by the debtor or the corporate debtor, as the case may be. For the purpose of initiating voluntary winding up, the default that has occurred in the past but has later been paid off shall not be considered and will be out of scope of voluntary liquidation under Section 59 of the Code.

A company may choose to be wound up voluntarily under several circumstances like- winding up as a result of expiry of period of operation fixed in its Articles of Association; or occurrence of a certain event for its dissolution as provided in its Articles of Association. Most commonly, a corporate entity chooses for voluntary liquidation when it turns insolvent and is further incapable of paying off its liabilities but at the same time has not committed any default in paying off its debt.

It is further pertinent to note that if a corporate entity initiates voluntary winding up, its liquidation must not result in defrauding of any person and must further be just and reasonable as per law.

For the purpose of ensuring that there is no default by the corporate entity, the majority of the directors of that company are to make a declaration along with an affidavit verifying that the corporate person is not in default or if any debts are due then it shall pay off the same under the proposed voluntary liquidation. Such declarations are required to be supplemented along with the statement of accounts and financial statements of the corporate entity and only after conducting an

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<sup>5</sup> Companies (Transfer of Pending Proceedings) Rules, 2016

<sup>6</sup> Section 3(7) of the Code - "corporate person" means a company as defined in clause (20) of section 2 of the Companies Act, 2013, a limited liability partnership, as defined in clause (n) of sub-section (1) of section 2 of the Limited Liability Partnership Act, 2008, or any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider;

audit of the financial statements and preparing a valuation report of the corporate person, any application for voluntary winding up shall be proceeded with.

***Pre-requisites for voluntary winding up***

After a declaration is submitted by the directors or partners of the corporate entity, within 4 weeks, a special resolution or a resolution is passed by the contributors requiring the corporate entity to be wound up and then an insolvency resolution professional is appointed as a liquidator. As per the Regulation of the Code, any person who is a member of the company or any other person who may financially contribute to the process of winding up of the corporate entity and which may further benefit the company as a whole is called a 'contributor' or 'contributory'. Such a resolution process is called a 'Contributors Resolution' for the purpose of voluntary liquidation.

Within seven days of passing of the said resolution, the creditors who represent two-third value of the total debt of the corporate entity must approve such resolution.

Under Section 59(4), the Registrar of Companies and the Insolvency and Bankruptcy Board of India are to be notified by such company going under voluntary liquidation after a resolution is passed or the approval has been taken by the creditors under section 59(3) of the Code.

***Proceedings***

The procedure of voluntary winding is simplified under Chapter V of the Code with specified time periods for each step of liquidation. Below mentioned are the steps for voluntary winding up of any corporate entity :-

**Step 1-** Company to convene the Board Meeting to approve the proposal of voluntary liquidation and to take a declaration from majority of Directors along with affidavit stating that full inquiry has been made into affairs of the company and the opinion is formed that either company has no debt or that it will be able to pay its debt from proceeds of assets sold in voluntary liquidation and that the intent of liquidation is not to defraud any person ("**Declaration**"). The Declaration should have the Audited Financial Statement and record of Business Operations (of previous 2 years or since incorporation, whichever is later) and Valuation Report of assets of company, if any, as attachment. The same needs to be submitted to the Registrar of Companies.

**Step 2-** A Special Resolution shall be passed to approve the process of voluntary liquidation of the corporate entity and to appoint an Insolvency Resolution Professional to act as a liquidator ("**Approval**"), within a time frame of four weeks after the submission of declaration. In a situation when there are any unpaid debts of the corporate entity, an approval of 2/3rd of the creditors shall be required.

**Step 3-** After the Approval, within 5 days of such Approval, a public notice is to be announced in a newspaper (*one English and one Regional Language with wide circulation at location of Registered Office and Principal Office, if any of the Company and other location in the of the liquidator and on the website of company & Board, if any*) along with an announcement displaying on the website of such

corporate entity undergoing liquidation so as to invite claims or if there are any objection to be raised by any of the stakeholders of the company.

**Step 4-** Within seven days of receiving such Approval, an intimation of such Approval is to be sent to the Registrar of Companies and the Insolvency and Bankruptcy Board of India.

**Step 5-** A preliminary report of the preliminary finding of the authorized capital, approximations of assets and liabilities, the proposed plan of action etc. is then prepared for the purpose of liquidation. The liquidator shall submit the said preliminary report to Company **within 45 days** from liquidation commencement date.

**Step 6-** The claims, if any, are then verified by the liquidator within 30 days from the last date of receipt of claims and these claims can either be rejected or admitted, in whole or in part, on the discretion of the liquidator.

**Step 7-** The liquidator shall open a bank account in the name of the corporate person followed by the words 'in voluntary liquidation', in a scheduled bank, for depositing all moneys due to the corporate person. All moneys, including cheques and demand drafts received by the liquidator as the liquidator of the corporate person shall be deposited into the said bank account.

**Step 8-** The process of sale of all the assets of the Corporate Person and the recovery of amounts which are due to the corporate person and the realization of capital which are uncalled or unpaid in nature or are contributions which are unpaid, shall be done.

**Step 9-** Distribution of all the amounts received from the realization of the assets of the corporate entity shall be done within a period of six months to all the stakeholders.

**Step 10-** The Insolvency Resolution Professional appointed as the liquidator shall then send a final report to the contributors of the corporate person, the Registrar of Companies and the Insolvency and Bankruptcy Board of India. This final report shall also be submitted to the adjudicating authority i.e. the National Company Law Tribunal.

**Step 11-** After application for dissolution of the corporate entity is to be submitted to the adjudicating authority.

**Step 12-** An order is passed by the adjudicating authority declaring that the corporate entity has been dissolved from the date of the passing of that order. This order is to be submitted to the Registrar of Companies within a period of fourteen days from the date of passing of dissolution order.

#### **DIFFERENCE BETWEEN PROVISIONS UNDER SECTION 10 AND SECTION 59 OF THE CODE**

One of the key differences is that under Section 59 of the Code, voluntary liquidation process can be initiated by a corporate debtor that has not committed any default whereas under Section 10, there

must be a default of minimum one crore rupees<sup>7</sup> for a corporate applicant to file an application for initiating CIRP. Further, the end result under a CIRP under section 10 is recovery of such corporate entity whereas under voluntary liquidation under section 59, a company gets dissolved. The intention of the legislature and the spirit of law behind Section 10 of the Code is to help the company revive and provide a resolution scheme to distressed companies which is contrary to the provision of voluntary liquidation under section 59.

### **CONCLUSION**

For any company to follow a simple exit route, section 59 of the Code expedites the entire process of voluntary winding up by bringing one simplified timeline in place. This procedure appears to be viable also because it ensures that there is no injustice caused to the possible stakeholders of the company by taking declarations from the directors or partners and keeping the Insolvency and Bankruptcy Board of India and the Registrar of Companies in the loop during the entire winding up procedure.

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### ***About Solomon & Co.***

Solomon & Co., (Advocates & Solicitors) was founded in 1909 and is amongst India's oldest law-firms. The Firm is a full-service firm that provides legal service to Indian and international companies and high net-worth individuals on all aspects of Indian law.

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<sup>7</sup> The Ministry of Corporate Affairs vide its notification dated 24<sup>th</sup> March 2020 has amended section 4 of the Code and increased the minimum default amount to Rupees One Crore from Rupees One Lakh for instituting CIRP proceedings.