Voluntary Winding up under Insolvency & Bankruptcy Code, 2016

A company comes into existence by the legal process of incorporation whereas liquidation is the process by which its existence comes to an end. Voluntary liquidation occurs when the members of a company formally resolve to voluntarily wind up the affairs of the company and dissolve it. The objective of voluntarily winding up a company is to enable the members and creditors to settle their affairs among themselves without seeking the assistance of the Tribunal. Voluntary winding up is an option available only to solvent companies. Apart from winding up voluntarily, a company can opt for the Fast Track Exit (FTE) mode, which is striking off the name/deregistration of a company from the Register of Companies under Section 560, subject to the fulfillment of certain conditions laid down by the Companies Act, 1956.

The provisions associated with voluntary liquidation of corporates are covered under the Insolvency and Bankruptcy Code, 2016 (the Code) which was enforced in 2016. The Code has further notified regulations which provide the process to be followed for voluntary liquidation.

Eligibility Criteria

- Corporates need to ensure that they have not committed any defaults.
- A majority of the Directors/Partners of the corporate should give a declaration of solvency stating that:
- They have made a full inquiry into the affairs of the corporate and they have formed an opinion that either the corporate has no debts or will be able to pay its debts in full from the proceeds of assets to be sold in the liquidation; and
- The corporate is not being liquidated to defraud any person.

Brief Process

- The Directors have to conduct an investigation into the affairs of the company to ensure the company is solvent.
- The shareholders/partners have to approve the corporate action in relation to the voluntary winding up of the corporate and appoint an insolvency professional as the liquidator of the corporate.
- In case the corporate has creditors, two-thirds of the creditors (in value) shall approve the resolution.
- A public announcement shall be made by the appointed liquidator inviting claims from all the stakeholders of the corporate.
- The corporate shall cease to carry on its business on the appointment of a liquidator except for its beneficial winding up.
- The liquidator shall collect, collate and verify all claims and prepare a list of stakeholders.
- The liquidator shall create a liquidation estate; then realise and distribute all the assets of the corporate.
- The liquidator shall make an application for the dissolution to the adjudicating authority, i.e. National Company Law Tribunal (NCLT), along with the final report. The key points which will come into final repot are given below:
  - Audited accounts of liquidation process
  - Statement demonstrating that the assets has been disposed of and the debt has been discharged to the satisfaction of the creditors and that no litigation is pending against the corporate or sufficient provision has been made to meet the obligations arising from any pending litigation
  - Sale statement in respect of all assets providing the details of the sale thereof

The corporate shall be wound up from the date of the dissolution order passed by the National Company Law Tribunal (NCLT).

Advantages of Voluntary Winding up

Limit on Director's liability: The most important difference between voluntary winding up and other means of closure is that the liabilities of a Director shall not continue post the dissolution of the company, except in the cases of fraud, misrepresentation, etc. whereas in other modes i.e. striking off the company from the Registrar of Companies (ROC), the liabilities of the Directors are open ended (they continue even after the company is dissolved). Post the enactment of the Companies Act, 2013, the penalties on account of non-compliances are stringent in nature and include monetary as well as non-monetary (like imprisonment) penalties.

No waiting period: In FTE, the intent is different. Operational companies cannot apply for striking off the name from the ROC, whereas in voluntary winding up, both operational as well as non-operational companies can make an application.

Licensed Professional: Previously, under the 1956 Act, any one could act as the liquidator. However, as per the new Code, only a licensed professional can act as the liquidator of the company which ensures speedy closure in the most appropriate way. A licensed professional is well-versed with the provisions of the Code to complete winding up on time.

Board continues to exist: The powers of the Board of Directors shall not cease and shall continue without hampering the independence of the liquidator, which was not the case in voluntary winding up under the 1956 Act.

Substantially private process: It is a private process run by the third party (the liquidator), wherein they have to make sure that each stakeholder is paid and is satisfied with their settlement. Under the Code, the private process has been clearly defined and will not lead to any uncertainty.

Single window for the entire process: The new Code is a single window legislative code under which closure of a company has become easier and more uniform compared to that under the Companies Act, 1956 and 2013.

Minimal intervention from the government: Previously, the voluntary liquidation process had high government intervention and was processed by various authorities such as the official liquidator and the High Court in addition to the company liquidator. Under the new Code, the process is single-handedly run by the liquidator with minimal involvement of the adjudicating authorities as the role of the official liquidator has been eliminated.

Critical Aspects

Listed below is some crucial information on the matter that was not provided by the statute that attains higher importance while making decisions during the winding up process:

Declaration of solvency: Formulating the declaration of solvency is a critical task of Directors as they have to consider various matters like the company's present/future, certain/contingent, and fixed/liquid liabilities. Any misrepresentation or false declaration can lead to penalties and punishments.

Disposal of assets:

- The fair procedure that should be opted for by the liquidator to dispose assets
- Whether the liquidator is obliged to dispose the assets at a fair price or does he have the power to dispose assets at a price less than the fair value in the case of distressed sales.
- Whether such decisions/transactions by the liquidator are questionable by any authority

Clearance from Income Tax (IT) Authorities: The Code does not provide for any specific notice or No Objection Certificate (NOC) requirements from the Income Tax Act (ITA). However, the ITA provides for a minimum period of three months to the IT Authorities from the date the notice was received from the liquidator to notify the amount which shall likely be payable by the company. Furthermore, the Code provides that all the claims have to be given a period of 30 days from the date of public announcement. The question which arises is whether the company will be dissolvable without the NOC from the IT department or non-completion of assessments.

Although the Code will override other laws, the stance of the NCLT will be important, and a question arises as to whether it will be in a position to direct the IT department to expedite the process at their end or if the liquidator will be at mercy of the IT department's feedback.

Tax clearance certificate: In the case of foreign shareholders, fund remittance will be allowed only when the shareholders produce an NOC or Tax Clearance Certificate from the IT department at the time of repatriating funds. There is also uncertainty regarding whether the IT department will issue the NOC on time, whether the entire process will be delayed, whether they can clear all tax assessment in a timely manner or if it will happen as per the normal provisions of the ITA.

Statutory funds: If there are statutory funds like the Employee Provident Fund that is still unclaimed or where the employee is untraceable for receiving the fund, the Code provides that such unclaimed funds shall be transferred by the liquidator to the company's liquidation account in the public account of India. If this money remains unclaimed for a period of 15 years, it shall be transferred to the general revenue account of the central government.

Failure to discharge all debt: If the liquidator believes that the company is unable to pay off its debts in full, he may apply for suspending the proceedings with the NCLT under voluntary liquidation and the NCLT shall pass an appropriate order. So far, it is uncertain what stand the authority will take in case of failure to pay all dues and whether there would be implications on the Directors who have given a solvency declaration.

Conclusion

The fundamentals of the process remains similar to the erstwhile provisions under the Companies Act, 1956, however, the Code seeks to reduce the intervention of regulatory authorities drastically. Once the affairs of the company are wound up entirely, the liquidator has to make an application to the Tribunal for passing the order of dissolution of the company. Furthermore, unlike the 1956 Act provisions, only solvent companies can file for voluntary winding up. Also, the approval of creditors is required which was not a condition previously.

The new process under the Code is a private process, independently driven by the liquidator with a shorter timeframe. The Code is running in the right direction and is in line with global practices removing overall hurdles which prevailed in the older laws, due to which closure of solvent companies has become a lot smoother.

To conclude, the new law has removed the concept of an official liquidator, shifting the onus of all activities and consequences onto the company liquidator, which is expected to improve the liquidation process.

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