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WINDING UP

MEANING

A company comes into existence by a legal process and when, for any reason, it is desired to end its existence, it must again go through the legal process of winding up its affairs. Winding up or liquidation is the process by which the management of a company's affairs is taken out of its directors' hands, its assets are realised by a liquidator, and its debts are paid out of the proceeds of relisation. If any balance remains in the hands of the liquidator, it is divided among the members of the company in accordance with their rights under the articles. In the words of Professor Gower: "Winding up of a company is the proces whereby its life is ended and its property administered for the benefit of its creditors and members. 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."[1]

Winding up and dissolution. One must understand here that winding up and dissolution of the company are not one and the same thing. A company is said to be dissolved when it ceases to exist as a corporate entity. Winding up precedes dissolution. It is the process by which the dissolution of a company is brought about. At the end of the winding up, the company will have no assets or liabilities, and it will therefore be simply a formal step for it to be dissolved, that is for its legal personality as a corporation to be destroyed. In between winding up and dissolution the legal entity of the company remains, and it can be sued in a court of law.

Winding up and insolvency. It should be noted that winding up a company is not the same things as bankruptcy of a company: (a) a winding up order can be made, even when the company is solvent. In other words, winding up is not confined to cases where a company is

[1]L.C.B. Gower, *The Principles of Modern Company Law, op. cit.*, 3rd edn., p. 647.

insolvent, but it may be adopted as means of enabling the company or memebrs to reincorporate with more extended objects or further powers or more efficient means of management; (b) on winding up, the company as such does not cease to exist, only its administration is carried on through the medium of a liquidator. The property of a company still belongs to the company, which can carry on business (for a limited purpose) and file suits in its own name. It is otherwise in the case of insolvency; (c) even where a company is wound up because it is in insolvent circumstances, all the provisions of the insolvency law do not apply to it. The principle of "Reputed owwnership" does not apply to companies in winding up.[2]

Modes of Winding Up

A company can be wound up in any of the following three ways:
(i) compulsory winding up under order of the court,
(ii) voluntary winding up, and
(iii) winding up subject to supervision of the court.

WINDING UP BY THE COURT

Section 433 lays down that a company may be wound up by an order of the court. This is also known as compulsory winding up. A company may be wound up by the court in the following cases:

(i) **Special resolution.** A company may be wound up by the court if the company itself has passed a special resolution to that effect. It may be noted here that the power of the court is discretionary and it may refuse to pass an order for winding up if it finds that this would be against the public interest or the interest of the company as a whole. Moreover, winding up on this ground is not generally common because if such a large number of shareholders want the company to be wound up, they would prefer the mode of voluntary winding up which is far speedier and cheaper than compulsory winding up. Moreover, in voluntary winding up, the members have dominating control over winding up proceedings.

(ii) **Default in holding statutory meeting or in delivering a statutory report to the Registrar.** If default is made in holding the statutory meeting or in delivering a statutory report to the Registrar the court may order the company to be wound up. A petition for winding up on this ground can be presented either by the Registrar or by a contributory. If it is brought by any other persons, it must be filed before the expiration of fourteen days from the last day on which the statutory meeting ought

[2]*Gorringe v. Irwell Works* (1884) 34 Ch. D. 129.

to have been held [Sec. 439(7)]. Furthermore, instead of making a winding up order, the court may direct that the statutory report shall be delivered or that a statutory meeting shall be held. [Sec. 433(3)]

(iii) **Failure to commence business within one year of incorporation, or suspending business for a whole year.** If the company does not commence its business within one year of its incorporation or if it has suspended business for a whole year, it may be wound up by order of the court.

The power of the court to order winding up on this ground is discretionary and the court refused to pass such an order where suspension of business for a whole year was sufficiently accounted for and the company had intention to start business within a reasonable time.[3] Moreover, even if the company has not carried on business for a year, the court will not wind it up if there are reasonabale prospects of it doing so at not too remote a date and if there are good reasons for the delay, for example, the company may be waiting for a trade depression to pass.[4] Similarly, the court will not order the company to be wound up if it has ceased to carry on one of several businesses unless that business is the main object of the company.[5]

Similarly, where a company was formed to carry on business in Great Britain and aboroad, but in fact only carried on business abroad, it was held that it had commenced business and a winding up order was therefore refused.[6]

But if it is obvious that the company will never have sufficient resources to commence business, the court will not hesitate to wind it up.[7] Accordingly, where a company's business had remained suspended for ten years, its capital having been lost in misappropriation and the Orissa Government, which was the major contributory, had refused further held, the court did not hesitate to wind it up.[8]

(iv) **Reduction in membership.** If the number of members is reducted, in the case of a public company, below seven, and in the case of a private company, below two, the company, may be wound up by an order of the court.

This ground for winding up is provided to enable a member to escape personal liability for the company's debts which he will incur as per

[3]*Murlidhar v. Bengal Steamship Co.* (1920) A.I.R. Cal., 772.
[4]*Re Middlesborough Assembly Rooms Co.* (1880) 14 Ch. D. 104.
[5]*Re Amalgamated Syndicate* (1897) 2 Ch. 600.
[6]*Re Capital Fire Insurance Association* (1882) 21 Ch. D. 209.
[7]*Re London and County Coal Co.* (1867) L.R. 3 Eq. 355.
[8]*In Re Orissa Trunks v. Enamel Works Ltd.,* (1973) 43 Comp. Cas. 503 (Ori).

Section 45. In practice, petitions are rarely presented on this ground because a member may aviod personal liability by transferring some of his shares to nominees for himself so as to raise the number of members at least equal to the statutory minimum.

(v) **Inability to pay debts.** The court will order the company to be wound up if it is unable to pay its debts. Section 434 lays down specific cases when the company is deemed to be unable to pay its debts:

(a) *Demand for payment neglected.* If a creditor, to whom the company is indebted for a sum exceeding five handred rupees, has served on the company a demand for payment and the company has for three weeks thereafter failed to pay or otherwise to satisfy the creditor; or

(b) *Decreed debt unsatisfied.* If the execution or other process issued on a decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or

(c) *Commercial insolvency.* If it is proved to the satisfaction of the court that the company is unable to pay its debts. 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.

The debt must be presently payable and the title of the petitioner demanding it should be complete.[9]

If the company *bona fide* disputes the petitioner's debts. no order for winding up can be made.[10] *Bona fide* dispute in regard to a debt means that the dispute is based on a substanial ground and if such a dispute is raised, the court will not make a winding up order even if only a part of the debt is disputed on substantial ground.[11]

But if the dispute is not genuine and *bona fide* and it is put forward to hide the company's inability to pay, a petition for winding up would be entertained and, accordingly, winding up would be allowed.[12]

At the same time the machinery of winding up is not allowed to be misused as a means for putting pressure on a company to realise debts.[13] But where the court is satisfied that the company is insolvent and its substratum is gone, the court should order the winding up of the company and the motive of the petitioner is irrelevant in such cases.[14]

A time-barred claim cannot sustain a winding up petition, but a debt becoming time-barred by the time of the winding up order does not

[9]*Re Jambad Coal Syndicate,* A.I.R. (1936) Cal. 628.

[10]*Re Gold Hill Mines* (1883) 23 Ch. D. 210.

[11]*New Finds (India) v. Vorion Chemicals and Distilleries Ltd.,* (1976) 46 Comp. Cas. 87.

[12]*Vanaspati Industries Ltd. v. Firm Prabhu Dayal* A.I.R. 1950 E.F. 142.

[13]*Re London and Paris Banking Corporation* (1874) L.R. 19 E.Q. 444.

[14]*Bachharaj Factories Ltd. v. Hirjee Mills Ltd.,* (1955) A.I.R. Bom., 355.

matter.[15]

It may be noted that "unable to pay debts" means that the company is commercially insolvent. A company is commercially insolvent "that is to say that its assets are such and existing liabilities are such as to make it reasonably certain--as to make the court feel satisfied--that the existing and probable assets would be insufficient to meet the existing liablities.[16] This test has also been applied in cases decided recently by courts in India.[17] But the commercial solvency of a company is of no relevance so long as there be a failure on the part of the company to meet the creditor's demand within 3 weeks from the service of the notice, and an order of winding up will be made on the petition by creditor. In such a case, it is really not necessary for the court to enquire whether the company is in fact solvent or not, nor can any such inquiry be undertaken by it.[18]

(vi) **Just and equitable.** If the court is of the opinion that it is just and equitable that the company should be would up, it may order the company to be wound up. The power of the court under this clause is not confined to cases of the same kind as given in other clauses for winding up by the court under Section 433. The powers of the court under this clause are very wide and discretionary. What is just and equitable depends upon the circumstances of each particular case. While passing an order for winding up under this clause the court must take into consideration the interests of creditors, shareholders, employees and the society in general. Under Section 433 (2) where the petititon is presented on the ground that it is just and equitable that the company should be would up, the court may refuse to make an order of winding up, if it is of the opinion that some other remedy is available to the petitioners and that they are acting unreasonably in seeking to have the company would up instead of pursuing that other remedy. Relief under the just and equitable is in the nature of last resort when other remedies are not enough to protect the interest of the company.[19]

The following cases are worth noting where the court has ordered the company to be would up under the just and equitable clause:

(a) *Loss of substratum.* Where the main object of the company has failed to materialise or the substratum of the company is gone, it is just

[15]*Modern Dekor Painting Contracts Pvt., Ltd. v. Jenson and Nicholson India Ltd.,* (1985) 58 Comp. Cas. 255 (Bom.)

[16]*Re European Life Assurance Society* (1869) L.R. 9 Eq. 122.

[17]*Registrar of Companies v. Sohanmath Golcha* (1972) Comp. Cas. 386; *Krishna Iyer & Sons. v. New Era Manufacturing Co. Ltd.,* (1965) I Comp. L.J. 179.

[18]*Hariprasad v. A.C. Traders Ltd.,* (1964) A.I.R. Mad. 519.

[19]*Hind Overseas Pvt. v. R.P. Jhunjhunwala and another* (1976) 46 Comp. Cas. 91.

and equitable that the court should order winding up. Thus, where a company was formed for the purpose of acquiring a particular gold mine in New Zealand and title to it completely failed[20] and where a company was formed to make coffee out of dates under a German patent and the patent could not be obtained, the court found it just and equitable to wind up the companies.[21]

The mere fact that a company has suffered trading losses will not destroy its substratum, unless there is no reasonable prospect of it ever makting a profit in the future and the court is most reluctant to hold that it has not such propects.[22]

It was held that the substratum of the company is gone when it becomes impossible for it to carry on its manufacturing work after its stock in trade, plants and machineries are sold out in execution of a decree obtained by the bank.[23]

(b) *Deadlock in the management of the company.* Where there is complete deadlock in the management of the company, the court may order the company to be wound up under this clause. Thus where there were two directors of a private company who were the only shareholders, and they were not on speaking terms with each other, so that neither the board not the company at general meeting could possibly conduct any business of the company, the court ordered a compulsory winding up.[24]

However, a winding up order cannot be made on the mere possibility of friction and deadlock in future.[25] Similarly, incompatibility of good relations between rival factions in the directorate is not a sufficient ground for winding up.[26]

(c) *Aggressive or oppressive policy towards minority shareholders.* "Where the directors of a company were able to exercise a dominating influence on the management of the company and the managing director was able to outvote the minority of the shareholders and retain the profis of the business between member of the family, and there were several complaints that the shareholders did not receive a copy of the balance sheet, nor was the auditor's report read at the general meeting and that dividends were not regularly paid and the rate was diminishing," this constituted sufficient ground for winding up.[27]

Similarly a winding up order was made under this clause where there

[20]*Re Haven Gold Mining Co.* (1882) 20 Ch. D. 151.
[21]*R. German Date Coffee co.*, (1882) 20 Ch. D. 169.
[22]*Re Suburban Hotel Co.* (1867) 2 Ch. App. 737.
[23]*Davco Products Ltd. v. Rameshwar Lal* A.I.R. 1954 Cal. 195.
[24]*Re Yenidge Tobacco Co. Ltd.* (1916) 2 Ch. 426.
[25]*Re Anglo Continental Produce Co.* (1939) 1 All. E.R. 99.
[26]*Seethiyah v. Venkatasubbiyah* A.I.R. (1949) Mad. 675.
[27]*R. Sabapathy Rao v. Sabapathi Press Ltd.* A.I.R. 1925 Mad. 489.

was justifiable lack of confidence in the conduct and management of the company's affairs.[28]

But the court will not order winding up simply because the minority does not see eye to eye with the majority or with its policy or practice.

(d) *Company having no property.* Where the company was a bubble having no property or not doing any business and it is obvious that the company will never have resources to commence business, it was held that there was sufficient ground for winding up.[29]

(e) *Fraudlent or illegal purpose.* Where the whole object of the company was fraudlent or illegal or when the business of the company becomes illegal, the court will pass an order for winding up under this clause. Thus when the object of the company was to conduct a lottery by means of creating prize funds through periodical contributions from members, the court pased an order for winding up.[30]

But mere fraud in the promotion of a company or fraudulent misrepresentation in the prospectus will not be sufficient ground for winding up, for the majority of shareholders may waive it.[31] Similarly a fraud against third parties would not provide a ground for winding up under this clause.[32]

(f) *Losses.* Where the business of a company cannot be carried on except at a loss and its insolvency is inevitable, it is considered just and equitable to wind up the company.[33] But mere apprehension on the part of some shareholders that the company will not be able to earn profits cannot be a just and equitable ground for winding up by the court.

Similarly, the court rejected a petition for windnig up where the company was under losses but there was a chance for its making profits and the majority of shareholdes were against winding up.[34]

Petition for Winding Up

The application to the court for a compulsory winding up order is made by petition. The following persons can make a petition to the court to get an order for winding up a company:

(i) **Petition by the company.** The company can present a petition to the court for winding up where the shareholders have passed a special resolution to this effect. When the directors make a petition on behalf of the

[28]*Loch v. John Blackwood Ltd.* (1924) A.C. 783.

[29]*Re London and County Coal Co.* (1867) L.R. 3 Eq. 355

[30]*Universal Mutual Aid Ass. v. V. Thappa Naidu* A.I.R. 1933 Mad. 16.

[31]*Oriental Navigation Co. v. Bhanaram* A.I.R. 1922. Cal. 365.

[32]*Re Haven Gold Mining Co.,* (1882) 20 Ch. D. 151.

[33]*Re Mohamandlal Shastra Prakashak Samiti Ltd.,* (1917) 15 All. L.J. 193.

[34]*Pothen v. Hindustan: Trading Corporation (Pvt.) Ltd.,* (1966) 2 Comp. L.J. 252.

company, it must have behind it the wishes of the general body of shareholders. Thus the managing director of a company could not present a petition without the sanction of a general meeting.[35] Petition by a company is rare as the shareholders generally go for voluntary winding up, which is far speedier and cheaper than compulsory winding up. [Sec. 439 (1) (a)]

(ii) **Creditor's petition.** The petition may be presented to the court bya creditor or creditors. The term creditor includes (a) secured creditor, (b) debenture holder, and (c) trustee for the debenture holders. [Sec. 439 (2)]

Even a contingent or prospective creditor is entitled to present a petition to the court provided the leave of the court has been obtained. The court will not grant leave unless it is satisfied that there is a *prima facia* case for winding up a company and reasonable security for costs has been given. [Sec. 439 (8)]

Failure or inability to pay income tax dues is sufficient to entitle the Government to apply for and obtain an order for compulsory winding up.[36] A creditor whose debt is *bona fide* disputed by the company is not entitled to present a winding up petition.[37] But a judgment creditor has a right to a winding up order even though the company has a disputed claim for a larger sum against him.[38]

(iii) **Contributory's petition.** The term "contributory' means every person liable to contribute to the assets of he company in the event of its being wound up and includes the holder of any shares which are fully paid up (Sec. 428). A contributory shall be entitled to present a petition for winding up a company, even though he may be a holder of fully paid up shares or that the company may have no assets at all or may have no surplus assets left for distribution among the shareholders after satisfaction of the liabilities. [Sc. 439(3)]

Grounds for presenting petition. If the ground for winding up a petition is reduction in membership below the statutory minimum, any contributory may present a petition for winding up. If the petition for winding up is on any other ground, the contributory must satisfy one of the following conditions: (a) the shares were originally allotted to him; or (b) they have been held by him and registered in his name for at least six months during the eighteen months immediately before the commencement of winding up; or (c) they have devolved on him through the death of a former holder. [Sec. 439(4)]

Court's discretion. It is at the discrction of the court to make an order

[35]*Re Patiala Banaspati Co.*, A.I.R. (1953) Pepsu. 195.

[36]*Combatore Transport Co. Ltd. v. G.G. in Council* (1948) 1 Mad. L.J. 407.

[37]*Re Gold Mines Co.* (1883) 23 Ch. D. 210.

[38]*Re Douglas Griggs Engineering Co.*, (1963) Ch. 19.

for winding up on a contributory's petition. Before making such an order it may also consider the wishes of other contributories and creditors and for this purpose meetings of creditors and contributories may be held. [Sec. 557(1)]

(iv) **Registrar's petition.** The Registrar shall be entitled to present a petition to the court for winding up on the following grounds:

(a) if default is made in delivering the statutory report to the Registrar or in holding the statutory meeting;

(b) If the company does not commence its business within a year of its incorporation or suspends its business for a whole year;

(c) if the number of members is reduced, in the case of a public company, below seven, and in the case of private company, below two;

(d) if the company is unable to pay its debts: and

(e) if the court is of the opinion that it is just and equitable that the company be wound up.

However, the Registrar shall not make a petition on the ground that the company is unable to pay debts, unless it appears to him either from the financial condition of the company as disclosed in its balance sheet or from the report of a special auditor appointed under Section 233 A or an inspector appointed under Section 235 or 237, that the company is unable to pay is debts.

Prior sanction of the Central Government. Further, the Registrar shall obtain the previous sanction of the Central Government to the presentation of the petition on any of the grounds aforesaid. [Sec. 439(5)]

The Central Government shall not accord its sanction unless the company has been afforded an opportunity of making its representations, if any. [Sec. 439 (6)]

(v) **Petition by any person authorised by the Central Government in that behalf.** The Central Government may authorise any person to present a petition for winding up where it appears to it from the report of the inspector appointed to investigate the affairs of a company under Section 235 that (a) the business of the company is being conducted with intent to defraud its creditors, members or other persons or for fraudulent or unlawful purpose or in a manner oppressive of any of its members or that the company was formed for any fraudulent or unlawful purpose; or (b) the persons concerned in the formation of the company or the mangement of its affairs have been guilty of fraud, misfeasance or misconduct towards the company or towards any of its members. (Sec. 243)

The petition shall be presented on the ground that it is just and equitable that the company should be wound up. [Sec, 439 (1)(f)]

Petition where company is being wound up voluntarily or subject to court's supervision. Where a company is being wound up voluntarily or

subject to the surpervision of the court, a petition for winding up by the court may be presented by (a) any of the above persons or (b) the Official Liquidator. The court shall not make a winding up order on the above petition unless it is satisfied that the voluntary winding up or winding up subject to the supervision of the court cannot be continued with due regard to the interests of the creditors or contributories or both. (Sec. 440)

Commencement of Winding up

The winding up of a company by the court shall be deemed to commence at the time of the presentation of the petition for the winding up. Where, before the presentation of a petition for winding up a company by the court, a resolution has been passed by the company for voluntary winding up, the winding up of the company shall be deemed to have commenced at the time of passing the resolution and all proceedings taken in the voluntary winding up shall be deemed to have been validly taken unless the court directs otherwise. (Secc. 441)

It may be noted here that voluntary winding up shall be deemed to commence at the time when the resolution for voluntary winding up is passed. (Sec. 486)

Consequences of a Winding Up Order

(1) *Intimation of winding up order.* Where the court makes an order for winding up a company, it shall cause its intimation to be sent to the Official Liquidator and the Registrar. (Sec. 444)

(2) *Filing a copy of winding up order with the Registrar.* On the making of a winding up order, it shall be the duty of the petitioner and the company to file with the Registrar a certified copy of the order within thirty days of the date of making the order. [Sec. 445(1)]

(3) *Notification of order in Official Gazette.* On the filing of a certified copy of the winding up order, the Registrar shall make a minute of the order in his books relating to the company and shall notify in the Official Gazette that such an order has been made. [Sec. 445(3)]

(4) *Winding up order deemed to be notice of discharge.* Such an order shall be deemed to be a notice of discharge to the officers and employess of the company except when the business of the company is continued. [Sec. 445(3)]

It was held that a company is not continuing the business when the business is carried on by the liquidator for the beneficial winding up of the company.[39]

[39]*Palai Central Bank Employees Union. v. Official Liquidator* (1965) 2 Comp. L.J. 110.

(5) *Suits stayed on winding up order.* When a winding up order has been made or the Official Liquidator has been appointed as a provisional liquidator, no suit or other legal proceeding shall be commenced except by the level of he court. If a suit or proceedings is pending at the date of the winding up order, it shall not be proceeded with against the company except by the leave of the court and subject to such terms as the court may impose. If any suit or procceeding is pending in any court, that may be transferred to and disposed of by the winding up court, except any proceeding pending in appeal before the Supreme Court or a High Court. (Sec. 446)

Since a secured creditor is outside the winding up, he can realise his security without the leave of the winding up court.[40]

(6) *Order to favour creditors and contributories.* An order for winding up a company shall operate in favour of all the creditors and all the contributories of the company as if it had been made on all the joint petitions of a creditor and contributory. (Sec. 447)

(7) *Official Liquidator to be liquidator.* On a winding up order being made in respect of a company, the Official Liquidator shall, by virtue of his office, become the liquidator of the company. (Sec. 449)

(8) *Board's powers to come to an end.* The powers of the board of directors come to an end and they shall now be exercisable by the Official Liquidator.

Liquidators in Winding Up by a Court Order

Official liquidator. For the winding up of companies by the court, there shall be attached to each High Court an Official Liquidator appointed by the Central Government. The Official Liquidator may be a full-time or part-time officer depending upon the volume of work. Similarly the official receiver attached to a district court for insolvency purposes or any prson appointed by the Central Government will act as an official liquidator. (Sec. 448)

It may be noted here that only an official liquidator can act as a liquidator in a winding up by the court. (Sec. 449)

Provisional liquidator. At any time after the presentation of a winding up petition and before the making of a winding up order, the court may appoint the official liquidator to be a liquidator provisionally. Before making such an appointment, the court should give reasonable opportunity to the company to make its representation. The provisional liquidator shall have the same powers as a liquidator unless the court restricts his powers by any order. On a winding up order being made, the official

[40]*Maksudpur Refrigeration Industries, In re.* (1977) 47 Comp. Cas. 67.

liquidator shall cease to be a provisional liquidator and shall become the liquidator. (Sec. 450)

The liquidator shall conduct the proceedings in winding up the company and perform such duties as the court may impose. The acts of a liquidator shall be valid not withstanding any defect that may afterwards be discovered in his appointment or qualification. (Sec. 451)

A liquidator shall be described by the style of "The Officla Liquidator" of the particular company in respect of which he acts and not by his individual name. (Sec. 452)

Statement of Affairs to be made to the Official Liquidator

Within twenty-one days of the date of the order of winding up or the appointment of the official liquidator as provisional liquidator, there shall be made out and submitted to the Official Liquidator a statement as to the affairs of the company in the prescribed form and verified by an affidavit.

Contents. The statement shall contain the following particualrs:

(i) the assets of the company, stating separately the cash balance in hand and at the bank and the negotiable securities;

(ii) its debts and liabilities;

(iii) the names, residences and occupations of its creditors, stating separately the amount of the secured and unsecured debts; and in case of secured debts, particulars of securities given, their values and the dates on which they were given;

(iv) the debts due to the company and the names, residences and occupations of the persons from whom they are due and the amount likely to be realised: and

(v) such further information as the Official Liquidator may require.

Extension of time. The court or the Official Liquidator has the power to extend the period of twenty-one days for the submission of the statement to a maximum period of three months.

Persons liable to submit the statement. The statement has to be submitted and verified by one or more of the persons who were directors, manager, secretary or other chief officer of the company on the date of appointment of Official Liquidator and in case where no such appointment was made, on the day the winding up order was made.

Expenses. The expenses considered reasonable by the Official Liquidator shall be paid to any person making the aforesaid statment and affidavit.

Inspection. The statement is open to inspection by creditors and contributories on payment of a prescribed fee. (Sec. 454)

The above provisions are intended to facilitate the work of the

liquidator and to put in his possession the important facts relating to the company.

Duties of the Official Liquidator

To conduct proceeding in winding up. The liquidator shall conduct the proceedings in winding up of the company and perform such duties as the court may impose. The acts of a liquidator shall be valid notwithstanding any defect that may afterwards be discovered in his appointment or qualification. (Sec. 451)

To make a report. As soon as practicable after receiving a statement of affairs but not later than six months from the date of the orders, the Official Liquidator shall submit a preliminary report to the court showing: (a) the amount of capital issued, subscribed and paid up and the estimated amount of assets and liabilities; (b) if the company has failed, the causes of the failure; and (c) whether, in his opinion, further inquiry is desirable into any matter regarding the promotion, formation or failure of the company or the conduct of its business. (Sec. 455)

Custody of company's property. Where a winding up order has been made or where a provisional liquidator has been appointed, the liquidator or the provisional liquidator, as the case may be, shall take into his custody or under his control all the property, effects and actionable claims to which the company is entitled. For this purpose he may obtain the assistance of the Chief Presidency Magistrate or the District Magistrate. (Sec. 456).

The comply with the directions of the creditors or conributories or the commitee of inspection. The liquidator shall have regard to any directions which may be given by resolutions of the creditors or contributories at any general meeting or by the committee of inspection. In case of conflict, any direction given by the creditors or contributories at any general meeting shall be deemd to override any directions given by the committee of inspection. [Sec. 460(1,2)]

To summon meetings of creditors and contributories. The liquidator may summon general meeting of creditors or contributories for the purpose fo ascertaining their wishes. But he must summon such meetings at such times as the creditors or contributories may, by resolution, direct or whenever requested in writing to do so by not less than one tenth in value of the creditors or contributories. [Sec. 460 (3)]

Directions from the court. The liquidator shall use his own discretion in the administration of the assets of the company and in the distribution of such assets among the creditors but he shall always be working subject to the control of the court. The liquidator may apply to the court for any directions in relation to any particular matter arising in the winding up.

[Sec. 460 (4, 5)]

Books to be kept by liquidator. The liquidator shall keep proper books in which he shall cause entries or minutes to be made of proceeding at meetings and of such other matters as may be prescribed. Any creditor or contributory may inspect any such books, personally or through his agent subject to the control of the court. (Sec. 461)

Audit of liquidator's accounts. The liquidator shall present to the court, twice a year, an account of his receipts and payments in the prescribed from in duplicate. The court shall cause the account to be audited and one copy of the audited accounts shall be filed and kept by the court and the other copy shall be delivered to the Registrar for filing. Such a copy shall be open to the inspection of any creditor, contributory or persons interested. The liquidator shall have the audited account printed and a printed copy of the account shall be sent to every creditor and every contributory. (Sec. 462)

Central Government's control of liquidators. Section 463 requires liquidators to perform their duties faithfully and observe all the requirements imposed on them by this Act. If any complaint is made to the Central Government by any creditor or contributory against the liquidator, the Central Government shall inquire into the matter and take such action as it may think fit. (Sec. 462)

Information as to a pending winding up. If the winding up of a company is not concluded within one year of its commencement, the liquidator shall file a statement in the prescribed from the containing the prescribed particulars duly audited by a person qualified to act as an auditor of the company with respect to the progress of the liquidation. This statement must be filed within two months of the expiry of such a year and thereafter until the winding up is concluded. This statement is to be filed (a) in the case of winding up by or subject to the supervision of the court, in court; and (b) in the case of a voluntary winding up, with the Registrar. [Sec. 551 (1)]

A copy of such a statement shall be filed with the Registrar and shall be kept by him with the other records of the company. [Sec. 551 (2)]

Powers of the Liquidator

Section 457 defines the powers of a liquidator in a winding up by the court. These powers have been classified under two heads: (*a*) those powers which the liquidator can exercise only with the sanction of the court; and (*b*) those powers which the liquidator can exercise without the sanction of the court.

Powers exercisable with the sanction of court. The liquidator in a winding up by the court shall have the power, with the sanction of the

court:

(*i*) To institute or defend any suit, prosecution, or other legal proceeding, civil or criminal, in the name and on behalf of the company.

(*ii*) To carry on the business of the company so far as may be necessary for the beneficial winding up of the company.

It was held that a liquidator cannot carry on the company's business indefinitely, but he may carry it on over an extended period with a view to the steady and more profitable relisation of the company's assets. If the power is exercised *bona fide*, he will be protected even if he has made a mistake.[41]

(*iii*) To sell the immovable and movable property of the company by public auction or by private contract.

(*iv*) To raise money on the security of the assets of the company.

(*v*) To do all such other things as may be necessary for winding up the affairs of the company and distributing the assets.

(*vi*) To appoint an advocate, attorney or pleader entitled to appear before the court to assist him in the performance of the duties. (Sec. 459)

(*vii*) To pay any classes of creditors in full or to make any compromise or arrangement with the creditors. [Sec. 546(1)(b)]

(*viii*) To compromise any call or liability to call, debt and liability capable of resulting in a debt, and take any security for the discharge of any such call, debt, liability or claim and give a complete discharge in respect thereof. [Sec. 546(1)(b)]

Power exercisable without the sanction of court. The liquidators may exercise the following powers without the sanction of the court:

(*i*) Do all acts and execute all deeds, receipts and other documents in the name and on behalf of the company and use the company's seal.

(*ii*) Inspect the records and returns of the company on the files of the Registrar without payment of any fee.

(*iii*) Prove, rank and claim in the insolvency of any contributory for any balance against his estate and to receive dividends in the insolvency.

(*iv*) Draw, accept, make and endorse any bill of exchange, hundis and promissiory notes in the name of the company.

(*v*) Take out, in his official name, letters of administration to the estate of a deceased contributory and to do necessary things to obtain payment.

(*vi*) Appoint an agent to do any business which he is unable to do himself.

Control of court over acts of liquidator. It is to be noted that while exercising any of the above powers, the liquidator shall always be subject

[41]*Re Great Eastern Electric Co. Ltd.* (1941), Ch. 241.

to the control of the court and any creditor or contributory may apply to the court with respect to the exercise of any of the powers. (Sec. 457)

Discretion of liquidator. Section 458 lays down that the court, may by order, provide that the liquidator may exercise any of the powers which he can exercise with the sanction of the court without its sanction or intervention. But the exercise by the liquidator of such powers shall be subject to the control of the court.

Committee of Inspection

Appointment and composition of committee of inspection. The court may direct that there shall be appointed a committee of inspection to act with the liquidator. Within two months of the date of such direction, the liquidator shall convene a meeting of the directors of the company for the purpose of determining who will be the members of the committee. Within fourteen days of the creditors' meeting, the liquidator shall convene a meeting of the contributories to consider the decision of the creditors' meeting with or without modifications or to reject it. In case the contributories do not accept the creditors' decision in its entirety, the liquidator shall apply to the court for directions with regard to the composition of the committee. (Sec. 464)

Constitution and proceedings of committee of inspection. The committee of inspection shall not consist of more than twelve members. It shall have the right to inspect the accounts of the liquidator at all reasonable times. It shall meet at such times as it may from time to time appoint. The liquidator or any member of the committee may also call a meeting of the committee as and when he thinks necessary. The quorum for a meeting of the committee shall be one-third the total number of members or two, whichever is higher. The committee may act by a majority of its members present at a meeting.

A member of the committee may be removed at a meeting of creditors if he represents creditors or at meeting of contributories if he represents contributories, by an ordinary resolution of which seven days' notice has been given. The vacancy is filled at a meeting of the creditors or contributories, as the case may be. If the liquidator is of the opinion that is unnecessary for the vacancy to be filled, he may apply to the court and the court may order that the vacancy not be filled. (Sec. 465)

General Powers of the Court in Compulsory Winding Up

The court enjoys wide powers in relation to the compulsory winding up of a company. These powers are listed below:

Power of the Court to stay winding up. Even after making a winding up order, the court can stay all the proceedings in relation to the winding

up, either altogether or for a limited period and on such terms and conditions as it thinks fit. A copy of such an order shall be filed with the Registrar. The application for stay of proceedings in the winding up may be made by the liquidator or any creditor or contributory. (Sec. 466)

Power of the court to settle the list of contributories. The court shall have the powers to settle the list of contributories and shall cause the assets of company to be collected and applied in discharge of its liabilities. The court also has the power to rectify the register of members in all cases where rectification is required. (Sec. 467)

Power to require delivery of property to the liquidator. The court has the power to require any contributory, trustee, receiver, banker, agent, officer or other employee of the company to pay, deliver, surrender or transfer to the liquidator, any money, property or books and papers in his custody or under his control to which the company is *prima facie* entitled. (Sec. 468)

Power of the court to make calls. The court has the power to make calls on contributories, to the extent of their liability, to satisfy the debts and liabilities of the company, to meet the costs, charges and expenses of winding up, and for the adjustment of the rights of the contributories among themselves. (Sec. 470)

Power to order payment into bank of moneys due to the company. The court may order any person from whom money is due to the company to pay the money into the public account of India in the Reserve Bank of India instead of paying it to the liquidator (Sec. 471). All moneys or securities paid or delivered into the Reserve Bank of India in the course of winding up a company by the court, shall be subject to the orders of the court. (Sec. 472)

Power to exclude creditors not proving in time. The court may fix a time within which creditors are to prove their debts or claims and may exclude creditors not proving within the fixed time, from the benefit of any distribution made before those debts and claims are proved. (Sec. 474)

Power to adjust the rights of contributories. The court shall adjust rights of contributories among themselves and distribute any surplus among the persons entitled thereto. (Sec. 475)

Power to order costs. In the event of the assets being insufficient to satisfy the liabilities, the court may make an order for the payment out of the assets, of the costs and charges and expenses of the winding up proceedings. The priority as regards these payments *inter se* may be determind by the court. (Sec. 476)

Power to summon persons suspected of having the property of the company, etc. The court has the power to summon before it any officer

of the company or person known or suspected to have in his possession any property or books or papers of the company, or known or suspected to be indebted to the company or any person whom the court deems capable of giving information concerning the promotion, formation, trade, dealings, property, books or papers of the company. Any such person may be examined on oath and the court may obtain his answer in writing and require him to sign it. The court may require him to produce any books and papers in his custody, relating to the company. If he claims any lien on them, the production shall be without prejudice to that lien and the court shall have the power to decide the question. If he fails to appear before it, the court shall cause him to be apprehended and brought before it for examination. If, on examination, he admits that he is indebted to the company or has any property in his possession, the court may order him to pay the money or deliver the property to the liquidator. (Sec. 477)

Power to order public examination of promoters, directors, etc. Where the Official Liquidator has made a report to the court stating that in his opinion a fraud has been committed by any person in the promotion or formation of the company or by an officer of the company in relation to the company since its formation, the court may direct that that person or officer shall attend before the court and be publicly examined. The Official Liquidator shall take part in the examination. The court may put such questions to the person examined as it thinks fit. Such a person shall be examined on oath and notes of the examination shall be taken down in writing and read over and signed by the person examined. A statement so recorded may be used in evidence against the person examined and it shall be open to the inspection of any creditor or contributory at all reasonable times. (Sec. 478)

Power to arrest an absconding contributory. If at any time either before or after making a winding up order, the court believes that a contributory is about to quit India or otherwise abscond, or is about to remove or conceal any of his property, for the purpose of evading payment of calls or of avoiding examination in respect of the affairs of the company, the court may (*a*) cause the contributory to be arrested and (*b*) cause the books and papers and movable property to be seized and safely kept until such time as it may order. (Sec. 479)

Power to order the dissolution of the company. When the affairs of the company have been completely wound up or where the court is of the opinion that the liquidator cannot proceed with the winding up of a company for want of funds and assets or if it is just and reasonable to do so, the court shall order that the company be dissolved from the date of the order, and the company shall stand dissolved. A copy of the order

shall be forwarded to the liquidator by the Registrar within thirty days of the date of the order. (Sec. 481)

VOLUNTARY WINDING UP

Of all the forms of winding up a company, voluntary winding up is by far the most common and popular form. It is altogether different from compulsory winding up. In voluntary winding up, the company and its creditors are left free to settle their affairs without going to the court. The members and creditors of a company sit together and put an end to the difficulties and disputes which may have arisen in connection with the running of the company's business. However, Section 518 permits them to apply to the court for direction or order if and when necessary.

Section 484 provides for voluntary winding up of a company in the following two ways:

(*a*) **By ordinary resolution.** A company may be wound up voluntarily by passing an ordinary resolution when the period, if any, fixed for the duration of the company by the articles has expired or when the event has occurred on the occurrence of which the articles provide that the company is to be dissolved.

(*b*) **By special resolution.** In other cases a company may be wound up voluntarily at any time and for any reason if a special resolution has been passed to that effect in a general meeting of the company.

It is to be noted that where a winding up resolution is followed by other resolutions which are *ultra vires* or invalid, the former is not necessarily invalid.[42] An irregularity in passing the special resolution, like shorter notice, will not invalidate the resolution if all the shareholders agree to waive such irregularity.[43]

Publication of resolution. Within fourteen days of passing the resolution, the company shall give notice of it by advertisement in the Official Gazette and also in some newspaper circulating in the district where the registered office of the company is situated. (Sec. 485)

Commencement of Voluntary Winding up

A voluntary winding up shall be deemed to commence at the time when the resolution for such a winding up is passed. (Sec. 486)

Effects of Voluntary Winding up

(1) *Effect on status of company.* From the commencement of voluntary

[42]*Thomson v. Henderson's Transvall Estates* (1908) 1 Ch. 765.
[43]*Re Bailey, Hay & Co. Ltd.,* (1972) Comp. Cas. 442.

winding up, the company ceases to carry on its business except so far as may be required for the beneficial winding up of such a business. (Sec. 487)

(2) *Corporate powers to continue until dissolution.*. The corporate state and corporate powers of the company shall continue until it is dissolved. (Sec. 487)

(3) *Board's powers to cease on liquidator's appointment.* On the appointment of a liquidator, all the powers of the board of directors and of the managing or whole-time directors and manager shall cease except for the purpose of giving notice to the Registrar of the appointment of the liquidator. But the company in general meeting or the liquidator or the committee of inspection or the creditors in a creditors' voluntry winding up, may sanction the continuance of their powers. (Secs. 491 and 505)

(4) *Effect on company's employees.* The mere fact of voluntary winding up has been held not to operate as a dismissal of the company's employees, as does the winding up order of the court in case of compulsory winding up.[44] But a voluntary winding up coupled with a sale of the company's business was held to operate as a dismissal.[45]

(6) *Avoidance of transfer of shares.* In the case of voluntary winding up any transfer of shares in the company or any alteration in the status of the members of the company made after the commencement of the winding up, shall be void except when it is made with the sanction of the liquidator. (Sec. 536)

Kinds of Voluntary Winding up

Voluntary winding up of a company is of two kinds:

(*i*) members' voluntary winding up; and

(*ii*) creditors' voluntary winding up.

A voluntary winding up will be a members' voluntary winding up if a declaration of solvency has been made in accordance with the provisions of the Act. Every other voluntary winding up would be a creditors' voluntary winding up. It is rightly pointed out in *Palmer's Company law* that the test is not whether the company is solvent or not but whether the declaration of solvency has been made before the general meeting passed the resolution for winding up. If this has been overlooked, such a declaration cannot be made after that general meeting. In that case the voluntary winding up would technically be creditors' voluntary winding up though the company may be solvent.

[44]*Midland Countries District Bank v. Attwood* (1905) 1 Ch. 357.

[45]*Reigate v. Union Manufacturing Co.* (1918) 1 K.B. 592 (C.A.).

Members' Voluntary Winding up

To bring about a members' voluntary winding up the following conditions must be satisfied:

(*i*) **Declaration of solvency.** The declaration must be made by the directors or a majority of them (where they are more than two) at a meeting of the board and verified by an affidavit. They have to make a declaration to the effect that they have made full inquiry into the affairs of the company and that having done so they have formed the opinion that the company has no debts or that it will be able to pay its debts in full within a specified period not exceeding three years from the commencement of winding up. Such a declaration will not be effective unless (*a*) it is made within five weeks immediately before the date of the resolution for winding up and is delivered to the Registrar before that date; (*b*) it is accompanied by a copy of the report of the auditors on the profit and loss account and the balance sheet of the company; and (*c*) it embodies a statement of the company's assets and liabilities as at the latest practicable date before the making of the declaration.

Any director of a company making declaration under this section without having reasonable grounds for the opinion that the company will be able to pay its debts in full within the period specified in the declaration, shall be punishable with imprisonment for a term which may extend to six months or with a fine which may extend to five thousand rupees or with both. If the company fails to pay its debts within the period specified in the declaration, it is presumed that reasonable grounds for making the declaration did not exist.

(*ii*) **Shareholders' resolution.** After the above statutory declaration, the shareholders must meet and pass an ordinary resolution or a special resolution, as the case may be, for the winding up of the company.

Provisions Applicable to Members' Voluntary Winding Up

Sections 490 to 498 apply in relation to members' voluntary winding up and are as follows:

(*i*) **Appointment of a liquidator.** The company shall appoint one or more liquidators for the purpose of winding up the affairs and distributing the assets of the company in general meeting. It shall also fix the remuneration to be paid to the liquidator or liquidators which cannot be increased in any circumstances. The liquidator shall not take charge of his office unless the remuneration is fixed. (Sec. 490)

(*ii*) **Board's powers to case on appointment of a liquidator.** On appointment of the liquidator, all the powers of the board of directors and of the managing or whole-time directors and the manager shall cease, except if the company in general meeting or the liquidator sanction them

to continue. (Sec. 491)

(*iii*) **Power to fill a vacancy in the office of a liquidator.** If a vacancy occurs by death, resignation or otherwise in the office of any liquidator appointed by the company, the company in general meeting may fill the vacancy. For this purpose a general meeting may be convened by any contributory or contributories or by the continuing liquidator or liquidators, if any. (Sec. 492)

(*iv*) **Notice of appointment of liquidator to be given to the Registrar.** The company must give notice to the Registrar of the appointment of a liquidator or liquidators. It must also give notice of every vacancy occurring in the office of the liquidator and of the name of the liquidator or liquidators appointed to fill every such vacancy. This notice must be given within ten days of the event to which it relates. (Sec. 493)

(*v*) **Power of liquidator to accept shares, etc., as consideration for sale of company property.** The liquidator cannot accept shares, policies or other like interests in consideration of the sale of the whole or any part of the company's business or property to another company with the object to distribute proceeds among the members of the transferor company, unless a special resolution is passed to that effect. The dissenting members can abstain the liquidator from carrying in the resolution into effect unless his interest in purchased at a price to be determined by agreement or by arbitration. (Sec. 494)

(*vi*) **Duty of liquidator to call creditors' meeting in case of insolvency.** If the liquidator is, at any time, of the opinion that the company will not be able to pay debts in full within the period stated in the declaration of solvency or if that period has expired without the debts having been paid in full, he shall summon a meeting of creditors and lay before them a statement of the assets and liabilities of the company. Thereafter, the winding up shall proceed in the manner of a creditors' voluntary winding up. (Sec. 495)

(*vii*) **Duty of liquidator to call a general meeting at the end of each year.** Where the liquidation continues for more than year, the liquidator shall call a general meeting of the company at the end of the first year and at the end of each succeeding year, or as soon thereafter as may be convenient within three months from the end of the year. He shall lay before the meeting an account of his acts and dealing and the progress of the winding up during the year. (Sec. 496)

(*viii*) **Final meeting and dissolution.** As soon as the affairs of the company are fully wound up, the liquidator shall make up an account of winding up showing how the winding up has been conducted and the property of the company has been disposed of. He shall call a general meeting of the company for the purpose of laying the account before it

and giving any explanation thereof. The meeting is to be called by advertisement in the Official Gazette and a local newspaper specifying the time, place and object of the meeting. Within a week of the meeting the liquidator sends a copy of the accounts and a return of the meeting to the Registrar and the Official Liquidator. If a quorum is not present at the meeting so called, he shall make a return that the meeting was duly called and that no quorum was present thereat.

The Registrar, on receiving the account and the return, shall register them. The Official Liquidator, on receiving the account and the return, shall make an scrutiny of the books and papers of the company and report to the court the result of his scrutiny. If the Official Liquidator makes a report to the court that the affairs of the company have not been conducted in a manner prejudicial to the interests of its members or to the public interest, then from the date of submission of the report to the court, the company shall be deemed to be dissolved.

If the report points out that the affairs were conducted in a manner prejudicial to the interests of members or to the public interest, the court shall direct the Official Liquidator to make further investigations of the affairs of the company. On receipt of the report of the Official Liquidator on such further investigation, the court may either make an order that the company shall stand dissolved with effect from the date specified in the order or make such other order as the circumstances of the case brought out in the report permit. (Sec. 497)

(*ix*) **Alternative provisions as to annual and final meeting in case of insolvency.** If in case of members' voluntary winding up, the liquidator finds that the company is insolvent, he shall also call a meeting of the creditors in addition to the meeting of the members at the end of every year and as soon as the affairs of the company are fully wound up. The winding up, thereafter, would proceed as if it were a creditors' voluntary winding up and not a members' members' voluntary winding up. (Sec. 498)

Creditors' Voluntary Winding Up

If the directors make no declaration of solvency before the members pass a winding up resolution, the winding up will be a creditors' voluntary winding up. The mode of a creditors' voluntary winding up is resorted to by insolvent companies. Since an insolvent company is unable to pay its debts in full, the law gives the creditors of the company a place of pride under this mode of winding up. The creditors have dominating control over the winding up proceedings.

Provisions Applicable to Creditors' Voluntary Winding Up

Sections 500 to 509 shall apply in relation to a creditors' voluntary winding up. These provide for:

(*i*) **Meeting of creditors.** The company shall call a meeting of the creditors either on the same day or the day next to the day when the resolution for voluntary winding up is passed. The notices of the meeting of creditors shall be posted to the creditors simultaneously with the notices of the meeting of the company. The notice of the meeting must also be advertised in the Official Gazette and in two newspapers, circulating in the district where the registered office or the company's principal place of business is situated. The board of directors will lay before the meeting a full statement of the position of the company's affairs and a list of creditors of the company and the estimated amounts of their claims. The creditors' meeting will be presided over by one of the directors appointed for the purpose by the board. (Sec. 500)

(*ii*) **Notice of resolution passed by a creditors' meeting to be given to the Registrar.** Notice of any resolution passed at a creditors' meeting must be given by the company to the Registrar within ten days of the passing thereof. (Sec. 501)

(*iii*) **Appointment of liquidator.** The creditors and the company at their respective meetings may nominate a liquidator for the purpose of winding up the affairs of the company and distributing its assets. But if the creditors and the company nominate different persons, the creditors' nominee will be the liquidator. But any director, member or creditor may apply to the court for an order that the company's nominee or official liquidator or some other person be appointed. This can be done within seven days of the date on which the nomination was made by the creditors. If no person is nominated by the creditors, the person nominated by the company shall be the liquidator. If no person is nominated by the company, the person nominated by the creditors shall be the liquidator. (Sec. 502)

(*iv*) **Appointment of a committee of inspection.** The creditors at the same meeting or at any subsequent meeting many appoint a committee of inspection consisting of not more than five persons. If such a committee is appointed, the company may appoint such number of person (not exceeding five) as they think fit to act as members of the committee. If the creditors do not accept the company's nominees, the matter may be referred to the court. The court's decision will be final in this respect. The powers of the committee of inspection are more or less the same as those of a committee of inspection appointed in a compulsory winding up under Section 465. (Sec. 503)

(*v*) **Fixing of liquidator's remuneration.** The committee of inspection,

or if there is no such committee of inspection, the creditors, may fix the remuneration to be paid to the liquidator or liqudators. Where the remuneration is not so fixed it shall be determined by the court. The remuneration once fixed cannot be increased in any circumstances. (Sec. 504)

(*vi*) **Board's powers to cease on appointment of a liquidator.** On the appointment of a liquidator, all the powers of the board of directors shall cease. However, the committee of inspection or the creditors in general meeting may sanction the board's powers to continue. (Sec. 505)

(*vii*) **Power to fill a vacancy in the office of a liquidator.** If a vacancy occurs by death, resignation or otherwise in the office of a liquidator (other than a liquidator appointed by, or by direction of the court) the creditors in general meeting may fill the vacancy. (Sec. 506)

(*viii*) **Power of liquidators to accept shares etc., as consideration for sale of company property.** The liquidator cannot accept shares, policies or other like interests in consideration of the sale of the whole or any part of a company's business or property for distribution amongst the creditors of the company without prior consent of the court or committe of inspection. (Sec. 507)

(*ix*) **Duty of a liquidator to call meeting of the company and creditors at the end of each year.** Where liquidation continues for more than a year, the liquidator shall call a general meeting of the company and a meeting of the creditors at the end of the first year and at the end of each succeeding year. He shall lay before the meetings an account of his acts and dealings and the progress of the winding up during the year. (Sec. 508)

(*x*) **Final meeting and dissolution.** The provisions regarding the final meeting and dissolution are the same as in the case of a members' voluntary winding up under Section 497. The provisions of Section 497 have already been discussed. The only difference here is that the liquidator shall have to call a meeting of the creditors in addition to a meeting of members. (Sec. 509)

Difference between Members' Voluntary Winding Up and Creditors' Winding Up

(1) In the case of a members' winding up the directors file a "Declaration of Solvency" with the Registrar which states that the company has no debts or that it will be able to pay its debts in full. In the case of a creditors' voluntary winding up, no such declaration is filed with the Registrar. In fact, the creditors' voluntary winding up is resorted to by insolvent companies which are unable to meet their liabilities in full.

(2) In the case of a members' voluntary winding up, there is no

meeting of creditors. Only a meeting of members is called to pass an ordinary or special resolution requiring the company to be wound up. In the case of a creditors' voluntary winding up, the company shall call a meeting of creditors either on the same day or the day next to the day when the company passes a resolution for voluntary winding up.

(3) There is no committee of inspection in a members' voluntary winding up, whereas in a creditors' voluntary up the creditors may appoint a committee of inspection.

(4) In a members' voluntary winding up, the members have dominating control over the winding up proceedings and the creditors do not participate directly, as the company is deemed to be solvent. In the case of a creditors' voluntary winding up, the creditors have dominating control over winding up proceeding as the company is deemed to be insolvent.

(5) In a members' voluntary winding up, the members appoint the liquidator in general meeting. In a creditors' voluntary winding up the liquidator is appointed in a different way. If the members and creditors nominate two different persons as liquidators, the creditors' nominee shall become the liquidator. If no person is nominated by the company, the person nominated by the creditors will be the liquidator. However, if no person is nominated by the creditors, the person nominated by the company shall be the liquidator.

(6) In a members' voluntary winding up, the liquidator can exercise some of his powers with the sanction of a special resolution of the company. In a creditors' voluntary winding up he can do so with the sanction of the court or the committee of inspection or of meeting of creditors.

Powers and Duties of the Liquidator in Voluntary Winding Up

Powers exercisable with sanction. Section 512 lays down the powers and duties of liquidators in voluntary winding up. These powers are just the same as those of the Official Liquidators in a winding up by the court. There is, however, one difference regarding the mode in which these powers are to be exercised. In the case of winding up by the court, the Official Liquidator has to obtain the sanction of the court to exercise certain powers. But in the case of members' voluntary winding up, the liquidators can exercise those powers with the sanction of a special resolution of the company. In the case of creditors' voluntary winding up, the liquidator shall have to obtain the sanction of the court or the committee of inspection or the meeting of the creditors if there is no committee of inspection.

In the exercise of the above powers, the liquidator shall be subject to

the control of the court, and any creditor or contributory may apply to the court with respect to any exercise or proposed exercise of any of the above powers.

Section 546 lays down certain powers which the liquidator in voluntary winding up can exercise with the sanction of a special resolution of the company and subject to the control of the court. There are:

(i) to pay any class of creditors in full;

(ii) to make any compromise or arrangement with creditors or persons claiming to be creditors; and

(iii) to compromise any call, or liability to call, debt and liability ca[illegible] resulting in a c[illegible]d any claim with c[illegible]tories or debtors of the company and take any security for the discharge in respect thereof.

Powers exercisable without sanction. The liquidator may exercise all the powers, that the liquidator in a compulsory winding up by the court may exercise under Section 457(2), without any sanction thereto.

In addition to the above powers, the liquidator can, without obtaining the sanction, exercise (a) the power of the court for settling a list of contributories; (b) the power of the court for making calls; and (c) the power of calling general meetings of the company for the purpose of obtaining the sanction of the company by ordinary or special resolution.

Joint Liquidators. Where several liquidators are appointed, any powers given by this Act may be exercised by such one or more of them as may be determined at the time of their appointment. In default of such determination, any power exercisable by them should be exercised by at least two of them. [Sec. 512(4)]

Where one of several liquidators accepted a bill of exchange without the authority of others, it was held that the company was not liable.[46]

Power to apply to court to have questions determined. The liquidator or any contributory or creditor may apply to the court to determine any question arising in the winding up of the company or to exercise all or any of the powers which the court may exercise if the company were being wound up by it. The court may make such order as it thinks just. (Sec. 518)

Public examination of promoters directors, etc. The liquidator may make a report to the court stating that in his opinion a fraud has been committed by any person in the promotion or formation of the company or by any officer of the company in relation to the company since its formation and the court may, after considering the report, direct that the person or officer shall appear for public examination. (Sec. 519)

[46]*Bolognesi's Case* (1870) 5 Ch. App. 567.

Duties of liquidator. Section 512(3) prescribes a duty on the liquidator that he shall pay the debts of the company and shall adjust the rights of the contributories among themselves.

Every liquidator in voluntary winding up shall pay the moneys received by him in his capacity as such into scheduled bank to the credit of special banking account opened by him in that behalf and called the Liquidation Account of the Company.

However, the court may allow a liquidator to maintain the account in a bank other than a scheduled bank if it deems it fit. If any such liquidator retains for more than ten days, a sum exceeding five hundered rupees or such other sum as the court may authorise him to retain, then, unless he explains the retention to the satisfaction of the court, he shall be liable to pay interest on the amount so retained in excees at twelve per cent per annum. He may also be required to pay such penalty as may be determined by the Registrar. He may even be removed from his office by the court. (Sec. 553)

WINDING UP SUBJECT TO SUPERVISION OF THE COURT

At any time after a company has passed a resolution for voluntary winding up, the court may make an order that the voluntary winding up shall continue but subject to such supervision of the court as the court thinks just. Further, the court may give such liberty to creditors, contributories or others to apply to the court as it thinks just. (Sec. 522)

The object of the supervision order is to protect the interests of the memebrs, creditors and the company. Such an order is passed by the court when there are irregularities or fraud in the voluntary winding up.

The effect of a petition for the continuance of voluntary winding up subject to the supervision of the court is that the court obtains jurisdiction over suits and legal proceedings as in the case of a petition for winding up by the court. (Secc. 523)

Power of Court to Appoint or Remove Liquidators

The court may also appoint an additional liquidator or liquidators. It may remove any liquidator so appointed or any liquidator continued under the supervision order and fill any vacancy occasioned by a removal, by death or by resignation. The court may appoint an official liquidator as a liquidator or to fill any vacancy caused by the removal of the previously appointed liquidator. The court may also appoint or remove a liquidator on an appliction of the Registrar in this behalf. (Sec. 524)

The liquidator appointed by the court shall have the same powers, be

subject to the same obligations and in all respects stand in the same position as if he had been appointed in accordance with the provisions of the Act relating to the appointment of liquidators in a voluntary winding up. (Sec. 525)

Effect of a Supervision Order

In supervisory winding up, the liquidator shall have the same powers as in a voluntary winding up, subject however to any restrictions the court may impose. The court can exercise all powers which it might have exercised if an order had been made for the compulsory winding up of the company by the court. (Sec. 526)

The court is empowered to pass an order for compulsory winding up in case of need, superseeding the supervisory winding up and the court may appoint any of the liquidators then acting as a liquidator in the winding up by the court. But such a liquidator will act in addition to and subject to the control of the Official Liquidator. (Sec. 527)

Conduct of Winding

The Act provides for three types of winding up: (a) compulsory winding up by order of he court; (b) voluntary winding up; and (c) voluntary winding up subject to the supervision of the court.

We have already discussed special provisions of the Act relating to each of the above three types of winding up. However, the Act also provides certain provisions which are applicable to every type of winding up. We shall now discuss provisions which are more or less uniform in their application irrespective of the mode of winding up.

Contributories

Meaning. On the commencement of winding up, the members of the company are known as contributories. Acccording to Section 428, the term "contributory" means every person liable to contribute to the asets of a company in the event of its being wound up, and includes the holder of any shares which are fully paid up.

A holder of fully paid up shares is to be put on the list of contributories not because he has to contribute anything to the assets of the company but in case there is anything to come to him.[47]

Persons Liable as Contributories

The following persons are liable as contributories:

(1) **Liability as contributories of present and past members.** In the

[47]*Re Aidall Ltd.* (1933) 1 Ch. 323.

event of a company being wound up, every present and past member shall be liable to contribute to the assets of the company to an amount sufficient for payment of its debts and liabilities and the cost, charges and expenses of the winding up and for the adjustment of the rights of he contributories among themselves. [Sec. 426(1)]

A list of contributories is made out in two parts, A and B. List A includes the names of present members of the company whose names appear on the register of members on the commencement of winding up of the company. List B includes the names of past memebrs of the company who have ceased to be members within a year preceding the winding up.

The liability of a present member (List A contributory) is as follows:

(i) in case of a company limited by shares, no contribution shall be required from him exceeding the amount remaining unpaid on the shares held by him; [Sec. 426(1)(d)]

(ii) in case of a company limited by guarantee, no contribution shall be required from him exceeding the amount undertaken to be contributed by him to the assets of the company in the event of its being wound up; [Sec. 426(1)(e)] and

(iii) in the event of the winding up of a company limited by guarantee which has a share capital every member of the company shall be liable to contribute to the extent that he guaranteed plus any sums unpaid on the shares held by him as if the company were a company limited by shares. [Sec. 426(2)]

The liability of a past member is as follows:

(i) a past member shall not be liable to contribute if he has ceased to be a member for one year or upwards before the commencement of the winding up; [Sec. 426(1)(a)]

(ii) a past member shall not be liable to contribute in respect of any debt or liability of the company contracted after he ceased to be a member; [Sec. 426(1)(b)] and

(iii) no past member shall be liable to contribute unless it appears to the court that the present members are unable to satisfy the contributions required to be made by them. [Sec. 426(1)(c)]

The extent of liability of a past member is the same as that of present members discussed above.

(2) **Obligations of directors and managers whose liability is unlimited.** Section 322 states that by virtue of the provisions of the memorandum of association of a company, the liability of any of its directors or manager may be made unlimited though the liability of members is limited. It is further provided in Section 427 that any of such directors or manager shall be liable, in the event of winding up of the company, in addition to

his liability as a shareholder, to make further contribution as if he were a memebr of an unlimited company. Both present and past officers of the company shall be liable under the above provisions. But a past director or manager is not liable:

(i) if he has ceased to hold office for a year or upwards before the commencement of the winding up;

(ii) if the debt or liability was incurred after he ceased to hold office; and

(iii) if the court does not deem it necessary to require further contribution. (Sec. 427)

(3) **Legal representative in case of a member's death.** If a contributory dies, his legal representatives shall be liable to contribute to the assets of the company in discharge of his liability, and shall be contributories accordingly. (Sec. 430)

The liability of the legal representative of a deceased contributory is limited to the value of estate coming into his hands.[48]

(4) **Official assignee or receiver in case of a member's insolvency.** If a contributory is adjudged insolvent, his assignees in insolvency shall represent him for all the purposes of the winding up and shall be contributories accordingly. (Sec. 431)

(5) **Liquidator of a body corporate which is a member.** If a body corporate, which is a contributory is ordered to be wound up, its liquidator shall be the contributory. (Sec. 432)

(6) **Any other person whom the court may so direct in case of fraudulent conduct of business.** If in a winding up it appears that any business of the company has been carried on with intent to defraud creditors of the company or any persons or for any fraudulent purpose, the court may declare that any persons who were knowingly parties to such business shall be personally liable for all or any of the debts of the company. The application may be made by the Official Liquidator, the liquidator, or any creditor or contributory the company. (Sec. 542)

Nature of the Contributory's Liability

Section 429 specifies the nature of the liability of a contributory. The liability of a contributory is in the nature of a debt but it does not become payable until a call is made. Thus the liability of a contributory, though commencing at the date of winding up, is only contingent, until a call is made. This section gives to the liquidator a new cause of action which a company itself might not have. For example, if the claim of the company for the realisation of any call from a member is barred by limitation, such

[48]*Re Bayswater Trading Co. Ltd.*, (1970) 1 A.E.R. 608.

a member becomes liable to pay all that has remained unpaid on his shares including the unpaid call when the company goes into liquidation.[49]

The liability of the contributory is not ex-contractu but ex-lege. This means that his liability does not arise by virtue of his contract to take shares from the company. Rather it arises by reason of the fact that his name appears ont he register of members of the company. The liability of the contributory is a statutory liability arising after winding up has started. It was held that it is no answer to a liquidator's claim against any person whose name appears on the register as member, that there was an agreement with the directors to exclude this statutory liability.[50]

Similarly, after a winding up order is made it is not open to a person whose names appears on the register of members, to object to his name being placed on the list of contributories on the ground that allotment to him was void.[51]

At the same time, a shareholder who has purchased shares from the company on the basis of a false and misleading prospectus can aviod his liability before the company has gone into liquidation. He cannot aviod his liability if the company goes into liquidation because upon the commencement of liquidation, the rescission of the contract and repayment of money to the subscriber would injure the creditors by decreasing the assets available for payment of their debts.[52]

Section 71 lays down that an irregular allotment shall be viodable at the option of the allottee within two months of the statutory meeting or within two months of the allotment where no statutory meeting is to be held. Such an allotment is viodable even if the company is in the course of winding up within the time specified. This means that a contributory can aviod his liability if he acts within the prescribed time even if company is in the course of winding up.

If the shares of a person have been forfeited for non-payemnt of calls more than a year before the commencement of the winding up, he shall be liable for the call amount with interest as a debtor of the company for which the company can file a suit. But he cannot be placed on the list of contributories.[53]

Contributory's right to set-off. The court make an order on any contributory to pay any money due to the company from him. The sum payable

[49]*Jagannath Prasad v. U.P. Flour Mills Co. Ltd.* 38 All. 347.
[50]*Geoffrey Cornwallis v. Sikdar Iron Works Ltd.* 59 Cal. 1099.
[51]*Laxmi Reddi v. Official Receiver* A.I.R. 1951 Mad. 890.
[52]*Oakes v. Turquand* (1867) L.R. 2 H.L. 325.
[53]*Ladies Dress Association v. Pulbrok* (1900) 2 Q.B. 376.

must be exclusive of any money payable by the contributory as a shareholder. [Sec. 469(1)]

In an unlimited company, the court may allow to the contributory, by way of set off, any money due to him on an independent dealing or contract with the company. But no set off will be allowed for any money due to him as a member of the company in respect of any dividend or profit. [Sec. 469(2)(a)]

In the case of limited company, the court may given the above allowance to any director or manager whose liability is unlimited. [Sec. 469(2)(b)]

In the case of any company, whether limited or unlimited, when all the creditors have been paid in full, any money due on any account to a contributory from the company may be allowed to him by way of set-off against any subsequent call. [Sec. 469(3)]

Payment of Liabilities

The liquidator is appointed to realise the assets of the company and pay off its liabilities. Where a solvent company is being wound up, all debts payable on a contingency and all claims against the company shall be admissible as proof against the company. A just estimate will be made of the value of such debts or claims as may be subject to any contingency, or for some other reasons may not bear a certain value. (Sec. 528)

Thus, where a solvent company is being wound up, all obligations, of the company, when proved, will be met in full and the surplus will be distributed among the contributories.

Where the company in liquidation is insolvent, the smae insolvency rules (as applicable to persons adjudged insolvent) shall apply with regard to (a) debts provables; (b) the valuation of annuities and future and contingent liabilities; (c) the respective rights of secured and unsecured creditors. [Sec. 529(1)]

Workmen's dues equated with those of secured creditors. In order to protect the interests of workmen in the event of winding the company, the dues of workmen have been equated with those of secured creditors by the Companies (Amendment) Act of 1985. It is provided that the security of every secured creditor shall be subject to a *pari passu* charge in favour of workmen. Where a secured creditor instead of relinquishing his security and proving his debts, opts to realise security:

(a) the liquidator shall be entitled to represent the workmen and enforce such charge;

(b) any amount realised by the liquidator by way of enforcement of such charge shall be applied rateably for the discharge of workmen's dues; and

(c) so much of the debt due to such secured creditor as could not be realised by him virtue of the foregoing provisions of this proviso or the amount of the workmen's portion in his security, whichever is less, shall rank pari passu with the workmen's dues for the purposes of Section 529A. [Proviso to Section 529(1)]

All persons who in any such case would be entitled to prove for and received dividends out of the assets of the company, may come in under the winding up, and make such claims against the company as they respectively are entitled to make by virtue of this section. [Sec. 529(2)]

It is further provided that if a secured creditor instead of relinquishing his security and proving his debt proceeds to realise his security he shall be liable to pay his portion of the expenses incurred by the liquidator (including a provisional liquidator, if any) for the preservation of the security before its realisation by the secured creditor.

For the purposes of this provision, the portion of expenses incurred by the liquidator for the preservation of a security which the secured creditor shal be liable to pay shall be the whole of the expenses less an amount which bears to such expenses the same proportion as the workmen's portion in realition to the security bears to the value of the security. [Proviso to Section 529(2)]

A secured creditor, part of whose debt is preferential and who realises his security for less than the amount owing to him, may appropriate the proceeds of sale to that part of debt which is non-preferential, thus leaving his preferential claim outstanding.[54]

For the purposes of Section 529, Section 529A and Section 530:--

(a) "workmen", in relation to a company, means the employees of the company, being workmen within the meaning of the Industrial Disputes Act, 1947;

(b) "workmen's dues", in relation to a company, means the aggregate of the following sums due from the company to its workmen, namely:

(i) all wages or salary including wages payable for time or piece work and salary earned wholly or in part by way of commission of any workman, in respect of services rendered to the company and any compensation payable to any workman under any of the provisions of the Industrial Disputes Act, 1947;

(ii) all accrued holiday remuneration becoming payable to any workman, or in the case of his dealt to any other person in his right, on the termination of his employment before, or by the effect of, the winding up order or resolution;

(iii) unless the company is being wound up voluntarily merely for the

[54]*Re Willian Hall (Contractors)* (1976) 2 All. E.R. 1150.

purposes of reconstructin or of amalgamation with another company, or unless the company has, at the commencemnt of the winding up, under such a contract with insurers as is mentioned in Section 14 of the Workmen's Compensation Act, 1923, rights capable of being transferred to and vested in the workman, all amounts due in respect of any compensation or liability for compensation under the said Act in respect of the death or disablement of any workman of the company;

(iv) all sums due to any workman from a provident fund, a pension fund, a gratuity fund or any other fund for the welfare of the workmen, maintained by the company;

(c) "workmen's portion", in relation to the security of any secured creditor of a company, means the amount which bears to the value of the security the same proportion as the amount of the workmen's dues bears to the aggregate of:

(i) the amount of workmen's dues; and

(ii) the amounts of the debts due to the secured creditors.

Illustration. The value of the security of a secured creditor of a company is Rs 1,00,000. The total amount of the workmen's dues is Rs 1,00,000. The aount of the debts due from the company to its secured creditors is Rs 3,00,000. The aggregate of the amount of workmen's dues and of the amounts of debts due to secured creditors is Rs 4,00,000. The workmen's portion of the security is therefore, one-fourth of the value of the security, that is Rs 25,000.

Over-riding preferential payments. Section 529-A, inserted by the Companies (Amendment)Act of 1985, provides that certain debts shall have priority over all other debts including preferential payments listed in Section 530. These debts have been termed as "over-riding preferential payments". These over-riding preferential payments include the following:

(a) workmen's dues as defined under Section 529

(b) debts due to secured creditors to the extent such debts rank *pari passu* with the workmen's dues under clause (c) of the proviso to sub-section (1) of Section 529.

The above debts shall be paid in full. If the assets are not sufficient to meet them, they shall abate in equal proportions.

Order of payment of liabilities. Subject to the rights of secured creditors, the liabilities of the company will be paid off in the following order:

(i) cost and charges of winding up;

(ii) preferential creditors;

(iii) creditors secured by floating charges;

(iv) unsecured creditors; and

(v) if any surplus is left, it will be paid first to preference shareholders and then to equity shareholders.

Preferential payments

According to Section 530, the following payments shall be treated as preferential payments and these shall be paid in priority to other debts but after over-riding preferential payments:

(1) All revenues, taxes, cesses and rates due from the company to the Central or a State Government or to a local authority. The amount should have become due and payable within twelve months before winding up.

(2) All wages or the salary of an employee in respect of sevices rendered to the company and due for a period not exceeding four months within twelve months before winding up. The amount shall not exceed one thousand rupee in case of one claimant.

(3) All accrued holiday remuneration becoming payable to an employee on termination of his employment on account of winding up.

(4) All amounts due in respect of contributions payable by the company during the twelve months next before the winding up under the Employees State Insurance Act, 1948, unless the company is being wound up voluntarity merely for the purpose of reconstruction or of amalgamation with another company.

(5) Unless the company is being wound up voluntarily merely for the purposes of reconstruction or of amalagamtion with another company or where it has taken out a Workmen Compensation Policy, all amounts due under the Workmen Compensation Act, 1923, in respect of the death or disablment of any employee of the company.

(6) All sums due to any employee from a provident fund, a pension fund, a gratuity fund or any other fund for the welfare of the employees, maintained by the company.

(7) The expenses of any investigation held in pursuance of Sections 235 or 237, insofar as they are payable by the company.,

All the above debts rank equally among themselves and must be paid in full. If the assets are insufficient to meet them, they shall abate in equal proportions.

Disposal of Unpaid Dividends and Undistributed Assets

If the liquidator has in his hands or under his control any money or assets, payable or distributable to any creditor or any contributory, which had remaind unpaid or undistributed for six months after the date on which they became payable or refundable, the liquidator shall pay the said money into the public account of India in the Reserve Bank of India

in a separate account to be known as the Company's Liquidation Account. The liquidator shall be entitled to a receipt fromt he Reserve Bank of India for any money paid to it, and such a receipt shall be an effectual discharge of the liquidator in respect thereof. Any person claiming to be entitled to any money paid into the Companies Liquidation Account may apply to the court for an order for payment and the court, if satisfied that the person claiming is entitled, may make an order for payment to that person of the sum due. The Central Governemnt is also authorised to make payments from the said account either on a certificate by the liquidator or the Official Liquidator or after taking such security from him as it may think fit.

Any money remaining unclaimed in the Companies Liquidation Account for a period of fifteen years shall be transferred to the general revenue account of the Central Government, but refund to the claimants shall be allowed as if such a transfer had not been made. (Sec. 555)

Effects of Winding Up on Antecedent and Other Transactions

Fraudulent preference. This is an act of the debtor by which one creditor is preferred to another in the matter of payment of his dues. Such fraudulent preference becomes void if the debtor is adjudicated insolvent within three months of the date when fraudulent preference occurred. This is according to the Law of Insolvency. Under Section 531 of the Companies Act, any such transaction entered into by a company within six months before the commencement of its winding up is deemed a fraudulent preference of its creditors, and is accordingly, invalid.

Avoidance of voluntary transfer. A voluntary transfer is a transfer without consideration, *e.g.,* a gift. Any transfer of property made within a period of one year before commencement of the winding up shall be void against the liquidator unless such a transfer is made (a) in the ordinary course of its business; or (b) in favour of a purchaser or encumbrancer, in good faith and for valuable consideration. (Sec. 531 A)

Transfer for the benefit of all creditors to be viod. Any transfer or assignment by a company of all its property to trustees for the benefit of all its creditors shall be viod. (Sec. 532)

Effect of a floating charge. Where a company is being wound up, a floating charge on the undertaking or property of the company created within twelve months immediately preceding the commencement of the winding up, shall be invalid unless it is proved that the company, immediately, after the creation of the charge, was solvent. Again, the charge would be valid to the extent of the amount of cash actually paid to the company together with interest on that amount at the rate of five per cent per annum or such other rate notified by the Central Government. (Sec. 534)

Disclaimer of onerous property. Where any part of the property of a company which is being wound up consists of (a) land of any tenure, burdened with onerous convenants; (b) shares or stock in companies; (c) any other property which is unsaleable or is not readily saleble by reason of the fact that it requires the possessor to perform certain acts or pay a sum of money; and (d) unprofitable contracts, the liquidator may disclaim any such property with the leave of the court at any time within twelve months after commencement of winding up or such extended period as may be allowed by the court. The disclaimer should be in writing and signed by the liquidator. Where any such property does not come to the knowledge of the liquidator within one month after the commencemnt of the winding up, the above period of twelve months shall commence from the date of his knowledge of such property.

The disclaimer shall release the company and the property from liability. It would not affect the rights of any other persons in respect of that proeprty. The court may, before granting the disclaimer require notice to be given to persons interested in the property and make such other order in the matter as it thinks just.

The liquidator shall not be entitled to disclaim any property in any case where an application in writing has been made to him by any person interested in the property, requiring him to decide whether he will or will not disclaim the same. The liquidator should, within twenty eight days given notice to the applicant that he intends to apply to the court for leave to disclaim. If he does not do so, he shall not be entitled to disclaim the property, and in case the property is a contract, he shall be deemed to have adopted it.

Any person injured by the operation of a disclaimer shall be deemed to be a creditor of the company to the amount of the compensation or damages payable in respect of the injury and may accordingly prove the amount as a debt in the winding up. (Sec. 535)

Avoidance of transfers, etc., after commencement of winding up. In a voluntary winding up, any transfer of shares in the company made without sanction of the liquidator, and any alteration in the status of the members of the company made after commencement of the winding up shall be void.

Similarly, in the case of winding up by or subject to the supervision of the court, any disposition of company's property and any transfer of shares in the company or alteration in the status of its members made after the commencement of the winding up, shall be void, unless the court otherwise orders. (Sec. 536)

Avoidance of certain attachments, executions etc. Where any company is being wound up by or subject to the supervision of the court (*a*) any

attachment or distress or execution put in force against the estate or effects of the company, without leave of the court after commencement of winding up; (*b*) any sale held, without leave of the court, of any of the properties of the company after such commencement, shall be void.

This is not applicable to any proceedings for the recovery of any tax or impost or any dues payable to the Government. (Sec. 537)

Books and Papers

Books and papers of company to be evidence. Where a company is being wound up, all books and papers of the company and of the liquidators shall, as between contributories of the company, be *prima facie* evidence of the truth of all matters purporting to be recorded therein. (Sec. 548)

Inspection of books and papers by creditors and contributories. At any time after the making of an order for the winding up of a company by or subject to the supervision of the court, any creditor or contributory of the company may, if the Supreme Court rules so permit, inspect the books and papers of the company. (Sec. 549)

Disposal of books and papers. When the affairs of a company have been completely wound up and it is about to be dissolved, its books and papers and those of the liquidators may be disposed of as follows:

(*i*) in the case of winding up by or subject to the supervision of the court, in such manner as the court directs;

(*ii*) in the case of members' voluntary winding up, in such manner as the company, by special resolution, directs; and

(*iii*) in the case of creditors' voluntary winding up, in such manner as the committee of inspection or, if there in no such committee, as the creditors of the company may direct.

After five years from the dissolution of the company, no responsibility shall rest on the company, the liquidator or any other person to whom the custody of the books and papers has been committed, by reason of any book or paper not being forthcoming to any person claiming to be interested therein. (Sec. 550)

QUESTIONS

1. What are the different modes of winding up a Joint Stock Company? [*Delhi, B.Com. (Hons.) 1977*]

2. (*a*) Under what circumstances may a company be wound up by the court? (*b*) Who are entitled to file a petition and when? [*Delhi, B.Com. (Hons.), 1985*]

3. Describe the circumstances when the court considers winding up of a company 'just and equitable.' [*Delhi, B.Com. (Hons.) 1990*]

company 'just and equitable.' [*Delhi, B.Com. (Hons.) 1990*]

4. (*a*) What is meant by 'Declaration of Solvency'?

(*b*) When can a court order for the compulsory winding up of a company? [*Delhi, B.Com. (Hons.) 1973*]

5. Write a short note on Committee of Inspection. [*Delhi,, M. Com. 1976*]

6. When shall a company be deemed to be unable to pay its debts for the purposes of Section 433 of the Companies Act? [*Company Secretary (Final), October 1974*]

7. What are the different classes of voluntary winding up provided by the Companies Act and indicate the procedures to be adopted for commencement of such winding up proceedings? [*C.A. (Final), May 1978*]

8. Distinguish between members' voluntary winding up and creditors' voluntary winding up. [*Delhi,, B.Com. (Hons.) 1974, 77, 79*]

9. Distinguish between voluntary and compulsory winding up. [*Delhi, B.Com. (Hons.) 1978*]

10. What consequences follow from the winding up proceedings in both the cases of compulsory and voluntary winding up. [*Delhi, M.Com., 1976*]

11. (*a*) Who is a contributory?

(*b*) What is the nature and extent of the liability of a contributory? [*Delhi, B.Com. (Hons.), 1984, 90*]

12. Discuss the rights of the contributories to claim set off against the company. Can the contributory avoid liability on the ground--

(*a*) that the shares were allotted to him before the minimum subscription was subscribed?

(*b*) that he subscribed the shares on the basis of a false and misleading prospects. [*Delhi, M. Com., 1975*]

13. Can a signatory to the memorandum of association whose name has not been put on the register of members be held liable as a contributory?

14. What are preferential payments that are required to be made during the course of winding up of a company before payment to any other creditor? [*C.A. (Final), November 1977*]
[*Delhi, M.Com., 1976*]

15. Who is an Official Liquidator? Explain his duties and powers.

16. What are the general powers of the court in relation to the compulsory winding up of a company?

17. State the powers and duties of the liquidator in voluntary winding up.

18. Write a short note on the liquidator's right of disclaimer.

PRACTICAL PROBLEMS

1. A company made a default in holding the statutory meeting within 6 months from the date at which the company was entitled to commence business. A petition for winding up this ground is presented to the court. Is the court bound to order winding up?

2. A company's trade has been suspended temporarily owing to the trade depression but it has *bona fide* intention to continue its operations when conditions improve. A prayer was made to court for winding up the company. Decide.

[*C.A., May, 1964*]

3. A company was formed to carry on business in India and abroad. In the first year of its incorporation, the company carried on business abroad only and no business was transacted in India during this period. Will the court order winding up of the company?

4. A creditor of a company applied for winding up of the company for its inability to pay his claim, after proper demand had been made by him and on the lapse of three weeks from the date of such demand. It was proved to the satisfaction of the Court, during enquiry, that the company was commercially solvent. Discuss. [*C.A., May, 1965*]

5. *B*, a shareholder in a company, is adjudicated insolvent and the Official Assignee applies to be registered as a member in place of *B*. The company refused to register him. Thereupon the Official Assignee petitions for the winding up of the company. Will the Court order the winding up of the company?

6. A company was formed for the purpose of manufacturing coffee from dates under a patent which was to be granted by the Government of Germany. The company was also to obtain other patents of similar kind. The German patent was not granted to the company and the latter purchased a Swedish patent and the company started making and selling coffee from dates. A petition is presented to the court for a winding up order. Decide.

7. A company was registered to carry on the testator's business and to divide the profits among the members of the family. The managing director had a prepondering voting power in the company. The directors omitted to hold meetings, submit accounts, or recommend dividends and they had laid themselves open to the suspicion that their object in so omitting was to keep the shareholders in ignorance of the company's position and to acquire the shares at an undervalue. An application for winding up is filed. Decide.

[*C.A. (Final), November, 1963*]

8. A company was formed to acquire the undertaking of four other companies carrying on an oil business in Russia. Before the undertaking could be acquired they were confiscated and since 1920 the company had been engaged in an endeavour to substantiate a claim against the Government of Russia. It had not otherwise carried on any business and had considerable assets. An application for winding up was made. Discuss the merits of this application.

[*C.A., November, 1964*]

9. A company, without passing a resolution in its general meeting and getting

sanction of the Court, allotted 500 shares at a discout to *G*, its Chairman, and placed his name on the register of members. In the winding up of the company, *G* claimed that he was not liable to be made a contributory as the allotment was made in contravention of the provisions of the Companies Act. Is *G's* contention justified in any way? [*C.A., May 1969*]

10. Can a holder of fully paid shares be placed on the list of contributories?

11. A shareholder of a company, who sold his shares, executed blank transfer deed and delivered it along with the share certificate to the purchaser. He writes to the company that he has sold the shares, but neither he nor the purchaser deposited the shares with transfer deed and consequently the transfer was not noted on the register of members. On the winding up of the company, who should be placed on the list of contributories? [*Delhi, M. Com., 1973*]

12. The claim of a company for the realisation of the amount due on a call becomes barred by limitation. Thereafter the company goes into liquidation. Can the liquidator realise the said amount barred by limitation? Will it make any difference if the amount is due on account of goods purchased from the company on credit by the contributory? [*Delhi, M.Com., 1962*]

13. A company was ordered to be wound up in January 1967. Among its liabilities the company owes Rs 10,000 as arrears of income tax for the assessment year 1963-64 in respect of which an assessment order was passed in Nov. 1965. The Income-Tax Department claims to be a preferential creditor under Section 530. Will the claim be upheld in the winding up proceedings?

[*C.A., November 1967*]

14. On 15th March 1959, a company created floating charge on its property in favour of *X*. On 1st June, 1959, an order for winding up the company was passed. What position would you assign to *X* amongst the creditors? Give reasons.

[*Delhi, M.Com., 1961*]

22

WINDING UP OF UNREGISTERED COMPANIES

MEANING

ACCORDING to Section 582, the term 'unregistered company' includes any partnership, association or company consisting of more than seven members at the time when the petition for winding up is presented before the court. It means an association of persons consisting of more than seven members but not more than 20 (10 in case of an association carrying on banking business) members carrying on business without being registered under the Companies Act or any other law for the time being in force in India. However, it shall not include:

(*a*) a railway company incorporated by any Act of Parliament or other Indian law or any Act of Parliament of the United Kingdom;

(*b*) a company registered under the Companies Act, 1956; and

(*c*) a company registered under any previous companies law.

The term 'unregistered companies' does not cover associations formed contrary to the provisions of Section 11 which are known as illegal associations.

Section 584 provides that where a body corporate incorporated outside India has been carrying on business in India, and ceases to do so, it may be wound up as an unregistered company, even though its existence had ceased according to the law of the country of incorporation.

Winding Up of Unregistered Companies

An unregistered company may be wound up under this Act and all its provisions with respect to winding up shall apply to an unregistered company with the exceptions and additions mentioned below. [Sec. 583(1)]

(*i*) For the purpose of determining the court having jurisdiction in the matter of the winding up, an unregistered company shall be deemed to be registered in the state where its principal place of business is situated and

the principal place of business, for all the purpose of the winding up, shall be deemed to be the registered office of the company [Sec. 583(2)]

(*ii*) An unregistered company can be wound up only by an order of the court. No registered company shall be wound up under this Act voluntarily or subject to the supervision of the court. [Sec. 583(2)]

(*iii*) The circumstances in which an unregistered company may be wound up are as follows: (*a*) if the company is dissolved or has ceased to carry on business or is carrying on business only for the purpose of winding up its affairs; (*b*) if it is unable to pay its debts; and (*c*) if the court is of the opinion that it is just and equitable that the company be wound up. [Sec. 583(4)]

(*iv*) An unregistered company shall be deemed to be unable to pay its debts:

(*a*) if a creditor, to whom the company is indebted for a sum exceeding five hundred rupees, has served on the company, a demand for payment of the sum so due, and the company has for three weeks after the service of the demand, neglected to pay the sum or to secure or compound for it to the satisfaction of the creditor;

(*b*) if any suit or other legal proceeding has been instituted against any member for any debt due from the company or from him in his character of member, and notice in writing of the institution of the suit or other legal proceeding has been served on the company, and the company has failed to pay the debt or get the suit or other legal proceeding stayed or indemnify the defendant to his satisfaction within ten days after the service of the notice; or

(*c*) if the execution or other process issued on a decree or order of any court in favour of a creditor is returned unsatisfied in whole or in part; or

(*d*) if it is otherwise proved to the satisfaction of the court that the company is unable to pay its debts. [Sec. 583(5)]

Contributories

In the event of an unregistered company being wound up, every person shall be deemed to be a contributory, who is liable to pay or contribute to the payment of (*a*) any debt or liability of the company or (*b*) any sum for the adjustment of the members among themselves; or (*c*) the costs, charges and expenses of winding up the company.

In the event of the death or insolvency of any contributory, his legal representative or assignee shall be liable for the amount of the liability. (Sec. 585)

Stay of Suits and Legal Proceedings

The provisions of this Act with respect to staying and restraining suits and legal proceedings against a company at any time after the presentation of a petition for winding up and before the making of a winding up order shall, in the case of an unregistered company where the application to stay or restrain is made by a creditor, extend to suits and legal proceedings against any contributory of the company. (Sec. 586)

Similarly, where an order has been made for winding up an unregistered company, no suit or other legal proceedings shall be proceeded with or commenced against any contributory of the company in respect of any debt of the company, except by leave of the court and except on such terms as the court may impose. (Sec. 587)

Directions as to Property in Certain Cases

If an unregistered company has no power to sue and be sued in a common name, or if for any reason it appears expedient, the court may direct that all or any part of the property belonging to the company or held by trustees on its behalf shall vest in the Official Liquidator by his official name.

The Official Liquidator may bring or defend in his official name any suit or legal proceeding relating to that property after given such indemnity as the court may direct. (Sec. 588)

Cumulative Effect of Above Provisions

All the above-mentioned provisions with respect to unregistered companies shall be in addition to, and not in derogation of, any provisions of the Act with respect to the winding up of companies by the court. The court or Official Liquidator may exercise any powers or do any act in the case of unregistered companies which might be exercised or done by the court or Official Liquidator in winding up of companies formed and registered under the Act. (Sec. 589)

QUESTIONS

1. What is an unregistered company? When and in what manner can an unregistered company be wound up under the Companies Act?
2. State the provisions of the Companies Act in relation to winding up of unregistered companies?

PRACTICAL PROBLEM

1. A foreign company formerly carrying on business in India is dissolved under the laws of the country in which it was incorporated. Can it be nevertheless wound up under any provisions of the Companies Act, 1956, on its ceasing to carry on business in India and, if so, under what provisions?

[C.A., May 1967]

23

DEFUNCT COMPANIES

MEANING

A defunct company is a company which is not carrying on business or which is not in operation. A company will be considered to be in operation if it is in the course of being would up and not carrying on any business so long as it remains undissolved.[1]

Power of Registrar to Strike Defunct Company Off the Register

Where the Registrar has reasonable cause to believe that a company is not carrying on business or is not operation, he shall send a notice to the company inquiring whether the company is carrying on business or is in operation. [Sec. 560(1)]

If the Registrar does not receive an answer within one month of sending the notice, he shall, within fourteen days after the expiry of the month, send to the company by registered post a letter referring to the first letter and stating that no answer has been received thereto. He shall also state that if answer is not received to the second letter within one month from its date, a notice will be put up in the Official Gazette with a view of strike off the company's name from the register. [Sec. 560(2)]

If the Registrar receives no reply as required above or receives an answer that the company is not in operation, he may publish in the Official Gazette and send to the company by registered post a notice that on the expiration of three months from the date of the notice, the name of the company shall be struck off the register and the company will be dissolved, unless cause is shown to the contrary. [Sec. 560(3)]

The same procedure is to be followed where a company is being would up and the Registrar has reasonable ground to believe either that no liquidator is acting or that the affairs of the company have been completely would up and returns required to be made by the liquidator have not been made for a period of six consecutive months. [Sec. 560(4)]

[1]*ReOutlay Ass. Society* (1887) 34 Ch. D. 479.

At the expiry of three months, if no cause is shown to the contrary by the company, the Registrar actually strikes off the name of such a company from his register and publishes the fact in the Office Gazette, and the company stands dissolved. The dissolution of the company would not affect (*a*) the liability, if any, of every director, manager or other officer who was exercising any power of management and of every member of the company; or (*b*) the power of the court to wind up a company. [Sec. 560(5)]

Restoration of the Company to the Register

The company whose name has been struck off the register, any member or creditor who feels aggrieved because of the removal of the name of the company from the register, is entitled to make an application to the court for restoration of the name of the company to the register within twenty years from the publication in the Official Gazette of the notice of the removal of the company's name from the register. The company's name may be restored to the register if the court is satisfied that the company was carrying on business at the time of the striking off. The court may also give such directions and make such provisions as seem just for placing the company, its creditors, debtors and members in the same position in which they were before the date on which the name of the company was struck off. [Sec. 560(6)]

The power of the court to restore the name of the company to register is a discretionary power and it will exercise its power for a substantial reason. One of such reasons for exercising the discretion in favour of restoring a company must be that after restoration the company will be in a position to carry on its business.[2] The court may restore the company to the register if it feels that otherwise it is just to do so, or that some object will be achieved by such restoration.

In another case, it was held that restoration shall operate with retrospective effect.[3]

A certified copy of such an order shall be delivered to the Registrar for registration and the company will be deemed to be in existence all through as if its name had never been struck off. [Sec. 560(7)]

A letter or notice to be sent to the company may be addressed to the company at its registered office or if no office has been registered, to the care of some director, manager or other officer of the company or if there is no director, manager or officer of the company whose name and address are known to the Registrar, may be sent to each of the persons

[2]*Mandal's (U.N.) Estate (Pvt.) Ltd., In re* (1959) A.I.R. Cal. 493
[3]*Re Box Co. Ltd.*, (1970) 2 All. E.R. 183.

who subscribed the memorandum addressed to him at the address mentioned in the memorandum. [Sec. 560(8)]

A notice to be sent to a liquidator may be addressed to the liquidator at his last known place of business. [Sec. 560(9)]

QUESTIONS

1 (*a*) Discuss the powers of the Registrar of Companies to strike off the name of a company from the Register.

(*b*) What factors should be considered by the court before ordering restoration of a company already struck off? [*C.A. (Final), May 1976*]

2. Write in lucid words what is meant by "Company's name struck off the register". In that case with whom the undisposed property would vest?

[*Company Secretary (Final), April 1975*]

3. Explain what is meant by a "defunct" company and examine the powers of the Registrar of Joint Stock Companies and the court with reference to the same.

[*C.A., June 1963*]

4. "The power of the Registrar of Companies to strike off the name of a defunct company is meant to be used in cases where a company is not legally dissolved when it should be so dissolved." Briefly discuss the legal provisions regarding striking off the names of defunct companies in the light of the above statement.

[*C.A., November 1965*]

5. Explain the power of the Registrar of Companies to strike off the name of a defunct company from the register of companies.

[*Delhi, B.Com. (Hons.), 1985*]

PRACTICAL PROBLEMS

1. Is is possible to restore to the Register the name of a company which has been previously struck off? If so, how can this be done?

[*C.A., November 1965*]

2. A private company was formed by the members of a family in 1950. During the last 30 years, it never met either in shareholders' meeting or in a directors' meeting in view of the disputes between the members. For more than 10 years, the company did not file any summaries or lists of shareholders. It has shown neither its balance sheet nor bank account. The Registrar removed the name of the company from the register as a defunct company. An application is made to the court for restoration of the name to the Register. Decide.

Appendix I

BRIEF HINTS FOR PRACTICAL PROBLEMS

Given at the end of each Chapter

CHAPTER 2

[Reference to page numbers within brackets is to the pages of this Book]

1. [No. Perpetual succession, p. 24]

2. *B* and five others shall be personally and severally liable to an unlimited extent for the whole debts of the company if the company carries on business for more than six months after the number of its members has been reduced below seven. [Sec. 45, p. 26]

3. Refer to answer to Problem 2 of this Chapter.

4. Ram, like any other sole trader, will be personally liable for all the debts incurred in such business to an unlimited extent. The benefit of limited liability will not accrue simply because the business undertaking is named as "Ram & Co. Ltd.", unless it is registered under the Company Law as a limited company. Besides, Ram will be liable to a fine upto Rs 50 for every day of such unauthorised use of the word 'Ltd.' under Sec. 631 of the Companies Act, 1956.

5. No, the insurance company is not liable to *M* as he does not have insurable interest in the company's property.

[Macaura v. Northern Assurance Co. Ltd., p. 25].

6. No. A company has a separate legal entity which is entirely distinct and independent of the persons who constitute it. Therefore, a sale of property by shareholders to the company is not a transfer from self to self but from one entity to another. [Commissioner of Income Tax, Calcutta v. Associated Clothiers Limited, p. 30]

7. Yes. A company is distinct from its members who constitute it. Although the income in the hands of the company was partly agricultural, yet the same income when received by the shareholders could not be regarded as agricultural income. [Bacha F. Guzdar v. Commr. of Income Tax, Bombay, p. 30]

8. The company has been formed to avoid an otherwise valid obligation. The company is a mere cloak or sham for the purpose of

enabling *X* and *Y* to commit a breach of the contract term. *Z* may have the comapny enjoined from competing with him. [Gilford Motor Co. v. Horne, p. 27; Jones v. Lipman, p. 29]

CHAPTER 3

1. Yes. [Sec. 43A(1), p. 43.
2. Refer to answer to Problem 1 of this Chapter.
3. No. To constitute a government company, fifty one per cent of the paid up share capital must be held by the Central or State Government. The Life Insurance Corporation of India and the Unit Trust of India are statutory corporations, but not the governments, or their departments and, therefore, eleven per cent shares held by these institutions cannot be taken as held by the Central Government. [Sec. 617, p. 50; Sec. 619-B, p. 52]
4. The suit is not competent, as the association is an illegal association (Sec. 11). The illegality of an illegal association cannot be cured even by subsequent reduction in the number of its members. [Madan Lal v. Janki Prasad, p. 57]
5. No. company *Y* is not a subsidiary of company *X*. The shares held by managing director and another director of company *X* shall not be taken into account since they hold shares in their private capacities.
6. Yes, the above organisation must be registered as a company under the Companies Act, 1956, as it consists of 12 persons carrying on banking business. [Sec. 11(3), p. 56.
7. No, it is not an illegal association because the total number of members of two families constituting the association does not exceed twenty, two minor sons being excluded. [Sec. 11(3), p. 56]
8. No, the association is not illegal because if the Karta of a joint Hindu family enters into partnership in his representative capacity on behalf of his family, he shall be treated as one person only. As such, the association consists of only two members and it is not required to be registered. [Mewa Ram v. Ram Gopal, p. 56]
9. No. Six member who were its past employees shall be excluded in determining the number of members of the company, which will be 48(54-6). As such, the private company has not made any default in complying with the restriction of maximum of 50 members and it is not necessary to convert it into a public company. [Sec. 3(1) (iii) (b), p. 37]

CHAPTER 4

1. No, *A* will not succeed. The company is not bound by contracts made before its incorporation. Since the company has not accepted the contract, no relief is available under Secs. 15 and 19 of Specific Relief Act, 1963. [Re English and Colonial Produce Ltd., pp. 65-66]

2. The allotment of shares is perfectly valid because the certificate of incorporation is conclusive evidence of all that it contains. The company is deemed to come into existence from June 10, the date mentioned in the certificate of incorporation, even if this is wrong. [Jubilee Cotton Mills Ltd. v. Lewis, p. 70]

3. No. It being only a provisional contract, the company is not legally bound by it until it obtains certificate of commencement of business. [Sec. 149(4), p. 73]

4. A preliminary contract is not binding on the company. Therefore, the company may very well decide not to proceed with the above contract. The promoters are personally liable on the contract. [Kelner v. Baxter, p. 65]

5. The certificate of incorporation is conclusive for all purposes and it cannot be challenged. Though there were no seven subscribers to the memorandum and the Registrar ought not to have granted the certificate, the certificate is conclusive for all purposes. [Moosa v. Ebrahim, p. 71]

6. The certificate of incorporation is not merely a *prima facie* answer, but a conclusive answer to objections by the signatories to the memorandum. When once the certificate of incorporation is given, nothing is to be inquired into as to the regularity of prior proceedings. The company stands duly incorporated under the Act. [Peel's case, pp. 70-71]

7. The certificate of incorporation is a conclusive evidence only with regard to the formation and registration of the company and the incorporation of a company is not invalidated because of its illegal objects. However, if objects of a company are illegal, they would not be rendered legal by the certificate. Therefore, the contention of the company is untenable. [Bowman v. Secular Society Ltd., p. 71]

CHAPTER 5

1. The second company is advised to change its name by passing an ordinary resolution and with the approval of the Central Government. Alternative, the first registered company may approach the Central Government and the latter may direct the second company to change its name. [Sec. 22(1), p. 83]

2. The second company may be directed by the Central Government to change its name under Sec. 22(1). Under the general law also, the plaintiff can obtain an injunction against the defendant to use similar name on the ground that people were likely to be confused into thinking of both the companies as one or closely related. [Sec. 22(1), p. 83; Ewing v. Buttercup Margarine Co., p. 78]

3. The company is not bound by such acceptance. However, it may still choose to pay the bill on due date. If the company fails to pay the bill, the directors who issued or authorized the issue of such a bill would be personally liable under it. [Sec. 147(1) (c), p. 79]

4. No, the holder of the bill cannot hold the directors personally liable since the omission of the word "Limited" is only accidental. Directors intended to make the company liable on the bill and it is the company which is liable for paying the bill on due date. [Determatine Co. Ltd. v. Ashworth, p. 250]

5. The company can make the above alteration on the ground that it will enable the company to carry on its business more economically or efficiently. A special resolution is required to be passed by the company in its general meeting. The approval of the Company Law Board for alteration of the objects clause has been dispensed with by the Companies Amendment Act, 1996. [Re Scientific Poultry Breeders' Association Ltd., pp. 84, 86]

6. The contract is *ultra vires* the company and if the company could not make it, much less could it be ratified. Therefore, it cannot be enforced against the company. [Ashbury Railway Carriage and Iron Co. Ltd. v. Riche. p. 88]

7. No, the contention of the Registrar will not prevail. The choice of new or additional business must rest with shareholders and directors of the company and not with the Registrar. The additional business to be carried on may be wholly different from the existing business of the company and yet be capable of being conveniently or advantageously combined with it. Whether one business can be conveniently combined with another is essentially a business question to be determined by the directors and shareholders and not by the Registrar. An alteration will ordinarily be confirmed except when the new business is detrimental to, or inconsistent with, the existing business. [Parent Tyre Co. p. 85]

8. No, the Registrar cannot register the above alteration. [Secs. 18 and 19, p. 87]

CHAPTER 6

1. No. The certificate issued is a mere forgery. Forgery is nullity. A company can never be held bound by forgeries committed by its officers.

The doctrine of indoor management only applies to irregularities that otherwise might affect a genuine transaction, but it cannot apply to a forgery. [Ruben v. Great Fingall Ltd., 108]

2. Yes, the company can exercise lien on all the shares of '*S*', including those fully paid-up. An alteration of articles with retrospective effect is valid provided it is *bona fide* and for the benefit of the company as a whole. [Allen v. Gold Reefs of West Africa, p. 101]

3. The above alteration of articles is perfectly valid since it has been done *bona fide* and for the benefit of the company as a whole, individual hardship being irrelevant. [Sidebottom v. Kershaw, Leese & Co., p. 103]

4. The alteration is not valid as it oppresses or defrauds the minority. [Brown v. British Abrasive Wheel Co. Ltd., p. 103]

5. A has no cause of action against the company because the right which he attempted to enforce was conferred upon him in a capacity other than of a member and that articles do not constitute a contract between a company and an outside. [Eley v. The Positive Government Life Assurance Co., p. 99]

6. The company is liable to pay the bill. *B* is advised to file a suit against the company for the amount of the bill. He is entitled to assume that the managing director had obtained the approval of board of directors in a meeting. *B* is not required to enquire into the regularity of company's internal proceedings. [Royal British Bank v. Turquand, p. 107]

7. Yes. Refer to answer to Problem 6 of this Chapter.

8. The alteration is valid. The power of alteration of articles is subject only to what is clearly prohibited by the memorandum, expressly or impliedly. In the above problem, the memorandum did not prohibit the issue of shares bearing a preferential dividend. Moreover, the rights of shareholders in respect of their shares were not required to be stated in the memorandum and these could be regulated by articles from time to time by special resolutions, unless dealt with in the memorandum.

9. No. The power to alter articles is a statutory power given by Sec. 31 and it cannot be negatived by a contract or any provision in the memorandum or articles. [Sec. 31, p. 101]

10. The company shall be liable only for Rs. 50,000. Since the directors have knowledge of internal irregularity, they will not be protected by doctrine of indoor management. [Howard v. Patent Ivory Co., p. 108]

11. No, the above mortgage is not binding upon company *B*. It may be presumed that company A had notice of irregularity through its directors [Pratt Ltd. v. Sasoon & Co. Ltd., p. 108]

CHAPTER 7

1. No. The remedy is available only to those who have taken shares directly from the Company. A purchaser of shares in the open market has no remedy against the company or promoters though he might have bought the shares on the faith of misrepresentation in the prospectus. [Peek v. Gurney, p. 124]

2. No. For reasons, refer to answer to Problem 1 of this Chapter.

3. No. For reasons, refer to answer to Problem 1 of this Chapter.

4. Yes, the above observation or statement is a mis-statement so as to render the maker criminally liable. Suppression of facts is as bad as disclosure of wrong facts. Truth, whole truth and nothing but truth must be disclosed. Half truth is no better than a downright falsehood. [Rex v. Kylsant, p. 123]

5. Yes. If a statement was true when it was made but subsequently became untrue when shares were allotted, the contract to take shares can be rescinded. [Re Scottish Petrolleum Co., p. 123]

6. No. A cannot rescind the contract as there is no misrepresentation of facts in the prospectus. The only fact asserted was the existence of the promise and the existence of a promise is not falsified by breaking of it.

7. No, the allottee cannot rescind the contract since the Companies Act restricts the rate of discount to 10 per cent. Misrepresentation of law gives no remedy to the aggrieved party.

8. No. After repurchasing the shares from *B, A* becomes a purchaser of shares in the open market and he cannot proceed against the company. [Croom's case, p. 124]

CHAPTER 8

1. No. Since the reissue of forfeited shares is not an allotment, but only a sale, no return of allotment is required to be sent to the Registrar in respect of these shares. Similarly, the reissue of forfeited shares at a premium does not involve violation of any provision of the Companies Act.

2. The surrender of shares is not valid. A company can accept surrender of shares under conditions and limitations subject to which shares can be forfeited. A valid call and a default must exist. Conditions as to forfeiture do not exist in the present problem. Moreover, surrender of shares should not be used as a device for relieving a shareholder from his liability.

3. No. A is not entitled to get the transfer registered in his name as it

would amount to recognition of fraudulent certificate. But the company must compensate *A* for the loss he has sustained by acting on the faith of the share certificate. [Dixon v. Kennaway & Co. p. 141]

4. No. The certificate issued is a mere forgery. Forgery is nullity. A company can never be held bound by forgeries committed by its officers. The doctrine of indoor management only applies to irregularities that otherwise might affect a genunine transaction, but cannot apply to a forgery. [Ruben v. Great Fingal Ltd., p. 142]

5. No, the company is not right in placing *A* on the list of contributories. If the certificate stated that on each of the shares full amount has been paid, the company is estopped from denying that the shares are fully paid and, therefore, *A* cannot be held liable as a contributory. [Bloomenthal v. Ford, p. 142]

6. Yes, the call is perfectly valid and it can be enforced. Sec. 290 lays down that the acts of directors would be valid even if it is afterwards discovered that there was some defect in the appointment or qualifications of such directors. [Sec. 290, p. 280]

7. No, the directors are not discharged or their liability to pay on their shares as the directors made the call to serve their personal ends and not for the benefit of the company [Re European Central Rail. Co. p. 150]

8. The allotment of shares is perfectly valid because the certificate of incorporation is conclusive evidence of all that it contains. The company is deemed to come into existence from June 10, the date mentioned in the certificate of incorporation, even if this is wrong. [Jubilee Cotton Mills Ltd. v. Lewis, p. 70]

9. *M* is liable on the call made. The former call was invalid because it did not mention the amount of the call or the time and place for its payment. An invalid call cannot support a valid forfeiture and, therefore, *M* continues to be a shareholder and he is liable to pay the fresh call. On his failure to pay it, the company can proceed against him and recover the amount due.

10. No. The call is not valid as it has not been made on a uniform basis on all shares falling under the same class. [Sec. 91, p. 148; Galloway v. Halley Concerts Society, p. 148]

11. No. The forfeiture is not valid as it has not been done in good faith and in the best interest of the company. The power of forfeiture cannot be exercised to relieve members from their liability and, therefore, directors continue as shareholders. [Re Esparto Trading Co., p. 151]

12. No, the above scheme is not legal as it indirectly resulted in issuing shares at a discount of twenty per cent which is against the provisions of Sec. 79 of the Companies Act. [Sec. 79, p. 137]

13. No. The condition on which *S* agreed to take the shares was never

performed and he, therefore, never became a shareholder in the company. [Simpson's case, p. 135]

14. Yes, *X* is bound to pay for the shares allotted to him. A condition which is to operate subsequently to allotment does not affect its validity. *X* will be deemed to have agreed absolutely to become a member [Elkington's case, p. 135]

CHAPTER 9

1. (*a*) Refer to sec. 106 for procedure for the variation of rights, p. 169.
(*b*) Refer to Sec. 107, p. 169-170.

2. Yes, the above offer is perfectly valid. The permission by the company to recover the amount in ten instalments amounts to provision of money by the company to its employees for the purchase of its fully paid shares. [Sec. 77, p. 172]

3. No. The preference shares continue to be cumulative in spite of the above alteration. The usual presumption is that preference shares are cumulative, and this presumption can be rebutted only if the contrary is provided by the articles in unambiguous terms. [Foster v. Coles, Foster and Sons Ltd, pp 160-161]

4. No, the preference shareholders cannot claim their arrears of dividend out of the profits of 1979. The above provision in the articles clearly prevented payment of arrears of dividend out of profits of subsequent years. It meant that the profits of each year only were to be paid in that way. [Staples v. Eastman Photographic Material Co., p. 161]

5. The scheme is fair and the court will sanction the scheme. The special circumstances here are that due to the loss of almost the whole of the paid-up capital of the company the only alternative to reduction is winding up in which case neither class of shareholders would have got anything.

6. No. A company cannot borrow money on the security of reserve capital as the latter cannot be called except in the event and for the purpose of winding up of the company. [Barlett v. Mayfair Property Co., p. 169]

CHAPTER 10

1. No. The transaction is void on the face of it and the father of the minor who signed the application cannot be deemed to have contracted for the shares and cannot be placed on the list of contributories in the

event of the company being wound. [Palaniappa v. Official Liquidator, p. 179]

2. The company should refuse to register transfer of shares when the transferee is known to be a minor. However, when the shares are fully paid, their transfer cannot be refused on the ground that the transferee is a minor. [Re Balaraman v. Buckingham and Carnatic co., p. 180]

3. No. The Company Law Board has recently decided that the registration of a transfer of shares in the name of a minor, acting through his or her guardian, especially when the shares are fully paid, cannot be refused on the ground that the transfered is a minor. (R. Balaraman v. Budkingham and Cranatic Co., p. 180)

4. No. Since the resolution of forfeiture was not passed by the directors, *X* continues to be a member. He is liable as a contributory and his liability is *ex-lege*.

5. No, *G's* contention is not justified in any way. In the event of winding up, the inability of a contributory is not *ex-contractu* but is *ex-lege* and flows from the fact that his name appears on the register of members. The validity of allotment of shares to *G* is not affected in any way. The only thing being that the shares could not be issued at a discount in the above manner. Hence, *G* can be held liable as a contributory with a liability to pay for the shares in full. [Ooregum Gold Mining Co. v. Roper, p. 138]

6. A will be liable for all the 200 shares by the very fact of subscription. The subscriber of the memorandum acquires, as soon as the company is registered, the full status of member with all the rights and liabilities. Neither application nor allotment of shares is necessary in his case [Official Liquidator v. Suleman Bhai, p. 177]

7. Yes, the contention of *X* is valid. Persons other than subscribers to memorandum should agree *i.e.* writing to become members of a company. [H.H. Mahabendra Shaw v. Official Liquidator, Indian Electric Tools Corporation Ltd., p. 176]

CHAPTER 11

1. No, *A* is not entitled to get the transfer registered in his name as it would amount to recognition of fraudulent certificate. But the company must compensate *A* for the loss he has sustained by acting on the faith of the share certificate. [Dixon v. Kennaway & Co., p. 141]

2. No, the application is not valid because it has not been made within the time allowed for making such an application under Sec. 111 of the Companies Act, 1956. [Sec. 111 (3), p. 201]

3. Yes. The power to refuse to register a transfer of shares must be exercised by a resolution of the board, majority of the board opposing registration. Since the board is equally divided, there being no casting vote, the power to refuse has not been exercised and, therefore, the transfer must be registered. [Re Hackney Pavilion, p. 200]

4. The company must remove the name of *C* and enter the name of *A* (the original owner) in the register of members. But the company is liable to indemnify *C*. On the other hand, the company is entitled to get damages from *B* who induced it to issue a share certificate on the basis of a forged transfer. [Forged transfer, p. 205]

CHAPTER 12

1. No, it is not obligatory for the company to appoint a third director. [Sec. 252, p. 211]

2. Yes. Out of three directorships offered to *A*, directorships of *BC* Private Ltd. and Indian Automobile Association are not to be counted within the limit of twenty directorship. Acceptance of directorship of *XYZ* Limited, a public limited company, will put the total number of directorships to twenty which is permitted by law. [Secs. 275 to 279, p. 214]

3. None. A bank, a partnership firm and a trust cannot be appointed as directors because Sec. 253 clearly lays down that only individuals can be appointed as directors. A minor is an individual but he is incompetent to enter into contracts. [Sec. 253, p. 210]

4. (*i*) If authorised by its articles or by a resolution passed by the company in general meeting, the board of directors may appoint an alternate director. Otherwise the company in general meeting can fill in the vacancy. [Sec. 313, p. 213]

(*ii*) If permitted by the articles, the board of directors may appoint an additional director. Otherwise the vacancy may be filled by the company in general meeting. [Sec. 260, p. 213]

(*iii*) A casual vacancy may be filled by the board of directors at its meeting and not by a resolution by circulation. [Sec. 262, p. 213]

5. (*i*) Refer to answer to Problem 4 (iii) of this Chapter.

(*ii*) Refer to answer to Problem 4(i) of this Chapter.

(*iii*) Refer to answer to Problem 4(ii) of this Chapter.

6. The company must alter its articles of association by passing a special resolution and the approval of the Central Government must also be obtained. [Sec. 259, p. 211]

7. A public company and its subsidiary private company cannot

provide in its articles that a person shall not be capable of being appointed as a director of a company if he is illiterate. However, an independent private company may do so. [Sec. 274, pp. 215-216; Cricket Club of India v. Madhav L. Apte, p. 216]

8. No. Where the articles provide for qualification shares, such qualification shares should be registered in the name of the director within two months of the appointment as director. Until the required number of shares are registered in the name of the director, he is not qualified. [Sec. 270, p. 215]

9. Yes, the call is perfectly valid and it can be enforce. Sec. 290 lays down that the acts of directors would be valid even if it is afterwards discovered that there was some defect in the appointment or qualifications of such directors. [Sec. 290, p. 280]

10. A public company and its subsidiary private company cannot lend money to their directors except with the previous approval of the Central Government. This restriction, however, does not apply to an independent private company and to a banking company [Sec. 295, p. 237]

11. In the above problem, there is a voilation of any provision of Sec. 295. The advance in question is not in the nature of a loan to directors for their personal purposes. However, directors must hold excess advance in trust for the company.

12. An interested directors shall not be taken into account for purposes of quorum. Since all directors are interested in the contract, a quorum cannot be formed at board meeting and, therefore, the company should refer the matter to the general meeting for approval. [Sec. 300, p. 235]

13. At least two disinterested directors are required to from a quorum at a board meeting. If all except one director are interested persons, a quorum is not formed and the meeting cannot transact the business validly. [Sec. 287, p. 279; Sec. 300, p. 235]

14. Directors are at liberty to proceed with the suit. Once the powers of management are vested in the directors, they and they alone can exercise these powers. Even a resolution of numerical majority at a general meeting cannot impose it-will on the directors when the articles have confined to them the control of the company's affairs. Directors are agents not of a majority of the shareholders, but of the company, of the whole entity made up of all the shareholders. [Automatic Self Cleansing, Etc. v. Cunninghame, p. 244]

15. The shareholder cannot repudiate the contract. Directors were under no obligation to disclose the negotiations to him. Directors occupy a fiduciary relationship only in relation to the company and not in relation to an individual shareholder. They are not trustees of individual

shareholders. [Percival v. Wright, p. 222]

16. Directors will be liable to compensate the company. Any provision in the company's articles or in any agreement which excludes liability for negligence, default, misfeasance, breach of duty or breach of trust, is void. [Sec. 201, p. 252]

17. (i) Approval of the company by a special resolution and also the prior approval of the Central Government are required. [Sec. 314, pp. 237]

(ii) Prior approval of the Central Government is required. [Sec. 295, p. 237]

(iii) Sanction of the general meeting by an ordinary resolution is required. [Sec. 293, p. 246]

18. Approval of the company by a special resolution is required. Since the monthly remuneration is less than twenty thousand rupees, approval of the Central Government is not required. [Sec. 314, p. 237]

19. Consent of the board of directors of the company and the prior approval of the Central Government are required. [Sec. 297 91), p. 234]

20. No, a person cannot be appointed as managing director of a company unless he is its director first. [Sec. 2(26), p. 254]

21. (a) Yes, her appointment in C Private Ltd. is valid since a person may be the managing director of any number of independent private companies.

(b) No, a person cannot act as a managing director of more than two companies at a time where at least one of the two companies is a public company or its subsidiary. [Sec. 316, p. 256]

CHAPTER 13

1. A public company limited by shares must hold a statutory meeting. [Sec. 165, p. 270]

2. No [Gardner v. Iredale, p. 271]

3. Yes. The meeting held on 31st March, 1935 was not a different meeting from the one which began on 30th December, 1934; it was the same meeting. Accordingly, the company can be prosecuted for not holding any meeting of the company in 1935. [Meenakshi Mills Co. Ltd. v. Asst. Registrar of Joint Stock Companies, p. 273]

4. Yes. A day declared by the Central Government as a public holiday will have no effect if the notice convening such meeting on that day has already been issued to the shareholders. [Sec. 2(38)

5. The directors are advised to apply to the Registrar for extension of time for holding the meeting under Sec. 166. [Sec. 166. p. 273]

6. Yes. [As per clarifications issued by the Deptt. of company Affairs, p. 274]

7. No. [Sec. 166, p. 273]

8. Any member may apply to the Company Law Board and the latter will call or direct the calling of the meeting and give such ancillary or consequential directions as it thinks expedient in relation to the calling, holding and conducting of the meeting. [Sec. 167, p. 274]

9. In the above problem, it is not mentioned whether the failure to give notice is accidental or deliberate. If the failure to send notice to twenty shareholders is purely accidental, it shall not invalidate the proceedings of the meeting and the business transacted at the meeting shall be valid inspite of such omission. But if the omission is deliberate or wilful, it shall invalidate the proceedings of the meeting. [Sec. 172, p. 285]

10. No, fresh notice of an adjourned meeting is not required because such a meeting is merely a continuation of the original meeting. But fresh notice of the adjourned meeting must be give if the original meeting was adjourned *sine die* or was adjourned for 30 days or more or if fresh business, other than such business as is left uncomplete at the original meeting, was to be discussed. In the above problem, the adjourned meeting shall become invalid if a fresh notice was required on account of reasons stated above. But if no fresh notice was required, the adjourned meeting and the proceedings of the meeting shall be valid.

11. Yes. 40 votes abstained will not be counted. [Sec. 189(2), p. 294]

12. The type of resolution required in each case is as follows:

(1) Ordinary Resolution,
(2) Special Resolution.
(3) Ordinary Resolution.
(4) Ordinary Resolution.
(5) Special Resolution.

13. The type of meeting at which the above items of business can be transacted are as follows:

(*i*) Shareholders' meeting.
(*ii*) Shareholders' meeting.
(*iii*) Shareholders' meeting.
(*iv*) Board Meeting.
(*v*) Meeting of debenture-holders.
(*vi*) Class meeting of preference shareholders.

14. No. Proxies are not entitled to vote in case of voting by a show of hands. They can vote only on a poll. Since there are only 5 votes in favour or the motion and 25 votes against the motion, the motion is lost. [Sec.

176, p. 289]

15. *X* Company Private Ltd. becomes a public company [Sec. 43-A(1)]. Secondly, the clause in the articles requiring very resolution to be passed by a majority of 75 per cent of the members present, is void *ab initio.* This is contrary to the provision of the Companies Act, 1956.

16. No, the company has not violated the provisions of Sec. 285 of the Companies Act, 1956. Sec. 285 requires at least one meeting of the board of directors in every three calendar months. In the above problem, the first meeting was held in the first quarter of 1977 and the second meeting was duly held in the second quarter of 1977. [Sec. 285, p. 278]

17. Yes. This is because he represents himself in two different capacities. Firstly, he is present in the meeting representing himself as a member. Secondly, Sec. 187 clearly lays down that a person representing a company in a general meeting is deemed to be personally present for the purpose of quorum. [Sec. 187(2), p. 286]

18. Yes. However, this is subject to the condition that the meeting was held by them within three months from the date of the deposit of the requisition. The requisitionists may hold the meeting at any suitable place if the registered office is not made available to them. [Sec. 169, p. 276; Rathanveluswami Chettiar v. Manickavelu Chettiar, p. 276]

19. No. Sec. 285 lays down that a board meeting must be held at least once in every three calendar months and at least 4 such meetings must be held in one calendar year. At the same time, Sec. 288 lays down that the provisions of Sec. 285 shall not be deemed to have been contravened by reason of the fact that a meeting of the board which had been called in compliance with the terms of that section could not be held for want of quorum. [Sec. 288, p. 279]

20. Yes, *X* can appoint a proxy to attend and vote instead of himself. [Sec. 187-A, p. 291]

21. (*i*) The vote given by the proxy will not be valid. Where a shareholder who, having appointed a proxy, personally attends and votes at the meeting, the proxy is revoked thereby and his right to vote is terminated. [Cousins v. Internation Brick Co., p. 291]

(*ii*) The vote cast by the proxy shall be invalid if the member appointing the proxy dies and the company comes to know of the death of the member before the commencement of the meeting. However, if the company has no notice of such death, the vote cast by the proxy shall be valid.

22. No, the proxy lodged is invalid because it has been executed only by one of the joint shareholders. Where shares are held jointly by two or more persons, all of them must sign the proxy form by which appointment is made.

CHAPTER 14

1. If the above company is a trading company, it has implied power to borrow as borrowing is incidental to trading. But if it is a non-trading company, its memorandum and articles must be altered to give such power before the company can borrow.

2. No. A company cannot borrow money on the security of reserve capital as the latter cannot be called except in the event and for the purpose of winding up of the company. [Bartlett v. Mayfair Property Co., p. 307]

3. The *ultra vires* lender will become a legal creditor of the company to the extent the money lent by him has been used to pay off legal debts (interest on debentures *A*) of the company. However, he will not be entitled to the priority of debentures *A*. [Neath Building Society v. Luce, p. 306; Re Wrexham Rly. Co., p. 306]

4. No, the plaintiff cannot recover the money from the company as the loan is *ultra vires* and void. But he can hold the directors personally liable for breach of warranty of authority. [Weeks v. Property, p. 306]

5. Sec. 534 defines the rights of a debenture holder with a floating charge. The charge shall be valid in full if it could be proved that the company was solvent on April 15, 1968. If the company was not solvent on that day, the charge shall be valid only to the extent of Rs 20,000 together with interest at the rate of five per cent. [Sec. 534, p. 310]

6. (*i*) The company or any interested party should make application to the Company Law Board for extension of time for registration of the charge with the Registrar. [Sec. 141, p. 314]

(*ii*) The charge shall be void against the liquidator and any creditor of the company. However, it shall remain good against the company. Money secured by the charge becomes immediately payable. [Sec. 125, p. 311]

CHAPTER 15

1. No. Where the annual general meeting of a company for any year has not been held on account of any reasons, there shall still be filed with the Registrar balance sheet and profit and loss account within 30 days from the latest day on or before which that meeting should have been held. [Sec. 220, p. 332]

2. Auditors are liable for misfeasance on account of their failure to report the above facts to the shareholders. An auditor is not discharged from his responsibility towards the members by simply giving them so much of information as is calculated to induce them to ask for more. Nor

is he discharged by giving shareholders means of information, instead of information. [Re London and General Bank (No. 2), p. 339]

3. A special resolution is required for the reappointment of M/s. Large & Co. as auditors. [Sec. 224-A, p. 334.

CHAPTER 16

1. The shareholder's resolution is not valid. The procedure for declaring dividend is that the board of directors will recommend a rate of dividend at the annual general meeting which is to be approved by the shareholders. The shareholders may reduce the rate of dividend but in no case do they have the right to increase the rate recommended by directors.

2. Since the meeting cannot increase the rate recommended by the board of directors, the dividend may be declared either at Rs 4 or at Rs 5 per equity share. The shareholders' suggestion that the dividend should be declared at Rs 6 per equity share cannot be executed.

3. No. Once a dividend is declared at an annual general meeting, a further dividend cannot be declared in respect of the same year at a subsequent general meeting. [Bishwanath Prasad v. New Central Jute Mills, p. 351]

4. The company can pay interest out of capital as per Sec. 208. [Sec. 208, p. 358]

5. Yes, the company can deduct from the dividend amount payable to *R* the sum of Rs 3,000 on account of calls in arrears under Regulation 89 of Table A.

CHAPTER 17

1. No, they will not succeed. [Foss v. Harbottle, pp. 360-361]

2. The suit filed by the minority shareholders is liable to be dismissed. If the directors are supported by the majority shareholders in what they do, the minority shareholders can do nothing about it. [Bhajekar v. Shinkar, pp. 361]

3. The majority resolution is void as it is neither just nor equitable, nor for the benefit of the company as a whole to purchase the shares of minority compulsorily. [Brown v. British Abrasive Wheel Co., p. 364]

4. The above alteration of articles of association is perfectly valid since it has been done *bona fide* and for the benefit of the company as a whole, individual hardship being irrelevant. [Sidebottom v. Kershaw, Leese &

Co., p. 364]

5. Yes, the minority shareholders can bring an action against the directors and hold them liable to account for profits made on the contract. The benefit of the contract belongs in equity to the company and the directors holding majority of votes cannot benefit themselves at the expense of the minority. [Cook v. Deeks, p. 363]

6. The proceedings of the meeting regarding election of directors are null and void. In the above problem, rejection of J's candidature for directorship is an individual wrong in respect of which a suit is maintainable. [Joseph v. Jos., p. 365]

CHAPTER 18

(*a*) Yes, *A* can proceed with his petition in the Company Law Board. Subsequent withdrawal of consent by some members will not affect the right of the applicant to proceed with the application. [Rajahmundry Electric Corporation v. A. Nageshwara Rao, p. 372]

(*b*) Yes, *A* must also show the circumstances justifying the making of a winding up order under the 'just and equitable' clause of Sec. 433. {Sec. 397, pp. 367-368]

2. The director is advised to apply to the Company Law Board under Sec. 409 for preventing the change in the board of directors which is likely to affect prejudicially the affairs of the company. [Sec. 409, p. 375]

3. The Company Law Board should reject the petition for no wrong has been done to them as members. A remedy under Sec. 397 is available to a member only in his capacity as a member and not in any other capacity. [Elder v. Elder and Watson Ltd., p. 369]

4. Yes. The right to apply for relief in case of oppression and mismanagement is not confined to oppressed minority alone. Relief can be granted even if the application is made by a majority, who have been rendered completely ineffective by the wrongful acts of the minority group. [In re Sindhri Iron Foundry (P) Ltd., p. 361.

CHAPTER 19

1. The above circumstances do not by themselves suggest either an intent to defraud or fraudulent management. Therefore, the order must be quashed. [Barium Chemicals Ltd. v. The Company Law Board, p. 379]

2. No. The above transactions may not be justified by commercial expediency but they are not suggestive of any fraud so as to justify an

order of investigation. [Jiyajeerao Cotton Mills v. The Company Law Board, p. 379]

3. No. It is only a breach of duty on the part of inspector and does not bring automatically the investigation to an end. [Ashoka Marketing Ltd. v. Union of India, pp. 381-382]

CHAPTER 20

1. There are two alternatives before *X* Co. Ltd.:

(*i*) *X* Co. Ltd. may acquire majority shares of *Y* Co. Ltd. under Sec. 395.

(*ii*) *X* Co. Ltd. may take over the assets and liabilities of *Y* Co Ltd. by entering into a scheme of compromise and arrangement under Sec. 391. [Sec. 395, pp. 391-392; Sec. 391, pp. 386-388]

2. Yes. Once the approval is accorded by at least nine-tenths in value of the shares whose transfer is involved, the transferee company is entitled to acquire the shares of even the dissenting shareholders on the terms on which the shares of other shareholders are to be transferred. [Sec. 395, pp. 391-392]

3. Yes, these creditors will succeed on the ground that the directors had failed to disclose material facts regarding the company's financial position. [Sec. 391, p. 386-388]

CHAPTER 21

1. No. The court may, instead of making winding up order, extend the time and fix a date for holding the meeting. [Sec. 433(3), pp. 396-397]

2. The court should dismiss the petition since the suspension is well accounted for and appears to be due to temporary or unavoidable causes and there is *bona fide* intention of the company to commence its business when conditions improve. [Re Middlesborough Assembly Rooms Co., p. 397]

3. No, the court will not order winding up on the ground that the company had not transacted any business in India. The requirement of law is that the company must commence its business within a year of its incorporation. This requirement is duly met in the above problem since the company carried on its business abroad in its first year. [Re Capital Fire Insurance Association, p. 397]

4. The company should be wound up by the court. Once a creditor has made a proper demand and there is a failure on the part of the company

to meet the creditor's demand within the prescribed period, winding up order shall be made and the commercial solvency of the company is of no relevance. [Hariprasad v. A.C. Traders Ltd., p. 399]

5. No, the court will not order the winding up of the company. The proper course for the Official Assignee is to make an appeal to the Company Law Board against the refusal of the company to register the transfer. Alternatively, he may apply for rectification of register of members. [Sec. 111]

6. The court will order the winding up of the company. The substratum of the company has failed and it is impossible to carry out the objects for which it was formed and, therefore, it is just and equitable that the company should be wound up. [Re German Date Coffee Co., p. 400]

7. The court should order the winding up of the company. In the above problem, there is justifiable lack of confidence in the conduct and management of the company's affairs and this constitutes a just and equitable ground for making a winding up order. [Loch v. John Blackwood Ltd., p. 400]

8. Refer to answer to Problem 6 of this Chapter.

9. No, G's contention is not justified in any way. In the event of winding up, the liability of a contributory is not *ex-contractu* but is *ex-lege* and flows from the fact that his name appears on the register of members. The validity of allotment of *G* is not affected in any way. The only thing being that the shares could not be issued at a discount in the above manner. Hence, *G* can be held liable as a contributory with a liability to pay for the shares in full. [Ooregum Gold Mining Co. v. Roper, p. 138]

10. Yes, a holder of fully paid-up shares can be placed on the list of contributories for the purpose of distribution of assets and other procedural purposes. But his liability is nil and he has not to contribute anything to the assets of the company. [Re Aidall Ltd., p. 423]

11. The transferor shall be placed on the list of contributories (List *A*) since his name appears in the register of members on the commencement of winding up. The transferee does not become a member of the company until the transfer is registered and his name is entered on the register of members.

12. The liquidator can realise from the contributories the amount barred by limitation where such amount is due on account of non-payment of calls. But this will not apply to the amount (time-barred) due on account of goods purchased from the company on credit by the contributory. [Sec. 429, pp. 425-426]

13. No, the claim of the Income Tax Department will not be upheld because the arrears of income tax have become due more than twelve months before the date of winding up of the order. [January 1967].

Hence, the Income Tax Department will not be treated as a preferential creditor for Rs 10,000. [Sec. 530, p. 430]

14. If it could be proved that the company was solvent on 15 March 1959, the charge will be valid to the full extent and *X* will be a secured creditor of the company for the whold of the amount. On the other hand, if the company was not solvent on that date, the charge will be invalid and *X* will be an unsecured creditor. However, *X* will be a securecd creditor to the extent of amount advanced in consideration of the charge plus interest at the rate of 5 per cent. [Sec. 534, p. 431]

CHAPTER 22

1. Yes, it can be wound up as an unregistered company. [Sec. 584, p. 437]

CHAPTER 23

1. Yes. [Sec. 560(6), p. 442.

2. The court should refuse to order restoration because the company could not be said to be in operation or business and in view of the disputes between the members of the family, it could not carry on business in future. [In re Mandal's (UN) Estate (Pvt) Ltd., p. 442]

Appendix II

TEXT OF SEBI GUIDELINES

Following is the text of the guidelines issued by the Securities and Exchange Board of India (SEBI) on 11-6-1992:

These guidelines will be applied to all issues to be made after the promulgation of the Ordinance No 9 of 1992 by which the Capital Issues (Control) Act has been repealed. All those, holding CCI consent prior to the promulgation of the Ordinance may proceed with the issues on the terms and conditions laid down therein, provided however that these guidelines are also followed where they are not inconsistent with the terms and conditions of the CCI consent.

A. First issue of companies:

A new company will be defined as one which has not completed 12 months of commercial operations and its audited operative results are not available, and where it is set up by entrepreneurs without a track record. They will be permitted to issue capital to public at par.

Where a new company is being set up by existing companies with a five year track record of consistent profitability, it will be free to price its issue provided the participation of the promoting company and the issue price is made applicable to all new investors uniformly, provided that the prospectus or offer documents shall contain justification for issue price.

A draft prospectus containing the disclosures will be vetted by Securities and Exchange Board of India before a public issue is made.

No private placement of the promoters share shall be made by solicitation of share contribution from un-related investors through any kind of market intermediaries. The shares of the above companies can be listed on either the Over the Counter Exchange of India or any other stock exchanges.

B. First issue by existing private closely held companies:

(i) Such companies with a three year track record of consistent profitability shall be permitted to freely price the issue and list their securities on the stock exchanges.

(ii) Not less than 20 per cent of the equity should be offered. (iii) The draft prospectus will be vetted by SEBI to ensure adequacy of disclosures. (iv) The pricing would be determined by the issuer and lead managers to the issue and would be subject to specific disclosure requirements including:

(a) disclosures of the net assets value of the company as per the last audited balance sheet

(b) justification for the issue price.

C. Public issue by existing listed companies:

(a) These companies will be allowed to raise fresh capital by freely pricing their further issues. (b) Pricing - the issue price will be determined by the issuer in consultation with the lead manager(s) to the issue. (c) Disclosures (i) Draft prospectus will be vetted by SEBI to ensure adequacy of disclosures.

(ii) The prospectus or offer documents shall contain the net asset value of the company and a justification for the price of the issue. (iii) High and low price of the shares for the last two years.

D. Underwriting

(a) Underwriting is mandatory for the full issue and minimum requirement of 90 per cent subscription is also mandatory for each issue of capital to the public. Number of underwriters would be decided by the issuers.

(b) If the company does not receive 90 per cent of issued amount from public subscription plus accepted devolvement from underwriters, within 120 days from the date of opening of the issue, the company shall refund the amount subscribed. In case of disputed devolvement, the company should refund the subscription if the above conditions are not met.

(c) The lead manager(s) must satisfy themselves about the net worth of the underwriters and outstanding commitments and disclose the same to SEBI. (d) The underwriting agreements may be filed with the stock exchanges.

E. Composite issues

Issues to the public by existing company can be priced differentially as compared to the issues to the rights shareholders.

F. Fully convertible debentures/partially convertible debentures/ non-convertible debentures:

(a) Issue of FCDs having a conversion period of more than 36 months will not be permissible, unless conversion is made optional with "put" and "call" option. (b) Compulsory credit rating will be required if conversion is made of FCDs after 18 months. (c) Premium amount on conversion, time of conversion, in stages, if any, shall be pre-determined and stated in the prospectus. The interest rates for above debentures will be freely determined by the issuer: (d) Issue of debenture with maturity of 18 months or less are exempt from the requirement of appointment of Debenture Trustee or creating a Debenture Redemption Reserve (DRR). In other cases, the names of the debenture trustees must be stated in the prospectus and DRR will be created in accordance with Section (N.1). The trust deed shall be executed within six months of the closure of the issue.

(e) Any conversion in part or whole of the debenture will be optional at

the hands of the debenture holder, if the conversion takes place at or after 18 months from the date of allotment, but before 36 months.

(f) In case of NCDs/PCDs credit rating is compulsory when maturity exceeds 18 months. (g) Premium amount at the time of conversion for the PCD shall be pre-determined and stated in the prospectus. Redemption amount, period of maturity, yield on redemption for the PCD/s NCDs shall be indicated in the prospectus.

(h) The discount on the non-convertible portion of the PCD in case they are traded and procedure for their purchase on spot trading basis must be disclosed in the prospectus.

(i) In case, the non-convertible portions of PCD/NCD are to be rolled over with or without change in the interest rate a compulsory option should be given to those debenture holders who want to withdraw and encash from the debenture programme. Roll over shall be done only in cases where debenture holders have sent their positive consent and not on the basis of their negative reply.

(j) Before roll over of any NCD or non-convertible portion of the PCDs, fresh credit rating shall be obtained within a period of six months prior to the due date of redemption and communicated to debenture holders before roll over and fresh trust deed shall be made.

(k) Letter of information regarding roll over shall be vetted by SEBI with regard to the credit rating, debenture holder resolution, option for conversion and such other items which SEBI may prescribe from time to time. (l) The disclosure relating to raising of debentures will contain amongst other things, the existing and future equity and long-term debt ratio, servicing behaviour on existing debentures, payment of due interest on due dates on term loans and debentures, certificate from a financial institution or bankers about their no-objection for a second or pari passu charge being created in favour of the trustees to the proposed debenture issues.

(m) SEBI may prescribe additional disclosure requirement from time to time, after due notice.

G. New Financial instruments:

Issuer of capital shall make adequate disclosures regarding the terms and conditions of redemption, security, conversion and any other relevant features of instruments such as Deep Discount Bonds, Debentures with Warrants, Secured premium notes etc., so that an investor can make reasonable determination of the risks, returns, safety and liquidity of the instruments. The disclosures shall be vetted by SEBI in this regard.

H. Reservation in Issues:

(a) Unreserved offer of equity or instruments convertible into equity shall

not be less than the minimum required for listing purposes in case of new issues made either by the new company or by the existing closely held/private companies going public.

(b) in case of issues of capital by new companies, reservations for employees of new companies, promoting companies, associate companies, working directors on a suitable percentage is permissible.

(c) Shareholders of group companies in case of existing companies can be offered capital on a preferential basis.

(d) Shareholders of promoters companies shall also be eligible for preferential allotment.

(e) Reservations for NRIs shall be according to the schemes prescribed by RBI from time to time.

I. Deployment of issue proceeds

(a) In case of issues, where on application and on allotment an amount together exceeding Rs 250 crore is raised, the issuer will voluntarily disclose and make arrangements for the use of proceeds of the issue as per disclosure to be monitored by one of the financial institutions. A copy of their monitoring report shall be filed with the SEBI by the institutions and by the company for purposes of record.

(b) In issue of the above size and beyond, the amount to be called up on application/allotment and on various calls should not exceed 25 per cent of the total quantum of issue.

J. Minimum interval time between two issues

(a) No bonus issues shall be made within 12 months of any public/rights issue.

(b) The promoters shall bring in capital in full before public issue.

(c) The capital issue should be made fully paid up within 12 months from the date of issue.

K. Employee stock option scheme

This is a voluntary scheme on the part of the company to encourage employees to have higher participation in the company. Suitable percentage of reservation can be made by the issuer for the employees of his company or the promoters of the company as the need may arise. Reservation should not be more than five per cent. Equitable distribution of shares among the employees will contribute to the smooth working of the scheme. The issuer may like to have non-transferability at his discretion in new-issues. In other cases, employees participation upto five per cent (maximum 200 shares) shall be non-transferable for a period of three years.

L. Promoter's contribution and lock-in period

(a) Equity capital to be subscribed in any issue to the public by the

promoters i.e. those described as the promoters, directors, friends, relatives and associates should not be less than 25 per cent of the total issue of equity capital up to Rs 100 crore and 20 per cent of the issues above Rs 100 crore. In the case of FCDs, one third of the issue amount should be contributed by promoters, directors, friends, relatives and associates by way of equity before issue is made. In case of PCDs, one third of the convertible portion should be brought in as contribution of promoters, directors, friends, relatives and associates before issue is made. Minimum subscription by each of the friends/ relatives and associates under promoters quota should not be less than Rs one lakh.

(b) This promoter's contribution shall not be diluted for a lock-in period of five years from the date of commencement of the production or date of allotment which ever is later. Promoters must bring in their full subscription to issues in advance before public issue.

(c) All firm allotments, preferential allotments to collaborators, shareholders of promoter companies whether corporate or individual shall not be transferable for three years from the date of commencement of production or date of allotment whichever is later.

(d) The share certificate issued to promoters, friends, relatives and associates etc. should carry the inscription "not transferable" for a period of three to five years as may be applicable from the date of commencement of production or date of allotment whichever is later.

M. Bonus Shares

[*Issued by the Primary Market Department of SEBI vide Press Release dated* 13.4.1994].

In keeping with current pace of liberalisation and reforms in the Primary Market, the Board of SEBI has decided to modify the extant guidelines for bonus shares, forming Section M of the Guidelines for Disclosure and Investor Protection issued by SEBI on June 11, 1992.

SEBI believes that the Board of Directors of the companies wishing to make bonus issues will take into due consideration the relevant financial factors while deciding on bonus issues and observe the following guidelines:

Section M

(a) These guidelines are applicable to existing listed companies who shall forward a certificate duly signed by the issuer and duly countersigned by its statutory auditor or by a company secretary in practice to the effect that the terms and conditions for issue of bonus shares as laid down in these guidelines have been complied with.

(b) Issue of bonus shares after any public/rights issue is subject to the condition that no bonus issue shall be made which will dilute the value or rights of the holders of debenture, convertible fully or partly. In other words, no company shall, pending conversion of FDCs/PCDs, issue any shares by way of bonus unless similar benefit is extended to the holders of such FDCs/PCDs, through reservation of shares in proportion to such convertible part of FCDs or PCDs. The shares so

reserved may be issued at the time of conversion(s) of such debentures on the same terms on which the bonus issues were made.

(c) The bonus issue is made out of free reserves built out of the genuine profits or share premium collected in cash only.

(d) Reserves created by revaluation of fixed assets are not capitalised.

(e) The declaration of bonus issue, in lieu of dividend, is not made.

(f) The bonus issue is not made unless the partly-paid shares, if any existing, are made fully paid-up.

(g) The company—

1. has not defaulted in payment of interest or principal in respect of fixed deposits and interest on existing debentures or principal on redemption thereof, and

2. has sufficient reason to believe that it has not defaulted in respect of the payment of statutory dues of the employees such as contribution to provident fund, gratuity, bonus etc.

(h) A company which announces its bonus issue after the approval of the Board of Directors must implement the proposals within a period of six months from the date of such approval and shall not have the option of changing the decision.

(i) There should be a provision in the Articles of Association of the company for capitalisation of reserves, etc. and if not, the company shall pass a Resolution at its General Body Meeting making provisions in the Articles of Association for capitalisation.

(j) Consequent to the issue of bonus shares if the subscribed and paid-up capital exceed the authorised share capital, a Resolution shall be passed by the company at its General Body Meeting for increasing the authorised capital.

(k) No bonus issue shall be made within 12 months of any public/rights issue.

It may be noted here that the revised guidelines have done away with certain requirements relating to the issue of bonus shares, namely, Profitability Test, Residual Reserve Test, etc.

N. Guidelines for the protection of the interest of debentureholders and Servicing of debentures

Subject to provisions of Section F, a debenture redemption reserve (DRR) shall be created by all the companies raising debentures on the following basis:

(a) A moratorium upto the date of commercial production can be provided for creation of the debenture redemption reserve in respect of debentures raised for project finance.

(b) The debentures redemptions reserve may be created either in equal instalments for the remaining period or higher amounts if profits permit.

(c) In the case of partly convertible debentures, DRR should be created in respect of non convertible portion of debenture issue on the same lines as applicable for fully non convertible debenture issue. In respect of convertible

issues by new companies, the creation of DRR should commence from the year the company earns profits for the remaining life of debentures.

(d) Companies may distribute dividends out of general reserves in certain years if residual profits after transfer to DRR are inadequate to distribute reasonable dividends.

(e) DRR will be treated as a part of general reserve for consideration of bonus issue proposals and for price fixation related to post-tax return.

(f) In case of new companies, distribution of dividend shall require approval of the trustees to the issue and the lead institution, if any.

(g) Company should create DRR equivalent to 50 per cent of the amount of debenture issue before debenture redemption commences. Drawal from DRR is permissible only after 10 per cent of the debenture liability has been actually redeemed by the company.

(h) In the case of existing companies, prior permission of the lead institution for declaring dividend exceeding 20 per cent or as per the loan convenants is necessary if the company does not comply with institutional condition regarding interest and debt service coverage ratio.

(i) Company may redeem debentures in greater number of instalments. The first instalment may start from 5th instead of 7th year.

Protection of debenture holders' interest

(a) Trustees to the debenture issue shall be vested with the requisite powers for protecting the interest of debenture holders including a right to appoint a nominee director on the board of the company in consultation with institutional debenture holders.

(b) Lead institution/investment institution will monitor the progress in respect of debentures for project finance/modernization/expansion/diversification/normal capital expenditure. The lead bank for the company will monitor debentures raised for working capital funds.

(c) Institutional debenture holders and trustees should obtain a certificate from the company's auditors in respect of utilization of funds during the implementation period of projects. In the case of debentures for working capital, certificate should be obtained at the end of each accounting year.

(d) Debenture issues by companies belonging to the groups for financing replenishing funds or acquiring shareholding in other companies will not be permitted.

(e) The companies shall, along with their application, file with SEBI, certificates from their bankers that the assets on which security is to be created are free from any encumbrances and the necessary permissions to mortgage the assets have been obtained or a no objection certificate from the financial institutions or banks for a second or pari passu charge in cases where assets are encumbered. The security should be created within six months from the date of issue of debentures. If for any reasons, the compa-

nies are not in a position to create security within 12 months from the date of issue of debentures, the company shall be liable to pay 2 per cent penal interest to debenture holders. If security is not created even after 18 months, a meeting of the debentures holders should be called within 21 days to explain the reasons thereof and the date by which the security would be created.

(f). The trustees to the debenture holders will supervise the implementation of the conditions regarding creating of security for the debentures and regarding the debenture redemption reserve.

General

(a) Subscription list for public issues should be kept open for at least three working days and disclosed in the prospectus.

(b) Rights issues should not be kept open for more than 60 days.

(c) The quantum of issue, whether through a right or public issue, shall not exceed the amount specified in the prospectus/letter of offer. No retention of over subscription is permissible.

(d) Within 45 days of the closures of an issue, a report in a prescribed form with a compliance certificate from the chartered accounts should be forwarded to SEBI by the lead managers.

(e) The gap between the closure dates of various issue, e.g., rights and Indian public should not exceed 30 days.

(f) In case of issues of debentures fully or partly made in the past, where the conversion was to be made at a price to be determined by the Controller of Capital Issues at a later date, the price of conversion and time of conversion shall be determined by the company in a duly organised meeting of the debenture holders and shareholders. The decision in the above meeting may be ratified by the shareholders in their meeting. Such conversions will be optional for acceptance on the part of individual debenture holders. The dissenting debenture holders shall have the right to continue as debenture holders if the terms of conversion are not acceptable to them. The letter of option to debenture holders should be vetted by SEBI.

(g) SEBI will have right to prescribe further guidelines for modifying the existing ones to bring about adequate investor protection, enhance the quality of disclosures and to bring about transparency in the primary market.

(h) SEBI shall have right to issue necessary clarification to these guidelines to remove any difficulty in its implementation.

(i) Any violation of the guidelines by the issuers/intermediaries will be punishable by prosecution by SEBI under the SEBI Act.

(j) The provisions in the Companies Act, 1956, and other applicable law shall be complied with in connection with issue of shares and debentures.