CHAPTER 14

RECONSTRUCTION AND AMALGAMATION

Ch. 14.1. Reconstruction :

A reconstruction takes place, when a Company's business and undertakings are transferred to another Company, formed for that purpose. The new company does the same business as the old one.

This reconstruction may become necessary

i) When a court does not allow major changes in the existing Company or

(ii) When the rights of share holders are to be changed. The new objects or changes may be made by the process of reconstruction.

Ch. 14.2. Amalgamation :

Amalgamation is not defined in the Companies Act. The ordinary meaning is Combination. The objective of amalgamation of one Company with another is to facilitate the reconstruction of the Amalgamating Company. This is the pereogative of the shareholders and an affair coming within the internal administra-tion of the companies.

The company should have a provision for amalgamation in the M/A. If not it may duly amend to include the power to amalgamate.

Amalgamation takes place where two or more companies combine to form another Company or when one Company absorbs another.

Forms : Amalgamation takes place in any of the following methods:

i) By sale of shares

ii) By sale of undertaking

iii) By sale and dissolution

iv) By a scheme of arrangement v) By Central Government in National interest **Procedure:**

The Companies Act has provided for a detailed procedure for Amalgamation.

The scheme for amalgamation made by the Company is to be approved by the court. The court makes its decision on the Report of the Company Law Board or Registrar. This Report must show that the Amalgamation was made for the benefit of the Company and not prejudicial to its members and creditors The courts objective is to protect public interest.

The scheme must be fair if the court is to approve the

amalgamation.

It must hear the Central Government before deciding. In Wood P'olymer Ltd. Company's case, the court held that the only purpose of amalgamation was to transfer the buildings to a new company to avoid Capital gains tax. The court refused to approve the amalgamation.

Certain restrictions have been imposed to prevent the tendency f making monopolies, e.g.

i) Restrictions relating to acquisition of shares.

ii) The court refusing to give the sanction

iii) The approval of the Central Government for such amalgamation.

14.2. Amalgamation in National Interest (Sn. 396) :

Besides the usual modes of amalgamation provided for in Sns. '94 and 395, occasions may arise when it may be desirable in the oiblic interest that 2 or more companies should amalgamate.

When amalgamation in the National interest is clearly a necessity, the observance of the usual procedure will lead to delay and may be detrimental to the public interests.

A special rule is, therefore made to amalgamate 2 or more Companies in such cases.

The Central Government may be order notified in the official gazette, amalgamate two or more companies, in public interest.

The powers, functions, rights, liabilities, privileges etc. of the amalgamated Company are stated by the Government in its order.

Every member or creditor of each of the combining, companies shall have as nearly as he had in the earlier companies as may be, the same interest in or rights against the Company. But if his interest is less in the new Company, he is entitled to compensation.

Before amalgamation, the Central Government should send a copy of the proposal to amalgamate, to each of the Companies. This enables the would be amalgamating companies, to file objections if any, within the time fixed by the Government (2 months).

Copies of order to amalgamate should be laid before both Houses of Parliament, by the Government at the earliest convenience.

CHAPTER 15

WINDING UP

Ch. 15.1. Winding Up

Winding up is a process whereby the life of the Company is ended and its property administered for the benefit of its creditors and members. A liquidator is appointed who takes control of the Company, collects its assets, pays its debts and finally distributes any surplus among the members in accordance with their rights (Gower).

Winding up, precedes dissolution. This means the status of the Company continues until the winding up proceedings are completed. Thereupon it is dissolved. Its life comes to an end.

Modes :

The Companies Act provides for 3 modes of Winding up :

1. Compulsory winding up under the orders of the court.
2. Voluntary winding up.
3. Voluntary winding up under the supervision of the court.

Ch. 15.2. Compulsory winding up :

Winding up on the orders of a court is called compulsory winding up.

1. Application or petition may be filed to the court by (a) the Company (b) A shareholder (c) The Registrar (d) A contributory (e) Central Government, as the case may be.

2. The circumstances for winding up are :

a) By special resolution:

By a special resolution, the General Meeting, may decide to wind up the company. The court at its discretion may order for winding up.

b) Not holding statutory meeting :

A company which has failed to hold its statutory meeting or submit its report, may be ordered to be wound up by the court. This may be done on the petition of the Registrar or a contributory.

c) Not commencing business:

If business is not carried on, or is suspended for one year and above, the court may order to wind up. The petition may be made by any shareholder (Muralidar V. Bengal Steamship Co.). The Company employed a steamer and took two flats for its business. During World War II, the Government acquired them. Hence, no business for one year. Held, no reason to windup.

d) Reduction in Membership:

When the number goes down below 7 (Public Companies) or 2 (Private Companies), the court may order for winding up.

e) Inability to pay debts:

1. To the creditors

cases :

i) Vanaspati Industries V. Dayal.
ii) Govardha Das V. Madhu Wollen Industries.

2. To the decreed debts case :
Mehta V. Steel Equipment.

Just and equitable grounds:

This is resorted to after giving due weight to the interests of the Company, its creditors, shareholders, its employees and in general public interest.

e.g. 1. Deadlock in the management: Yendije Tobacco Co. Ltd. case. In this case hostility developed between the only two Directors of a private Company resulting in a deadlock - court ordered winding up, even though business was good.

2. Squeezing the minority, by oppression.

3. Main object itself is lost or not materialising.

Ch. 15.3 Voluntary winding up :

1. A/A :

The provisions relating to voluntary winding up contained in the A/A are to be followed.

2. Special Resolution:

B a 3/4 majority the General Meeting should resolve to wind up the Company, Winding up commences from the date of the resolution. But the status and powers continue, until finally dissolved. The business comes to a stop, except so far as is necessary for the beneficial winding up.

3. Notification:

Gazette and newspaper notification should be given within 14 days of the resolution.

4. Solvency test :

A majority of the Directors, with an affidavit, may make a declaration about solvency of the Company and its capacity to pay within a maximum of 3 years. Such a declaration must be made by a special resolution and registered with the Registrar. Copies of profit and loss accounts, Balance Sheet and Assets and liabilities should also be filed. The objective is to make the winding up the members choice.

If the above procedure is not followed it becomes creditor's choice of voluntary winding up. If the Directors fail to pay within 3 years as per declaration then also it is creditors choice to wind up.

In member's winding up, a liquidator is appointed and his remuneration is fixed by the general meeting. This is reported to the Registrar. The liquidator should call a meeting of the shareholders within a year and present the accounts. He files the document with the registrar and the official liquidator. If the accounts are not prejudicial he reports to the court. The court if satisfied with the Report, orders dissolution.

In the Creditors winding up, the official liquidator also calls a meting of the creditors. The other procedures are the same as in Member's winding up.

Ch. 15.4. Official Liquidator:

1. The Central Government by notification in the official gazette may appoint, attached to each High Court an Official liquidator and an official receiver attached to district court.

2. It is the duty of the official liquidator to conduct the proceedings in the winding up of the company and also to perform such other duties as directed by the court.

3. Directors statement:

The Directors should submit a statement of the affairs of the Company, with all details of assets and liabilities etc., to the official liquidator within 21 days of the winding up order of the court. Within 6 months, the liquidator should submit a preliminary report to the Court furnishing all details and the progress made. He must submit accounts to the court twice a year and file a copy with the Registrar. He must send copies to the creditors and contributories.

4. Powers:

With the sanction of the court the liquidator may exercise the following powers:

i) To institute or defend any suit or prosecution in the name and on behalf of the company.

ii) To carry on the business, for beneficial winding up.

iii) To sell movable and immovable properties and actionable claims (by auction or otherwise),

iv) To raise any requisite money, on the security of the asset.

v) To do all other things as may be necessary for winding up.

5. Other powers:

He has many other powers which he can exercise without the sanction of the court.

i) To execute all documents with the seal of the company,

ii) To inspect the records, and the returns of the company,

iii) To draw or accept any Negotiable Instruments P/N, B/E, draft, cheque on behalf of the Company,

iv) To collect money from contributories. v) Any other power incidental thereto.

***6.* Duties :**

He must call the meetings of the Members or Creditors or Contributories as the case may be as provided under the winding up proceedings.

7. Removal:

He may be removed and necessary action taken by the Central Government, on complaint received for the dereliction of duty, abuse or misuse of authority.

8. Dissolution:

The official liquidator continues to exercise his powers, until the court makes its order of dissolution of the company.

9. Filing :

The liquidator files a copy of the order with the Registrar.

Ch: 15. 5. Effects (or consequences) of winding up : ..

Winding Up :

Winding up is a process whereby the life of a company is ended & its property administered for the benefit of its creditors and members. The liquidator appointed takes control of the company, collects its assets, pays its debts and finally distributes any surplus among the members according to their rights.

When the winding up proceedings are completed, the company is dissolved and its life comes to an end.

The modes of winding up may be

i) under orders of the Court, ii) voluntary of iii) winding up under the supervision of the court.

Effects:

Winding up of the company has many consequences or effects. These are to be examined with reference to : i) Contributories. ii) Creditors, iii) Officers, Servants, iv) The Company,

i) **Effects on contributories, members.**

Means every person who is liable to contribute to the assets of the company in the event of its winding up. The definition includes past and present members.

As Pennington,,leading authority, says the term 'Contributory' is misleading. It seems to be confined to holders of partly paid up shares, or members of a company limited by guarantee, and

members of an unlimited company.

The courts have held that a fully paid up shareholder is also a contributory. But such a member has nothing to contribute towards payment of the company's debts, but he has an interest in the company meeting its debts and paying surplus, If any, to the members.

Liability: It is not contractual, but it is ex lege i.e., by virtue of his name in the register as a shareholder (member).

The liability arises only when the winding up court makes an order, and a call-notice is served on the contributory. This becomes a debt. Hence, the unpaid balance of the share-amount should be paid by the contributory to the company.

The liability extends to the past members also. But a past member is not liable if he had ceased to be a member for one year before the commencement of winding up.

The primary liability is on the present members. It may then be on the past members subjects to certain conditions, as per the Companies Act.

Members :

Transfer of shares by members after the commencement of winding up proceedings is void in case of voluntary winding up. In case of winding up under court order, the transfer of share is void unless the court otherwise directs. (Sn. 536)

ii) Effect on Creditors:-

The creditors to the company may be secured, or unsecured creditors.

A secured creditor may rely upon the security offered to him, and, ignore the liquidator. He may realise his dues from the security. But, he may, in the alternative, Join the unsecured Creditors & claim & abandon his security.

In respect of unsecured creditor the Companies Act, puts all of them equally and provides for payment pari passu.

iii) Officers Servants etc.

Officers of a Company mean, Directors, Secretaries, Treasurers, Managers, but does not include an Auditor. But, it includes an accountant and Cashier.

According to the Companies Act, on the winding up, the directors etc cease to have their powers.

The officers are liable for misfeasance or breach of trust. They are subject to examination by the court. The court may order for restoring the property or money to the company in case of breach of

trust or misappropriation.

The Palani Central Bank's case payment of dividend was made by showing false entries under profits.

It was held that though there was no fraud, there was gross & culpable negligence and hence directors etc were liable.

Criminal liability:-

Under Sn 539, the officers of a company are liable for punishment for falsification, destruction, mutilation etc of books of account papers, securities of the company, if the intention is to defraud any person^

Failure to keep proper accounts is also punishable.

However, if the offer has acted honestly & reasonably in the circumstances then the court may relieve him (Sn. 633).

iv. Effects on proceedings against company.

When the winding up proceedings start, the court under Sn. 442, stays all suits against the company.

After the winding up order is made by the Court, no suit or legal proceedings can be initiated by any person, against the company except with the permission of the Court.

For example income tax proceedings can continue with the permission of the court. Similarly secured creditors should take the permission of the Court, if they proceed against the "Security" that belongs to the company.

CHAPTER 16
I MISCELLANEOUS

Ch. 16.1. Investigation:

The Central Government may appoint inspectors to investigate into the affairs of any Company and to report thereon (Sns. 235,236).

Under S. 237 the Central Government shall initiate investigation, if the Company by a Special resolution, or the Court by an order, declares that the affairs of a Company ought to be investigated. The Inspectors may, if directed by the Central Government, make an interim report to the Government and shall make a final report at the conclusion of the investigation. A copy of it, is to be given to the Company.

If from the report, it appears that any official is guilty of a criminal offence against the Company, the Central Government may give legal notice and institute a prosecution against such persons.

The Government has powers to start proceedings (Sn. 234) :

i) For the winding up of the Company on the ground that it is just and equitable to do so (through petition).

ii) For relief in case of oppression and mis-management.

iii) For the recovery of damages in respect of any fraud, misfeasance or other misconduct in connection with the promotion or formation or management of the affairs of the Company.

iv) For recovery of any property which has been mis-applied or wrongfully retained.

The expenses of investigation shall be borne by the Government in the first Instance. It may be recovered from the convicted person or from persons who are to pay damages or from the Company to the extent of property recovered by it.

Ch. 16.2. Committee of Inspection:

The court, at the time of an order for winding up of a Company or at any time thereafter, direct that there shall be appointed a Committee of inspection to act with the liquidator. The liquidator shall, within two months from the date of such director convene a meeting of the creditors of the Company for the purpose of determining who are to be the members of the Committee.

It shall consist of not more than 12 members (being creditors and contributories of the Company). It shall have the right to inspect the accounts of the liquidator. It shall meet at suitable intervals. It acts on majority decision. There must be a quorum for its meetings. It is a coordinating body.

Ch. 16.3. Contributories (Sn. 428):

Means every person who is liable to contribute to the assets of the Company in the event of its winding up. The definition includes past and present members.

As Pennington points out, the term contributory is misleading. It seems to be confined to holders of partly paid up shares, or members of a Company limited by guarantee and members of an unlimited company.

The courts have held that a fully paid up shareholders is also a contributory. But such a member has nothing to contribute towards payment of the company's debts, but he has an interest in the Company meeting its debts and paying surplus, if any, to the members.

Liability : It is not contractual, but it is ex lege i.e., by virtue of his name in the register as a shareholder (member).

The liability arises only when the winding up court makes an order, and a call notice is served on the contributory. In case of Voluntary winding, the "Call" may be made by the liquidator, without the orders of the Court. This becomes a debt. Hence, the unpaid balance of the share amount should be paid by the contributory to the Company.

The liability extends to the past members also. But a past member is not liable if he had ceased be a member for one year before the commencement of winding up.

The primary liability is on the present members; it may then be on the past members, subject to certain conditions, as per the Companies Act.

Ch. 16.4. Conversion of Private Company into Public :

A Private Company has many privileges and exemptions and it may enjoy these benefits, as long as it maintains its character as a Private Company. When this character is lost, the private company becomes public and the provisions of the Company act relating to public companies become applicable to such a company.

Circumstances:

i) Default: The Court may examine to find out whether any provisions of the Companies Act have been violated by the Company. If the default is due to inadvertence or some sufficient cause based on just and equitable grounds, the court may declare that Company as Private; otherwise as public.

ii) Operation of Law: Deemed Public Company:

a) Conversion: No public money is to be involved in a Private company. But a Public Company may incorporate a number of Private Companies who may still maintain private character. These

are not allowed to have the privileges of a private company. Hence, it is provided (Sn 43-A) that if 25% or more of the paid up capital is held by a Public company, such a private company becomes public.

b) Turnover: As per 1988 Amendment, if the turnover exceeds a sum fixed by Central Govt. the company becomes public. This conversion is effective on the expiry of three months from the end of the accounting year.

c) Notice: Notice, within 3 months of such a Private Company becoming public, must be given to the Registrar, who shall effect the necessary changes.

d) Special features : Such a deemed Public company may (i) retain the characteristics of a Private company (ii) the membership may be below 7.

iii) Conversion by Choice: A private company may by passing a special resolution, changing its articles, convert itself into a Public Company. Within 30 days it must file a prospectus (or statement in lieu of prospectus) with the registrar. It must comply with all other requirements of a public company, e.g. increasing the membership to 7, appointment of Directors etc.

Ch. 16.5. Conversion of a Public Company into Private Company:

A Public Company may be passing a Special Resolution, changing its articles, convert itself into Private Company. However, the approval of the Central Government is essential, for such a change.

Ch. 16.6. Foreign Companies:

a) It is a company incorporated outside India. It is still a Foreign Company, if it has a place of business in India. However, such a company must file the relevant documents with the Registrar of the State (where incorporated) and also at New Delhi.

i) Certified copy of its charter or M/A and A/A

ii) Address and Place of Business.

iii) List of Directors and Secretary - their names and addresses.

iv) Contact person to serve notice etc.

b) If this procedure is not followed, the foreign company, may do business, but it cannot sue in the courts in India.

c) It may issue a prospectus, but must comply with all the requirements of the Companies Act.

d) It must maintain its accounts and file its balance sheets etc., as per the Companies Act.

Ch. *16. 7.* Government Companies (Sn. 617):

It is a company in which the paid up shares capital of fifty one percent and is held by the central Government or by a State Government or by State Governments or jointly by Central Government and State Governments. It includes a subsidiary company of a Government Company.

Some special provisions are applicable to such Government Companies.

i) The auditors of such companies are appointed by the Central Government on the advice of the Controller and Auditor General of India. The Auditor prepares annual audit report, which shall be submitted to the Annual General Body Meeting.

ii) Within 3 months of such meeting, a report on the affairs of the company should be placed before the Parliament or the State legislature, as the case may be.

iii) The Central Government by Gazette Notification declares what provisions of the Companies Act are applicable to such companies. It shall not appoint any Managing Agent. Further, the Govt. Company is not an Agent of the Govt.(Central or state) It has a juristic personality of its own. All other provisions of Companies Act are applicable to it.

Ch. 16.8. Holding Company and Subsidiary: Sn. 4.

a) Definition: Where one company called H is having control over another company called S, H is Holding Company and S is the subsidiary.

b) Modes of Formation:

i) If H Company controls the Board of Directors of S company, H is a holding company and S is the subsidiary.

ii) If H company holds a majority of the shares in S company, then H is a holding company and S, a subsidiary.

iii) If S company is subsidiary of H and C company is a subsidiary of S company, then C company is a subsidiary of H. (Majority holdings, or power of appointment of Directors in the test) :

c) Special Provisions:

i) The Holding Company should submit its Report to the Registrar, along with the balance sheet, audit report etc., of each of its subsidiary.

ii) A subsidiary is not allowed to have its membership or shares in the holding company.

Ch. 16.9. Bonus shares:

A Company which has undistributed profits may convert that into shares capital, by issuing bonus shares. These are ordinary shares, issued as fully paid up shares. These are issued in proportion to the holdings of the shareholders e.g. one bonus share to every 3 shares held.

The A/A must authorise the company to convert its accumulated undivided profits into bonus shares.

The bonus shares are financed from the above undivided profits, or from share premium account or from Capital Redemption Reserve Account.

Ch. 16.10. "Company Law Board" (Sn. 10 E) :

The Companies Act has provided for a Company Law Board to exercise those powers and to discharge those functions fixed on the Central Government by the Companies Act.

1. Composition:

It consists of 9 members. One of them is appointed as the Chairman, by the Central Government.

2. Powers and functions:

The Board is empowered:

i) To confirm any alteration of M/A or A/A

ii) To issue shares at a discount

iii) To call a general meeting.

3. Judicial Powers:

It is deemed to be a Civil Court. The Board has the powers of the Civil court in the following:

i) Inspection of documentary evidence,

ii) To enforce attendance of witnesses,

iii) To examine witnesses on Oath.

iv) To punish for Contempt of the Board.

v) To execute its orders.

4. Appeal:

From the orders of the Board, appeal is allowed to the High court, by any person who is aggrieved by the order, within 15 days from the date of receipt of such order on any question of law.

Ch. 16.11: Defunct Company: Sn. 560.

If a Company exists for name's sake without doing any business as per its M/A or A/A, but continues on the register of Companies in the Registrar's office, without being dissolved, the Registrar is empowered under Sn.560 to strike off the name of the Company from the register. The reason is, no useful purpose is served by continuing its name in the Register Before doing so, he should issue notices and

if no reply is received, he should publish in official Gazette., Then after giving 3 months notice, he may strike off the name, in which case, the Company stands dissolved.

Courts Power:

If the Company, or a member or a creditor is aggrieved, a application may be filed to restore the name on the register. If the Court is satisfied, at its discretion, it may issue on order to restore the name of the Company in the Register.

Courts have power to declare such removal as void. (Wood V. Martin]

The period of limitation is 20 years.

[Purushotham Dass V. Registrar]

THE END