# 8 COMPANY FAILURE – WINDING-UP AND INSOLVENCY

## 8.1 Introduction

The insolvency of a company is akin to the serious illness of a physical person; the winding up of the company (or its liquidation, as it is also called) is its death. It used to be that insolvency was a precursor to liquidation. This has been changed by the recent enactment of the Insolvency Act 2013, which allows the survival of a company which is in financial difficulty. On the other hand, companies which are not in financial difficulty can also be wound up, and usually are through the process of voluntary liquidation.

The Companies Act, 1972 which had hitherto been the sole repository of the substantive law regarding winding up (the procedural law being in the Companies (Winding up) Regulations 1975) has now been joined by the Insolvency Act which in many respects duplicates the provisions of the Companies Act, without repealing them. Consequently, the two statutes will have to be read together.

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| **Insolvency Act 2013, section 388** |
| The provisions of this Act shall be in addition to and not in derogation of the provisions of the Companies Act. |

## 8.2 Winding up

This is the process by which a company’s assets are collected and realised, its debts paid and any surplus distributed in accordance with its articles of association (usually among the shareholders, pro rata). In order to complete the process, a company which is liquidated is dissolved. Winding up can be either voluntary or compulsory (by the court).

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| **Section 202 (1)** |
| The winding up of a company may be either -  (a) by the court; or  (b) voluntary. |

### 8.2.1 Compulsory Winding up

This occurs where the court orders the company wound up upon an application made by a person having the right to do so. This mode of winding up is called winding up by the court in both Acts.

#### 8.2.1.1 Grounds

The grounds in the Companies Act are the following six:

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| **Companies Act, section 205** |
| (a) the company has by special resolution resolved that the company be wound up by the court;  (b) the company does not commence its business within a year from its incorporation or suspends its business for a whole year;  (c) the number of members is reduced below two;  (d) the company is unable to pay its debts;  (e) the company is a proprietary company and a ground exists on which the court may make an order expelling a member (other than the petitioner) from membership of the company; [[1]](#footnote-1)  (f) the court is of opinion that it is just and equitable that the company should be wound up. |

To these the Insolvency Act has added another three:

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| **Insolvency Act 2013, Section 96** |
| (e) the directors have acted in the affairs of the company in their own interests rather than in the interests of the shareholders as a whole, or in any other manner which is unfair or unjust to other shareholders;  (f) the directors or managers of the company have acted to conceal the assets of the company or remove  the assets of the company outside the jurisdiction with intent to defeat the creditors;  (g) the period, if any, fixed for the duration of the company by its memorandum and articles has expired or the event, if any, on the occurrence of which  the memorandum  and articles provides that the company is to be dissolved, has occurred. |

With regard to the ground of inability to pay debts, both Acts make provision for certain deeming provisions in order to prove the ground. These are identical in both Acts and are to be found in sections 206 and 97 respectively. In the following instances a company is deemed to be unable to prove its debts and thus is liable to be wound up under ground (d):

* A creditor has served a notice on the company requiring it to pay R1000 (under the Companies Act) or R10,000 (under the Insolvency Act) and the company has failed to pay the same for a period of three weeks[[2]](#footnote-2)
* Execution of a judgment against the company has returned unsatisfied in whole or in part
* The debts of the company exceed its immediately realisable assets.

With regard to the just and equitable ground, UK courts have held the following to be included under the ground:

* the loss of substratum
* deadlock
* oppression of minority shareholders
* companies acting as partnerships.

The Seychelles courts have had occasion to consider the loss of substratum in two cases. In *In re Societe d’Exploitation Hoteliere, Touristique et Commerciale de l’Ocean Indien Ltd* [1984] SLR 129, the court refused to order a winding up on the basis that there was a possibility that the company could undertake its objects later and asked the company to consider a voluntary liquidation. In *In re Ailee Development Corporation* SCA 13/08, LC 344, the Court of Appeal considered that the substratum had disappeared where the main object of the company had become impracticable, including where the conduct of the management had given rise to a justifiable lack of confidence in it.

#### 8.1.1.2 Who may Petition?

Under the Companies Act the following persons may petition the court for the liquidation of a company:

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| **Section 207** |
| (a) the company; or  (b) any creditor or creditors (including any contingent or prospective creditor or  creditors); or  (c) any shareholder; or  (d) any contributory; or  (e) any debenture holder; or  (f) any persons belonging to two or more of the foregoing categories together; or  (g) the Registrar under section 190(3). |

The Insolvency Act (section 98) has added two further possible petitioners:

(f) A liquidator

(g) An administrator when the company is in reorganisation.

However, the vast majority of petitions are by creditors.

A winding up petition is usually filed supported by affidavit of the facts and supporting documents. The petition is usually determined on affidavits, and not after a contested hearing, although there is no reason why in appropriate cases a hearing may not be conducted.

#### 8.1.1.3 Powers of Court

The court has very wide powers under section 208 of the Companies Act and 100 of the Insolvency Act. These include:

* Making a winding up order
* Dismissing the petition
* Adjourning the petition conditionally or unconditionally
* Adjourning to enable reorganisation
* Making any other order deemed fit.

If the court makes a winding up order, the procedure for winding up now starts. This is described below.

### 8.2.2 Voluntary Winding up

There are two modes of voluntary winding up – by members, or by creditors.

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| **Section 247 (1)** |
| A company shall be wound up voluntarily if -  (a) a general meeting of the company so resolves by special resolution; or  (b) a general meeting of the company so resolves by an ordinary resolution which states that the company is unable to pay its debts. |

The first provision above is a members voluntary winding up, and is made when the company is solvent. The second is a creditors voluntary winding up, and is limited to cases where the company is insolvent. In a members winding up, the directors of the company must first, within 5 weeks of the passing of the resolution, make a written declaration of solvency to the effect that they have carried out an inspection of the affairs of the company and they have concluded that it is able to pay its debts: s 253 CA; s 151 IA. This is not required for a creditors voluntary winding up.

Any member or shareholder of the company can apply to the court within 14 days for the cancellation of the resolution voluntarily winding up a company.

Once the resolution is passed, this must be advertised in the Gazette within 7 days (s 248) and, within the same period, notified to the Registrar of Companies (s 249).

The company must then cease to carry on business, except in connection with the winding up: s 251. It will appoint a liquidator in a general meeting: s 255 CA; s 152 IA and the liquidator will proceed with the winding up of the company.

The members winding up can, at any time that the liquidator concludes that the company is unable to fully pay its debts, be converted into a creditors voluntary winding up: s 257 CA; s 154 IA.

## 8.3 Liquidators

In a court winding up a provisional liquidator can be appointed even before the winding up order is made: s 211 CA; s 112 IA. This will usually be when the company is in deep financial trouble and the outcome of the hearing of the winding up petition cannot be awaited. The court has power to restrict the powers of the provisional liquidator as is required by the exigencies of the matter.

Where the court had given the provisional liquidator extensive powers to bring in the assets of the company in liquidation, the court held that these included the power to institute proceedings without court authority: *Michel (Provisional Liquidator Awilsel Ltd) v Anglo Welsh Investment Limited* [1979] SLR 77.

After a winding up order is made, the court can appoint a liquidator to wind up the affairs of the company. This may be a person chosen by the court or the Official Receiver. A body corporate cannot be a liquidator: s CA; s 167 IA. If a provisional liquidator has been appointed, it is usual for that person to become the liquidator: s 217 CA; s 113 IA.

The powers of the liquidator appointed by the court are extensive. They are divided into two categories – power to be exercised subject to the sanction of the court (or the committee of inspection) and power to be exercised without sanction of the court.

### 8.3.1 Powers subject to court sanction (s 222 (1) CA; s 119 (1) IA):

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| **Section 222 (1) Companies Act** |
| (a) to bring or defend any action or other legal proceeding in the name and on behalf of the company;  (b) to carry on the business of the company, so far as may be necessary for the beneficial winding up thereof;  (c) to appoint a legal adviser or agent to assist him in the performance of his duties;  (d) to pay any creditors in full if the assets of the company remaining in his hands will suffice to pay in full the debts and liabilities of the company which rank for payment before, or equally with, the debts or claims of the first mentioned creditors;  (e) to make any compromise or arrangement with creditors or debenture holders or persons claiming to be creditors or debenture holders, or having or alleging themselves to have any claim, present or future, certain or contingent, ascertained or sounding only in damages against the company, or whereby the company may be rendered liable;  (f) to compromise all calls and liabilities to calls, debts, and liabilities capable of  resulting in debts and all claims, present or future, certain or contingent, ascertained  or sounding only in damages, subsisting or supposed to subsist between the company and a contributory, or alleged contributory, or other debtor or person apprehending liability to the company, and all questions in any way relating to or affecting the assets or the winding up of the company, on such terms as may be agreed, and take any security for the discharge of any such call, debt, liability or claim, and give a complete discharge in respect thereof. |

### 8.3.2 Powers not requiring court sanction (s 222 (2) CA; s 119 (2) IA):

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| **Section 222 (2) Companies Act** |
| (a) to sell the assets of the company by public auction or private contract, with power to transfer the whole thereof to any person or company, or to sell the same in parcels;  (b) to do all acts and to execute, in the name and on behalf of the company, all deeds, instruments, receipts, and other documents, and for that purpose to have instruments authenticated by notarial act;  (c) to prove, rank, and claim in the bankruptcy, insolvency, or winding up of any contributory, for any amount owing to the company, and to receive dividends in the bankruptcy, insolvency, or winding up in respect of that amount;  (d) to draw, accept, make, and indorse any bill of exchange, cheque or promissory note in the name and on behalf of the company, with the same effect with respect to the liability of the company as if the bill, cheque or note had been drawn, accepted, made, or indorsed by or on behalf of the company in the course of its business;  (e) to raise on the security of the assets of the comраnу any money required for the  purposes of the winding up;  (f) to take out in his official name letters of administration or representation to the estate of any deceased contributory, and to do in his official name any other act necessary for obtaining payment of any money due from a contributory or his estate or its assets which cannot be conveniently done in the name of the company, and in all such cases the money due shall, for the purpose of enabling the liquidator to take out the letters of administration or representation or to recover the money, be deemed to be due to the liquidator himself;  (g) to appoint an agent to do any business which the liquidator is unable to do himself;  (h) to do all such other things as may be necessary for winding up the affairs of the company and distributing its assets. |

One of the principal duties of the liquidator in a winding up is to ensure that fraudulent trading by the officers of the company prior to the winding up is corrected.

## 8.4 Fraudulent Trading

The liquidator (or any creditor, shareholder, contributory, debenture holder) has the power, during the course of the liquidation of the company, to take action through the court against any director or officer of the company who has conducted the affairs of the company fraudulently. This is a drastic action as it results in the director being personally liable for the loss to the company caused by his or her actions. This then contributes to the assets of the company in liquidation. What constitutes fraudulent trading is set out in section 290 of the Companies Act:

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| **290 (1)** |
| If in the course of the winding up of a company it appears that any business of the company has been carried on:-  (a) with intent to defraud creditors of the company or the creditors of any other person, or for any fraudulent purpose; or  (b) with reckless disregard of the company’s obligation to pay its debts and liabilities; or  (c) with reckless disregard of the insufficiency of the company’s assets to satisfy its debts and liabilities |

Under the Insolvency Act 2013, fraudulent trading is now categorised as voidable preference and voidable transactions: ss 324, 330.

The liquidator is released when the affairs of the company have been fully wound up: s 228 CA.

## 8.5 Committee of Inspection

In a court winding up, the creditors and shareholders may appoint a committee of inspection to act with the liquidator to ensure that the respective rights of both sets of persons are respected: s CA; s 229; s 123 IA. The liquidator, once the winding up order has been made, is an agent of the creditors and shareholders and not the petitioner any longer. To that end, the liquidator must take into consideration, during the course of the winding up, the directions given to him or her by the creditors and shareholders: s 223 CA.

## 8.6 Dissolution of Company

Once the process of liquidation is over, it is time to bury the dead company. This process is called the dissolution of the company. This is done by the court upon application made: s 245, 259 CA.

## 8.7 Insolvency Act Innovations

As part of its modernising of the law of insolvency, including company insolvency, the Insolvency Act makes provision for the reorganisation of companies in difficulty as an alternative to liquidation. The most important innovation is Company Reorganisation under Part VI of the Act. This allows the company, liquidator or the court to appoint an administrator to take control of the affairs of the company, protect its assets, prepare a rescue plan and effectively put an ailing company back on the road to recovery.

1. Only a shareholder may petition on this ground [↑](#footnote-ref-1)
2. The court has no power to extend this period: *Tropicolor (Pty) Ltd v Hetherington & Ors* 1990 SCAR [↑](#footnote-ref-2)