

Block**5****DIVIDEND, ACCOUNTS, AUDIT AND
WINDING UP**

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BLOCK 5 DIVIDEND, ACCOUNTS, AUDIT AND WINDING UP

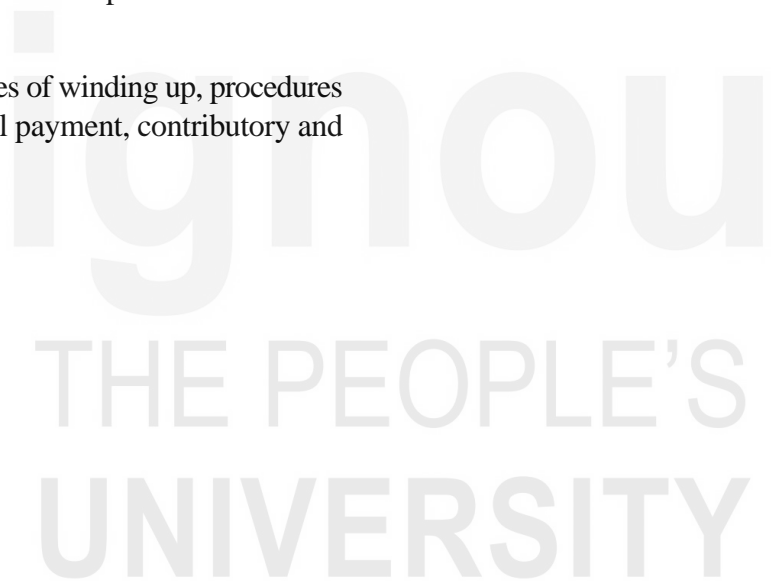
This block consists of the following four units.

Unit 17: It explains the meaning and provisions relating to dividend, sources of dividend, interim dividend. It further explains payment of dividend, unpaid dividend and investor education and protection fund.

Unit 18 : It discusses books of account, inspection of books of account, persons responsible for keeping books of account, account books of a branch, period for which account books are to be retained. It further explains reopening of accounts on court/tribunal order, voluntary revision of financial statement and provisions relating to books of account.

Unit 19 : It deals with audit, provisions relating to audit, appointment of an auditor, disqualifications of an auditor, first auditor, subsequent auditor, tenure and ceiling. It also covers rotation of an auditor, auditor's report and secretariat audit.

Unit 20 : It explains the concept of winding up, modes of winding up, procedures for winding up order. It further explains preferential payment, contributory and removal of name of the company.



UNIT 17 DIVIDEND

Structure

- 17.0 Objectives
- 17.1 Introduction
- 17.2 Meaning of Dividend
 - 17.2.1 Provisions Relating to Dividend
- 17.3 Sources of Dividend
 - 17.3.1 Declaration of Dividend
 - 17.3.2 Interim Dividend
- 17.4 Payment of Dividend
- 17.5 Unpaid Dividend
- 17.6 Investor Education and Protection Fund
- 17.7 Let Us Sum Up
- 17.8 Key Words
- 17.9 Answers to Check Your Progress
- 17.10 Terminal Questions

17.0 OBJECTIVES

After studying this Unit, you should be able to:

- explain the meaning of a dividend;
- describe provisions relating to dividend and its declaration;
- explain the sources of dividend and interim dividend;
- distinguish between paid and unpaid dividend; and
- explain Investor Education and Protection Fund.

17.1 INTRODUCTION

There is a difference between profit and divisible profit. All profits of a company are not divisible. Divisible profits are profits available for distribution. The profit available for dividend means profits which the directors consider should be distributed after making provision for past losses, transfer to reserves or for other purposes. In this unit you will learn about meaning and provisions relating to dividend, sources of dividend, declaration of dividend, You will also learn about payment of dividend, unpaid dividend and investor education and protection fund.

17.2 MEANING OF DIVIDEND

The word 'Dividend' has not been defined in the Act. Section 2 (35) says "Dividend includes any interim dividend". In **CIT vs Girdhar Das & Co. (P)**

Ltd (1967) 21 Comp. L J Supreme Court defined 'Dividend' as under:

"As applied to a company, which is a going concern, it ordinarily means the portion of the profit of the company which is allocated to the holders of shares in the Company". Thus, it is the share of company's profit distributed among the members not retained in the company".

Bonus shares issued by capitalising accumulated profits to existing shareholders are not dividend. Equity shares with 'differential rights as to dividend and voting' can be issued by a company (Section 43(a) (ii)).

17.2.1 Provisions Relating to Dividend

The provisions relating to dividend are as follows:

- i) A company may, if so authorised by its articles, pay dividend in proportion to the amount paid up on each shares (Section 51).
- ii) The amount of dividend, including interim dividend shall be deposited in a scheduled bank in a separate account within five days from the date of declaration of dividend.
- iii) The dividend shall be paid to registered shareholders only or to his order or to his banker. No dividend shall be payable except in cash. Any dividend payable in cash may be paid by cheque or warrant or any other electronic mode.
- iv) In case of preference shares dividend is always paid at a fixed rate.
- v) No dividend can be paid if the provisions under section 73 and 76 relating to acceptance of public deposit are not complied with.
- vi) The dividend not claimed within thirty days from declaration date shall be transferred to 'unpaid dividend account'.

17.3 SOURCES OF DIVIDEND

The dividend may be paid:

- i) Out of profits of current financial year after deducting depreciation in accordance with provisions of Schedule II **or**
- ii) Out of profits for any previous financial year or years arrived at after providing for depreciation as per schedule II and remaining undistributed or out of the reserves **or**

Out of Both (i) and (ii)

But in computing profits any amount representing unrealised gains, notional gains or revaluation of assets and any change in carrying amount of an assets or of a liability on measurement of the asset or liability at fair value shall be excluded **or**

- iii) Out of money provided by Central or State Government for payment of dividend by the company in pursuance of a guarantee given by that government.
 - a) Provided the company may, before declaration of dividend in any financial year, as it may consider appropriate transfer such percentage of its profits to the Reserves.

- b) Provided due to inadequate or absence of profits in any financial year, any company proposes to declare dividend out of accumulated profits earned by it in previous years and transferred by company to the free reserves, such declaration shall be made according to rules framed by Central Government.

17.3.1 Declaration of Dividend

- i) No Dividend shall be declared or paid by a company from its reserves other than free reserves.
- ii) A company shall not declare dividend unless carried over previous losses and depreciation not provided in previous year or years are set off against profits of the company of the current year.
- iii) A company which fails to comply with provisions of Section 73 and 74 (acceptance and repayment of public deposits) shall not, so long as such failure continues, declare any dividend on its equity shares.
- iv) In case of preference shares, under Section 43(a), payment of dividend, either a fixed amount or an amount calculated at a fixed rate, which may either be free of or subject to income tax, be paid before equity shares.
- v) The company in annual general meeting may declare dividend, but no dividend shall exceed the amount recommended by the Board (Table F(80)). However a company which could not declare dividend at an annual general meeting may do so at a subsequent general meeting.

17.3.2 Interim Dividend

A company may distribute a part of the profits before its final accounts are passed and dividends are declared in the annual general meeting. Such dividends are called “Interim Dividends”.

The provisions relating to interim dividend as per section 123(3) are as follows:

- 1) The Board of Directors of a company may declare interim dividend during any financial year or at any time during the period from closure of financial year till holding of annual general meeting out of the surplus in the profits and loss account or out of profits of the financial year in which such interim dividend is sought to be declared or out of profits generated in the financial year till quarter preceding the date of declaration of the interim dividend.

Provided that in case the company incurred loss during the financial year upto the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during immediately preceding three financial years.

- 2) Table F(81) lays down that subject to Section 123, the Board may from time to time pay to the members such interim dividend as appear to it to be justified by the profits of the company.
- 3) Interim dividend like final dividend is considered as a debt due. Directors cannot revoke it by a resolution except under circumstances under which final dividend may be revoked.

A general meeting cannot pass a resolution for payment of interim dividend. It may rescind it before payment is made.

Check Your Progress A

- 1) What is dividend?
.....
.....
.....
.....
- 3) What is interim dividend?
.....
.....
.....
- 4) State whether the following statement are True or False.
 - a) Decision by directors to pay an interim dividend does not create a debt.
 - b) Preference Shares have an inherent right to a fixed dividend.
 - c) Payment of dividend can be effected by credit to a shareholders account.
 - d) Divisible profits and profits are the same.
 - e) A decision for payment of final dividend can be revoked.

17.4 PAYMENT OF DIVIDEND

- i) No dividend shall be paid by a company except to the registered shareholder of such share or to his order or to his banker.
- ii) If transfer of shares has not been registered, it shall transfer dividend to 'Unpaid Dividend Account'.

The shareholder can authorise company in writing to pay dividend to the transferee as mentioned in instrument of transfer.
- iii) No dividend shall be paid except in cash or by cheque or by electric mode or by warrant. However, capitalisation of profit or reserves of the company for the purpose of issuing fully paid up bonus shares or paying up any amount, for the time being unpaid on any shares held by the members of the company is not prohibited.
- iv) In case of joint shareholders, dividend shall be paid to shareholder whose name appears first in the register of members, or such person and to such address as the holder or joint holders may in writing direct.
- v) The amount of dividend, including interim dividend, shall be deposited in a scheduled bank within five days of the date of declaration of such dividend by the company (except a Government Company).
- vi) Dividend warrant or cheque should be posted within thirty days. It is not an offence if the shareholder does not receives it or not within this time.

Penalty : In case of failure to distribute dividend, every director of the company,

if he is knowingly a party to the default, be punishable with imprisonment which may extend to two years and with fine, which shall not be less than one thousand rupees for every day during which such a default continues and company shall be liable to pay simple interest at the rate of eighteen percent per annum during the period for which such default continues

Defences:

- a) Where the dividend could not be paid by reason of the operation of any law.
- b) Where a shareholder has given direction to the company regarding the payment of dividend and those directions cannot be complied with and the same has been communicated to him.
- c) Where there is a dispute regarding the right to receive the dividend.
- d) Where dividend has been lawfully adjusted by the company against any sum due to it.
- e) Where for any other reasons, failure to pay the dividend or to post the warrant within the specified period was not due to any default on the part of the company.

17.5 UNPAID AND UNCLAIMED DIVIDEND

According to Section 124 where a dividend has been declared by a company but has not been paid or claimed within thirty days from the date of declaration to any shareholder entitled to the payment of the dividend, the company shall, within seven days from the date of expiry of the said period of thirty days, transfer the total amount of dividend which remains unpaid or unclaimed to a special account to be opened by the company in that behalf in any scheduled bank to be called "unpaid dividend account".

The company shall within a period of ninety days of making any transfer to unpaid dividend account prepare a statement containing names, their last known address and the unpaid dividend to be paid to each person and place it on the website of the company, if any or any other website.

If any default is made in transferring the total amount, it shall pay from the date of such default, interest on so much of the amount as has not been transferred, the company shall pay interest at the rate of 12% p.a.

Any person claiming dividend shall apply to the company. All money transferred to unpaid dividend account, unpaid or unclaimed for a period of seven years shall be transferred to the fund established under section 125(1) **Investor Education and Protection Fund** to be managed by administrating authority of the fund, which will issue a receipt to the company.

All shares in respect of which dividend has not been paid or claimed for seven consecutive years or more shall be transferred by the company in the name of aforesaid Fund. However any claimant of shares transferred above shall be entitled to claim the transfer of shares from Investor Educational Protection Fund in accordance with such procedure and on submission of such document as may be prescribed.

Penalty : If the company fails to comply with any requirements of this section,

the company shall be punishable with fine which shall not be less than five lakh rupees, but which may be extended to twenty five lakhs rupees and every officer of the company who is in default shall be punishable with fine which shall not be less than one lakh rupee but which may extend to five lakh rupees. [Sub Section (7)].

17.6 INVESTOR EDUCATION AND PROTECTION FUND

The Central Government set up this Fund Under Companies Act, 1956. The Companies Act, 2013, under section 125 lays down the sources and purposes for which the fund monies can be utilised. An authority called “Investor Education and Protection Fund Authority” administers it. It has a chairperson, members not exceeding seven and a Chief Executive Officer.

Sources: The following amount shall be credited to the funds:

- a) The amount given by Central Government by way of grants after due appropriation made by Parliament by law in this behalf for being utilised for the purposes of the fund;
- b) Donations given to the Fund by the Central Government, State Governments, companies or any other institution;
- c) The amount in the Unpaid Dividend Account of Companies;
- d) The amount in the general revenue account of the Central Government and amount lying in the Fund under the Companies Act 1956 as it stood immediately before the commencement of the Companies (Amendment) Act 1999 and remaining unpaid or unclaimed on the Commencement of this Act.
- e) The amount lying in the investor Education and Protection Fund under Section 205C of Companies Act, 1956.
- f) Interest or other income received out of investment made from the fund;
- g) Amount received under section 38(4) i.e., amount received through disgorgement or disposal of securities;
- h) The application money received by companies for allotment of any securities and due for refund;
- i) Matured deposits with companies (except banking companies);
- j) Matured debentures with companies;
- k) Interest accrued on amounts referred above in (g) and (h);
- l) Sale proceeds of fractional shares arising out of issuance of bonus shares, merger and amalgamation for seven or more years;
- m) Redemption amount of preference shares remaining unpaid or unclaimed for seven or more years.
- n) Such other amount as may be prescribed.

Amount referred in (h) to (j) will not form part of the fund unless such amount has remained unclaimed and unpaid for a period of seven years from the date it became due for payment.

Utilisation : The fund shall be utilized for :

- a) The refund in respect of unclaimed dividends, matured deposits, matured debentures, application money due for refund and interest thereon;
- b) Promotion of investors’ education, awareness and protection;
- c) Distribution of any disgorged amount among eligible and identifiable applicants for shares, or debentures, shareholders, debenture holders or depositors who have suffered losses due to wrong action by any person, in accordance with the orders made by the court which has ordered disgorgement;
- d) Reimbursement of legal expenses incurred in pursuing class action suits by members, debenture holders or depositors as may be sanctioned by the Tribunal; and
- e) Any other purpose incidental thereto.

Check Your Progress B

1) What is investor education and investor fund?

.....

2) What are the penalties if the dividend is not paid by the Company?

.....

3) Mention any four sources of ‘Investor Education and Protection Fund’.

.....

4) Fill in the blanks:

- a) The shareholder can transfer in writing the dividend to
- b) In case of joint shareholders, dividend should be paid to
- c) The dividend declared by a company has not been paid or claimed within thirty days is transferred to.....
- d) All shares in respect of which dividend has not been paid or claimed for a period of seven consecutive years shall be transferred by the company to.....

17.7 LET US SUM UP

There is a difference between profits and divisible profits available for. It may be paid out of profits or past revenues. Dividend is paid at a fixed rate amount to preference shareholders. Interim Dividend is dividend paid between two annual general meetings. Dividend is paid to registered shareholder or to his order or

to his banker. Dividend, including interim dividend shall be deposited in a scheduled bank in a separate account within five days from its declaration. Dividend payable in cash may be paid by cheque or warrant. Unclaimed and unpaid dividend within 30 days from its declaration, shall be deposited in separate account 'unpaid dividend account' within 7 days after expiry of said 30 days by the company. The amount in the unpaid account is transferred to 'Investor Education and Protection Fund'. The dividend is to be credited to this fund should not have been paid or claimed for seven consecutive years or more.

17.8 KEY WORDS

Dividend: It is that share of company's profit which is distributed among the members.

Interim Dividend : The dividend that is declared and paid in the middle of an accounting year before a company has determined its year earnings, of the year.

Investor Education and Protection Fund (IEPF): The fund created by the Central Government under provisions of Company Act. The fund is utilised for promoting investor awareness and protection of investor interest.

17.9 ANSWER TO CHECK YOUR PROGRESS

- A) 4 (a) false (b) true (c) true (d) false (e) false
B) 4 (a) to any person (b) shareholder whose name appears first
(c) unclaimed dividend account (d) Investor Education and Protection Fund

17.10 TERMINAL QUESTIONS

- 1) What are the provision of the Act relating to unpaid and unclaimed dividend?
- 2) Discuss "Investor education and protection fund".
- 3) "Dividend cannot be paid by a company except out of profit". Discuss.
- 4) Explain the rules relating to interim dividend.
- 5) What provisions and rules have been observed by a company before declaring dividend?

Note: These questions will help you to understand the unit better. Try to write answers for them but do not submit your answers to the University. These are for your practice only.

UNIT 18 ACCOUNTS

Structure

- 18.0 Objectives
- 18.1 Introduction
- 18.2 Books of Account to be Kept
- 18.3 Inspection of Books of Account
 - 18.3.1 Persons Responsible for Keeping Books of Account
 - 18.3.2 Books of Account of a Branch
 - 18.3.3 Period for which Account Books to be Retained
 - 18.3.4 Reopening of Accounts on Court or Tribunal Order
 - 18.3.5 Voluntary Revision of Financial Statements
- 18.4 Financial Statements
- 18.5 Provisions Relating to Books of Accounts
- 18.6 Corporate Social Responsibility Committee
- 18.7 Let Us Sum Up
- 18.8 Key Words
- 18.9 Answers to Check Your Progress
- 18.10 Terminal Questions

18.0 OBJECTIVES

After studying this Unit, you should be able to:

- describe the books of account kept by a company and persons responsible for keeping them;
- explain how inspection of books of account is done;
- discuss voluntary revisions of financial statements and accounts books of a branch;
- describe the various legal provisions relating to books of account; and
- discuss about corporate social responsibility committee.

18.1 INTRODUCTION

The 'books of account' are to be maintained by a company as per Companies Act. The form of Balance Sheet and Profit and Loss Account is prescribed in schedule III of the Act. In consolidated financial statements additional information is to be given of parent and subsidiaries (Indian and Foreign), minority interest in all subsidiaries Associates (Indian and Foreign) and Joint Ventures (Indian and Foreign). The Financial statements should be prepared according to prescribed accounting standards. The rates of depreciation for assets are prescribed in Schedule II. In this unit you will study about Books of Accounts

to be kept, inspection of Books of Accounts, Persons responsible for keeping them and accounts books of a branches. You will also learn about period for which these books are retained, reopening of books of account and provisions relating to book of account and corporate social responsibility committee.

18.2 BOOKS OF ACCOUNT TO BE KEPT

The Books of Account include record maintained with respect to :

- a) All sums of money received and expended by the company and the matters in respect of which receipts and expenditure take place;
- b) All sales and purchases of goods by the company;
- c) All assets and liabilities of the company; and
- d) The items of cost as may be prescribed (Section 2(13)).

Every Company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statements for every financial year which give a true and fair view of the state of affairs of the company, including that of its branch office or offices, if any, and explain transactions effected both at registered office and its branches and such books shall be kept on accrual basis and according to the double entry system of accounting.

The Books of account should be kept at the registered office of the company unless decided by Board of Directors at other place. In such a case company is required to file full address of that other place by giving a written notice to the Registrar within seven days. Branch office is required to send proper summarised returns to the Head Office or other place referred.

The Company may maintain books of account and other relevant documents in electronic form. (Section 128(1). The Proper books of account constitute such books of account as are necessary to exhibit and explain transactions and the financial position of the business of the company. The proper books of account also include Cost Accounting records and stock records. The Central Government may order that companies engaged in production of such goods or providing such services, as may be prescribed, to maintain detailed cost records including utilization of material or labour or other items of cost.

18.3 INSPECTION OF BOOKS OF ACCOUNT

Books of account and other books and papers shall be open for inspection by any director during business hours. Inspection of a subsidiary company accounts is permitted only by a person duly authorised by the Board of Directors by passing resolution in this regard (Section 128(3)).

The Registrar, by a written notice, may call on the company to produce the books of account, books, papers and explanations as may be required (Section 206(1)).

The Registrar shall record his reasons in writing for issuing such notice.

The Central Government also may appoint an inspector to carry out inspection of books of account and papers to investigate into the affairs of the company (Section 206 (5)).

The Directors, officers and employees of the company are duty bound to produce all such documents, other statements, information and explanations before the registrar or inspector. Registrar or inspector can make or cause to be made copies of books and account and other books and papers.

When default is made by any director, officer or employee in above matters, they shall be punishable with fine which shall not be less than rupees twenty five thousand, but which may extend to rupees one lakh and also with imprisonment for a term which may extend to one year. Further, the director or officer, if convicted, shall, on and from the date of conviction, be deemed to have vacated his office as such and shall be disqualified for holding such office in any company. This disqualification extends to private companies as well (Section 207(1)).

18.3.1 Persons Responsible for Keeping Books of Account

The managing director, the whole time director in charge of finance, the Chief financial officer or any other person who has been given the responsibility of keeping proper books of account and other matters shall be held responsible for keeping proper books of account.

Punishment : In case of contravention of these provisions, the above persons shall be punishable with imprisonment for a term which may extent to one year or with fine which shall not be less than rupees fifty thousand, but which may extend to five lakh rupee or both. There is no provision in the Act to prosecute the company concerned. Only the functionaries identified in these sections who alone can be charged and prosecuted.

18.3.2 Books of Account of a Branch

Where a company has branch office in or outside India, the books of account relating to the transactions effected at the branch office are kept at that office and proper summarised returns periodically are to be sent by the branch office to the company at its registered office or at any other specified place (Section 128(2)).

18.3.3 Period for which Books of Account to be Retained

The books of accounts of every company relating to the period of not less than eight years immediately preceding the current year shall be preserved in good order, along with relevant vouchers. If the company is in existence for less than eight years, then it should keep books of account and related vouchers in good order right from the first accounting year of the company Section 128(5).

18.3.4 Re-Opening of Accounts on Court's or Tribunal's Order

A company shall not reopen its books of account and shall not recast its financial statements, unless an application in this regard is made by the Central Government, Income tax authorities, the Securities and Exchange Board, any other statutory body or authority or any person concerned and an order is made by Court or Tribunal to that effect that –

- i) The relevant earlier account were made in a fraudulent manner; or
- ii) The affairs of the company were mismanaged during a relevant period, casting a doubt on the reliability of financial statements.

The Court or Tribunal shall take into consideration the representations if any, made by above authorities.

No order shall be made in respect of reopening of books of account relating to a period earlier than eight financial years immediately preceding current financial year. The Central Government may order more than eight years for reopening the accounts (Section 130), if the central government has ordered that books of accounts to be kept for more than eight years. The accounts so revised shall be final.

18.3.5 Voluntary Revision of Financial Statements or Board's Report

If it appears to directors of the company that

- a) the financial statements of the company ; or
- b) the report of the Board do not comply the legal provisions, they may prepare a revised financial statements or revised report in respect of any three financial years after taking the approval of the Tribunal, on an application made by the company, and a copy of the order passed by Tribunal shall be filed with the Registrar.

The Tribunal shall give a notice to the Central Government and income tax authorities. The revised financial statement or report shall not be prepared or filed more than once in a financial year. The detailed reasons for revision of such financial statement or Board's report shall be given in Board's report.

18.4 FINANCIAL STATEMENTS

“Financial Statements” in relation to a company include:

- i) a balance sheet at the end of the financial year;
- ii) A profit and Loss account; in case of company carrying on any activity not for profit, an income and expenditure account for the financial year;
- iii) Cash Flow Statement for the financial year;
- iv) A statement of changes in equity, if applicable; and
- v) Any explanatory note annexed to or forming part of, any document referred to in (i) to (iv) above (Section 2(40)).

The cash flow statement need not be prepared in case of one person company and small company.

18.5 PROVISIONS RELATING TO FINANCIAL STATEMENTS

- i) Financial statements shall give a true and fair view of the state of affairs of the company. (except insurance company or banking company or company engaged in generation or supply of electricity. To such companies their respective Acts apply). The financial statements shall be in accordance with accounting standards as per section 133.
- ii) Where a company has one or more subsidiaries or associate companies, a consolidated financial statement of such companies shall be laid before

the annual general meeting. A separate statement with salient features of financial statements of such companies shall be attached with company financial statements. Copies of financial statements including consolidated financial statements shall be filed with the Registrar.

- iii) According to Section 134(1) the financial statements including consolidated financial statement, if any, shall be approved by the Board of Directors. They shall be signed at least by the chairperson of Board or by two directors out of which one shall be managing director, if any, and the Chief Executive Officer. They are also required to be signed by Chief Financial Officer and the Company Secretary of the company if appointed, and in case of one man company, only by one director. The financial statements of all companies shall be approved by the Board of directors before they are signed on behalf of the Board in accordance with this section and before they are submitted to the auditors for their report.
- iv) Each member shall have right to get a copy of audited financial statements.
- v) The various documents shall be attached to every financial statement which include:
 - a) The auditor's report;
 - b) The report by the Board of Directors. Among others, this report shall include:
 - i) The web address, if any, when annual return has been placed;
 - ii) Number of meetings of the Board;
 - iii) Directors Responsibility Statement;
 - iv) Details about fraud reported by auditors;
 - v) A statement on declaration given by independent directors;
 - vi) The state of company affairs;
 - vii) The applicable accounting standards (Section 134);
 - viii) The Composition of Corporate Social Responsibility Committee (Section 135);
 - ix) Particulars of loans, guarantees or investments (Section 186);
 - x) The amount, if any, proposed to carry to any reserve;
 - xi) The amount, if any, recommended to be paid by way of dividend.

18.6 CORPORATE SOCIAL RESPONSIBILITY COMMITTEE

Every Company having a net worth of rupees five hundred crore or more or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during immediately preceding financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be independent director. If there is no independent director two or more directors shall constitute CSR Committee.

The CSR Committee shall (a) formulate and recommend to the Board CSR policy which shall indicate to the activities to be undertaken by the company in areas or subjects as prescribe in schedule VII (amended in 2014) (b) recommend the amount of expenditure to be incurred on such activities (c) monitor the CSR policy of the company from time to time.

The company shall spend in every financial year, at least two per cent of the average net profit made during three immediately preceding financial years in the pursuance of CSR policy.

The company shall give preference to the local areas and areas around it where it operates for spending the amount ear marked for CSR activities.

Check Your Progress A

1) What is ‘books of account’?

.....
.....
.....

2) What are Financial Statements?

.....
.....
.....

3) State whether following statements are True or False.

- a) Items of Cost may not be included in ‘Books of account’.
- b) Chief Financial Officer also has responsibility for keeping proper “Books of Account”.
- c) For preparation of financial statements accounting standards are compulsory to be complied with.
- d) Members are not authorised to get copy of the audited financial statements.

4) Fill in the Blanks

- i) Company _____ reopen books of account.
- ii) The Registrar may call on the company to _____ Books of Account.
- iii) Securities and Exchange Board of India can apply to Tribunal for _____ of a company.
- iv) Corporate Social Responsibility Committee of Board should consist three or more directors with at least one _____
- v) Financial statements also includes _____ statement.

18.6 LET US SUM UP

The Act requires a company to keep at its registered office certain books, known as statutory books and also keep copies of certain documents and deed. Among

various statutory books are Books of Account. Books of account are to be kept at registered office of the company unless decided by the Board of Directors to keep it at other place. The Registrar is to be informed. The transactions that effect only branch in or outside India, they are to be kept there. The books of account are open for inspection at head office. The books of accounts are to be kept for a period of at least eight years. The managing director, whole time director of finance, the Chief finance officer or any other person given such responsibility are responsible for keeping proper books of accounts.

The Financial Statements along with directors report and explanations are to be circulated to each member, be presented in general meeting and a copy should be sent to Registrar. They should be drawn according to format given in Schedule III and accounting standards. They can be reopened by Court or Tribunal on their own or on application of central government, income tax authorities and securities and Exchange Board of India. Insurance companies and Banking Companies have to draw their financial statements as per law relating to them.

The Act requires certain companies to constitute a Social Responsibility Committee of the Board. Board's report shall include report on CSR. The amount to be spent on CSR areas is given in schedule VII of the act.

18.7 KEY WORDS

Books of Account: It includes record maintained with respect to all sums of many received and expanded. Sales and purchases, assets and liabilities and items of cost.

Financial Statement : This include balance sheet, profit and loss accounts, cash flow statement, a statement of changes in equity.

18.8 ANSWERS TO CHECK YOUR PROGRESS

4. (a) False (b) True (c) True (d) False (e) True
 5. (i) Can (ii) Produce
 2. Reopening of Accounts (iv) Independent Director
(v) Cash Flow
-

18.9 TERMINAL QUESTIONS

- 1) How the inspection of books of accounts is done. Explain
- 2) The Books of Account can be re-opened. Discuss.
- 3) Who are the responsible persons for keeping books of account?
- 4) What are the provisions relating to financial statements?

Note: These questions will help you to understand the unit better. Try to write answers for them but do not submit your answers to the University. These are for your practice only.

UNIT 19 AUDIT

Structure

- 19.0 Objectives
- 19.1 Introduction
- 19.2 Provisions Relating to Audit
- 19.3 Appointment of an Auditor
 - 19.3.1 Who can be Appointed as an Auditor
 - 19.3.2 Who cannot be Appointed as an Auditor
 - 19.3.2.1 Disqualification due to Fraudulent Acts
 - 19.3.2.2 Disqualification due to Professional Misconduct
 - 19.3.3 Appointment of First and Subsequent Auditors, Tenure of Appointment and Ceiling on Audit
 - 19.3.4 Casual Vacancy, Resignation and Removal of an Auditor
- 19.4 Rotation of an Auditor
- 19.5 Rights of an Auditor
- 19.6 Auditor's Report
- 19.7 Secretarial Audit
- 19.8 Let Us Sum Up
- 19.9 Key Word
- 19.10 Answers to Check Your Progress

19.0 OBJECTIVES

After studying this Unit, you should be able to:

- describe provisions relating to audit;
- explain appointment, tenure and rotation of an auditor;
- describe the contents of an audit report; and
- discuss Secretarial Audit.

19.1 INTRODUCTION

After the financial statements are ready, they need to be audited. The object of audit is two fold (a) to detect and prevent errors and (b) to detect and prevent frauds. Every concern, small or big, sole proprietorship, partnership or company etc. should get accounts audited. For listed companies and for specified unlisted public companies and private companies accounts must be audited compulsorily. An auditor must be a qualified chartered accountant certain companies must have internal audit department. Cost audit is done by a qualified cost accountant. An auditor has certain rights and duties as well. Any breach of legal duty by

an auditor invites punishment under Act. An auditor has to follow the prescribed auditing standards. In this unit, you will learn about provisions relating to audit, appointment of an auditor, qualifications, disqualifications, first auditor, subsequent auditor, tenure and ceiling. You will also learn about rotation of an auditor, auditor's report and secretarial audit.

19.2 PROVISIONS RELATING TO AUDIT

1) **Audit Committee** : The Board of Directors of every listed public company or such other class or classes of companies, as may be prescribed shall constitute an audit committee. It shall consist of minimum three directors with independent directors forming a majority. The Chairman and majority of members should have ability to read and understand the financial statements. The Committee shall have terms of reference as may be specified by the Board of Directors. The terms of reference, amongst others, shall include:

- i) The recommendation for appointment, remuneration and terms of appointment of auditors of the company;
- ii) Review and monitor the auditor's independence and performance, and effectiveness of audit process;
- iii) Examination of financial statements and auditor's report thereon;
- iv) Approval or any subsequent modification of transactions of the company with related parties.

Provided that the Audit Committee may make omnibus approval for related party transactions proposed to be entered into by the Company subject to such conditions as may be prescribed.

Provided further that in case of transactions other than third party related transactions and where Audit Committee does not approve the transaction, it shall make its recommendations to the Board.

Provided also that in case any transaction involving any amount not exceeding one crore rupees is entered into by a director or officer of the company without obtaining the approval of Audit Committee and it is not ratified by the Audit Committee within three months from the date of the transaction, such transaction shall be voidable at the option of the committee and if the transaction is with the related party to any director or is authorised by any other director, the director concerned shall indemnify the company against any loss incurred by it.

Provided that these provisions shall not apply to a transaction between holding company and its wholly owned subsidiary.

- v) Scrutiny of inter corporate loan and investment
- vi) Valuation of undertaking or assets of the company
- vii) Evaluation of internal financial controls and risk management systems
- viii) Monitoring the end use of funds through public offers and related matters.

The Committee shall have to hear at their meetings the auditors and other managerial personnel. A vigil mechanism for directors and employees shall be established to report genuine concerns, and the committee shall make provision for adequate safeguard against victimisation of persons using the mechanism and provide direct access to chairperson of the Audit Committee (Section 177)

- 2) **Internal Audit :** Internal audit may be conducted by the employees of company or by a Chartered Accountant or a Cost Accountant or any other professional. The scope, period, functioning and methodology shall be determined by Audit Committee. It is mandatory to appoint an internal auditor by listed or unlisted company having paid up share capital of rupees fifty crores or more or turnover of rupees two hundred crores rupees or more during the preceding financial year or outstanding loans or borrowings from banks or public financial institutions exceeding one hundred crore rupees or more or outstanding deposits of twenty five crore rupees or more at any point of time during the preceding financial year. Every private company also having turnover of rupees two hundred crore rupees or more or outstanding loans or borrowings from banks or public financial institutions exceeding rupees one hundred crore or more at any point of time during preceding financial year shall appoint an internal auditor (Section 138).
- 3) **Cost Audit :** This audit is done for verifying cost of manufacture or production of an article on the basis of accounts as regards utilisation of materials or labour or other items of cost maintained by the company. Only a cost accountant holding valid certificate of practice from Institute of Cost and Management Accountants of India can conduct such audit. The Cost Audit is conducted in addition to audit of financial statements. The cost auditor shall comply with costing standards, as are issued by Institute of Cost and Management Accountant of India (Section 148). The cost auditor is subject to the same qualifications, disqualifications rights, duties and obligations as prescribed under section 143 of the Act for the auditors appointed under Section 139.
- 4) **Auditing Standards :** Section 141 (9) requires the auditor to comply with the auditing standards as laid down by the Institute of Chartered Accountants of India in consultation with the National Financial Reporting Authority.

19.3 APPOINTMENT OF AN AUDITOR

19.3.1 Who can be Appointed as an Auditor (Qualifications)

Section 141(1) of the act prescribes the qualifications and disqualifications for the appointment of an auditor.

- 1) A person shall be eligible for appointment or reappointment as an auditor, commonly called statutory auditor, only if he is a Chartered Accountant i.e., who holds a valid certificate of practice under Chartered Accountants Act, 1949. (Section 141(1)).
- 2) Where a firm including limited liability partnership is appointed as an auditor or reappointed, only the partners who are Chartered Accountants shall be authorised to act and sign on behalf of the firm.

19.3.2 Who cannot be Appointed as an Auditor (Disqualifications)

The following persons/entities cannot be appointed as an auditor of a company [Section 141 (3)].

- a) A body corporate other than a limited liability partnership registered under the limited liability Partnership Act, 2008;
- b) An officer or employee of the company;
- c) A person who is a partners or who is in the employment, of an officer or employee of the company;
- d) A person who or his relative or partner:
 - i) is holding any security of or interest in the company or its subsidiary or of its holding or associate company or a subsidiary of such holding company. However, the relative may hold security or interest in the company of face value not exceeding, one thousand rupees or such sum as may be prescribed;
 - ii) is indebted to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company, in excess of such amount as may be prescribed; **or**
 - iii) has given a guarantee or provided any security in connection with the indebtedness of any third person to the company or its subsidiary or its holding or associate company or a subsidiary of such holding company for such amount as may be prescribed;
- e) A person or a firm, whether directly or indirectly has business relationship with the company or its subsidiary or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed;
- f) A person whose relative is a director or is in employment of the company as a director or key managerial personnel;
- g) A person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor. If such person or partner is at the date of such appointment or reappointment holding appointment as auditor of more than twenty companies;
- h) A person who has been convicted of an offence involving fraud and a period of ten years has not elapsed from the date of such conviction;
- i) A person who, directly or indirectly, renders any service prohibited to the company or its subsidiary company.

19.3.2.1 Disqualification due to Fraudulent Acts

The Tribunal either **Suo Motu** (on its own) or on an application by the Central Government or by any person concerned, is satisfied that auditor, directly or indirectly, acted in a fraudulent manner or abetted or colluded in any fraud by or in relation to the Company or directors or officers direct the company to change the auditors. Within fifteen days on application of Central Government, the Tribunal may order and Central Government may appoint any other Auditor. An auditor against whom a final order has been passed shall not be eligible

for appointment as an auditor of any company for a period of five years from the date of passing the order. He shall be tried for offence of fraud.

19.3.2.2 Disqualification due to Professional Misconduct

In case of professional or other misconduct, the National Financial Reporting Authority (NFRA) has the power to debar the member or the firm from being appointed as an auditor or internal auditor for undertaking any audit in respect of financial statements or internal audit of functions or activities of any company or body corporate or performing any valuation as provided under Section 247. The debarment would be for a minimum period of six months but may extend upto ten years [(Section 132(4)].

19.3.3 Appointment of First and Subsequent Auditors, Tenure of Appointment and Ceiling on Audit

The first auditors shall be appointed by Board of Directors within thirty days from the date of registration of the company. The first auditor/auditors shall hold office until the conclusion of first annual general meeting. If the first auditor is not appointed by the Board then members shall appoint first auditors in an extraordinary general meeting.

As per section 139(1) an auditor is appointed by the company from the conclusion of first annual general meeting until sixth annual general meeting and thereafter till the conclusion of every sixth meeting. If the annual general meeting is adjourned, the auditor shall continue till the conclusion of adjourned meeting. The matter relating to such appointment shall be placed for ratification by members at every annual general meeting. The subsequent auditor/auditors are appointed by members in annual general meeting by passing an ordinary resolution. The company has a right to remove the auditor before the tenure is over. Similarly, an auditor may resign from his office before his term is over, but he has to clearly state his reasons of resignation.

A person cannot be an auditor of more than twenty companies. Only public companies and private companies having paid up capital of Rupees one hundred crore or more are to be considered. One person companies, small companies and private companies having paid up capital less than rupees one hundred crore are excluded in this counting.

19.3.4 Casual Vacancy, Resignation and Removal of an Auditor

- j) If there arises a casual vacancy by any reason other than resignation by the auditor, the Board of Director has the power to appoint the auditor within thirty days.
- ii) If casual vacancy is caused by resignation of auditor, it can be filled only by company in general meeting to be convened within three months of the recommendation of Board.
- iii) If auditor resigns before his term he needs to file a statement within thirty days of his resignation with the Registrar, failure to file a statement would make him liable to a penalty fifty thousand rupees or an amount equal to his remuneration, whichever is less. If the failure continues, a further penalty of five hundred rupees each day after the first during which such failure continues, however it cannot exceed five lakh rupees.

- iv) An auditor may be removed before the expiry of the term by passing a special resolution after obtaining prior approval of the Central Government and giving the auditor a reasonable opportunity of being heard. The matter of his removal is first consideration at Board meeting and Board's resolution is passed. Within sixty days of the Central Government approval , the general meeting of members shall be held for passing the special resolution.

19.4 ROTATION OF AN AUDITOR

The Act provides for compulsory rotation of the auditors for listed companies, unlisted public companies having paid up capital of rupee ten crore or more and all private limited companies with paid up share capital of twenty crores or more. Companies having public borrowings from financial institutions, banks or public deposits of rupees fifty crore or more are also covered even if their paid up capital be lower than amount prescribed.

No listed company or a company belonging to such class or classes of companies as may be prescribed shall appoint or reappoint:

- a) an individual as a auditor for more than one term of **five** consecutive years in the same company whereas
- b) an audit firm as auditor for more than two terms of five consecutive years in the same company.

A company may resolve to appoint more than one auditor to audit its accounts. In such a case the company may follow the rotation of auditors in such a manner that both or all of the joint auditor do not complete their term in same year.

As per provisio to Section 139(2) an individual auditor or audit firm that has completed the prescribed tenure of five or ten consecutive years respectively shall have a cooling off period of five years during which it shall not be eligible for reappointment as auditor in the same company. The act has prescribed a company break up of five years before an auditor or a firm becomes eligible for reappointment as auditor in the same company.

In case of central or State Government owned companies or jointly owned by them, the Comptroller and Auditor General of India shall appoint a duly qualified auditor (section 139).

19.5 RIGHTS OF AN AUDITOR

The rights of an auditor are as follows:

- i) Rights to access the books and account.
- ii) Right to obtain explanation or information.
- iii) Right to sign the report.
- iv) Right to receive notice of general meetings.
- vi) Right to visit the branch offices.
- vii) Right to claim remuneration.

The remuneration of an auditor is fixed by the company in the general meeting or in a manner as may be determined in the general meeting. In case of first auditor/auditors remuneration may be fixed the Board. The remuneration mentioned shall in addition to the fee payable to an auditor, includes the expenses,

if any, incurred by the auditor in connection with the audit of the company and any facility extended to him.

An auditor cannot render certain services like internal audit, actuarial services, investment services, management services and account and book keeping services and any other kind of services as may be prescribed.

19.6 AUDITOR'S REPORT

The auditor has a duty to report to members on the accounts examined by him and on every financial statements which are required to be laid before the company in general meeting. The report shall also confirm that accounting and auditing standards have been followed and matters which are required to be included have been duly included.

The auditor should report whether to the best of his information and knowledge the said accounts and financial statements give a True and Fair view of the state of affairs at the end of financial year and Profit and Loss and cash flows for the financial year.

The auditor shall include in his report the following:

- a) Whether he has sought and obtained all the information and explanations which to the best of his knowledge and belief were necessary for audit.
- b) Whether in his opinion, proper books of account as required by law have been kept by the company so far as appears from his examination of those books and proper returns adequate for the purpose of his audit have been received from branches not visited by him.
- c) Whether the report on accounts of any branch office audited under section 143 (8) by a person other than company's auditor has been sent to him and how he has dealt with the same in preparing auditor's report.
- d) Whether company's Balance Sheet and Profit and Loss Account dealt with in the report are in agreement with books of account and returns.
- e) Whether the report the Profit and Loss Account and Balance Sheet have complied with accounting standards.
- f) The observations and comments of the auditor on financial transactions or matters which have any adverse effect on the functioning of the company.
- g) Whether any director is disqualified from being appointed as director.
- h) Any qualification, reservation or adverse remarks regarding maintenance of accounts and other matter connected therewith.
- i) Whether the company has adequate internal financial controls with reference to financial statements in place and operative effectiveness of such controls.
- j) Other matters to be reported :
 - i) Whether the company has disclosed the impact, if any, of pending litigation on its financial position in its financial statements.
 - ii) Whether the company has made provisions as required under any law

or accounting standards for material foreseeable losses, if any, on long term contracts including derivatives contracts.

- iii) Whether there has been any delay in transferring amounts required to be transferred to Investors Education and Protection Fund by the Company (Section 143).

19.7 SECRETARIAL AUDIT

According to Section 204 (1) the following types of companies shall have mandatory secretarial audit and the secretarial report by a secretary in practice.

- i) Every listed company;
- ii) Every public company having a paid up capital of rupee fifty crore or more; or
- iii) Every public company having a turnover of rupees two hundred and fifty crore or more.

The secretarial audit is required to be conducted by a company secretary in practice.

The secretary in practice report shall be annexed to the Board’s report. The company shall provide all assistance and facilities to the company secretary in practice. The Board shall explain about any qualification or reservation or other remarks made in secretary in practice report.

The company or any officer shall be fined rupees not less than rupees one lakh but which may extend to rupees five lakhs in case of any contravention. The secretary in practice may also be fined similarly. (Section 204).

Check Your Progress A

- 1) Who can be appointed as an auditor?
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.....
.....
- 2) What is an audit committee?
.....
.....
.....
- 3) State whether following statements are True or False
 - a) A firm of auditors can be appointed as an auditor of a company.
 - b) An officer or employee of the company cannot be appointed as an auditor.
 - c) Sometimes the first auditor(s) is are named in Articles of Association.
 - d) The auditors of a listed company may not be compulsorily rotated.

- e) An auditor cannot be removed before the expiry of his term.
- f) The Profit and Loss Account and Balance Sheet, in the opinion of the auditor, should comply with auditing standards.

4 Fill in the blanks:

- i) A person cannot be an auditor of more than _____ companies.
- ii) The first auditor or auditors of a company shall be appointed by the Board of Directors within _____ days.
- iii) The period of rotation of an auditor is _____ consecutive years.
- iv) The auditor's report should state that the accounts and financial statements give a _____ state of company's affairs.
- v) Secretarial Audit should be done by a _____ .

19.8 LET US SUM UP

Only Chartered Accountant holding a certificate of practice is eligible to be appointed as an auditor. Cost audit can only be done by a cost accountant holding a valid certificate of practice. The secretariat audit is required to be conducted by company secretary in practice. A person cannot be an auditor of more than twenty companies. First auditors of a company are appointed by Board of directors, subsequent auditors shall be appointed in first annual general meeting. An individual shall hold office for a period of five consecutive years. A retiring auditor shall be reappointed subject to certain conditions. An auditor can resign at any time. An auditor can be removed before expiry of his term. An auditor has certain rights e.g. to attend annual general meeting or to sign audit report etc. An Auditor is required to give his report on certain specified matters and language. He should conduct audit according to auditing standards. He can be penalised for contravention of provisions under section 139 to 146. A company should have an audit committee of the Board of directors. The remuneration of an auditor, cost auditor and auditor for secretarial audit is determined by members in general meeting. There should be an internal audit department for certain companies.

19.9 KEY WORDS

Audit : It is official examination and inspection of books of account by an auditor.

Secretarial Audit: It is required to be conducted by a Company Secretary in practice.

19.10 ANSWERS TO CHECK YOUR PROGRESS

- 3) (a) True (b) True (c) True (d) False (e) False (f) true
- 4) (i) 20 (ii) 30 (iii) Five (iv) True and fair
(v) Company Secretary in practice.

19.10 TERMINAL QUESTIONS

- 1) Describe the provisions relating to audit.
- 2) Discuss the qualifications and disqualifications of an auditor.
- 3) What is secretarial audit?
- 4) How first and subsequent auditors are appointed?
- 5) Discuss about the ceiling, rotation and removal of an auditor.
- 6) When auditor's report is given ? What information is given in auditor's report?

Note: These questions will help you to understand the unit better. Try to write answers for them but do not submit your answers to the University. These are for your practice only.

UNIT 20 WINDING UP

Structure

- 20.0 Objectives
- 20.1 Introduction
- 20.2 Meaning of Winding Up
- 20.3 Modes of Winding Up
- 20.4 Procedures for Winding Up Order
 - 20.4.1 Preferential Payments
 - 20.4.2 Contributory
- 20.5 Removal of Name of a Company
- 20.6 Let Us Sum Up
- 20.7 Key Words
- 20.8 Answers to Check Your Progress
- 20.9 Terminal Questions

20.0 OBJECTIVES

After studying this Unit, you should be able to:

- explain the meaning of winding up of a company;
- distinguish between winding up and dissolution of a company;
- describe the modes of winding up of a company;
- explain the procedure for winding up of a company;
- define preferential payments and contributory; and
- explain the procedure for removal of name of a company.

20.1 INTRODUCTION

A company is a person, artificial, invisible, intangible and exists in the eyes of law. It has a perpetual succession. It never dies. The end of a company comes only through its winding up procedure. The Companies Act 2013 came into force on 29th August, 2013. It has been amended in 2015, 2017, 2018 and 2019. Latest changes have been brought by the Insolvency and Bankruptcy Code 2016, mainly in provisions of winding up of a company. The mode of voluntary winding up has totally been dropped by this code given in part II from sections 304 to 323 of the Act 2013. A company now be wound up under the Companies Act, 2013 only by the tribunal. In this unit you will learn about meaning of winding up, difference between winding up and dissolution, modes of winding; procedures for winding up, and preferential payments and contributory and removal of the name of the company.

20.2 MEANING OF WINDING UP

The “winding up” or “liquidation” is a process of bringing about an end to the life of a company. In the words of Gower “winding up of a company is the process 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 liabilities and finally distributes the surplus among the members in accordance with their rights.

Even a solvent company may be wound up. After winding up, a company is “Dissolved formally and will not have any assets or liabilities. The legal personality of the company shall come to an end.

When a company is unable to pay its debts, its liquidation will be under newly passed. “Insolvency and bankruptcy code 2016”. The code relates to insolvency, liquidation, voluntary liquidation or bankruptcy. The Company shall thus be wound up either under Companies Act, 2013 or liquidated under Insolvency and Bankruptcy Code 2016, as applicable.

Difference between Winding up and Dissolution

Winding and dissolution of the company are not the same thing. A company is not dissolved immediately on the commencement of winding up proceedings. Winding up is the prior stage and dissolution is the next. On dissolution, the name of the company is struck off by the Registrar from the Registrar of Companies i.e., it ceases to exist. While on winding up the Company’s name is not struck off from the register. The legal entity of a company remains even after the commencement of winding up and it can be sued in a court of law. Dissolution is the final stage of the Company’s winding up process. But a company can be dissolved without winding up under certain circumstances such as when it merges with another company. In winding up the assets of the company are sold and the proceeds are utilized in paying off the debts and other liabilities of the company. It is the first stage of terminating the life of a company. While the dissolution is the next stage and after this company ceases to exist. The winding up proceedings are carried out by a liquidator of the company while in case of dissolution no such proceedings are carried out. Creditors can prove their debts in the winding up but not in the dissolution of the company.

20.3 MODES OF WINDING UP

Winding up by the Tribunal

Winding up may be ordered by the Tribunal in following cases, which are grounds for **compulsory winding up**:

- a) If a company has, by special resolution, resolved that the company be wound up by the Tribunal;
- b) If the company has acted against the interest of sovereignty and integrity of India, the security of state, friendly relations with foreign states, public order, decency or morality;
- c) If on an application made by Registrar or any other person authorised by the Central Government by notification under the Act, the Tribunal is of the opinion that the affairs have been conducted in a fraudulent manner

or the Company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affair have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;

- d) If the company has made default in filing with the Registrar its financial statements or annual returns for immediately preceding five consecutive financial years; or
- e) If the company is unable to pay its debts.
- e) If the Tribunal is of the opinion that it is just and equitable that the company should be wound up (Section 271)

20.3.1 Winding Up by Special Resolution

The Company may by a special resolution resolved that the company to be wound up by the Tribunal. The Tribunal has to examine whether the resolution is in the interest of the company or is not opposed to public interest. If not, the winding up may not be ordered. The company can file a petition before the Tribunal for winding up even without passing a special resolution (Section 272). A company whose name is not in the register of companies is not entitled to file a winding up petition.

20.3.2 Company Acting against the Sovereignty and Integrity of India, Security of the State, the Friendly Relations with Foreign States, Public Order, Decency and Morality.

If the company acting against the interest of sovereignty and integrity of India, the security of state, the friendly relations with foreign states, public order, decency and morality, the petition on this ground shall be made by Central or a State Government to the Tribunal. The words 'decency' and 'morality' have not been defined in the Act.

20.3.3 Affairs being Conducted in a Fraudulent or Unlawful Manner

The Registrar or any other person authorised by the Central Government may make an application to the Tribunal for winding up on this ground. The Tribunal may order winding up on the following grounds.

- i) The affairs of the company are being conducted in a fraudulent manner; or
- ii) The Company was formed for fraudulent or unlawful purpose; or
- iii) The persons concerned in the formation of the company or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith.

It may be noted, besides above provision, Central Government may directly file a petition for winding up in case of inspector's report on investigation.

20.3.4 Default in Filing Financial Statements or Annual Returns with to the Registrar

The company has to file two separate documents (a) financial statements and (b) annual return to the Registrar.

The default in not filing these documents should have been for immediately preceding five consecutive financial years, only then winding up may be ordered. If default is for two or three or four years, this provision cannot be invoked. Again, it may be noted that winding up may be ordered if the default relates to either non-filing of financial statements or annual returns. It is not necessary that the default has to be for both financial statements and annual return. The default has to be in respect of immediately preceding five consecutive financial years. It means that default in the earlier year is not a ground for winding up under the clause.

20.3.5 Inability to Pay its Debts

A company shall be deemed to be unable to pay its debts,

- a) if a creditor by assignment or otherwise, to whom the company is indebted for an amount exceeding one lakh rupees then due, has served on the company, by causing it to be delivered at its registered office, by registered post or otherwise, a demand requiring the company to pay the amount so due and the company has failed to pay the sum within twenty-one days after the receipt of such demand or to provide adequate security or re-structure or compound the debt to the reasonable satisfaction of the creditor;
- b) if any execution or other process issued on a decree or order of any court or tribunal in favour of a creditor of the company is returned unsatisfied in whole or in part; or
- c) if it is proved to the satisfaction of the Tribunal that the company is unable to pay its debts, and in determining whether a company is unable to pay its debts, the Tribunal shall take into account the contingent and prospective liabilities of the company.

20.3.6 Just and Equitable

These words have not been defined in the Act. The power under this clause, according to A. Ramaiya, should be used only “when there is a strong ground because companies as far as possible, should be left to self governance and self determination through the wishes of majority of shareholders”. The Tribunal should not make an order on this ground for winding up, if there is any other remedy available. It is a remedy of last resort.

The following grounds, based on leading cases, have been held as “Just and Equitable”.

- a) **Loss of Substratum:** It means sole purpose or main objects, for which company was formed, cannot be achieved e.g. it fails to obtain a patent for invention on the assumption that it will be granted or it fails to acquire the business which the company was formed to purchase or fails to build a building on ground that local authority did not grant permission. In re, **Kailtal and General Mills Co. Ltd (1955)** 31 Comp. Cons. 46], the Court laid down the following test to determine as to whether the substratum of the company has disappeared:
 - a) Where the subject matter of the company has gone; or
 - b) The object for which it was incorporated has substantially failed; or
 - c) It is impossible to carry on the business of the company except at

loss which means that there is no reasonable hope that the object of trading at a profit can be attained or

- d) The existing or probable assets are insufficient to meet the existing liabilities.
- b) **Illegality of objects and fraud:** If any company's objects are illegal or become illegal by change of law, it will be wound up by Tribunal. Similarly, if a company is promoted in order to perpetrate a serious fraud or deception on the person who are invited to subscribe for its shares, the Tribunal will wind it up.
- c) **Deadlock in management:** If a private company has only two members-directors and the two are not on speaking terms. Tribunal will make a winding up order, even though there is a provision in articles that one director shall have a casting vote at board meetings or that the disputes shall be settled by arbitration. If there is a loss of confidence in the Board of directors or refusal by one of the three directors to attend meeting to make a quorum.
- d) **Bubble Company:** If the company is just on paper and never carried on its business.
- e) **Oppression:** A winding up petition may lie where the majority shareholder have adopted an aggressive policy towards minority under Section 241. Also, any member of a company may complain that the affairs of the company have been or are being conducted in a manner prejudicial to public interest or oppressive to him and other members. Under section 242 (1b) the Tribunal can order winding up on "just and equitable" ground.
- f) **Other:** If the number of members fall below the statutory minimum, its winding up can be ordered on "just and equitable ground". Similarly, if company is not following democratic principles of fairness or lacking in commercial morality or where directors making charges against each other the Tribunal can order winding up of the company.

Who can file Petition?

The following can file petition to the Tribunal for winding up of a company.

- 1) The Company; or
- 2) The contributory or contributories i.e., persons who are liable to contribute to the assets of the company; or
- 3) The Registrar; or
- 4) The Central or State Government or any other person authorised by Central Government; or
- 5) Any creditor or creditors;
- 6) No (1), (2) and (5) together

20.4 PROCEDURE FOR WINDING UP

In brief, the following procedure is followed in winding up:

- 1) **Filing of Petition:** It is presented by the company to the Tribunal, along with the statement of affairs. If it is filed by any other person, company is allowed to file objections.

Provisional Liquidator: At any time after presentation of winding up petition and before the making of a winding-up order, the Tribunal may appoint a provisional liquidator. Before making such appointment, however, the Tribunal must give notice to the company so as to enable it to make its representation in the matter unless, for reasons to be recorded in writing, it thinks fit to dispense with such notice. The powers of the provisional liquidator are the same as those of a liquidator unless limited by the Tribunal.

- 2) **Company Liquidator:** On a winding up order being made in respect of a company, the Tribunal shall appoint official liquidator or liquidator. The liquidator should be registered under insolvency and bankruptcy Code 2016. A liquidator can be replaced or removed.
- 3) **Winding up Committee:** Within three months of winding up order, the company liquidator shall make an application to form a winding up committee to assist and monitor progress of winding up. A monthly report along with the minutes of meeting of the winding up committee shall be placed before the Tribunal by company liquidator, the convener.

The company liquidator must submit a preliminary report to the Tribunal within sixty days from the winding up order.

- 4) **Advisory Committee:** The Tribunal may, at the time of making winding up order of a company, or at any time thereafter direct to form an advisory committee to act with company liquidator and to report to Tribunal on such matters as Tribunal may direct. The maximum members of the committee is twelve, being creditors and contributories. The committee has the right to inspect books of accounts and other documents, assets and properties of the company under liquidation at reasonable time. The quorum is 1/3rd of total members or two whichever is higher.

The company liquidator shall chair the meetings of the Advisory Committee.

5) **Dissolution of the Company**

When the affair of a company have been completely wound up, the company liquidator shall make an application to the Tribunal for dissolution of the company.

Upon receipt of the report from the company liquidator or otherwise, the Tribunal on forming an opinion that it is just and reasonable to order dissolution, shall make an order for dissolution of the company. The company shall be dissolved effective from the date of order.

When the company is dissolved, no suit or proceeding will lie against the company because a dissolved company has no existence in the eyes of law.

20.4.1 Preferential Payments

In the event of winding up certain payments are to rank in priority to others. These are called preferential payments. Under section 326 the following shall be paid in priority to other debts:

- 1) Workmen dues;
- 2) Where a secured creditor has realised a secured asset, so much of debts due to such secured creditor, as could not be realised by him or the amount of workmen's portion in his security if payable, under law, whichever is less, PariPassu with workmen's dues.

Under Section 327, order of priority subject to section 326 is given below:

- 1) All revenues, taxes, cesses and rates due 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 order.
- 2) All wages or salary of an employee due for a period not exceeding four months.
- 3) All accrued holiday remuneration becoming payable to an employee on his termination or death.
- 4) All amount due in respect of contributions payable during twelve months under Employees State Insurance Act.
- 5) All amounts in respect of any compensation payable under Workmen's Compensation Act.
- 6) All sums due to an employee from provident fund, a pension fund, a gratuity fund or any other fund
- 7) Expenses of any investigation, held in pursuance of section 213 or 216 in so as they are payable by the company.

Thus the order of priority in paying off debts in winding up shall be follows:

- a) workmen's dues and debts due to secured creditors
- b) Cost and expenses of winding up
- c) Preferential debts
- d) Floating charge
- e) Unsecured Creditors

20.4.2 Contributory

A contributory is a person liable to contribute to the assets of a company in the event of winding up and includes the holder of any shares which are fully paid up (section 2(26)). A holder of fully paid up shares shall have rights as a contributory and no liability as a contributory.

The following persons shall be liable as a contributories on the winding up of a company.

- a) **Present and Past Members:** Every present and past member liable to contribute to the assets of the company for payment of debts, liabilities and costs of winding up and for adjustment of rights of the contributories is a contributory. A past member shall be liable to contribute the amount unpaid on the shares in respect of which he is a contributory or the amount he has guaranteed to pay in the event of winding up. A past member shall not be liable to contribute:
 - i) if he ceased to be a member for one year or more before commencement of winding up; or
 - ii) in respect of any debt or liability contracted after he ceased to be member; or
 - iv) the present members are able to the satisfy the contribution required.
- b) A director and manager whose liability is unlimited except if he ceased to hold office for a year or upward before commencement of winding up.

A past director or manager shall not be liable for contribution if the debt and liability of the company was contracted after he ceased to hold that office.

- c) Assignee of a contributory, legal representative of a deceased member, liquidator of a company which is a member and Debtors are other contributories.
- d) Subscribers to the Memorandum: Subscribers to the Memorandum shall be deemed as contributories for the amount unpaid on the shares they agreed to subscribes for.

20.5 REMOVAL OF THE NAME OF THE COMPANY

Once the affairs of the company are fully wound up, the official liquidator shall submit a final report to the Central Government, with a copy to Tribunal. The Cental Government shall order dissolution of the company and Registrar shall strike off the name of the company from the register of companies and publish a notification to this effect. The company will cease to be an artificial person created by law.

Check Your Progress A

- 1) What is Winding Up?
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.....
.....
- 2) List the 'Just and Equitable grounds' of winding up?
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.....
.....
- 3) Who can file petition for winding up?
.....
.....
.....
- 4) Fill in the Blanks
 - i) A Company can be wound up under the Companies Act 2013 only by _____
 - ii) The Company can be wound up if it makes a default in filing with the Registrar its financial statements and annual returns for immediately preceding _____consecutive financial years.
 - iii) Within_____ of winding up order the company liquidator shall form a winding up committee time.
 - iv) Company liquidator has to make an application to the Tribunal for constitution of a_____
 - v) When a company is dissolved by the Tribunal, it ceases to be a_____

20.6 LET US SUM UP

Winding up of a company means a process whereby its legal personality is ended. The process begins by a petition to Tribunal by specified mode. The Tribunal appoints a Liquidator. He makes a list of creditors and assets. The assets are sold and the money so realized is distributed among creditors. For deficiency contributories are asked to pay for any amount due. After this process he prepares a report submits it to the Tribunal. The Tribunal orders dissolution of the company. The Tribunal has wide powers and may order winding upon 'Just and equitable' ground.

The petition may be filed by the company, contributories, Registrar, Central or State Government or any person authorised by Central Government. The Tribunal may allow liquidator to constitute a winding up committee to assist him as well as advisory committee, consisting of creditors and contributories of not more than twelve persons. The Liquidator has to make certain payment to rank in priority to others. They are called "Preferential Payments".

20.7 KEY WORDS

Winding Up: A process by which the life of a company comes to an end.

Dissolution: The company ceases to exist.

Liquidator: The person who helps the court to complete the liquidation proceedings.

Just and equitable: Any ground which in the opinion of the court, is reasonable and is in the interest of the concerned parties.

20.8 ANSWERS TO CHECK YOUR PROGRESS

(B) (i) Tribunal (ii) Five Consecutive years (iii) three months (iv) Advisory committee and winding up committee (v) Legal person

20.9 TERMINAL QUESTIONS

- 1) What do you understand by winding up of a company ? How is it different from dissolution of a company?
- 2) Discuss the winding up of a Company by the Tribunal.
- 3) Writes a Short notes on:
 - a) Advisory Committee
 - b) Preferential Payments
 - c) Winding Up Committee
- 4) Explain the 'just and equitable grounds' for winding up of a company.

Note: These questions will help you to understand the unit better. Try to write answers for them but do not submit your answers to the University. These are for your practice only.

SUGGESTED READINGS

G. K. Kapoor and Sanjay Dhamija, Company Law, Taxmann.

Avtar Singh, Introduction to Company Law, Eastern Book Company.

Sharma J. P., An Easy Approach to Corporate Laws, Ane Books Pvt. Ltd.
New Delhi.

(Latest Edition of the book is recommended)



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