

Financial Accounting
B.Com. I Semester
Topic: LIQUIDATION OF COMPANY

Presented by

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Liquidation or winding up is a legal procedure through which the affairs of a company is wound up by law.

A company is the creation of law, it cannot die itself as an natural death. So it comes to its end by law through the process of liquidation.

Meaning of Liquidation of Company

The Liquidation or winding up a company is a process through which life of company and its all affairs is wound up and its property administered for benefits of its creditors and members.

An administrator, who is called liquidator, is appointed to take control of company, collect its assets, pay its debts and finally if any surplus assets are left, they are divided among the members of the company in proportion to their rights under the articles.

Steps of Liquidation

1. Selling of the assets of the company.
2. Paying off the liabilities of the company.
3. If there is any deficiency to pay to the creditors and the shareholders are called upon to pay unpaid amount on their articles.
4. In case of surplus, after paying off the liabilities, it may be distributed to the contributories according to their rights under the articles.

Types of Liquidation

I. Compulsory Liquidation by the Court

In the following case company may be wound up by the court:

- 1. When company is unable to pay its debts**
- 2. If company is carrying any illegal business**
- 3. In case of non maintenance of accounts**
- 4. When the statutory meaning is not conducted then the Court may give orders to wind up the company**
- 5. In case of non submission of Statutory Report to the Registrar**
- 6. If company unable to start its business within a year after incorporation**

II. Voluntary winding up by members or creditors

Voluntary Winding up by creditors takes place when a company becomes insolvent and is unable to discharge its liabilities or , if it is unable to carry on its business,

III. Winding up under the supervision of the court

When company has passed special or extra-ordinary resolution for its liquidation or winding up, court can pass an order on application of creditors, contributors or other persons for conducting of liquidation or winding up of company under supervision of court.

Accounts Related to Liquidation of Company

I. Liquidator's Final Statement of Account

In every mode of winding up, the liquidator is required to keep proper books to record receipt and payment which is known as liquidator's final statement. The liquidator has to submit a report along with the audited final accounts to the Company registrar office. The liquidator has to submit the statement to the court in the case of compulsory liquidation and to the company in a voluntary liquidation.

Specimen of Liquidator's Final Statement of Account

Receipt	Amount	Payments	Amount
Assets Realised: Cash in hand Cash at bank Trade receivables Inventory Freehold Property Plant & Machinery Furniture & Fittings Patent, Trademark etc. Surplus From Fully Secured Creditors Realisation From Un-paid Calls		Legal Expenses Liquidator's Remuneration: (% onamount realized on assets) (% on amount distributed) Debentureholders (including interest outstanding) Secured Creditors Unsecured Creditors: Preferential Others Return to Contributories: Preference Shareholders Equity Shareholders Surplus , if any to be distributed among equity shareholders/as per law	
Total		Total	

I. Receipt Side Of Liquidator's Final Statement

- (i) **Assets Realized:** The liquidator would collect the amount by selling the assets of liquidating company. Such an amount received from sold out of assets comes under this heading.
- (ii) **Surplus from securities:** It is related with secured creditors. The secured creditors provide the loan against the security.
- (iii) **Collection of unpaid calls:** The liquidator can collect the unpaid calls if there is a shortage of amount to discharge the liability. These unpaid calls are collected from shareholders. Similarly, if there are any due calls, in that case the liquidator can also make calls and can collect money from them.

Payment Side Of Liquidator's Final Statement

- (i) Liquidation Costs: It is an expense incurred by the liquidator while liquidating the company. It includes **liquidator's remuneration** any legal expenses on the process of liquidation.

- (ii) Debenture Holders: It includes the amount of payable to debenture holders with outstanding interest therein. The debenture interest should be paid up to the date of liquidation if it is insolvent and if the company is solvent, the interest on debentures will be paid up to the date of payment.

- (iii) Secured Creditors: While raising a long term debt, a company may mortgage its property as a security to the debt provider. Such a debt comes under secured creditors. In other words, the secured creditor is such a loan which has been taken from the loan provider on collateral securities.

- (iv) **Preferential Creditors:** It is placed in third position in order of payment. It includes the amount payable to government and employees. Taxes, Fees, Electricity charges, Water supply charge etc. are the examples of payable due to government. Similarly, salaries and wages, provident fund, gratuity and other amount payable to the employee are some of the examples of due to employees.
- (v) **Unsecured Creditors:** If the loan is raised by a company without any collateral securities, it is known as unsecured creditors. Bank overdraft, creditors, outstanding expenses etc. are the examples of unsecured creditors.
- (vi) **Payment made to contributories:** After paying all the above dues, the turn goes towards the shareholders. Among the shareholders, the first priority must be given to preference shareholders. The preference shareholders will get the principal plus arrear of dividend. The last party to receive anything left, after the payment of preference shareholders, is equity shareholders.

Illustration:

ABC Ltd. went into liquidation on 1st January, 2014. The liquidator is paid to paid remuneration at 3 % on the amount realized on sale of assets and 2 % on amount distributed to shareholders. The liquidator sold out all the assets of company. On January 1, 2014, Company's position was as under:

Cash realized on assets	Rs. 700,000
Liquidation Expenses	Rs. 12,600
Creditors(including salaries for one month Rs. 8,400)	Rs. 95,200
7000, 6 % Preference Share of Rs. 30 each (on which Dividend is in arrear for one year)	Rs. 210000
14000 Equity shares of Rs. 10 each, Rs 9 per share called and paid	Rs. 126000
General Reserve Rs. 168000, P & L Statement Rs. 28000	

Under Article of Association of the company the Preference Shareholders have right to receive 1/3 rd of surplus after repaying the Equity Share Capital. Prepare Liquidator's Final Statement of Account.

1. * 2 % on 500000 = 11200

$$\text{Rs. } 700000 - (21000 + 12600 + 8400 + 86800) = 571200$$

$$2 \% \text{ Remuneration} = 571000 * 2 / 102 = 11200$$

$$\text{Total Amount Paid to shareholders} = \text{Rs. } 571000 - 11200 = 560000$$

2. * Creditors Rs. 95200 out of which 8400 related to salaries that is preferential creditors therefore, unsecured creditors will be $(95200 - 8400 = 86800)$

3. * Arrear of preference dividend = $210000 * 6 / 100 = 12600$

4. * Surplus :

$$700000 - (32200 + 12600 + 8400 + 86800 + 210000 + 12600 + 126000) = 211400$$

* Part of Preference Shareholders $211400 * 1/3 = 70467$

* Part of Equity Shareholders $211400 * 2/3 = 140933$

Thank You