



MALAYSIAN INSTITUTE
OF ACCOUNTANTS
ACCOUNTANTS: MANAGERS OF VALUE

MIA 7/2010

INSOLVENCY

Learning the Essentials of Corporate Liquidation

A close-up photograph of a hand holding a white rectangular card. The card is held between the thumb and index finger, with the other fingers visible in the background. The card has the text 'Liquidated Co.' printed on it in a bold, black, sans-serif font. The background is a blurred image of a person's face and a striped shirt.

**Liquidated
Co.**

April 2010

INTRODUCTION

Economic downturn, rapid market changes, failure of customers to pay overdue accounts or strategic errors — any of these can plunge a company into serious financial distress. When it becomes apparent that trading cannot continue, some companies may resort to discontinue or dissolve its operation due to short fall of capital or cutting down the cost of doing business.

Usually, the directors of the company were responsible upon the dissolution of its company. One of the ways to dissolve the company is by putting it under winding-up (which is also called as 'liquidation').

What is liquidation?

In layman terms, liquidation is **the process by which a company is brought to an end, and the assets and property of the company redistributed**. Liquidation is **a method whereby the corporate structure of the company is dismantled and its property administered for the benefit of the creditors and members**.

A liquidator (who is normally an accountant who possesses the pre-requisite license) will be appointed to be in charge of the liquidation process. The liquidator takes full control of the company by collecting and realizing all its assets, settle all the creditors' claims and distributes the surplus (if any) to its shareholders in accordance with their respective rights accorded under **Section 292 of Companies Act 1965** ("CA 1965").

Law Governing Liquidation Exercise

The law governing liquidation of companies is derived from statues passed by parliament. **Part X** of the **CA 1965** is the main regulation that governs liquidation process. Other related regulations include, amongst others:

- Companies Winding-Up Rules 1972
- Bankruptcy Act 1967
- Sales Tax Act 1972
- Service Tax Act 1975



Modes of Liquidation

There are generally **two (2)** categories of liquidation:

1 Compulsory Winding-Up (also known as Court-Ordered Winding-Up)

In insolvency (unable to pay debts)

This is a winding-up of an insolvent company which is triggered by a court order on the application of one or more parties. Such parties may include a creditor, a contributory or the personal representatives of a deceased contributory or the trustee in bankruptcy. This type of winding-up requires the petitioner to state the grounds of winding-up as set out in **Section 218(1) of CA 1965**.

On Other Grounds

The court has the power to wind up a company on grounds other than insolvency. The court may instruct a company to wind up simply because of the breakdown of relationship between two groups of shareholders even though the company is solvent. An application has to be made in order to wind up the company stating the grounds for such proceeding in accordance with **Section 218** of **CA 1965**.

2 Voluntary Winding-Up

Members' Voluntary Liquidation ("MVL")

MVL is the liquidation of a solvent company where the directors must form an opinion that the company will be able to pay its debts in full within a period of twelve (12) months after commencement of winding-up as stated under **Section 257 of CA 1965**. To facilitate understanding on the MVL process, a checklist is included as Exhibit 1 to this publication for reference.

Creditors' Voluntary Liquidation ("MVL")

CVL is the liquidation of an insolvent company where the directors will make a declaration stating that the company cannot by its reason of liabilities continue its business. Subsequent to that, a meeting of the company and its creditors will be summoned within one (1) month from the date of the declaration. This declaration must be lodged with the Registrar and the Official Receiver ("OR") as stated under **Section 255** of the **CA 1965**.

Commencement Date of Liquidation

In liquidation, it is important to pay attention to the following dates:

- date of commencement of winding-up
- date of winding-up
- date when the liquidator takes over the affairs of the company

Each date related to winding-up will have different implication towards winding-up company as follows:

1. Voluntary Winding-up

Section 219 of CA 1965 states that the commencement of the winding-up of a company under voluntary winding-up shall be deemed to have commenced at the time of the passing of the resolution. In other cases the winding-up shall be deemed to have commenced at the time of the presentation of the petition of winding-up.

Commencement Date of Liquidation

2. Compulsory Winding-up

The compulsory winding-up will only occur when the court order is obtained. Therefore, the date of the commencement of winding-up mentioned in Section 219 of CA 1965 will differ from the date that the court orders the winding-up. Furthermore, the date where the liquidator takes over the affairs of the company from directors also may be different from the date of the court order winding-up as the liquidator is not capable of acting as a liquidator unless he has notified his appointment to the Registrar and given security to the Official Receiver as stated under Section 228 of CA 1965.

Responsibilities and Duties of Directors

Directors' duties and responsibilities upon the winding-up company include the following:

- Maintain the affairs of the company until the liquidator takes full possession of the company.
- Pass all assets including books and records of the company to the liquidator.
- Ensure that during the transition period all statutory requirements as provided in the CA 1965 are fulfilled, for instance filing tax returns and maintaining books and accounts.

Effects of Liquidation on Directors

Company's directors should be fully conversant with the effects of a winding-up prior to their decision to proceed to pass the special resolution for winding-up. Therefore, the directors should pay more attention on the provisions stated under the CA 1965 which will affect them most as follows:

- **Section 258(2)** – All the powers of the directors shall cease unless the liquidator or the company in a general meeting with the consent of the liquidator approves the continuance thereof.
- **Section 256(1)** – The company, shall from the commencement of the winding-up cease to carry on its business, except so far as may be necessary for the beneficial winding-up thereof.
- **Section 256(2)** – Any transfer of shares, except for transfer made with the sanction of the liquidator and any alteration in the status of members, made after the commencement of the winding-up, shall be void.

Consequences of Liquidation

The modus operandi of a company will inevitably change upon commencement of the winding up process. Some of the consequences are set out below:

1. Appointment of Provisional Liquidator

The directors should be aware that there is a chance where the assets of the company will be dissipated by an irresponsible individual before getting the court decision on winding-up. The appointment of a provisional liquidator will ensure the safeguard of the assets of the company which has been wound up.

The court may appoint the Official Receiver or an approved liquidator provisionally at any time after the presentation of a winding-up petition and before making of a winding-up order. The provisional liquidator shall have and may exercise all the functions and power of a liquidator subject to limitations as may be provided or the court may impose.

2. Inadmissibility of debt incurred after the petition

As a general rule, debts or claims arising after the commencement date of winding-up will be rejected by the liquidator.

3. Legal Action

The directors are not allowed to take any legal action or proceedings against the company once the court has decided that the company be wound up or where a provisional liquidator is appointed. **Section 226(3) of CA 1965** however empowers the court to allow such action or proceedings to continue with some terms that the court may impose.

4. Restrain Proceedings Against the company

To afford some protection to the company where the assets may be dissipated by a creditor continuing to seek remedies to their claim ahead of other creditors by legal means and to ensure equal distribution of assets, the court provides that any time after the presentation of a winding-up petition and before a winding-up order has been made, the company or any creditor or contributory may, where any action or proceedings is pending, apply to the court to stay or restrain the proceedings on such terms as it thinks fit.

5. Disposition of Assets Void

To ensure there is no improper disposition of assets between the time of presentation of the winding-up petition and the winding-up order, any disposition of property of the company, including the transfer of shares or alteration in the status of the members of the company made after the commencement of the winding-up by the court shall be void unless the court otherwise orders.

Consequences of Liquidation (continued)

6. Undue Preference

To ensure that all creditors are treated equally and there is no preference in making payment to them from the date of winding-up, CA 1965 provides that any transfer, mortgage, delivery of goods, payment, execution or other act relating to property made or done by or against a company shall be void or voidable. Pursuant to the Bankruptcy Act 1967, these transactions are void or voidable over six (6) months before the commencement of the winding-up (except for bona fide purchaser through or under a creditor of the bankrupt).

7. Failure to submit Statement of Affairs

Directors have the obligation to submit the statement of affairs on time. The statement of affairs of the company as at the date of winding-up order showing the assets and liabilities and other information as prescribed must be submitted to the Official Receiver or the liquidator. The statements of affairs should be submitted by one or two persons who are at the date of the winding-up order is a director, company secretary or liquidator.

Any person (including directors) who without reasonable excuse defaults in complying with this provision shall be guilty of an offense under the CA 1965. The penalty imposed for non-compliance is imprisonment of three (3) years or ten thousand ringgit (RM10,000) or both.

8. Declaring Solvency Without Reasonable Grounds

Directors are required to make a written declaration after taking into consideration and inquiry to the company's affair that the company will be able to pay its debts in full without exceeding twelve (12) month period after commencement of the winding-up. The directors shall be guilty if the declaration is made without having the reasonable grounds that the company will be able to pay debts in full within the stipulated period. The penalty imposed for non-compliance is imprisonment of three (3) years or ten thousand ringgit (RM10,000) or both.



Looking for More Insolvency References?

MIA Insolvency Guidance Notes

The Malaysian Institute of Accountants ("MIA") has issued a set of Insolvency Guidance Notes ("IGNs"). These IGNs serve as a form of best practice and aims to harmonize the approach of insolvency practices.

The IGNs comprise twelve (12) documents which are categorized into three (3) groups as follows:

IGN No.	Title of IGNs
Preface	Preface to Insolvency Guidance Note
<u>GENERAL</u>	
IGN G1	Minimum Standards of Practice for Insolvency Practitioners
IGN G2	Professional Conduct and Ethics in Insolvency Practice
IGN G3	Remuneration of Insolvency Office Holders
IGN G4	Handling of Funds in a Liquidation Administration
IGN G5	Preparation of Statement of Receipts and Payments by Insolvency Practitioners
<u>LIQUIDATION</u>	
IGN L1	Members' Voluntary Winding-Up
IGN L2	Procedures for Creditors' Voluntary Winding-up
IGN L3	A Liquidator's Assessment and Review into the Affairs of an Insolvent Company
IGN L4	Summoning and Holding Meeting of Creditors under Court Winding-up
<u>RECEIVERSHIP</u>	
IGN R1	Suggested Receivership Checklist (for Receiver appointed under a Debenture)
IGN R2	A Receiver's Responsibility for the Books and Records of the Company
IGN R3	A Receiver's Responsibility to Preferential Creditors

A copy of the IGNs can be downloaded at the Institute's website at www.mia.org.my/handbook/guide.



Exhibit 1: The Checklist for MVL

The checklist on the steps to be taken for winding-up process for Members' Voluntary Liquidation (MVL) is illustrated in Exhibit 1 below:

No.	Steps to be Taken	Related Section of CA 1965	Prescribed Form	Action Required
1	To conduct Board of Directors' Meeting.	Not Applicable	Not Applicable	The Board of Directors will have to determine status of solvency of the company.
2	To make Declaration of Solvency.	257	66	The Declaration of Solvency must be made and signed by at least 2 directors (majority of them if more than 2) at the directors' meeting. It has to be lodged within 5 weeks with the Registrar before notice of Extraordinary General Meeting (EGM) is circulated.
3	To convene an EGM.	254(1)(b) & 258(1)	Not Applicable	The company's members at the EGM pass the special resolution for MVL and also appoint a liquidator.
4	To lodge notice of special resolution.	254(2)(a)	11	Notice of Resolution will be lodged to Registrar within 7 days after the EGM.
5	To advertise the special resolution.	254(2)(b)	Not Applicable	Advertisement on the special resolution has to be made within 10 days after the EGM in a newspaper together with the notice proof of debts requesting creditors to claims any debts (if any) within 30 days from the date of notice.
6	To lodge notice of appointment and situation of office of liquidator for MVL.	280(1)	71	Notice of appointment and the situation of office of liquidator need to be lodged to the Registrar and Official Receiver within 14 days after the appointment of Liquidator.
7	To make rubber stamp to notify that a company is in liquidation.	283(1)	Not Applicable	Rubber stamp with the word 'in liquidation' added after the name of company should be made and to ensure all the invoices, notices, letterhead and other relevant documents to the company should used the same name appeared on the rubber stamp.
8	To obtain clearance from relevant government agencies such as IRB, EPF, SOCSO and Customs.	Not Applicable	Not Applicable	The letters should be sent to the relevant government authorities to ensure all the debts incurred with them are settled.

Exhibit 1: The Checklist for MVL (continued)

The checklist on the steps to be taken for winding-up process for Members' Voluntary Liquidation (MVL) is illustrated in Exhibit 1 below:

No.	Steps to be Taken	Related Section of CA 1965	Prescribed Form	Action Required
9	To prepare the Liquidators' Statement of Accounts.	281(1)	75	Within 1 month after the expiration of the period of 6 months of the commencement date of liquidation and for every subsequent of 6 months, the liquidator is required to prepare the Liquidators' Statement and lodge to Registrar and Official Receiver.
10	To summon a general meeting of the company if the winding-up continues for more than 1 year.	271	Not Applicable	The liquidator shall summon a general meeting at the end of the first year from the commencement of winding-up and of each succeeding year or not more than 3 months after the end of the year if the winding-up is unable to dissolve within a year.
11	To inform Registrar if any changes in liquidator's address.	280(1)	73	Any changes on the liquidator's address need to be lodged to Registrar within 14 days after the change.
12	To inform Registrar if any resignation or removal of liquidator.	280(3)	74	Any resignation or removal of liquidator need to be lodged to Registrar and Official Receiver within 14 days.
13	To placed any unclaimed dividend or other moneys to Official Receiver.	286(1)	76 & Unclaimed Money Form	Any unclaimed dividend or other moneys which remained unclaimed for more than 6 months shall be placed to the Companies Liquidation Account and also shall obtain a Certificate of Receipts from the Official Receiver for the amount paid.
14	To convene Final Meeting.	272(2)	Not Applicable	Advertisement on Notice of Final Meeting shall be published in a newspaper circulating generally throughout Malaysia at least 1 month before the meeting.
		272(3)	69	The Return by Liquidator Relating to Final Meeting together with a copy of the accounts need to be lodged to Registrar and Official Receiver within 7 days.
		281(1)	75	The Liquidators' Accounts or Statement of Receipts and Payments need to be lodged to Registrar within 1 months after the Final Meeting.

The Malaysian Institute Of Accountants (“MIA”)

MIA is a statutory body established under the Accountants Act, 1967 to regulate and develop the accountancy profession in Malaysia. To date, MIA has close to 25,000 members. For more information please visit: www.mia.org.my

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In Malaysia, the word “accountant” is protected as provided for under the provisions of the Act which states that no one can hold himself out or practise as an accountant unless he is registered as a member of MIA.

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