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THE STUMBLING BLOCK IN WINDING UP OF FOREIGN COMPANIES

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I. INTRODUCTION

International trade and the fast pacing growth of global economy vis-à-vis any national economy has escalated insolvency proceedings in various countries to a whole new level. It may be in its simplest form having creditors in more than one country or it may be in a form where in a parent company would have its assets, subsidiaries and others in various other countries and not in the country of its incorporation.

One of the most conspicuous drawback of international insolvency law is the lack of legal structures either formal or informal to deal with insolvency that converge the national borders. An important consideration in the context of global economy, has been the expansion and growth of international trade about the aspects such as choice of law and the conflicts that may arise in circumstances of adverse municipal laws. Companies may be affiliated to more than one jurisdiction either by foreign creditors who may make claims or by having assets or branches in multiple countries which in turn would result in decrees that may be passed in different legal jurisdictions resulting in further complexities in enforcement and recognition.

In the abovementioned disguise, the issue of Cross Border Insolvency poses a serious challenge to India. There are insufficient provisions in the Indian common law system to enable the Indian courts to recognize, administer and enforce the rights and claims of the foreign creditors and the decree passed by the courts in foreign jurisdiction. There is nullity of provisions in the existing insolvency enactments or in any legislations in India to deal with Cross Border Insolvency cases, above all. In the light of such circumstances, it has been strongly proposed that India should ratify and adopt the United Nations Commission on Trade Law (UNCITRAL) Model Law on Cross Border Insolvency which would be an ideal solution in the current circumstances.

Indian laws do not *per se* recognise cross border insolvency and insolvency proceedings in India are presently governed by the recently promulgated Insolvency and Bankruptcy Code, 2016. Any insolvency outside India does not affect the Indian entity, unless the Indian entity is also under liquidation due to its insolvency under applicable law. However, if any foreign

judgment needs to be enforced in India, the same may be initiated in accordance with the provisions of the Civil Procedure Code (CPC), 1908.[1] The remedy for execution of such decree of a foreign court is as per Section 44A of CPC as long as such court belongs to a country of reciprocating territory, but in view of the fact that such decree is non-executable as per Section 13 of CPC, and if such decree is non- enforceable, there is no valid claim which can be made as the basis for invoking the power of this Court for winding up of the Insolvent Company.[2]

II. INDIAN COMPANIES ACT ON INSOLVENCY OF FOREIGN COMPANIES

About the Companies Act 2013, it is very essential to note that most of it is based on the English Companies Act 2006 and it recognises similar aspects of international insolvency laws as that of the U.K.[3] The U.K. has a very transparent system of dealing with insolvency proceedings as they follow United Nations Commission on Trade Law (UNCITRAL) Model Law on Cross Border Insolvency. On the contrary, India has not adopted the same and that has been clearly reflected in the Insolvency and Bankruptcy Code 2016 as most of the provisions do not adhere to the Model Law of Insolvency[4]. India therefore, is on a step lower than the U.K and the U.S when it comes to cross border Insolvency, as not much cooperation is sought to recognise international creditors and other such aspects.

"Company" is defined as a company incorporated under this Act or under any previous company law.[5] Therefore, a foreign company not being a registered company under Companies Act 2013, it shall qualify as an unregistered company. Hence, foreign companies shall be dealt under sections 375 and 376 of Companies Act 2013.

Section 375 of Companies Act 2013 is applicable to Foreign Companies in such a manner as to whatever be their number of members, they shall be wound up as unregistered companies.[6] A Foreign company may be wound up as an unregistered company, irrespective of the number of its members, if it has assets in England and notwithstanding it has been dissolved or has ceased to exist as a company under or by virtue of the laws of the country under which

[1] §44A Civil Procedure Code, 1908, (India).
[2] Vanguard Textiles Limited v. GHCL Ltd 9 2007 (5) Bom. C.R.684 10 Company Petition 20 of 2009 decided 26 August 2009
[3] IAN F. FLETCHER, The Law of Insolvency, 4th Edn. 2009
[4] UNCITRAL Model Law on Cross-Border Insolvency (1997)
[5] Section 2(20) Companies Act 2013.
[6] *Cf. Re.*, Travencore National and Quilon Bank Ltd. AIR 1939 Mad 318, Strauss & Co. Ltd., Re, AIR 1937 Bom 15.

it was incorporated.[7] The same principle is applied under the Indian Companies Act as specified under Sections 375 and 376[8]. This can come to a standstill when it can be thought of in such a manner as to how, a company that has ceased to exist in the country of its incorporation would satisfy the orders of winding up in another country through parallel proceedings? To adhere to such orders of winding up in another country there should be the existence of the company in its original sense.

When a winding up order of the company has been made in another country the dissolved company must be revived to satisfy such winding up orders to secure the effective collection and distribution of assets. [9] This is similarly followed in India. Contrary to this, it is to be observed that, when there would be cooperation among different courts under different jurisdictions the thought of reviving a dissolved or an inexistent company does not arise and the creditors abroad as well as in its country of incorporation shall be very well satisfied if a uniform law shall be adopted with access, recognition, relief, cooperation and coordination among different courts under different jurisdictions.[10] A foreign company was dissolved by a foreign court. Therefore, the company had ceased to exist by an act of the country by whose acts and under whose laws it was made a juristic entity and must accordingly be treated as non-existent by all courts applying English law. As the company ceased to exist, it had necessarily ceased to carry on business and could be wound up.[11] Here, it may be very well noted that had the foreign company that had been dissolved affected all the creditors, multiplicity of suits under different jurisdictions could be avoided and for this sake it would be better to adopt UNCITRAL Model Law of Insolvency.[12]

In as much as Section 376[13] is concerned, the justification for creating a statutory exception where by the courts are empowered to wind up a foreign company, even when that company has been dissolved or is in the process of winding up in its home country, is to be found in the overriding necessity to safeguard the legitimate interests of parties in this country, and especially those whose dealings with the foreign company have taken place within the jurisdiction of Indian Courts. Such persons might well suffer prejudice if their fate were

[7] HALSBURY'S LAWS OF ENGLAND, 4th Edn, Vol. 7. Para 1865, Page 999: [1996 Reissue, Vol. 7(3), paras 2899 and 2909]
[8] Companies Act 2013, (India).
[9] *Ibid.*
[10] Key Provisions of UNCITRAL Model Law on Cross-Border Insolvency (1997)
[11] Dairen Kisen Kabushiki Kaisha v. Shiang Kee, (1942) 12 Com Cases 1,3,4 (PC).
[12] UNCITRAL Model Law on Cross-Border Insolvency (1997)
[13] Companies Act 2013, (India)

subjected exclusively to the law of the state of incorporation.[14] The rules of law applied within the foreign legal system might prove to be unfair and discriminatory from the point of view of any creditor who may not be personally attached to that country in question.[15]

Therefore, a Uniform approach shall be made to recognise creditors internationally and to the rule of *pari passu* to be applied to all the creditors by adopting a uniform insolvency law to inculcate cooperation of courts under different jurisdictions. After winding up order is made, the liquidator must deal with the entire body of creditors and not just the creditors within India. [16] The law is that any creditor has a right to approach the Company Court pointing out that its admitted debt is not paid. The Company Court then considers whether the company needs to continue or be wound up and the assets be distributed. The considerations for entertaining a petition for winding up are thus different from entertaining a suit. The jurisdiction is also different. Merely because the creditor is a decree holder, it does not change the character of it as a creditor for maintaining petition for winding-up. There is no warrant to make a distinction between creditors based on decree of which Court they hold.[17] Section 166[18] provides for an application to the court for the winding up of a Company. Any creditor or contributory is entitled to apply for the winding up of the Company. No distinction is made between the creditors residing in India or outside India. Section 167[19] clearly and specifically states that an order for winding up of a Company shall operate in favour of all the creditors and of all the contributories of the Company as if made on the joint petition of a creditor and of a contributory, as the case may be. It is not possible, therefore, to urge successfully, that the order of winding up of an unregistered Company, does not operate in favour of all the creditors and of all the contributories of the Company. All the creditors of the Company can take advantage of the winding up of the Company as operating in India, when it has ceased to carry on business there. There is no reasonable basis for depriving them from participating in the distribution of the assets collected by the Official Liquidator in the winding up proceedings. All the creditors including the foreign creditors will get rateably out of the assets of the Company which have been collected. When that Company itself is wound up, all of them would be entitled to similar rateable share in the assets collected during the

[14] IAN F. FLETCHER, THE LAW OF INSOLVENCY, 4th Edn. 2009
[15] *See*, K NADELMANN, CONFLICT OF LAWS, INTERNATIONAL AND INTERSTATE (The Hague: Nijhoff, 1972) at pp.340 et seq.; *See*, J. HOBSON IN I.F. FLETCHER (ed.) CROSS BORDER INSOLVENCY: COMPARATIVE DIMENSIONS (THE ABERYSTWYTH INSOLVENCY PAPERS) (1990), Ch. 7 at pp.124-130.
[16] Rajah of Vizianagaram v. Official Liquidator, Vizianagaram Mining Co. Ltd, AIR 1952 Mad 136
[17] *Ibid.*
[18] §166 Companies Act 2013, (India).
[19] §167 Companies Act 2013, (India).

winding up proceedings of the Company in the country where it is incorporated."[20] Though these observations were made interpreting the Companies Act, 1913, there is no change in the position under the 1956 Act, that any creditor is entitled to bring a petition for winding up. What this decision indicates is that irrespective of status of the creditor a distinction amongst them is not warranted.[21]The Companies Act do not have any direct provisions where in it does not distinguish between different classes of creditors.

If a creditor with or without a decree of an Indian Court can file a petition for winding up based up on an original cause of action, pending the suit and after decree, there is no warrant to deprive a creditor with a decree of Foreign Court to present a petition for winding up, independently of the decree, in the Company court having jurisdiction.[22]

The Companies Act 2013 does not contemplate such exclusion. To deprive a creditor with a decree of foreign court of this statutory right, will also not be in larger public interest. If a foreign creditor with decree of foreign Court is barred from presenting a petition for winding up on the original course of action and till the decree by Indian Court is passed in its favour, it will make a distinction between two classes of creditors. This will lead to the Indian companies adopting unhealthy practices of borrowing capital abroad and then refuse to repay admitted debts and resist winding up. This will have negative effect on the cross-border flow of capital and international commerce.[23] Therefore, it would be better for such creditors to have a single petition that affects upon the countries in which their interest lies and for the same it is proposed that cooperation must be sought among different courts under different jurisdictions. When there is a decree/judgement of a foreign Court for fastening the liability, it cannot be prima facie said that there would not be any liability at all of the insolvent company.[24] In any case, the aspects of non-enforceability may be required to be considered in execution proceedings, if resorted to, but such cannot be a sole ground to deny the entertainment of the petition for winding up of the Company, on the basis of such liability. Therefore the insolvent company being already adjudged to be liable, it therefore has to consider to make relevant payments to all its creditors and not just one class of creditors.[25]

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[20] *Ibid*.
[21] SIMS Metal Management Limited, Australia v Sabari Exim, Chennai 2015 Indlaw MAD 1480, [2015] 191 Comp Cas 293
[22] Intesa Sanpaolo S.P.A v. Videocon Industries Limited. 2014 183 CC 395 (Bom)
[23] *Ibid*.
[24] Enernorth Industries Inc. v. VBC Ferro Alloys Ltd. reported at [2006]133 Comp Case 130 (AP)
[25] *Ref*, Art. 13 UNCITRAL Model Law on Cross Border Insolvency.

All though there must be assets of a foreign company within the jurisdiction of Indian courts and also a reasonable chance of winding up order would benefit the petitioner before an order of winding up can be made, the assets can be of any nature and do not have to be in the ownership of the company and can come from any source.[26] A Foreign company incorporated in a foreign country may be wound up here, if it has office and assets in India, and the pendency of a foreign liquidation does not affect the jurisdiction to make a winding up order.[27]Where a foreign company is already being wound up in the country of its domicile, the winding up here will be ancillary to the foreign liquidation, and the liquidator's powers in this country are restricted to dealing with assets in this country.[28] Under such circumstances under such judgements, it can rightly be asserted that Indian Companies Act need to adhere to a universal mechanism in order to dispose cases of cross border insolvency of Corporates. This creates a deep chaos and confusion as to the certainty of winding up order in case of cross border insolvency.

III. INSOLVENCY AND BANKURPTCY CODE 2016 ON CROSS BORDER INSOLVENCY

There may be many foreign creditors of an insolvent company who would want to ensure that their rights and claims are enforced even though they may not be connected to the country where the insolvency resolution is taking place. The Insolvency and Bankruptcy Code (IBC) deals with this situation by implication, as it does not differentiate between domestic and foreign creditors. By including "persons not resident in India" in the definition of persons[29]. This new legislation permits foreign creditors to file petitions for winding up and participate in such proceedings under the IBC. Foreign creditors also have the same rights as those of the domestic creditors as regards distribution of assets due to winding up of an insolvent company.

As part of insolvency proceedings, creditors of an insolvent company would want to access the assets of such company which lie under different jurisdictions. Insolvency proceedings may be commenced and ongoing in more than one country with respect to the same debtor. This is notably common when corporate entities face financial difficulties and proceedings against different legal entities within the group are initiated in different jurisdictions. Such

[26] *Re,* Eloc Electro Opiteck and Communicatie B.V., (1981) All ER 1111 (Ch D).
[27] *Re,* Tovarishestvo Manufacture Liudvig-Rabenek (1944) 2 All ER 556.
[28] *Re,* Victoria Society (1913) 1 Ch 167.
[29] § 3(25) Insolvency and Bankruptcy Code 2016 (India).

circumstances are not dealt within the IBC, which presently has inadequate mechanisms for cooperation and coordination among jurisdictions or for an Indian court or tribunal to gain the cooperation of a foreign court or insolvency authority when an insolvency proceeding may have transnational implications.

The Joint Parliamentary Committee's Report[30] induced two new clauses to address these issues.[31] The Central Government may enter into an agreement with the Government of any country outside India for enforcing the provisions of this Code.[32] In situations where a debtor's assets may be located abroad, IBC allows the designated court or tribunal in India to issue a letter of request to a foreign court or tribunal in procuring its assistance.[33] Even these two clauses are subject to bilateral or reciprocal agreements from different countries which may be time consuming and pose certain difficulties due to the need of negotiation between countries. Hence, UNCITRAL Model Law of Insolvency would be more appropriate, if adopted.

IV. CONCLUSION

Adopting the Model Law would hold several merits for India as opposed to relying on several bilateral agreements alone. Firstly, it is a widely accepted standard that has already been adopted by other nations and one with which foreign creditors are familiar. Adopting the Model Law would, therefore, bring much needed certainty for foreign creditors on the rules of access and recognition of foreign insolvency proceedings. Secondly, it would be much faster and easier to adopt and would save the cumbersome process of negotiating bilateral agreements, at least with those nations that have already adopted the UNCITRAL Model Law. Furthermore, India would be permitted to make any changes to suit its needs when enacting legislation based on the Model Law. The Model Law itself foresees such changes, including the exclusion of certain kinds of institutions and exceptions based on public policy. It is perhaps for these reasons that two committees that examined insolvency law reform in India viz., the Eradi Committee in 2005 and the N.L. Mitra Committee in 2001 also recommended that India adopt the Model Law with suitable modifications and accommodations according to Indian standards and practices, though this was never carried out.

[30] *See*, Joint Parliamentary Committee Report of April 2016.
[31] §§ 234 and 235 of Insolvency and Bankruptcy Code 2016.
[32] § 234 Insolvency and Bankruptcy Code 2016.
[33] § 235 of Insolvency and Bankruptcy Code 2016.