

Closure of legal entity in India

Background

One of the pivotal factors for attracting investments in any country is to make available an easy exit option for the investor. It is as important as setting up a new business. Investors put many tangible and intangible resources in a legal entity and hence they deserve an easy and peaceful exit whenever they want to.

A legal entity in India may be required to be closed in following situations:

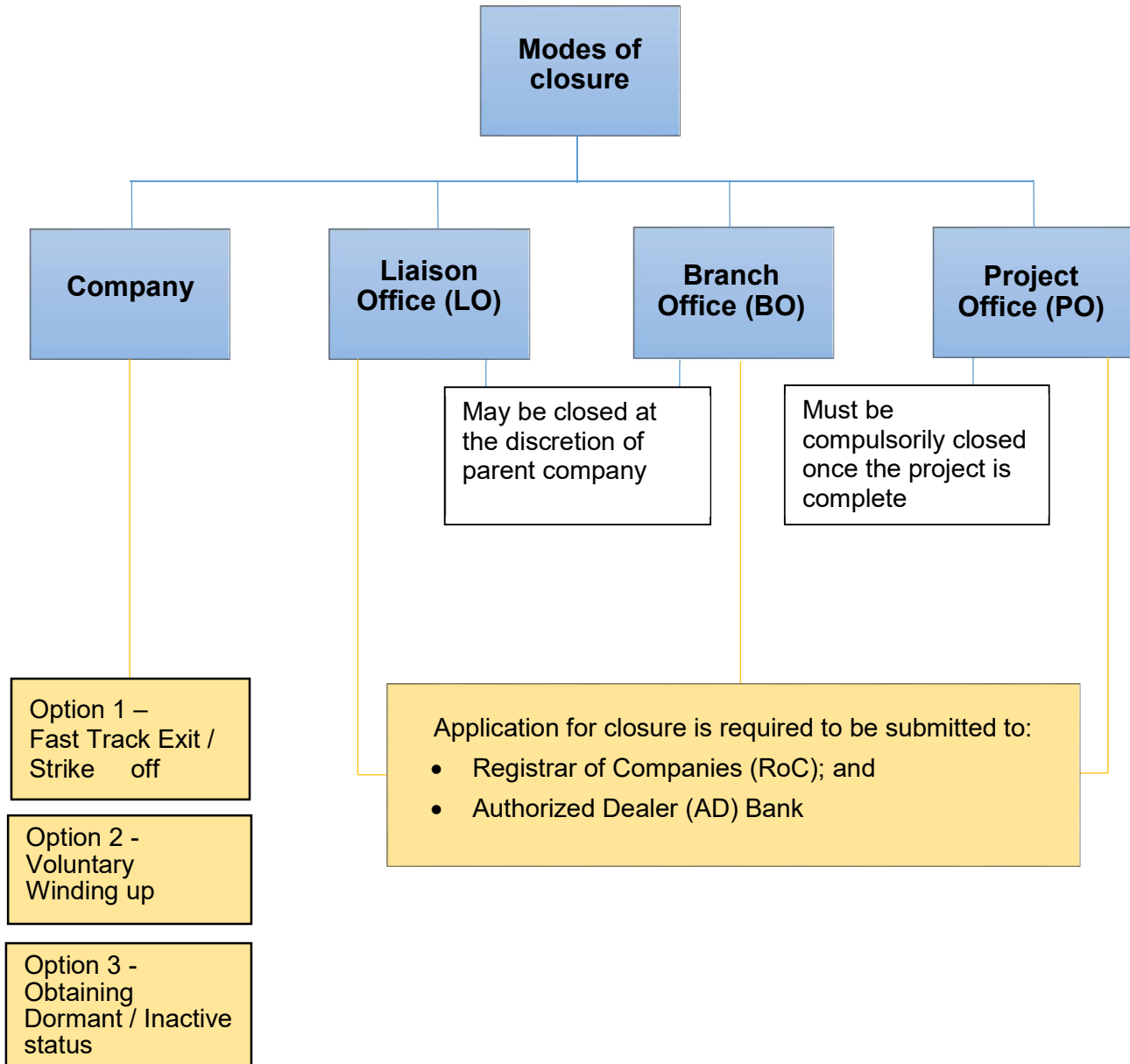
- In case of a liaison office (also called representative office), branch office or project office set up by a foreign company, once the purpose of setting up the liaison office, branch office or project office has been fulfilled, the foreign company may be willing to wind it up
- Losses and / or lack of alternative viable options. If the revenues do not justify the costs incurred, exiting may be a wise option.
- Natural catastrophic events such as a pandemic. A very recent example is exit of many investors due to COVID-19
- Sometimes it is seen that laws / enactments of a particular state or jurisdiction are not very conducive to business. As a result, investors may resort to closure options.

In absence of an efficient exit strategy, investors may suffer significant losses or liabilities.

How to close a legal entity in India?

The main statutes which deal with closure of a legal entity in India are:

- Companies Act, 2013
- Insolvency and Bankruptcy Code, 2016
- Foreign Exchange Management Act, 1999 (FEMA) (in case of foreign investment)



Closure of Company

Option 1 - Fast Track Exit (FTE) / Strike - off

The following conditions are a pre-requisite before a company can apply for closure under FTE / Strike – off mode.

- In case of newly incorporated company, if it has failed to commence business within 1 year of its incorporation
- In case of existing company, if it has not undertaken any business operations during the preceding 2 financial years
- Company should have NIL assets and NIL liabilities at least 30 days before the date of filing application for strike-off
- Company should have closed its bank account in India
- Company must have completed all its annual filings in Forms AOC-4 and MGT-7 with the RoC
- Company must have submitted its tax returns in India
- There must be no pending litigation or proceeding against the company with any statutory authority in India

The process for closure of company under FTE / Strike – off mode is given below.

Step	Action	Details
1	Board of directors' approval for strike off (subject to shareholders' consent)	Convene a meeting of the board of directors of the company to: <ul style="list-style-type: none"> • Approve company's strike off, and • Convene extra-ordinary general meeting of the company's shareholders to obtain their approval for strike off
2	Shareholders' approval for strike off	Convene extra-ordinary general meeting of the company's shareholders for obtaining their approval by way of special resolution for company's strike off
3	Submission of application for strike off along with supporting documents with RoC in e-Form STK-2	Once the shareholders' approval is obtained, company is required to electronically submit the application for strike off along with following documents with RoC in e-Form STK-2: <ul style="list-style-type: none"> • Statement of accounts in Form STK-8 duly certified by a Chartered Accountant, reflecting NIL assets and NIL

		<p>liabilities of the company at least 30 days before the date of filing application for strike-off</p> <ul style="list-style-type: none"> • Certified true copies of the board resolution and shareholders' resolution for company's strike off • Notarized indemnity bonds to be given by each director of the company in Form STK-3 • Affidavits to be given by each director of the company in the prescribed Form STK-4 • Statement regarding pending litigations, if any, involving the company • Company's bank account closure certificate • Latest income-tax return filed by the company • Any other additional documents / information which RoC may require during the course of the strike off process
5	Publication of notice of strike-off by RoC in the official gazette of Government of India	<p>After scrutiny of the application for strike off along with supporting documents / information, RoC shall publish the notice of strike off in the following media:</p> <ul style="list-style-type: none"> • Official gazette of the Government of India • Official website of the Ministry of Corporate Affairs (MCA) • 1 English newspaper and 1 vernacular language newspaper widely circulating in the state where company's registered office is situated
6	Approval of application by RoC	<p>If RoC does not receive any objection against the application for strike-off within 30 days from the date of issue of strike off notice in the official gazette, it shall remove the company's name from its Register and the company shall be considered as struck off / dissolved.</p>

Option 2 - Voluntary Winding up

Voluntary winding-up involves complete dissolution of the company. It can be initiated if below pre-requisites are fulfilled:

- Company has NIL debts. Alternatively, it has sufficient assets to pay off the debts
- Company wants to repatriate surplus funds to the parent company, post its winding up

Voluntary winding up is a detailed, time-consuming, court-driven process and involves appointment of a Liquidator who must be an Insolvency Professional registered under Insolvency and Bankruptcy Code, 2016.

The process for closure of company under voluntary winding up mode is given below.

Step	Action	Details
1	Board of directors' approval for voluntary winding up (subject to shareholders' consent)	<p>Convene a meeting of the board of directors of the company to:</p> <ul style="list-style-type: none"> • Approve voluntary winding up of company • Approve appointment of Insolvency Professional as Liquidator of company • Approve declaration of solvency provided by majority of directors of the company • Convene extra-ordinary general meeting of the company's shareholders to obtain their approval for voluntary winding up
2	Shareholders' approval for voluntary winding up	<p>Convene extra-ordinary general meeting of the company's shareholders for obtaining their approval by way of special resolution for:</p> <ul style="list-style-type: none"> • Voluntary winding up of company • Appointment of Insolvency Professional as Liquidator of company • Declaration of solvency provided by majority of directors of the company
3	Creditors' approval, if any	<p>If company has creditors, representing 2/3rd in value of the total debt of the company, then company shall also seek approval of its creditors within 7 days from the date of extra-ordinary general meeting of the shareholders</p>

4	Public Announcement	<p>The Liquidator shall make a public announcement of voluntary winding up within 5 days from the date of extra-ordinary general meeting of the shareholders, in both English and vernacular language newspapers widely circulating in the state where company's registered office is situated.</p> <p>The public announcement shall call upon the stakeholders to submit their claims, if any, within 30 days from the date of extra-ordinary general meeting of the shareholders</p>
5	Submission of Form MGT-14 with RoC	Company shall submit special resolution passed at the extra-ordinary general meeting of the shareholders in Form MGT-14 with RoC within 7 days from the date of the extra-ordinary general meeting
6	Intimation to Income-tax department and Insolvency and Bankruptcy Board of India (IBBI)	Company shall intimate the Income-tax department and IBBI about the voluntary winding up
7	Opening of separate bank account	<p>Liquidator shall open a separate bank account of the company followed by the words 'in voluntary liquidation', in a scheduled bank within 30 days from the date of extra-ordinary general meeting of the shareholders.</p> <p>Going forward, all the winding up related transactions such as payment of claims to the stakeholders, liquidation cost, etc shall be made out of this bank account.</p>
8	Receipt of claims from stakeholders and distribution of proceeds	<ul style="list-style-type: none"> • Liquidator shall receive claims from all the stakeholders in the prescribed form within 30 days from the date of extra-ordinary general meeting of the shareholders • Liquidator shall verify the claims received from the stakeholders, and • Liquidator shall distribute claim proceeds to the concerned stakeholders within 6 months from the date of receipt of claims
9	Preparation and submission of reports with IBBI	<p>Liquidator shall prepare and submit the following reports with IBBI :</p> <ul style="list-style-type: none"> • Preliminary report within 45 days from the date of extra-ordinary general meeting of the shareholders, containing the capital structure of the company and estimates of assets and liabilities

		<ul style="list-style-type: none"> • Progress Report within 15 days from the end of each quarter, stating the progress of winding up of the company
10	Time period for completion of winding up	<p>Liquidator shall endeavour to complete the process of winding up within 1 year from the date of extra-ordinary general meeting of the shareholders.</p> <p>In case winding up is not completed in 1 years' time period, Liquidator shall hold annual meeting of the company's shareholders within 15 days from the end of each year till the time company is finally wound up</p>
11	Preparation and submission of Final report with IBBI, RoC and National Company law Tribunal (NCLT)	<p>Once all the affairs of the company have been wound up, Liquidator shall prepare and submit Final report with IBBI, RoC and NCLT, alongwith the following documents:</p> <ul style="list-style-type: none"> • Audited accounts of liquidation • Statement of assets that have been disposed of • Debts of the company that have been discharged, and • Other matters pertaining to liquidation
12	Submission of final petition of winding up with NCLT	Liquidator shall prepare and submit final petition of winding up of the company with NCLT in the prescribed form.
13	Issue of final order of winding up by the NCLT and its subsequent submission with RoC	<p>If the petition along with all the submitted documents is found to be in order, then NCLT shall issue the final order for voluntary winding up of the company.</p> <p>On receipt of the final order, the same is required to be submitted in Form INC-28 with the RoC within 14 days from the date of the order.</p> <p>Once Form INC-28 is approved by the RoC, the company shall stand dissolved and completely wound up for all records</p>

Comparison between FTE / Strike - off and Voluntary Winding up

Parameter	FTE / Strike-off	Voluntary Winding up
Pre-requisite before submission of application for closure	<ul style="list-style-type: none"> • Company must not have undertaken any business operations during the preceding 2 financial years • Company must have NIL assets and NIL liabilities at least 30 days before the date of filing application for strike off • Company should close its bank account 	Company must have NIL debts, or in case of debts company must have sufficient assets to pay off the same
Governing law	Companies Act, 2013	Insolvency and Bankruptcy Code, 2016
Repatriation of surplus funds to parent company after closure	It is not possible to repatriate surplus funds to parent company after strike off (since 1 of the prerequisite conditions for strike off is that, company should have NIL assets and NIL liabilities)	It is possible to repatriate surplus funds to parent company after winding up
Tenure	Since there is no involvement of Court, the time period for completion of entire process ranges between 6 to 8 months (approx.), thereby making it simpler and faster process compared to winding up	Due to the involvement of Court, it is a time consuming and lengthy procedure and may take 1 to 2 years (approx.) to complete. The time period may vary since ultimate discretion to grant approval lies in the hands of the Court
Revival after closure	The company once struck-off may be revived at the discretion of the management within 20 years from its closure	The company once wound up cannot be revived at the discretion of the management

Option 3 - Obtaining Dormant / Inactive status

An alternative to completely closing the company (through strike off or voluntary winding up) is to continue the company but under 'dormant' or 'inactive' status. The benefit of this option is, in case the company / promoters want to restart the business operations in future, they can do so without the hassle of reviving the company. It usually takes about a month or so to obtain dormant / inactive status for a company.

The following conditions are a pre-requisite for a company to obtain dormant / inactive mode.

- The company must not have undertaken any business operations during the preceding 2 financial years, or
- The company must not have undertaken any 'Significant Accounting Transactions' during the preceding 2 financial years. 'Significant Accounting Transactions' for this purpose means any transaction except the following:
 - ✓ Payment of statutory fees to RoC
 - ✓ Payment to fulfil requirements under Companies Act, 2013 or any other law
 - ✓ Allotment of shares to fulfil requirements of Companies Act, 2013
 - ✓ Payments for office maintenance and records

A dormant / inactive company remains alive but only upto 5 years from the date of obtaining the dormant / inactive status. In case the business operations are to be revived within 5 years, an application for business revival needs to be submitted in Form MSC-4 with RoC. Annual compliances such as return of dormant company is required to be submitted with RoC in Form MSC-3 indicating the financial position of the dormant company, duly audited by the Chartered Accountant on or before 30 April each year. Thus, certain minimum annual costs are required to be incurred by the promoters to keep the company alive (dormant / inactive) for these 5 years.

In case the company remains dormant / inactive for more than 5 years, RoC removes its name from the 'Register of Dormant Companies' maintained by it. Thereafter, the company is treated as closed / dissolved.

Closure of LO / BO / PO

LO / BO / PO are treated as extension in India of the foreign parent company.

An LO can do only liaison activities in India and thus, act as a communication channel between its overseas head office and Indian parties. LO is not allowed to undertake any commercial activities.

Unlike LO, BO can undertake commercial activities and earn profits in India. Profits earned by a BO are freely remittable from India, subject to payment of applicable taxes in India.

PO is common in infrastructure / construction sector. PO cannot carry out any activity other than those which are related to or incidental to the project for which it is set up. PO must be closed once the specific project is complete.

The process for closure of LO / BO / PO is explained in brief below.

Step	Action	Details
1	Submission of application for closure with RoC in e-Form FC-2	<p>LO / BO / PO is required to submit application with RoC in e-Form FC-2 along with the following documents:</p> <ul style="list-style-type: none"> • Letter of approval issued by AD Bank / Reserve Bank of India (RBI) for opening of LO / BO/ PO in India • Power of Attorney / Board resolution from the parent company authorizing closure of LO / BO / PO <p>Once the e-Form FC-2 is approved, Certificate for closure of place of business is issued by the RoC. The LO / BO / PO is considered as closed in the records of RoC.</p>
2	Submission of application for closure with AD Bank	<p>Since LO / BO PO are incorporated only after obtaining approval from AD Bank / RBI, it is necessary to get them closed in records of AD Bank / RBI. This is done by submitting an application for closure manually with the AD Bank along with following documents:</p> <ul style="list-style-type: none"> • Letter of approval issued by AD Bank / RBI for opening of LO / BO/ PO in India • Auditors certificate certifying the following: <ul style="list-style-type: none"> ✓ The LO / BO / PO has no pending liability in India (such as gratuity, benefits to employees or otherwise, etc.) ✓ No income arising from sources outside India has remained unrepatriated to India ✓ In case of remittance of surplus funds to the parent company, the exact manner in which remittable amount has been

		<p>computed, duly supported by a statement of assets and liabilities</p> <ul style="list-style-type: none"> • Declaration from the parent company that no legal proceedings are pending against the LO / BO / PO • Certificate for closure of place of business issued by RoC • Confirmation that all Annual Activity Certificates have been filed till date • Any other additional documents / information which AD Bank may specifically require during the course of the closure
3	Issue of closure letter by AD Bank	After scrutiny of the application, AD Bank shall issue the closure letter on satisfaction. Thereafter, the LO / BO / PO shall be considered as closed in the records of RBI.
5	Bank account closure	Once the LO / BO / PO is closed, its bank account shall also be closed subject to clearance of all pending dues, if any
6	Surrender of tax registrations	The LO / BO / PO shall surrender its tax registrations in India such as Permanent Account No (PAN), Tax Collection Account Number (TAN) and Goods and Services Tax (GST)

How KrayMan can support

- Analysis of suitable options for closure of legal entity in India
- Preparation of road map for closure of legal entity
- Handholding the client in the process for closure of legal entity
- Preparation, submission of applications and representation before the RoC, RBI and other statutory authorities on behalf of client
- Obtaining final order / certificate of closure from statutory authorities
- Surrender of tax and other registrations after closure of legal entity

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