Compulsory winding up

Legal information for companies limited by guarantee and incorporated associations

This fact sheet covers:

- when your organisation can be compulsorily wound up
- winding up in insolvency
- winding up on other grounds, and
- what happens if a court makes a winding up order.

Winding up

The process of 'winding up' requires an organisation to take all steps necessary to stop operating (including selling off assets) and eventually 'dissolve'.

The winding up process can happen if:

- the court makes a 'winding up order', referred to as 'compulsory winding up', or
- the members or creditors of an organisation decide they want to wind up voluntarily ('voluntary winding up').

The process of compulsory winding up is set out under the *Corporations Act 2001* (Cth) for companies limited by guarantee and the State-based incorporated associations' legislation for incorporated associations.

RELATED RESOURCES

This fact sheet does not discuss 'voluntary winding up' by members, which can occur only where an organisation is solvent. For more information, see the Ending the organisation page of the Not-for-profit Law Information Hub at www.nfplaw.org.au/windingup.

When can your organisation be compulsorily wound up?

Compulsory winding up occurs when a person or organisation makes an application to the court to make a winding up order. Although this is described as 'compulsory' winding up, in many cases the organisation may consent to the court's order to be wound up. Compulsory winding up usually happens in one of two circumstances:

1. **Insolvency:** An organisation is insolvent when it is unable to pay its debts when they become due and payable. An application can be made to the court that an organisation be wound up because it is insolvent.
2. **Other grounds:** An application to be wound up might also be made even if an organisation is solvent. The circumstances in which that might occur are discussed below, but generally include where there is a special resolution by the organisation to do so, there is a breakdown or failure in management of the organisation, or where the organisation has become defunct, or never started operating.

There are limits on who can make an application for a winding up order (see discussion below).

Winding up in insolvency

Who can apply?

Generally, an application to wind up an organisation can be made by:

- the organisation itself
- a creditor
- a member
- a director or liquidator (for companies only)
- the regulator (ie. for companies, the Australian Securities and Investments Commission (**ASIC**)).

There may also be others who can apply, depending on the type of organisation (ie, company or incorporated association) and where the association is located. In some circumstances, approval of the court is needed before an application can be made.

In most cases, the application will be made by a creditor who must prove to the court that the organisation is insolvent. Usually, this will involve:

- a creditor who is owed money by the organisation providing the organisation with a document called a 'statutory demand' or a 'creditor's demand'
- the organisation failing to pay the statutory demand or creditor's demand, or commencing a court proceeding to have the demand set aside within 21 days after the demand is received. If the organisation fails to pay the demand, or the court proceeding is dismissed, a presumption that the organisation is insolvent arises, and
- the creditor then commencing court proceedings, seeking an order that the organisation be wound up.

RELATED RESOURCES

For more information on insolvency, read Not-for-profit Law's 'Insolvency and your organisation' fact sheet on the Governance page of the Information Hub at www.nfplaw.org.au/governance.

The organisation can only oppose a winding up order in certain circumstances. The organisation would generally also need to prove it is solvent given the presumption of insolvency which arises following non-payment of the statutory demand or creditor's demand.

NOTE

There are many other ways an organisation can be wound up in insolvency, but almost all of them begin with a statutory demand or creditor's demand, or legal proceedings (or both). There are very specific rules that relate to the form of the demand and the time limits which apply to this process. If you are served with a demand, you should seek legal advice immediately.

What should we do if we receive a statutory demand or creditor's demand, or we are struggling to pay our debts?

If your organisation receives a statutory demand or creditor's demand, or you are concerned that your organisation may not be able to pay its debts when they become due, the consequences of doing nothing can be extremely serious. Your organisation should urgently seek legal advice or advice from an accountant specialising in insolvency. You can find a list of firms that offer insolvency services on the Australian Restructuring Insolvency & Turnaround Association website and the Turnaround Management Association website at www.turnaround.org.au/member-search.php.

One of the things your organisation might be advised to do is to appoint a 'voluntary administrator' before an application for compulsory winding up is made. This is explained briefly below.

What is 'voluntary administration'?

One option open to most organisations facing insolvency is for its directors or committee members to resolve that:

- in the opinion of the directors or committee members voting for the resolution, the organisation is insolvent or is likely to become insolvent at some future time, and
- an administrator of the organisation should be appointed (called a 'voluntary administrator').

A voluntary administrator must be a specialist accountant or lawyer who is registered with ASIC as a liquidator. A firm offering insolvency services should be able to recommend a voluntary administrator. You can check if the person you are considering is registered by searching the ASIC online database.

The voluntary administrator takes full control of the organisation to investigate its affairs. They prepare a report to the creditors on the organisation's options, and a meeting of the creditors is then held to decide the future of the organisation. The options that are considered by the creditors are whether:

NOTE

A decision to appoint a voluntary administrator has very serious consequences and should not be taken before your organisation has obtained legal and/or other professional advice.

- the organisation be returned to the control of the directors or the committee members
- a 'deed of company arrangement' is to be entered into by the organisation. This is a binding agreement between the organisation and its creditors about how the organisation's affairs are to be handled. A deed of company arrangement usually means the organisation would continue, or
- the organisation be wound up (this is called a creditor's voluntary liquidation).

The main advantages of voluntary administration for an organisation are:

- if the directors or committee members act promptly, a decision to appoint a voluntary administrator may protect them from personal liability (legal responsibility) for allowing the organisation to incur new debts when it is insolvent, and

- it provides a chance for an organisation that is struggling financially to restructure and reduce its debts, in order to continue its operations in a more sustainable manner.

Winding up on other 'non-insolvency' grounds

An organisation can also be compulsorily wound up on a number of 'non-insolvency' grounds. The exact grounds available depend on the type of organisation (eg. whether it is a company limited by guarantee or incorporated association) and where the association is located. However, they generally include when:

- the organisation has resolved by special resolution to be wound up by the court
- the organisation has not commenced any activities or has suspended its activities, generally for a period of at least a year
- the organisation does not have the minimum number of members, or
- the court believes it is 'just and equitable' that the organisation be wound up.

Other grounds for winding up a company limited by guarantee include when:

- in conducting the affairs of the company, the directors have acted in their own interests rather than in the interests of the members as a whole, or in any other manner which appears unfair or unjust to members
- the affairs of the company are being conducted in a manner that is oppressive or unfairly prejudicial to, or unfairly discriminatory against a member
- the company or a group of its members does something (or fails to do something) which is or would be oppressive, unfairly prejudicial or unfairly discriminatory against a member or members, or the interests of the members as a whole, or
- ASIC has prepared a report stating that, in its opinion, the company cannot pay its debts or it is in the interests of the public that the company be wound up.

Other grounds for winding up an incorporated association generally include when:

- the association has provided pecuniary (monetary) gain for its members, or
- the association has engaged in activities outside or inconsistent with its purposes.

Generally, a compulsory winding up would be ordered by the court. However, some States and Territories allow the regulator to wind up or cancel the registration of an incorporated association without seeking the court's permission.

Who can apply?

An application to a court on any of these grounds can generally be brought by:

- the organisation itself
- a creditor
- a member
- a liquidator of the organisation, or
- various government bodies (eg. ASIC or State-based regulators).

In some circumstances, an application to wind up a company can also be brought by a former member or a person whom ASIC thinks appropriate. This could occur if the application to wind up the organisation is brought because of conduct which is or would be oppressive, unfairly prejudicial or unfairly discriminatory against a member or members, or the interests of the members as a whole.

What are the steps for applying to a court for winding up on non-insolvency grounds?

An application to a court for winding up on grounds other than insolvency requires a court application to be prepared in the approved form. The application must set out the reasons relied on to seek winding up orders. That application must also be supported by a sworn statement or statements (called affidavits) which verify the grounds for making those orders.

In a simple uncontested case (for example, where the organisation has resolved by special resolution to be wound up by the court), the application will be reasonably straightforward and the supporting affidavit will simply confirm that the resolution was validly passed. Simple, uncontested applications should be determined within a few weeks.

However, in cases where the application is made in the context of some alleged mismanagement or a dispute, the application will be much more complex and be similar in scale to contentious litigation.

In either case, the application and affidavits must be:

- lodged with a court (either the relevant State's Supreme Court or the Federal Court), and
- served on (ie. provided to) various interested parties (in particular, the organisation if it is not the one making the application).

In more complex applications, the court registry will usually allocate the application to a judge, and a court listing will be set a few weeks from the lodgement of the application so that the judge can hear from the interested parties and make directions for any further steps that need to be taken before a final hearing. It would be unusual for more complex applications to be finally heard and determined in less than a few months, and in some cases, they can take much longer.

What happens if a court makes a winding up order?

If the court agrees with the application for winding up (whether it be on grounds of insolvency or otherwise), the court will order that:

- the organisation be wound up, and
- a liquidator or liquidators be appointed to the organisation.

Usually, the applicant will have obtained a signed consent to act from a suitable liquidator before the court makes its final decision, and the court will appoint that person as the liquidator.

There are consequences for the organisation once liquidators are appointed – it is not 'business-as-usual'. Upon appointment of the liquidator, control of the organisation passes immediately to them. They then proceed to collect and sell the organisation's assets, pay off creditors, investigate the organisation, provide annual reports and so on, with a view to ending the organisation's affairs.

RELATED RESOURCES

To answer your frequently asked questions on ending an organisation, see our FAQs resource on the Not-for-profit Law Information Hub at www.nfplaw.org.au/windingup.

Following a compulsory winding up:

- there must be a notification in all public documents and negotiable instruments (eg. cheques or bills of exchange) that the organisation is in liquidation
- the organisation's property can only be disposed of by the liquidator in a certain way
- legal proceedings against the organisation cannot be commenced or continued without the court's permission, and
- depending on the specific circumstances, certain transactions entered into by the organisation for a period prior to the compulsory winding-up or voluntary administration could be voidable (not valid and therefore not enforceable).

There may be additional consequences for current or former directors or committee members of the organisation, including:

- the liquidator bringing legal proceedings against them for allowing the organisation to incur new debts while it was insolvent, and
- in certain circumstances, ASIC disqualifying, or applying to a court for orders disqualifying that person from managing corporations if they were involved with another organisation which also entered liquidation.

Resources

Related Not-for-profit Law Resources

- Changing or ending your organisation – www.nfplaw.org.au/changingorending

This Not-for-profit Law page on the Information Hub provides information on changes to an organisation's constitution, changes to an organisation's structure, the ending of an organisation and voluntary cancellation or deregistration.

- Governance – www.nfplaw.org.au/governance

This page features resources on the legal duties of boards, committees and office holders, and insolvency.

Other Related Resources

- Australian Securities and Investments Commission (ASIC)

This ASIC webpage provides information on closing down a company.

- ASIC Professional Register

This ASIC webpage allows you to search in its Professional Registers.

- Australian Restructuring Insolvency & Turnaround Association (ARITA)

ARITA is a professional body for insolvency practitioners.

- Turnaround Management Association (TMA)

TMA is a professional body for insolvency practitioners.

Legislation

- *Associations Incorporation Reform Act 2012* (Vic)
- *Associations Incorporations Act 2009* (NSW)
- *Associations Incorporations Act 1981* (QLD)
- *Associations Incorporations Act 2015* (WA)
- *Associations Incorporations Act 1985* (SA)
- *Associations Incorporations Act 1991* (ACT)
- *Associations Incorporations Act 1964* (Tas)
- *Associations Act* (NT)
- *Corporations Act 2001* (Cth)

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