

LESSON 13: DISSOLUTION, LIQUIDATION AND EXTINCTION OF COMPANIES

SUMMARY:

- 1.-Dissolution
 - a) Causes
 - b) Requirements and procedure
 - c) Advertising
- 2.-Liquidation
 - a) Liquidation bodies
 - b) Procedure
- 3.-Extinction
- 4.- Vocabulary

1.-Dissolution

A company can be considered, on one hand, a contract signed by at least two people and, on the other hand, a legal person which has several legal relationships with third parties. In order to protect those third parties, as well as the company itself and its partners, the final extinction of a company should go through two different stages. The first one would be dissolution, in which the company continues to be a legal person but ceases its commercial purpose and starts the liquidation. The second one would be liquidation, in which the company compensates its credits and debts vis-à-vis third parties and distributes the corporate assets resulting from the liquidation among all shareholders. Once the liquidation procedure is finished, the registered entries of the dissolved company will be cancelled. From this moment, the company will be extinguished.

CAUSES:

Three different types of causes can be distinguished:

a) Causes which lead to an automatic dissolution of the company (art. 360 LSC)

- Expiry of the term established in the articles of association of the company. In order to avoid dissolution in this case, a general meeting resolution will be required to extend the duration of the company agreement.
- When the company has not been converted, dissolved or its capital share has not been increased within a year after being obligated to reduce its share capital below the minimum amount established by law.

- In case of a merger or spin-off
- When the company fails to comply with a Court decision which obligates it to change the company name within a year because it infringes a previous trademark.
- A company's bankruptcy does not lead to an automatic dissolution of the company. The company is only dissolved when the liquidation phase is opened during the insolvency procedure.

b) Causes which require a general meeting resolution (arts. 363 and 364 LSC)

- When the company has ceased its commercial purpose for more than one year.
- When the company's commercial purpose has been met.
- When the company's commercial purpose is obviously impossible to meet.
- When there is a deadlock between the governance bodies which renders the company's operations impossible. This event especially affects the general meeting. A deadlock among the administration body can be solved using alternative directors or other possible legal solutions.
- When there are losses that reduce the company's assets to less than half of the share capital established in the articles of association of the company. In order to avoid dissolution in this case, it will be necessary to reduce or increase share capital or increase the company's assets without amending the share capital established in the articles of association.
- When there is a share capital reduction to below the minimum amount of share capital established by law for each type of company. In order to avoid dissolution in this case, it will be necessary to increase share capital to an amount which is equal to or higher than the minimum amount of share capital established by law for that type of company or to convert the company into another type which requires a lower amount of share capital.
- When the par value of shares without voting rights exceeds half of the share capital already paid in by the shareholders for more than two years.

- In any other events established in the articles of association of the company.

c) Dissolution of the company by a general meeting resolution adopted according to the quorums and majorities required by the law or the articles of association (art. 368 LSC).

In partnerships, some dissolution causes affecting one or several partners should be added to the list. In this type of company, the death or insolvency of one partner may lead to the dissolution of the company, unless otherwise established in the articles of association.

REQUIREMENTS AND PROCEDURE

As we have already studied, there are some events which automatically lead to the dissolution of the company. Other events, nevertheless, need a general meeting resolution as a prior requirement to dissolve the company. In these cases, any shareholder can ask the administrative body to convene the general meeting, but the administrative body also has the obligation to convene the general meeting within two months after one of the causes for dissolution occurs, in order to adopt the suitable resolution (art. 365 LSC). In the event that the general meeting is not convened or held or the resolution to dissolve the company is not adopted, any interested party can request the Commercial Court Judge of the company's domicile to dissolve the company (art. 366 LSC).

Apart from this, the administrative body has strict liability when breaching this obligation. The directors will be jointly and severally liable for all the company's debts arising after the cause for dissolution (art. 367 LSC).

ADVERTISING

The company dissolution should be entered in the trade Register and published in the BORME.

2.-Liquidation

The liquidation starts with the adoption of the resolution to dissolve the company and the appointment of the liquidating body which will manage the liquidation operations. These operations consist basically of paying all the company's debts and distributing the resulting assets among all shareholders in proportion to each ones' contributions to the share capital. During this period, the company continues to be a legal person but its activity will be orientated towards the final extinction of the company.

LIQUIDATION BODIES

1.-*Liquidating body*. Once the liquidation period starts, the directors of the company suspend their activities and are replaced in their duties by the liquidating body. The liquidating body should be formed by an odd number of members appointed by the general meeting, unless otherwise established in the articles of association of the company (arts. 374 and 375 LSC).

2.-*General meeting*. The general meeting continues its activity during this period. The LSC sets out that all the rules concerning the notice and correct functioning of the general meeting continue to be applicable. The only difference is that the activity of the general meeting should be orientated towards the liquidation and final extinction of the company.

3.-*Receivers*. Regarding public LLCs, shareholders who represent 20% of share capital are allowed to request the Commercial Court Judge of the company's domicile to appoint a receiver who can supervise the liquidation operations and the final liquidation balance sheet (art. 381 LSC).

PROCEDURE (arts. 383 to 394 LSC)

- The resolution to dissolve the company which should be executed in a public deed and registered in the trade register implies the commencement of the liquidation period of the company. At the beginning of this period, an initial liquidation balance sheet will be drawn up.
- Once the liquidation period is open, the liquidating body will start to discharge its duties consisting mainly of managing the transactions to cancel outstanding liabilities of the company and to realize its assets (credits, real estate, etc.). During that period, the company may continue performing its business as a legal person although its activity will be affected by the fact that the company is close to its extinguishment. In order to make this public, the company should add the statement "under liquidation" to its name.
- Upon conclusion of the liquidation transactions, a final liquidation balance sheet will be drawn up by the liquidating body, including full information about the liquidating operations carried out and the proposed distribution of the company's assets resulting from the liquidation. The final liquidation balance sheet should be approved by the general meeting and the general meeting resolution can be challenged by all shareholders who voted against this.
- Finally, the assets resulting from the liquidation are distributed to the shareholders according to certain rules:
 - 1.-Shareholders who own shares without voting rights have preference when receiving the liquidating dividend.

2.-The distribution of the liquidating dividend should be made in proportion to the par value of the shares owned by each shareholder, unless otherwise established in the articles of association.

3.-The articles of association of the company may establish that certain shareholders receive the assets resulting from the liquidation in kind or through the restitution of non-monetary contributions.

3.-Extinction

In order to extinguish the company, it is necessary that the liquidating body executes the public deed of extinction in which some information is required. The public deed should report that (art. 394 LSC):

- the general meeting has approved the final balance sheet,
- nobody has challenged the general meeting resolution during the period in which they can do this, or that the Commercial Court Judge's decision on this issue has become final.,
- all the company's debts have been paid,
- all the shareholders have received their liquidating dividend.

Once the public deed is executed by the liquidating body, the Trade Register is requested to cancel the registered entries of the dissolved company, which will then be finally extinguished and will cease to be a legal person.

The LSC takes into account the possibility that new company credits or debts may arise after cancelling the registered entries.

- In the case of new company credits, the LSC sets out that the liquidation body will have to distribute the additional liquidation dividend to all shareholders according to the rules applied in the liquidation period (art. 398 LSC).
- In the case of new company debts, shareholders will be jointly and severally liable for them but they cannot exceed the amount received in their liquidating dividend. Apart from this, the liquidating body will be liable for damages when the new debts are the consequence of its negligent action (art. 399 LSC).

4.- Vocabulary

Dissolution- Disolución

Liquidation- Liquidación

Extinction- Extinción

To cancel the registered entries of the company- Cancelar los asientos de la sociedad

Deathlock between the company's bodies- Paralización de los órganos de la sociedad

Liquidating body- Liquidadores

Receivers- Auditores

Liquidating dividend- Cuota resultante de la liquidación

To receive the liquidation dividend in kind- Recibir la cuota resultante de la liquidación en especie

Final liquidation balance sheet- Balance final de la liquidación