

No. 19(928)CF/ISS/96-
SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
(Monitoring & Enforcement Division)
State Life Building, 7-Blue Area,
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Subject: **ORDER TO ISSUE NOTICE UNDER SECTION 472 READ WITH SECTION 496 IBID OF THE COMPANIES ORDINANCE, 1984 IN CASE OF MIS. SITARA ENERGY LIMITED**

The examination of accounts of M/s. Sitara Energy Limited revealed that the company paid donations amounting to Rs. 6,609,169/- in year 1998 and Rs. 38,487,202/- in the year 1999 out of which Rs. 6,209,543/- and Rs. 37,023,000/-for the years 1998 and 1999 respectively were paid to Aziz Fatima Trust. Further, six directors of the company including the Chief Executive are the trustees of the said Trust as per information given in the relevant notes to the account. Karachi Stock Exchange also reported this irregularity to the Commission through its letter No.KSE/SECP/945, dated 21-02-2000.

2. A review of the Company's Memorandum of Association revealed that it does not contain any clause authorizing it to pay donations. The main object the company is to carry on the business of Electric Power Supply and to fulfill this object, the company may do such acts which are incidental to the main business and conducive to attaining the main object. Since quantum of donation paid was very high i.e. in the year 1999 it calculate to above Rs.2 per share, it was decided to inquire from the company about the details of donations and justification thereof. It was also decided to obtain minutes of the board's meetings in which donations were authorized. In response to Commission's letter dated 30th January, 2000, the company vide its letter dated 7th February, 2000 explained its position in the following manner:-

QUOTE

01. "Our Company owns the biggest Power Plant in private sector and is making good profits and paying handsome dividend to the shareholders. No energy company in private sector is

paying such a higher rate of dividend.

<u>Year Ending</u>	<u>Cash Dividend</u>
30.06.1999	60%
30.06.1998	35%
30.06.1997	25%
30.06.1996	30%

It is evident from the above that donation is not given at the expense of the shareholders who are getting ample return on their investment.

02. No pecuniary interest of Directors/Trustees is involved in both the hospitals. Rather, they make donations from their own pockets in addition to those made by the company.
03. It is purely a charitable donation which is not prohibited under Companies Ordinance, 1984.
04. Pakistan being less developed country, Government sources are limited which make it difficult to provide adequate medical care to the people. So, by giving such liberal donations, we are supplementing the Government welfare activities. Such efforts therefore ought to be encouraged and appreciated.
05. Two modern hospitals namely Aziz Fatimah Trust Hospital having 200 beds and Ghafoor Bashir Children and Maternity Hospital having 100 beds are being run under the aegis of Aziz Fatimah Trust. Aziz Fatimah Trust Hospital has a team of Specialist Doctors in the field of medicine, surgery, coronary care, Gynecology, neuro medicine, neuro surgery and urology. The facilities of Ultra Sound, X-ray, well-equipped Laboratory, ICU, CCU and Dialysis are also available. Centrally fitted Oxygen supply in medical and surgical wards. Ghafoor Bashir Children and Maternity Hospital is the first pediatric hospital in private sector at Faisalabad. In this hospital the facilities of Pediatric general surgery for emergency and routine operations, Xray and Ultra Sound, well-equipped Laboratory for hematological, biochemistry, microbiological and

serological tests including electrophoresis system are available. Centrally fitted Oxygen supply is also available in medical and surgical wards. Neonatal Intensive Care Unit having incubators and ventilators which is the first modern facility in Faisalabad. To sum up, it is a beautifully designed and built hospital in Faisalabad.

Both the hospitals are providing adequate medial care to the poor, needy and suffering humanity, on charitable basis. The special facilities at Children hospital are rarely available in Government or private hospitals in Faisalabad.

06. For your information year-wise accounts of out-door patients for the last three years is appended in respect of both hospitals:

<u>Year</u>	<u>Aziz Fatimah Trust Hospital</u>	<u>GhafoorBashir Children and Maternity Hospital</u>
1996-97	84,721	34,228
1997-98	82,376	37,673
1998-99	82,200	35,636

07. The annual expenditure of both the hospitals is nearly 35,000 million.
08. The donations have been made for the uplift, modernization and upgrading of the existing medical and surgical facilities so that the people of Faisalabad and surrounding areas may not go to Lahore/ Islamabad / Karachi for getting treatment.

Unquote.

3. The Minutes of boards meeting held on 23rd February, 1997 revealed the proceedings and resolution in the following manner :-

QUOTE

“Haji Bashir Ahmed Chairman of the Company, stated that Aziz Fatimah Trust is a charitable institution duly approved by the Central Board of Revenue, Islamabad under section 47(1) (d) of the Income

Tax Ordinance, 1979. Renewal of the same is accorded by the Regional Commissioner Income Tax on year-to-year basis. This trust is running two full-fledged hospitals namely Aziz Fätimah Trust Hospital having 200 beds and Ghafoor Bashir Children & Maternity Hospital having 100 beds. The affairs of which are managed and supervised by the Directors of the Company, as Trustees.

Aziz Fatimah Trust Hospital was started in the year 1978 and its formal inauguration was performed on 25.06.1980 by General Muhammad Zia-ul-Haq the then President of Islamic Republic of Pakistan while Ghafoor Bashir Children & Maternity Hospital is regularly functioning for the last about 5 years. Both the above hospital are rendering meritorious services for the general public at large and particularly for the poor and needy people. These hospitals are not self-sufficient even and are running on donations. Therefore, I propose that an adequate amount, out of the profits of the Company, may be donated to Aziz Fatimah Trust for the expansion, uplift modernization and upgrading of the existing medical and surgical facilities at both the hospitals. The Directors present agreed with the proposal in the larger interest of the sick and suffering humanity.

THEREFORE, IT WAS UNANIMOUSLY RESOLVED.

“That an adequate amount, out of the profits of the Company, be donated to Aziz Fatimah Trust for the expansion, uplift, modernization and upgrading of the existing medical and surgical facilities at Aziz Fatimah Trust Hospital and Ghafoor Bashir Children & Maternity Hospital Faisalabad.

FURTHER RESOLVED

“That Haji Bashir Ahmed and Mian Javed Iqbal, Chairman and Chief Executive of the Company respectively be an are hereby authorized and empowered singly and/or jointly to donate to Aziz Fatimah Trust, Faisalabad and to any other person/ institution any sum or sums from time to time, as they deem proper but not exceeding the amount as is

admissible under the Income Tax Ordinance, 1979.

Unquote

4. The company, in its reply has not denied the fact that its memorandum of association does not authorize such payments and has tried to convince Commission that in view of noble intentions and purposes behind the donation it should not be questioned. The resolution of board of directors appears to have been passed totally disregarding position of memorandum of association and interestingly does not even quantify the donation but gives power to the Chairman and Chief Executive of the company to make donation to an extent as admissible under Income Tax Law. The matter of donation was not considered as a regular item on agenda of the board, rather it was considered as "any other item with permission of the Chairman". Further, the details furnished by the company include huge amount which are not paid through cheques and contains such items as Sadqa Expenses (Goats), marriage of poor girls etc. It has been noticed that directors have given heavy donations in the years 1996 and 1997 also and the overall position in this regard comes to as under:-

<u>Year</u>	<u>Total Amount</u>	<u>Donation paid to Ajiz Fatimah Trust</u>
1996	Rs. 2, 683,500/-	Rs.2,666,000/-
1997	Rs 9,840,098/-	Rs. 4,674,403/-
1998	Rs. 6,609,179/-	Rs.6,209,543/-
1999	Rs.38,487,202/-	Rs.37,023,000/-
	Rs.57,619,979/-	Rs.50,572,946/-

5. Some of the law commentaries/reported judgments are reproduced below which helps us to understand the legal position with regard to those acts of companies directors including payment of donation etc., when not authorized by memorandum of associations to pay donations of such companies :-

- (a) "The money and the other assets of a company cannot, as a rule, be employed for any purposes other than those

pertaining to the objects specified in the memorandum of association of the company, or purposes, incidental to those purposes. Neither the directors, nor the company, in general meeting by an ordinary or special resolution, can authorize the use or payment of the company's money so as to bind the minority shareholders outside the company's object except in the case of a scheme of arrangement sanctioned by the Court. "(Halsbury's Laws of England Vol. 6) (Page 170, para 357)."

- (b) "It is ultra vires for a company to act beyond the scope of its memorandum. Any attempted departure will be invalid and cannot be validated even if assented to by all the members of the company. By ultra vires is meant an act or transaction of a company, which, though it may not be illegal, is beyond the company's powers by reason of not being within the objects of the memorandum of association. The memorandum is, so to speak, the area beyond which a company cannot travel". *Ashbury Ry. Carriage Company v. Riche*, (1875)LR 7 HL 653.
- (c) "An act beyond the objects mentioned in the memorandum is ultra vires and void and cannot be ratified". *Dr. Lakshmanaswami Mudaliar v. LIC* (1963) 33 Com Cases 420: AIR 1963 SC 1185.
- (d) "Where no connection or nexus exists between the exercise of a power and the attainment of an Object, exercise of power will be ultra vires". *Radha Cinema & Co. v. Chitralipi Films* 1974 Tax LR 2180 at 2180 (Cal).
- (e) "A transaction which is within the powers, express or implied of the company, but is entered into for a purpose not authorized by the objects clause is itself ultra vires the company" (*Re Introductions Ltd.* (1969) 1 All ER 887.

- (f) "The Power of the company incorporated in company law are bounded by memorandum of Association of the company and any act done and otherwise than in the exercise of such powers is ultra vires of the company and void, even if the shareholders assent to it and such contract is incapable of ratification". Ashbury Ry. Carriage & Iron Co. Vs. Riche, (1875) LR 111 653.

6. In view of above quoted commentaries/judgments, it is not difficult to understand that it is not lawful for a company to use its assets for any purpose except to promote prosperity of a company and the donation may be paid only if so authorized by the memorandum of association of the company. It may be mentioned here that in the neighboring Country i.e. India even if memorandum of the company authorises payment of donation, directors cannot, without consent of shareholders in general meeting pay donations of more than Rs. 50,000 (Rupees fifty thousand only) or 5% of the profits whichever is greater. Lord Justice Bown in the famous case reported as Hutton v. West Coast Railway & Co. (1883) 23.Ch.D.154 observed that "Charity has no business to sit at Board of directors qua-charity. There is however a kind of charitable dealing which is for the interest of those who practice it, and to that extent and in that garb, charity may sit at the board, but for no other purpose".

7. It has been further held by Courts that even if memorandum authorize payment of donations, admissibility of the expenses on this account is subject to the very condition that it should facilitate Company's business or should otherwise be incidental to the business carried out by the company. Charity can be practiced out of the company's assets only for the purpose of promoting the company's objects (Dr. Lakshmanaswami Mudaliar v. LIC, (1963) 33 Com Cases 420: AIR 1963 SC 1185. Donations and charity which is not reasonably incidental to the main business of the company is *ultra vires* of

the company and void. Directors are not authorized to contribute to donations and charities to unlimited extent as has been resolved and done in this case. In this case not only very heavy amount has been paid on account of donation, a major part of donation has been paid to a trust in which the majority of directors of the company have interest as trustees. What-ever the justification of payment for donation may be, fact remains that it has been paid out of assets belonging to the members of a company memorandum of association of which does not permit so. May be the Trust and other donee Institutions which have received this donation are doing something very good for humanity, but I regret to say that memorandum of association of Sitara Energy Limited did not authorize this act and donation was paid without any lawful authority. If companies are allowed to allocate their assets in a manner not permitted by their charter, the very spirit of law will be defeated. In view of this, notice may be issued under Section 472 of the Companies Ordinance, 1984 read with section 496 ibid. to the following directors of the company to take obligation personally and to deposit the total sums of Rs. 57,619,979/- in company's account within 30 days namely

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|-------------------------|-----------------|
| 1. HaJi Bashir Ahmed, | Chairman, |
| 2. Mr. Javed Iqbal, | Chief Executive |
| 3. Mr. Muhammad Adrees, | Director |
| 4. Mr. Tariq Mahmood | Director |
| 5. Mr. Muhammad Anis | Director |
| 6. Mr. Imran Ghafoor | Director |

(M. Zafar - ul - Haq Hijazi)
Commissioner (Enforcement)

Place: Islamabad
Dated: 05-04-2000