

THE KOTAGALA FIASCO

The Sunday Leader of December 31, 1995 reported that, the then Chairman, Public Enterprise Reform Commission [PERC], Rajan Asirwatham had confirmed, that President Chandrika Bandaranaike Kumaratunga had directed PERC, to consider taking immediate legal action against George Steuart & Co. Ltd., [GS&CL], on allegations pertaining to the sale of Kotagala Plantations Ltd., [KPL]. *The Sunday Leader* of January 7, 1996 reported that, Julius & Creasy, Attorneys-at-law, acting on behalf of PERC, in consultation with Romesh de Silva P.C., had written to George Steuarts Management Service (Pvt) Ltd., [GSMSPL], querying the basis on which they had sold KPL ? *The Sunday Leader* on March 1, 1998 disclosed that, Julius & Creasy had addressed a letter dated January 2, 1996, reference RSR/CG/NT, to GSMSPL marked "*extremely urgent*". Julius & Creasy had stated -

UNAWARENESS OF PERC A COMEDY ?

"We act for the Public Enterprise Reform Commission and are writing to you under instructions from them - Our client's attention has been drawn to several recent press reports to the effect that some part of the shareholding of George Steuarts Management Services (Pvt) Ltd has been sold to a foreign Company. - We shall be obliged if you will be good enough to let us know by return, whether any part of the capital of George Steuarts Management Services (Pvt) Ltd., has in fact been acquired by a foreign Company and if so, will you please let us have the following information. — i). The percentage of shares acquired by the foreign Company — ii). The name and address of the foreign Company — iii). Purchase consideration paid therefor. — The above information is required to enable the Public Enterprise Reform Commission to respond to the information reported in the newspapers. We would greatly appreciate your immediate attention to this matter. We trust that it would be possible for you to let us have a reply in the course of Wednesday the 3rd January".

Has it not been a comedy, that PERC had engaged a firm of lawyers, incurring considerable legal costs, to write to GSMSPL, to solicit so very urgently, such informations, whereas, would not such informations, have been known to the then Chairman, PERC, Rajan Asirwatham, whose company Secretaries & Registrars Ltd., [S&RL] had processed the application to BOI for foreign investment into GSMSPL and furthermore, whose firm, KPMG Ford, Rhodes, Thornton & Co., had been stipulated in the Agreement of December 4, 1995 to receive notices thereunder, on behalf of the foreign investors of GSMSPL, and which said Agreement had set out clearly, such informations that had been so called for by PERC ? Similarly, would not such informations have been known to PERC member, Thilan Wijesinghe, Chairman/Director General, BOI, who had received and approved such application for foreign investment into GSMSPL?

Would it mean, that even in the face of controversial exposures in the media and President Kumaratunga having given directions to PERC to take legal action, that there had been an ominous silence and no disclosure, whatsoever, before PERC, of such requisite informations, resulting in PERC calling for such informations through lawyers from GSMSPL, that too at the instance of its then Chairman, Rajan Asirwatham ? How could this be explained?

MORE INFORMATION CALLED FOR ON SHAREHOLDINGS ?

F.J. & G. De Saram, lawyers acting for GSMSPL, had promptly replied to Julius & Creasy on January 4, 1996, reference LK/HB, giving the informations called for, including the name and address of the foreign investor of GSMSPL, Rovenco Co. Ltd., Thailand. Consequently, by letter dated January 25, 1996, reference RSR/CG/NT, Julius & Creasy, had written to F J & G De Saram, inter-alia, stating — "Under further instructions from the Public Enterprise Reform Commission we write to request you to furnish the following further information ... iv). Your client's confirmation that apart from the 40% of the shares allotted to Rovenco Co. Ltd., Thailand, that the balance 60% of the shares are held by Sri Lankan shareholders beneficially for their own account and not as nominees for any Sri Lankan or non Sri Lankans. It may well be that neither yourselves, nor your clients may be in a position to furnish this

information. In such event, please let us know and we shall write to the shareholders concerned directly — PERC appreciates the prompt response to our letter of the 2nd January and they would greatly appreciate, if the information sought in this letter can be furnished expeditiously so that a full report in this matter can be furnished to the Government — cc: R.N. Asirwatham Esqr. Chairman - Public Enterprise Reform Commission" — Thereafter, Julius & Creasy on February 15, 1996, on a further communication received from then Chairman, PERC, had addressed another letter, reference RSR/CG/NT, to F.J. & G. De Saram, with copy to R.N. Asirwatham, Chairman PERC.

COST OF KOTAGALA ACQUISITION ?

The Sunday Leader understands from reliable sources, that shortly thereafter, on April 1, 1996, a Memorandum of Understanding had been entered into, by and between Lankem Ceylon Ltd., and the foreign investor of GSMSP and that consequently, on Friday, April 19, 1996, a Sale & Purchase Agreement had been entered into, by and between the said same parties, for the acquisition by Lankem Ceylon Ltd., of the entire shareholdings of GSMSP, which owned 51% shareholding of KPL. *The Sunday Leader* further understands, that the foreign investors of GSMSP, in representations made to the government, had disclosed, that they had banked to their SIERA Bank Account at Commercial Bank, Borella, on the following Monday, the sale proceeds of Rs. 400 million, they had received on the sale of GSMSP shareholdings.

The Annual Report of KPL for the 15 month period to March 31, 1997, dated September 12, 1997, at page 38, has disclosed that 51% shareholding of KPL, that was owned by GSMSP, was in the name of Lankem Tea & Rubber Plantations (Pvt) Ltd., [LT&RPL], it having been disclosed, that GSMSP name had been changed to LT&RPL. It has also been disclosed, that the Rs. 120 million mandatorily convertible debentures of KPL, was now being held by Lankem Plantations Holdings Ltd [LPHL]. At page 26 of the KPL Annual Report, it has been disclosed, that a new investment of 20 million shares amounting to a value of Rs. 200 million, had been made by KPL in LPHL, a holding of 48.78% thereof.

UNEXPLAINABLE DEAL ?

LT&RPL (GSMSP) had also been the managing agent of KPL and had charged from KPL, as managing agent's fees Rs. 51.95 million for the period ended 31st March 1997 and Rs. 35.67 million for the year ended December 31, 1995 — and together with the dividend of Rs. 20.4 million for the period ended 31st March 1997, LT&RPL (GSMSP) had received a total sum of Rs. 108 million from KPL, whereas they had paid only Rs. 102 million to acquire the 51% shareholding of KPL. That is how the members of PERC had done their homework!!

The Annual Report of Lankem Ceylon Ltd., for the year ended 31st March 1997, dated October 17, 1997, at page 11, has stated — "The controlling interests in Kotagala Plantations Limited was acquired in April, 1996. The financial year of the company which had hitherto been the calendar year has now been amended to the fiscal year. As a result comments in this Report relate to the fifteen month period to 31st March, 1997" — The Annual Report of Lankem Ceylon Ltd., at page 34, has disclosed, that an investment in 8,342 shares of LT&RPL (GSMSP), at a cost of Rs. 1.998 million had been made, affording a 44% control thereof. At the same page, an investment in 18 million shares amounting to a value of Rs. 180 million has been disclosed have to have been made in LPHL.

INVESTMENT IN LAKNEM PLANTATIONS HOLDINGS LTD ?

On page 35 of the Annual Report of Lankem Ceylon Ltd., it has been disclosed that an investment in 20 million shares amounting to a value of Rs. 200 million had been made in LPHL, giving the following note — "The Capital restructure programme undertaken by the Lankem Group during the current financial year, resulted in Kotagala Plantations Ltd., having an indirect cross holding in Lankem Plantations Holdings Ltd. In terms of Section 29 of the Companies Act, a subsidiary having an investment in the holding company shall not have any right to vote at meetings of the holding company

or any class of members thereof. As such the investment in Lankem Plantation Holdings Ltd. [LPHL] by Kotagala Plantations Ltd [KPL], amounting to Rs. 200 million (representing 49% of the issued share capital of LPHL) has not been used for purpose of consolidation in the absence of control or significant influence and shown under Other Investments".

**Extracts of interview given by then
Chairman PERC, to *The Sunday
Island* of June 9, 1996**

Q: Isn't it strange that Lankem borrowed and paid a huge sum for this estate? Can they ever pay this money back to the banks?
A: When these things were privatised we had 10 profit making companies. We put them in the order that they had made profits in case we decide to put some on the market earlier than the other and George Steuarts was either number one or two. So this meant that they had made a huge profit. This year they have a fair amount of rubber. Tea prices have gone up this year.

Q: The initial Kotagala transaction was no hidden issue with everyone going public with accusations. Despite that, Bank of Ceylon and NDB have gone ahead and funded the purchase by Lankem. This is another rather suspicious factor?
A: Now Lankem has been a corporate client of the Bank of Ceylon for a long time and as far as the Bank of Ceylon is concerned there is a terrific competition from private banks. Here if you walk down the road, every hundred yards you have a bank. If we are not funding it, almost certainly almost inevitably, another bank would gladly fund it. Rupees hundred million, I grant what you say, is a large sum from the view of a particular company. But from the point of view of any bank it is not a large sum because it is just US \$ 2 million....

Q: Have you taken any action against Julius and Creasy?
A: We asked Senathi Rajah's explanation on this matter. We told him, look everyone is uncomfortable because your firm was retained purely because we couldn't go direct to the counsel and you advised as counsel what steps to be taken. Now to our horror we find that a firm connected to you has purchased this. It doesn't look well at all in the public eye and we will be in trouble because we have bent over backwards to see that the investigation is done properly.

Q: He had inside information?
A: So he assured later that he was not involved in this transaction. His explanation is that he was only an alternate director of Lankem and he says that the chairman and the MD run the day-to-day affairs of the company. Then, we put it to him again. "Look a transaction of this magnitude running into such a large amount of money, can you leave it to one of two people and that it shouldn't do" and he said that he cannot recollect whether he has signed any resolution or anything like that and he doesn't think he has.

Q: His brother is a director of Lankem?
A: He said that his brother is in the business of take-overs, amalgamations, restructuring etc. and that he had nothing to do with the raising of the funding and that he was only an alternate director and that he had no part in this transaction. But still the president who is the minister in charge of PERC has also been discussing this matter with me. She is also uncomfortable and she has directed that as a first step no further work be given to Julius & Creasy.

Q: Have they been reported to the Chief Justice or anyone?
A: No. No. Yesterday we got their report which was inconclusive. In the report they said that they want to rest their probe into this deal and that they may want to have this reviewed by another lawyer. The report is dated the 24th but it arrived yesterday. What they say is that they have no response from the Central Bank and due to the recent media reports that they should now report to us. They end by saying, "in view of the fact that the partner dealing with this matter is an alternate director of Lankem you may wish to have our reports and annexures reviewed and dealt with by other lawyers of your choice."

Q: But he is also on the board of E.B. Creasy?
A: They work together I think. So what we said is we will refer all these papers to the Attorney General and ask him to report. Julius and Creasy themselves have suggested that we go to another lawyer but for reasons of etiquette a private lawyer may not want to get involved. These guys want investigations done when it suits them and once they've acquired what they want, the investigation stopped. As responsible bodies and associations they must —
 a) be quite sure of their facts before they accuse somebody —
 b) if you're holding posts in bodies or associations you must be more careful because what is sauce for the goose is also sauce for the gander.

Page 19 of the Annual Report of Lankem Ceylon Ltd., has disclosed that 78.06% of Lankem Ceylon Ltd., had been owned by E.B. Creasy & Co. Ltd. The Annual Report of E.B. Creasy & Co. Ltd., for the year ended 31st March 1997 dated November 3, 1997, at page 9 has stated — "The controlling interests in Kotagala Plantations Limited was acquired in April, 1996. The financial year of the Company which had hitherto been the calendar year has now been amended to the fiscal year. As a result comments in this Report relate to the fifteen month period to 31st March, 1997"

The Annual Report of the E.B. Creasy & Co. Ltd., at page 3, inter-alia, has reported, that Lankem Ceylon Ltd., Lankem Plantation Holdings Ltd., Lankem Tea & Rubber Plantation (Pvt) Ltd., Kotagala Plantations Ltd. and Agarapatana Plantations Ltd., are subsidiaries of E.B. Creasy & Co. Ltd. at page 40 thereof, a 78% company holding and a 81% group holding of Lankem Ceylon Ltd., has been disclosed. It has also been disclosed, that an investment in 3 million shares amounting to Rs. 30 million has been made in LPHL giving a group holding of 51% thereof. Page 41 of the Annual Report of E.B. Creasy & Co. Ltd., under group companies interest an investment of Rs. 200 million in LPHL has been disclosed, giving the following note thereto —

"The capital restructure programme undertaken by the Lankem Group during the current financial year, resulted in Kotagala Plantations Ltd having an indirect cross holding in Lankem Plantations Holdings Ltd. In terms of Section 29 of the Companies Act, a subsidiary having an investment in the holding company shall not have any right to vote at meetings of the holding company or any class of members thereof. As such the investment in Lankem Plantation Holdings Ltd. [LPHL] by Kotagala Plantations Ltd.[KPL] amounting to Rs. 200 million (representing 49% of the issued share capital of LPHL) has not been used for purpose of consolidation in the absence of control or significant influence and shown under Other Investments."

UTILISATION OF KOTAGALA FUNDS ?

Would it not therefore appear, that Rs. 200 million of KPL funds, belonging to all its shareholders had been invested in LPHL, and that this Rs. 200 million had been directly and/or indirectly utilised to finance part of the Rs. 400 million acquisition cost of 51% controlling interest of KPL, including the payment for the Rs. 120 million mandatorily convertible transferable debentures, that had been owned by GSMSPL, now known as LT&RPL ? If not, what have these funds been utilised for ? Has it been for the acquisition of Agarapatana Plantations Ltd., which has also been disclosed as a subsidiary of E.B. Creasy & Co. Ltd. The Lankem Ceylon Ltd. Annual Report at page 12 states — " The majority stake in Agarapatana Plantations Limited was purchased in October 1996. In this instance too the financial year has been amended from the calendar year to the fiscal year."

Section 29 of the Companies Act No. 17 of 1982 states — "(1) Except in the cases hereafter in this section set out, a body corporate cannot be a member of a company, which is its holding company, and any allotment or transfer of shares in a company to its subsidiary shall be void. —(2) The provisions of this section shall not apply where the subsidiary is concerned as legal representative, or where it is concerned as trustee, unless the holding company or a subsidiary thereof is beneficially interested under the trust and is not so interested only by way of security for the purposes of a transaction entered into by it in the ordinary course of a business which includes the lending of money — (3) The provisions of this section shall not prevent a subsidiary which is, on the appointed date, a member of its holding company, from continuing to be such member but, subject to the provisions of sub section (2), the subsidiary shall have no right to vote at meetings of the holding company or any class of members thereof".

Section 55(1) of the Companies Act, states — (1) "Subject as provided in this section, it shall not be lawful for a company to give, whether directly or indirectly, and whether by means of a loan, guarantee, the provision of security or otherwise, any financial assistance for the purpose of or in connection with a purchase or subscription made or to be made by any person of, or for any shares in, the company, or, where the company is a subsidiary company, in its holding company"

STATUTORY DUTIES OF SEC ?



Director General SEC, Kumar Paul

The Annual Accounts of E.B. Creasy & Co. Ltd., Lankem Ceylon Ltd. and Kotagala Plantations Ltd., have been audited by KPMG Ford, Rhodes, Thornton & Co., a senior partner of which, was then Chairman PERC, Rajan Asirwatham. KPL had been audited previously by Kreston M.N.S. & Co., Chartered Accountants and KPMG Ford, Rhodes, Thornton & Co., had been appointed auditors at a fee of Rs. 800,000/- after George Steuarts had disposed of their interest in KPL. The Annual Reports of E.B. Creasy & Co. Ltd. and Lankem Ceylon Ltd. disclose, the lawyers to these companies to be Julius & Creasy, Mr. R. Senathi Rajah, senior partner of Julius & Creasy has been reported to have resigned, as a Director of E.B. Creasy & Co. Ltd., on August 20, 1996.

The Annual Report of KPL, at page 7 has stated -"The Securities & Exchange Commission [SEC] has filed legal action in September, 1997 in the Colombo Fort Magistrate's Court against Kotagala Plantations Ltd [KPL] and its Directors for alleged delay in making disclosure as required by the SEC Act No. 26 of 1991 and the Colombo Stock Exchange Rules regarding the change in the controlling interest in two of its subsidiaries Lankem Plantation Holdings Ltd [LPHL] and Agarapatana Plantations Ltd. [APL]. We have submitted an appropriate appeal to the SEC requesting withdrawal of such action."

It is therefore quite clear, that SEC had in fact concerned itself, with the affairs of KPL, LPHL and APL and had consequently, filed action in the Magistrate's Court for an alleged offence of delay in making disclosure. In such circumstances, how is it that SEC had been unconcerned about the method and/or manner, in which Rs. 200 million of KPL funds, belonging to all its shareholders, had been utilised for the benefit of a party/parties directly and/or indirectly owning 51% of its shareholdings, perhaps even to have directly and/or indirectly financed the cost of acquisition of such very shareholdings or some other shareholdings in their own interests?. Would this not have affected the interests of the other shareholders of KPL? If so, why had the SEC not taken any action discharging its statutory duty of protecting the interests of investors?

The Registrar of Companies, D.K. Hettiarachchi, Deputy Secretary Treasury, D.Y. Liyanage, Deputy Governor of the Central Bank, S. Easparathasan nominated by the Governor and the President of the Institute of Chartered Accountants, M.R. Mihular, Partner, KPMG Ford, Rhodes, Thornton & Co., had been statutorily ex-officio members of the SEC. Precedent Partner, KPMG Ford, Rhodes, Thornton & Co., G.C.B. Wijeyesinghe had also been a member.

Would not the SEC owe a public pronouncement to the investing public of this country, stating as to whether, the aforesaid transactions have been examined and as to whether, they do not tantamount to the expropriation of the interests of the minority shareholders ? Would the expropriation of minority shareholders' interests be condoned by Courts of law, as per decided Cases?

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