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SEC restrains the management of M/S Universal Leather and Footwear Industries Limited from making advances of Rs. 30 million to its associated company M/S MIMA Cotton Mills Limited

The Enforcement Division of the Securities and Exchange Commission of Pakistan (SEC), through its timely action, has restrained the management of M/S Universal Leather and Footwear Industries Limited from making interest-free and unsecured advances of Rs. 30 million to its associated company M/S MIMA Cotton Mills Limited, which would have caused losses to its shareholders.

Universal Leather and Footwear Industries Limited, which is a listed company, convened its annual general meeting on December 31, 2001 and published a press notice for the same. According to the agenda disclosed in the said notice, the Company proposed to pass a Special Resolution authorizing its Chief Executive to invest an amount of Rs. 30 million in the form of interest free, unsecured advances to its associated company. On receipt of the notice of the meeting, the issue was examined by the Enforcement Division of the SEC, and it was observed that interest free loan to associated company would have the effect of siphoning of the gains to the shareholders of the company accruable from the loan proposed to be advanced to associated company. It was, therefore, considered unfair to the shareholders of Universal Leather and Footwear, as it would benefit the shareholders of the associated company at the cost of the shareholders of the investing company.

The proposal violated the provisions of Section 208 of the Companies Ordinance, 1984, which do not envisage interest free loans to associated companies. The company was accordingly advised by the SEC, that it should obtain return on the proposed loan at not less than its borrowing cost. On this direction, the company has agreed that it will charge mark up on the aforesaid loan, however, it was clarified that as the company was not availing any finances from banks which would be available to it under Export Refinance Scheme, the mark up would be charged at not less than the cost of the said available funding to the company.