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KENYA NATIONAL ASSEMBLY

TENTH PARLIAMENT - FOURTH SESSION

REPORT



OF THE

DEPARTMENTAL COMMITTEE

ON FINANCE, PLANNING & TRADE

ON

**COOPER MOTORS CORPORATION (CMC)
HOLDINGS**

**Kenya National Assembly
Parliament Buildings
NAIROBI**

September, 2012

1. O PREFACE

Hon. Speaker Sir,

On behalf of the Departmental Committee on Finance, Planning, & Trade and pursuant to the provisions of Standing Order No. 198 (e) and (f), it is my pleasure and duty to present to the House, the Committee's Report on Cooper Motors Corporation (CMC) Holdings.

The Committee membership comprise of the following:-

The Hon. Chrysanthus Okemo, EGH, MP - (Chairman)

The Hon. (Prof.) Philip Kaloki, MP - (Vice Chairman)

The Hon. Jakoyo Midiwo, MGH, MP

The Hon. Musikari Kombo, EGH, MP

The Hon. Lucas Chepkitony, MP

The Hon. Lenny M. Kivuti,

The Hon. Nelson Gaichuhie, MP

The Hon. Ntoitha M'Mithiaru, MP

The Hon. Shakeel Ahmed Shabbir, MP

The Hon. Nkoidila Ole Lankas, MP

The Hon. Sammy Mwaita, MP

The Finance, Planning & Trade Committee is one of the Departmental Committees established under Standing Order No. 198 whose functions are:-

- (i) To investigate, inquire into, and report on all matters relating to the mandate, management, activities, administration, operations and estimates of the assigned Ministries and departments;
- (ii) To study the programme and policy objectives of the Ministries and departments and the effectiveness for the implementation;
- (iii) To study and review all legislation referred to it;

- (iv) To study, assess and analyze the relative success of the Ministries and departments as measured by the results obtained as compared with their stated objectives;
- (v) To investigate and inquire into all matters relating to the assigned Ministries and departments as they may deem necessary and as may be referred to them by the House or a Minister; and
- (vi) To make reports and recommendations to the House as often as possible, including recommendations of proposed legislation.

The subjects falling within the purview of the Departmental Committee on Finance, Planning & Trade are:-

- ◆ Public Finance, Banking and Insurance;
- ◆ Population, Planning and National Development;
- ◆ Trade, Tourism promotion and management;
- ◆ Commerce and Industry.

Mr. Speaker Sir,

On Thursday, 3 November 2011, there was a proposal by a section of members in the House that the Departmental Committee on Finance, Planning and Trade should conduct an investigation into the affairs surrounding the suspension of trading of shares of the CMC Group at the Nairobi Stock Exchange.

This proposal was opposed by the then Minister of Finance on the grounds that the relevant authority, the Capital Markets Authority (CMA), was seized of the matter and had already commissioned an independent forensic auditor to conduct the investigations and that it was prudent to wait for the outcome of the said investigation. He reiterated that the CMA was diligently acting to protect the interest of the shareholders and that subsequent investigations by the Departmental committee would not only be unnecessary but also erroneous.

It was at this point that Mr. Speaker reminded hon. members that the Standing Orders have conferred departmental committees with a general mandate to inquire into and investigate all matters that fall within their portfolio. Further, Mr. Speaker, declined to direct the Committee on Finance, Planning and Trade to conduct the investigations and ruled that the Committee was at liberty to inquire into the matter if it deemed it appropriate to do so.

The Committee considered the matters raised on the floor of the House and formed the view that these issues fell within its mandate. The Committee resolved that there was need to investigate the appropriateness of the procedure followed by the CMA in suspending the company's shares from the NSE, the conduct and possible criminal culpability of some of the directors of CMC Holdings and the suitability of these directors in governing a publicly listed company. The Committee further noted the need to protect investors from a recurrence of similar circumstances and the need to consider the development or amendment of the existing legislation.

The Committee deemed it necessary in line with its mandate to invite the following to shed light on the matter:-

- (i) The Capital Markets Authority as the regulator of publicly listed companies;
- (ii) The Minister for Immigration and Registration of Persons;
- (iii) The management, directors and former directors of Cooper Motors Corporation (CMC) Holdings;
- (iv) Representatives from General Motors Ltd; and
- (v) Representatives from Andy Forwarders Services Ltd.

The Committee sought to establish the following:-

- The genesis of the CMC holdings wrangles that has seen a very high turnover in management over the last few years;
- The reasons for the suspension of CMC from trading in the NSE;

- The profitability status of CMC;
- The validity of the working permit of the current Chief Executive Officer;
- The measures CMA is taking to safeguard the investments of CMC shareholders;
- The specific powers CMA has to safeguard the interests of the shareholders' investment and the extent of their application with regard to CMC.

Mr. Speaker Sir,

On behalf of the Departmental Committee on Finance, Planning & Trade, I have the honour and pleasure to present the Committee's Report and recommendations on Cooper Motors Corporation Holdings. May I take this opportunity to thank all Members of the Committee for their input and valuable contributions during the deliberations on the matter.

Thank you

**Hon. Chrysanthus Okemo, EGH, MP
Chairman,
Departmental Committee on Finance, Planning &
Trade**

Signed 

Date 13/9/2012

2.0 CONSIDERATION OF THE FORENSIC INVESTIGATIONS CONDUCTED AT CMC HOLDINGS BY PRICEWATERHOUSECOOPERS LIMITED (PWC) AND WEBBER WENTZEL (WEBBER)

2.1 Introduction

Pricewaterhousecoopers ("Pwc") Limited was engaged by CMC Holdings Limited ("CMC"), to conduct a forensic audit investigation into the affairs of the CMC Group with one of its key suppliers – Andy Forwarders Services Limited ("AFS") - the sole supplier of logistic services to the Group from 1997 to September 2011.

Pwc also undertook an investigation on Mr. Peter Muthoka who is the principal shareholder in both companies, the chairman of AFS and was previously a Director CMC Holdings. Pwc's primary focus was to establish whether Mr. P. W. Muthoka abused his directorship at CMC Holdings to obtain beneficial contracts on behalf of AFS to the detriment of the CMC Group.

2.2 Background information on the company

- The CMC Group has been involved in motor dealership and assembly in Kenya since its first affiliate was incorporated in 1948. The main trading entity within the Group is CMC Motors Group Limited ("CMC Motors") which mainly deals with vehicle sales.
- CMC Motors on behalf of CMC Group has had a trading relationship with AFS from 1997. By 2003, AFS had effectively become the sole provider to CMC Motors and had started providing substantial services to the other CMC Group subsidiaries.
- In May 2006, AFS CEO and Chairman Mr. Peter Muthoka, became a Board member of CMC Holdings. After Mr. Muthoka's appointment to the Board of CMC Holdings, AFS increased its business within CMC

Group from transactions worth around Kshs 500m to Kshs 1.2bn per year.

- Recently, there have been major upheavals at the boardroom of CMC Holdings. Long standing Chairman, Mr. Jeremiah Kiereini stepped down in April 2011, and was replaced by Mr. Peter Muthoka. Thereafter, the Group CEO Mr. Martin Forster was reportedly forced out and replaced by Mr. William Lay. More recently, in September 2011 Mr. Peter Muthoka was forcibly removed as Chairman by the CMC Board and replaced by Mr. Joel Kibe. This resulted in various allegations and counter-allegations, which played out in the media and caused a lot of apprehension in the investors, financiers and trading partners of CMC Holdings.
- On 16 September 2011, the CMA suspended the trading of CMC Holdings shares pending investigations into the affairs of the company. This suspension was further extended for an indefinite period and is yet to be lifted.

2.3 OVERVIEW OF THE DISPUTE AND ALLEGATIONS OF WRONGDOINGS

The dispute is based on allegations by the current management of CMC Group that Mr. Muthoka, as a director of CMC Holdings abused his position to procure contracts between CMC Motors and AFS and further, that these contracts were prejudicial to CMC since the logistic services provided by AFS were materially overpriced compared to the going market rate.

2.3.1 Overview of the trading relationship between CMC Group and AFS

- The relationship began sometime in 1997 and later developed to a point where AFS substantially became the *de facto* sole clearing and forwarding (“C&F”) agent for CMC Motors.

- Prior to 1997 the Group used Clearing & Forwarding services from several other companies but later decided to tender for new providers following dissatisfaction with the quality of services offered to it. AFS responded quoting competitive prices, and was appointed in December 1997 as one of the Groups three C&F agents. AFS became the sole C&F agent of CMC Motors sometime between 2001 and 2003, though the circumstances under which this was done are not very clear.
- During 2005 and 2006, AFS expanded the services it offered to CMC Motors. In June 2010, through a contract executed by the then Group CEO Mr. Martin Forster and AFS, AFS was contracted as the exclusive C&F agent for the CMC Group.
- In May 2011, Mr. Bill Lay was appointed as the CEO of CMC Holdings. He informed the Board that the products of CMC Group were uncompetitive owing to the high logistic costs incurred by the Group. Mr. Lay noted that the Group could save up to Kshs 250m annually on logistic costs if they renegotiated the costs paid to AFS. Following this assertion, the Board gave me Mr. Lay the go ahead to initiate an open tender for C&F services.
- In September 2011, Mr. Lay presented a memo to the CMC Board setting out the quotes obtained from the tender process. The quotations indicated that rates charged by AFS were substantially higher than the prevailing market rates.
- Following the presentation, the Board resolved that AFS be given a chance to match the lowest bid. AFS declined this offer after which the management cancelled CMCs contract with AFS and appointed new service providers.

2.3.2 The Role of Mr. Muthoka in the relationship between CMC Group and AFS

Mr. Muthoka is the Chairman, CEO, and principal shareholder of AFS and was central in key transaction between AFS and CMC Group.

He was also a board member of CMC Holdings between March 2006 and September 2011 and voted in as the Chairman of the CMC Holdings Board on 4 April 2011 following the resignation of Mr. Kiereini. It was at this board meeting that Mr. Muthoka first declared his interests in AFS and acknowledged that AFS had business dealings with CMC Group. On 8 September 2011, Mr. Muthoka was voted out as the Board Chairman and replaced by Mr. Joel Kibe.

2.4 Assessment of allegations of wrongdoing against Mr. Muthoka

- Mr. Muthoka was the focus of most allegations of wrongdoing because of his peculiar position as a director and principal shareholder of both companies. This led to concerns by the Management of CMC Holdings as to the possibility of conflict of interest between Mr. Muthoka's personal interests and his obligations to the Board of CMC Holdings.
- Pwc stated that they came across evidence suggesting that Mr. Muthoka may have engaged in collusion or undue influence. However, Pwc was unable to substantiate these claims owing to a lack of powers to summon and compel witnesses. Following the terms of engagement, Pwc were unable to investigate these matters to a level where they could make definite findings of criminal culpability on the part of Mr. Muthoka. Based on competitive pricing , It was clear that the CMC Group procured services from AFS on a systemic and on-going basis, under the terms that were highly unfavourable to the former.

2.4.1 Allegations of collusion

The following issues were identified as factors that could evidence collusion between Mr. Muthoka and key staff of CMC Motors:-

- a) Mr. Muthoka was described as a common visitor at CMC Motors and was reportedly close to various CMC officers involved in procurement.
- b) According to various reports, Mr. Muthoka had employed the children of two CMC Group officers at AFS.
- c) Mr. Muthoka, in the period in which he was the Chairman of the Caretaker Committee at CMC Holdings, promoted and doubled the salaries two staffers who were directly involved in negotiating deals with AFS.
- d) Mr. Martin Foster admitted that he signed the 2010 “exclusivity” contract with AFS in exchange for Mr. Muthoka protection in the Board. Mr. Foster position at the helm of the company was under pressure because of the poor performance of the company.

Pwc noted that possible criminal sanctions may be sustained against Mr. Muthoka and/or CMC Group employees if upon further investigations; evidence can be obtained to prove collusion between the parties.

2.4.2 Allegations of undue influence

Undue influence would arise where, as a director of CMC Holdings, Mr. Muthoka abused his position of power over the staff of CMC Holdings.

Some examples of claims of undue influence made against him include the following: –

- a) Mr. Roy Kyalo claimed that Mr. Muthoka had set him up for dismissal following his efforts in stopping the irregular transactions involving AFS and for his refusal to authorise a controversial LPO for the payment of clearance charges incurred in 2007;

- b) Martin Forster claimed that his dismissal in March 2011 was due to his plan to sign a deal that would take away freight business from AFS;
- c) Mrs. Mary Ngige (CMC Group Financial Director (GFD)) indicated that she had found out that Mr. Muthoka would “*punish or reward*” CMC officers based on how responsive they were to his requirements;
- d) Mr. Gitangu indicated that Mr. Muthoka was a “*feared*” man at CMC Motors with a reputation of being “*vindictive*”.
- e) Mr. Mbaluka indicated that he felt “*powerless*” in interactions involving AFS.

2.5 Assessment of Mr. Muthoka’s conduct in relation to his duties as a director

Section 200 of the Companies Act in Kenya makes it mandatory for directors to declare their interests in any contract involving the company of which they are directors. This should be done at the earliest opportunity and should be done in a full Board meeting. Section 200 of the Companies Act, Cap 486 reads as follows:-

(1) Subject to the provisions of this section, it shall be the duty of a director of a company who is in any way, whether directly or indirectly, interested in a contract or proposed contract with the company to declare the nature of his interest at a meeting of the directors of the company.”

(2) In the case of a proposed contract the declaration required by this section to be made by a director shall be made at the meeting of the directors at which the question of entering into the contract is first taken into consideration or if the director was not at the date of that meeting interested in the proposed contract, at the next meeting of the directors held after he became so interested, and in a case where the director

becomes interested in a contract after it is made, the said declaration shall be made at the first meeting of the directors held after the director becomes so interested.

(3) For the purposes of this section, a general notice given to the directors of a company by a director to the effect that he is a member of a specified company or firm or acts for the company in a specified capacity and is to be regarded as interested in any contract which may, after the date of the notice, be made with that company or firm or with himself in such specified capacity shall be deemed to be a sufficient declaration of interest in relation to any contract so made:

Provided that no such notice shall be of effect unless either it is given at a meeting of the directors or the director takes reasonable steps to secure that it is brought up and read at the next meeting of the directors after it is given.

(4) Any director who fails to comply with the provisions of this section shall be liable to a fine not exceeding two thousand shillings.

(5) Nothing in this section shall be taken to prejudice the operation of any rule of law restricting directors of a company from having any interest in contracts with the company.”

Mr. Muthoka was appointed as a director in May 2006 and the minutes do not reflect any declaration of personal interest in AFS or in the contracts between AFS and CMC Motors. Mr. Muthoka only made this declaration when he was appointed as the Chairman of the Board of CMC Holdings in April 2011.

2.6 Irregularities in AFS dealings with CMC Group

- Investigations by Pwc revealed that internal controls within the CMC Group were extremely weak. Most notably, procedures for key

procurement processes were not laid down in writing or else were applied on an ad hoc basis without adherence to the written policies.

- It appeared to Pwc that Mr. Muthoka abused his position as a director of CMC Holdings by taking advantage of the weaknesses within CMC Motors to obtain contracts for AFS at inflated prices.
- Mr. Muthoka also took advantage of the weak enforcement of CMC Motor's sales policy to purchase vehicles for AFS at terms that were highly prejudicial to CMC Motors.
- Pwc confirmed that Mr. Muthoka started taking advantage of the weak internal control environment at CMC Group shortly after joining the Board. Within 8 months of his appointment to the Board, AFS had succeeded in achieving two price increases for its services and had obtained a contract for new services. None of which went through any tender process pursuant to applicable procedures in place. This pattern continued up to September 2011 when dealings between CMC Group and AFS were formally terminated by the Board.
- Pwc formed the view that although it could be argued that the contracts between CMC and AFS were on an arm's length basis, the same could not excuse a director who had knowledge of such wrongdoing and who subsequently failed to act in the company's best interests. This is particularly so for a director who has experience and expertise in such contracts and who must reasonably be considered to have been aware of the consequences such wrongdoing to the company.

Pwc expressed doubt as to whether the contract appointing AFS as the exclusive C&F agents for CMC Motors was binding and advised that CMC Group should seek advice on the matter.

2.7 Computation of CMC Group's loss

Pwc found that as a result of transactions between CMC and AFS, the former suffered great financial loss, which Pwc computed to around 1bn – 1.1bn. Pwc established that the loss could have been avoided had CMC used a different C&F agent.

2.8 Legal analysis of the claims and remedies

Pwc were of the view that based on the irregularities cited above, CMC would have claims against the following:

- Some directors of CMC Holdings and CMC Motors
- AFS
- Certain employees of CMC Motors and CMC Holdings

2.8.1 Directors

A claim against a director can arise where it can be shown that a company suffered loss because of one or more of the following four matters:

- A director acting contrary to the interests of the company

There should be no conflict between a director's personal interest and the interests of the company, unless the company has at a Board meeting and with full material disclosure, waived the benefit of this rule.

- A director acting in breach of his fiduciary duties

A director should not place himself in a position where he is directly competing with the company as a director is both an agent and a trustee of the company.

- A director acting in breach of his duty of care, diligence, and skill

Directors are required to use such skill as they possess and such care and diligence as would be displayed by a reasonable man in similar circumstances. A director with additional understanding of the

company's business has a duty to use his/her skill for the benefit of the company.

- Failure by a director to declare his interest in trade contracts with the company

The burden is on the director concerned to give notice and to ensure that the notice comes to the Board of Directors.

Based on the foregoing analysis, the company would have a claim against the following directors: -

(i) Mr. Peter Muthoka – AFS MD, CMC Holdings Director, CMC Motors Director

- Conflict of interest. – failing to disclose to the Board of CMC Holdings that he had personal interests in AFS, a company that was trading with CMC Holdings.

Even though the position of different members of the Board as to how the Board treats contracts with directors was not unanimous, it was clear that there was an unwritten policy on directors' contracts requiring that all contracts that were not at arm's length had to be presented to the Board for approval. AFS contracts with CMC Motors were not on competitive terms and should have been presented to the Board.

- Competing with the company. During his tenure as a director at CMC Holdings, he obtained very favorable contractual terms for AFS under terms that were highly prejudicial to CMC Holdings. He did this despite the fact that he was under a duty to protect the interests of CMC Holdings.

Pwc indicated in their report that the scale of overcharging by AFS on contracts to CMC Motors caused significant financial loss to CMC Group.

- Breach of duty to exercise due care and skill.

This duty requires a director to act as a reasonable man, possessed of similar qualifications and with a similar background, would if the company was his own personal business. As a seasoned practitioner in the logistics industry, it would appear that Mr. Muthoka did not use his expertise and knowledge to promote the interest of CMC Holdings.

- Unjust enrichment.

This claim would arise if it can be demonstrated that as a result of Mr. Muthoka's wrongdoing, AFS made super profits from its contractual dealings with CMC Motors resulting in the unjust increment of Mr. Muthoka's wealth. The remedy in this case would be restitution where CMC Group would need to make a claim for the resulting personal gain enjoyed by Mr. Muthoka.

Pwc noted that given the serious implications of a finding of guilt against Mr. Muthoka, there would be a question as to whether a person so convicted would be a suitable director of a publicly listed company.

(ii) **Joseph Mumo Kivai – Director of CMC Holdings and AFS**

- It appeared to Pwc that Mr. Kivai joined the CMC Holdings Board in March 2011 and that he was also a director of AFS, though this was not properly verified. There is no record of any declaration of interest in any matter relating to CMC Group.

- If indeed he was a director of AFS, he would be liable for failing to declare such interest as required by law. Secondly, he would be liable for breach of the duty of care by failing to act in the best interests of the CMC Group vis a vis the interests of AFS. However, he would only be liable for any loss suffered by CMC Group during the time he was a director.
- Pwc recommended CMC should undertake additional investigation to confirm the position regarding Mr. Kivai's status within AFS.

(iii) Martin Forster – GCE, Director of CMC Holdings and CMC Motors

- Mr. Forster was the senior-most executive director throughout the material period when CMC suffered the overcharge by AFS.
- The cause of action that CMC Group may have against Mr. Forster relates to breach of duty of care in the dealings with AFS. This is evidenced by his failure to recover monies that were clearly meant to be refunded to CMC Motors and failure to avoid conflict of interest. He admitted that he only signed a 5 year exclusive agreement with AFS so as to safeguard his position as CEO of the company.
- Mr. Forster also failed to keep the Board fully updated on material and injurious transactions relating to logistics and in particular the contracts with AFS.
- If Mr. Forster obtained any personal financial benefit by his actions or inaction, then CMC Group may also have an action for unjust enrichment.

(iv) **Joseph Mukuna – FD CMC Motors, Director CMC Motors**

As Financial Director, Mr. Mukuna had a primary role in the procurement process. In discharging his role, Mr. Mukuna breached his duty of care as Director of CMC Motors by failing to act in the best interests of the company as regards the various contracts and price revisions set with AFS. If Mr. Mukuna derived a personal benefit from the transactions then the Group may have an action for unjust enrichment.

(v) **Other CMC Holdings and CMC Motors Board members**

There is need for further investigations as to whether the other directors may have failed in their individual capacities to exercise due care and skill by permitting the exploitative contracts with AFS to continue for so long and for allowing the laxity of controls.

2.8.2 Andy Forwarders Services Limited (AFS)

- Pwc were of the view that CMC could sustain a claim against AFS where they can prove that AFS overcharged the CMC Group in circumstances, which were irregular, as a result of which AFS was unjustly enriched and CMC Group suffered loss. In such cases, the remedy available to the Group would be restitution.
- Pwc were also of the view that the company could seek a constitutional remedy for breach of consumer rights. They argued that CMC Holdings as a consumer of AFS's services could bring a petition for breach of Article 46 of the Constitution. For this claim to be successful, CMC Group would need to show that its dealings with AFS were "oppressive" and that AFS acted without "care" for the welfare of CMC Group as a consumer. This claim would relate only to losses suffered since 27 August 2010.

- Pwc recommended that the merits of such a claim be researched further to assess feasibility given the novelty of such an action.

2.8.3 Certain employees of CMC Holdings and CMC Motors

Pwc argued that a claim could be sustained against two employees who appear to have been heavily involved in procurement with AFS. On the contrary, it could also be argued that these employees acted in concert with an executive director and may have been following lawful instructions.

2.9 Recommendations by Pwc

CMC Holdings should consider the findings in the Pwc report in conjunction with independent legal advice.

CMC Holdings should consider undertaking further investigations. This would be with a view to seek evidence of criminal conduct on the part of certain former and current directors.

2.10 THE CAPITAL MARKETS AUTHORITY FORENSIC INVESTIGATION REPORT INTO THE AFFAIRS OF CMC HOLDINGS SUBMITTED BY WEBBER WENTZEL. FINAL REPORT PRESENTED 31 JANUARY 2012

2.11 Introduction

The Capital Markets Authority (“CMA”) appointed Webber Wentzel to conduct a forensic investigation into the financial operations of CMC on 14 November 2011. This was done pursuant to the provisions of section 11 (3) (h) and (m) of Cap 485.

Section 11 (3) (h) and (m) provide for the following:-

“For the purpose of carrying out its objectives, the Authority may exercise, perform or discharge all or any of the following powers, duties and functions –

(h) inquire, either on its own motion or at the request of any other person, into the affairs of any public company the securities of which

are publicly offered or traded on an approved securities exchange or on an over the counter market;

(m) appoint an auditor to carry out a specific audit of the financial operations of any public company, if such action is deemed to be in the interest of the investors.”

2.12 Objectives

The principal objective of the investigation was to conduct an independent audit and come up with recommendations that would assist the CMA make a decision on how best to protect the interests of both investors and potential investors in CMC Holdings.

The defined aspects were:

- a) Corporate governance and recent activities affecting the board and management;
- b) The integrity of the Internal control environment at the company;
- c) Allegations of irregularities affecting procurement possibly resulting in financial loss;
- d) Compliance with international accounting standards (IAS) and International Financing Reporting Standards (“IFRS”);
- e) Allegations of ‘over-invoicing’ by certain suppliers or their agents and the diversion of the ‘over-invoiced’ amounts into offshore bank accounts;
- f) Unusual or irregular practices, transfers of funds and arrangements with suppliers, customers and third parties; and
- g) Circumstances under which the management of CMC Holdings allegedly:
 - Engaged a commission agent without Board approval;
 - Reversed Board approved salary increments; and
 - Proposed relocation of the entity’s operations without Board approval;

2.13 FINDINGS AND RECOMMENDATIONS ON THE CONDUCT OF AFFAIRS AT THE COMPANY

2.14 Criminal Matters involving directors of CMC Holdings

2.14.1 On the issue of offshore accounts

- Webber noted that some of the current and former directors of CMC Holdings are currently under investigation for the alleged over-invoicing of imported vehicles from certain manufactures and transfer of the over-invoiced foreign currency amounts into foreign bank accounts. This money was ostensibly placed in an offshore trust by the name The Fair Valley Trust for the purported benefit of past current and future employees of the CMCH Group. It was further alleged these irregular commissions were not separately disclosed on the invoices and were not reflected in the contracts with the concerned suppliers.
- The Trust was established in 1978 by Mr. Jack Benzima (deceased) who managed it until 1995 when he was succeeded by J G Kiereini, M H Forster, P K Jani (deceased) and Hon. Charles Njonjo (current director). The four were signatories to the offshore bank accounts.
- Of the four directors, Webber established that Mr. J G Kiereini and Mr. M. H. Forster were the only directors who were beneficiaries of the Trust. There was no evidence to suggest that the late Mr. Jani and Hon. Njonjo have ever benefited from the Trust.
- The report concluded that some of the former and current directors of CMC Holdings were involved in the corrupt practice of funding offshore bank accounts for their personal benefit. Webber called for further investigations to determine the source of funding of the Trust, the quantum, the distributions made to various directors and

ultimately establish the culpability of the directors involved in the running and management of the Trust.

To facilitate full investigations into the matter, Webber through the CMA, sought the assistance of the Attorney General of Kenya and the Jersey regulators. the investigations are still ongoing.

2.14.2 Allegations of irregularities affecting procurement possibly resulting in financial loss

- There were allegations that being a director and chairman of the CMC Holdings Board, Mr. Muthoka abused his position by securing contracts with AFS, a company in which he was the Chairman, Chief Executive Officer and principal shareholder, that were highly adverse to the interests of CMC Holdings. Moreover, it was alleged that Mr. Muthoka breached his duties as a director by failing to declare to the Board of CMC Holdings his interests in AFS.
- Webber's mandate was modified to exclude investigations under this head since this was the subject of another investigation conducted by Pwc. Webber were however tasked to consider the report submitted by Pwc and to give their reasoned opinion on the same.
- From the report prepared by Pwc, Webber were of the view that:-
 - a) The report did not present any evidence of criminal activity on the part of AFS or Mr. Muthoka in the dealings between AFS and CMC Motors;
 - b) although Pwc observed that they found strong evidence of irregularities in the dealings between AFS and CMC Motors, their findings were open-ended and full of disclaimers and could therefore not be relied on to reach a sustainable conclusion. Further, the report could not be relied on to reach a decision on

the suitability of Mr. Muthoka's on-going role as a director of CMC Holdings due to the uncertainty of the actual findings and evidence contained in the report;

- c) there was evidence of bad business practices being adopted by CMC in the on-going procurement of logistic services from AFS but little to no evidence of AFS making undisclosed profits from CMC Holdings;
- d) AFS was able to charge for logistic services at uncompetitive rates that were higher than the prevailing market rates because of poor negotiation practices adopted by CMC Motors;
- e) AFS and Mr. Muthoka took advantage of the weak internal controls at CMC Group and enriched AFS at the expense of the CMC Group but that this was done based on contracts executed at arm's length by both companies;
- f) Mr. Muthoka's business interests in AFS were in conflict with the interests of the CMC Group;
- g) material conflicts of interest clearly arose during the tenure of Mr. Muthoka as a Board Member of CMC Limited;
- h) Mr. Muthoka was in breach of the corporate guidelines issued by the CMA in failing to declare any existing conflicts of interest to both the boards of CMC Holdings and CMC Motors; and
- i) the Pwc report neither condemns nor exonerates Mr. Muthoka.

Webber were of the view that Mr. Muthoka's ongoing appointment as a director is an issue that falls to be dealt with by the company itself. Further, if Pwc had evidence that points to collusion and undue influence there could very well be a breach of fiduciary duties.

2.15 Technical Breaches by the Company

2.15.1 Group Company Secretary

Mr. Shah retired as Group Financial Director and Group Secretary on 6 August 2010 and was replaced by his deputy Mr. Musotsi. Mr. Musotsi took over all the secretarial duties and was described as the Group Company Secretary in the company's annual reports yet he was not a member of the Institute of Certified Public Secretaries of Kenya (ICPSK). This was in contravention of the Guideline 2.5.3 of the Guidelines on Corporate Governance Practices by Public Listed Companies in Kenya ("the Guidelines"), which provides that a Company Secretary must be a member of ICPSK.

This error was corrected when Ms. Catherine Munene, a certified public secretary, was appointed as Group Secretary on 12 January 2011 and Her appointment backdated to 6th August 2010 the date when Mr. Shah retired.

2.15.2 Composition of Board of Directors

- Following the resignation of Mr. Kiereini as Chairman of the Board, Mr. Muthoka was appointed the Chairman of CMC Holdings, with effect from 4 April 2011.
- Mr. Muthoka's appointment was made in breach of Guideline 3.2 (iii) which provides that the Chairmanship of a public listed company should be held by an independent and non-executive director. Mr. P Muthoka was not independent as envisaged in the guidelines. This was because he served as the Chairman and CEO of AFS, which was the sole provider of logistical services to the CMC Group.
- CMC Holdings remained in breach of the Guidelines until Mr. Muthoka was replaced by Mr. Joel Kibe as Chairman on 8 September 2011.

2.15.3 Private Transfers of CMCH's shares

- Webber investigated allegations of irregular private transfers of shares made between Kingsway Nominees Limited to Kingsway Family Holdings on 17th October 2011 and between CFC Stanbic, a nominee company, and AFS and found them to be unsubstantiated. These transfers did not involve any change of beneficial ownership and therefore did not require any disclosure in the annual reports. In addition the transfer between CFC and AFS was effected with due approval from the CMA.
- Webber established that there were no trades by or between the directors outside of the accepted price ranges. there was also no evidence of any insider trading in the shares of CMC Holdings.
- However, Webber found that CMC Holdings breached the Guidelines by failing to disclose the share acquisition by AFS in the quarter ended 31 March 2011. Clause D. 01 of the Capital Markets Securities Public Offers Listing and Disclosures Regulations requires all issuers to disclose at the end of each calendar quarter to the securities exchange every person who holds or acquires 3% or more of the issuer's ordinary shares. The share acquisition by AFS in the quarter ended 31 March 2011 represented (3.47%) increment in its shareholdings in CMC Holdings.

2.15.4 Take-over procedures

There was a breach of the Regulations when AFS, and by extension Mr. Muthoka, exceeded the 25% holding in CMCH shares and failed to declare its intention with regard to taking over the company.

2.16 Corporate governance and recent activities affecting the Board

- Webber Wentzel found that certain former Directors of CMC Holdings directed the Group to engage in the high-risk strategy of borrowing to lend over many years. The company borrowed heavily from various institutions at various rates and in turn sold its products on credit at a fixed interest rate that was hardly revised to take into account the rising cost of finance. This was done haphazardly since the company did not have an effective credit policy to guide the sales made under the Deferred Purchase Agreements Scheme.
- Webber were of the opinion that this strategy was geared towards generating increased corrupt commission income for the beneficiaries of the offshore Trust. They were also of the opinion that this practice adversely affected the Groups profitability since the Group's borrowing costs always exceeded the interest income recognized on the credit sales. Webber also faulted the Board for failing to implement a comprehensive policy to monitor, manage and hedge all such risks associated with the activity of borrowing to lend.
- Secondly, Webber noted that public disclosures made by the Board at times failed to properly disclose the true and accurate financial position of the company. Accordingly, this led to overstated profits.
- Thirdly, Webber found that there were no set policies and procedures in place for dealing with conflicts of interest in relation to directors and shareholders. CMC did not maintain a register of interest in contracts in which all declarations of interest should be recorded.
- Lastly, Webber formed the opinion that the Board is currently dysfunctional and engaged in harmful and destructive practices motivated by self-interest.

2.17 Allegations leveled against the current Management of CMC Holdings

some directors accused the current management of overstepping its mandate and usurping the directives issued by the Board. Webber agreed with most of these allegations but formed the view that Mr. Muthoka made the allegations in retaliation after he was removed as Chairman of the CMC Holdings Board. He did this with a view to:

- Divert attention from his alleged misconduct.
- To change the composition of the Board so as to gain control and terminate the investigation into the alleged overcharging by AFS.

The allegations leveled against management concerned the following:-

2.17.1 The appointment of a Commission Agent – Pewin Motors

It was alleged that the current management had entered into an onerous contract with a commissioned agent for the sale of their products and that there were many irregularities surrounding the appointment of the agent.

Webber established the following:

- The agent earns a flat rate of 6% on all sales of CMC products initiated by himself
- That on scrutiny of the amounts paid to the agent, it was discovered that a commission of Kshs 2,533,632 was paid and a further commission of Kshs. 227,328 has accrued to the agent in respect of LPOs authorized before the agent was appointed.
- That the company paid the agent commissions in respect of two LPOs where the cost of sales exceeded the sales value of the aggregate retail sales. The payment of the agent's commission further compounded the agent's loss. The contract is therefore flawed as it should have been drafted to exclude the payment of commission on loss making sales.

- That the appointment of the agent by CMC Motors was not approved by the Board of Directors and that the GFD signed the contract against the wishes of Mr. Muthoka, a director of the company.

2.17.2 Salary Increments

- That the increments were granted by the Caretaker Board Committee, appointed on 14 March 2011, after a joint review of the payroll with the current Group Financial Director.
- That the two largest increases were given to two logistics managers, which represented an increase of 100% and 120% of their basic salaries.
- That these two employees were directly involved in negotiating contracts between CMC Motors and AFS and were given the increments despite poor performance reviews.
- That the GMD reversed the salary increments with the approval of the Human Resources Management Committee.
- That this action usurped the decision by the Caretaker Board and was in direct contravention of the directive of the Board.

2.17.3 Proposed relocation to Sameer Business Park

It was alleged that the current Group Managing Director planned to move certain franchises of the company from the CMC headquarters to Sameer Business Park even after the Board rejected the same. Webber found that the proposal was put before the Board and rejected. The management therefore did not usurp the Boards directives on this.

2.18 Allegations leveled against the former Management of CMC Holdings

Webber were of the opinion that:-

- The system of internal control was compromised on numerous occasions by the former Group Managing Director.

- CMC products were frequently sold on unsecured cash sale basis without adequate security from the customer
- Customers who were unable to obtain bank finance were granted credit by CMC Motors
- That the company has not updated its internal audit manual or charter as recommended after an audit on the same was carried by Deloitte and Touché.
- That credit transactions in excess of Kshs. 50m were not presented to the Board of CMCM or to CMCH for authorization as required by the current Deferred Payments Arrangement (“DPA”) put in place by the Audit Committee of the Board.
- That fixed interest rates charged on deferred purchase arrangements were calculated on arbitrary basis by the GFD in contravention of the DPA policy which was at times disregarded by management. the policy by the Audit Committee was taken to be a guideline and was not always adhered to.
- That there was no procurement committee to review tenders and contracts awarded to suppliers.
- The company operated without an internal auditor.
- That the financial director of CMC Motors deliberately understated the overdraft balance in the financial information presented to management at 31 December 2009.

2.19 RECOMMENDATIONS OF THE WEBBER REPORT ON THE MEASURES TAKEN BY CMA

2.19.1 Suspension of shares

In considering the lifting of the suspension of the company’s ordinary shares the CMA should impose certain conditions on the company and its directors. The minimum conditions to be imposed should include the following:

- 1) That the Board of Directors, and each member thereof, agrees in writing not to trade in the ordinary shares of the Company for a stipulated “closed” period and that the directors’ existing shareholding, whether direct or beneficial be frozen and marked as such by the CDSC.
- 2) That current directors involved in the ‘Offshore Banking Scheme’ should be disqualified as directors with immediate effect.
- 3) That the two directors associated with AFS be suspended in taking part in any of the business dealings and governance of CMC Holdings Group of companies pending further investigation of issues raised in the Pwc Report.
- 4) That these suspensions could be lifted if further investigations establish that the two directors did not act against the interests of the Company and in breach of their duties. However, the two must be barred from holding directorship positions if the investigations reveal otherwise.
- 5) That the company should enforce its policy of rotating its external auditors every 5 years by way of a competitive tendering process.
- 6) That the company should appoint an internal auditor with the requisite qualifications, skills and experience forthwith.
- 7) That the company should commit to the upgrading of its systems and controls and should implement “adequate procedures, systems and controls” to prevent any person from entering into corrupt arrangements with any other person for and on behalf of the company.
- 8) That the company should repatriate all monies held in offshore banking accounts and investment portfolios following the completion of the investigation by the Kenyan and Jersey authorities.
- 9) That the company commits to assisting the prosecuting authorities in Kenya (and other jurisdictions if required to do so) in any criminal cases which may result from the past activities of the directors of the company.

- 10) That the company renegotiates all financing arrangements with suppliers in order to put an end to the corrupt commissions channeled to offshore accounts.
- 11) That the company adopts a new business model to eliminate the risks of extending credit on unfavourable terms to customers on the sale of its products; and
- 12) The suspension of trading of the CMC shares should only be lifted if the company is able to meet these conditions to the satisfaction of the CMA.

Further, the company should, unless the CMA decides otherwise:

- 1) Continue to comply with all its continuing obligations.
- 2) Submit to the CMA a monthly progress report pertaining to its current state of affairs and any action proposed to be taken in order to have the listing reinstated.
- 3) Advise the holders of securities, on a quarterly basis, concerning the current state of affairs and any action taken in order to have the listing reinstated, including the date on which the suspension is expected to be lifted.

2.19.2 Trading Rules

The trading rules of the NSE should be changed to introduce the concept of “closed periods” to better control the trading activities of directors of public listed companies in Kenya.

2.19.3 On the conduct of CMA in suspending the shares of CMC

Webber was of the view that CMA was at fault by:-

- 1) Suspending the company’s shares before conducting a preliminary investigation into the circumstances at CMC.
- 2) Failing to give CMC notice that it was considering delisting CMC’s shares from the NSE. Further CMA should have given CMC an

opportunity of making written representations in its defence prior to the CMA making any decision to suspend the listing of its shares.

- 3) Failing to impose such conditions as it may, in the circumstances, deem appropriate for the lifting of such suspension at the time it was suspending the listing of the shares.

3.0 SYNOPSIS OF THE CASE BY PETER MUTHOKA AGAINST THE CAPITAL MARKETS AUTHORITY, CMC HOLDINGS AND THE CARETAKER COMMITTEE OF CMC AND THE REGISTRAR OF COMPANIES

3.1 Facts of the case

- Peter Muthoka, the plaintiff herein, was appointed to the Board of Directors of the 1st defendant on 2nd March, 2006 and was re-elected in 2007 and continued to serve in that capacity until 12th March, 2012 when he was removed from the Board. He contends that the move that resulted in his removal was unlawfully instigated by the 2nd defendant in conduit with some of the directors of CMC Holdings.
- The plaintiff's application dated 14th March, 2012 sought a multiplicity of orders mainly to the effect that the plaintiff should be reinstated as director of CMC Holdings and that the board should not appoint other board members to his exclusion.
- The plaintiff claimed that he was still a director and that his office had not been vacated. He further claimed that he was not present at the meeting where the nominees of CMA were incorporated into the Board.
- The plaintiff submitted that following disagreements among the members of the Board, the CMC organized for a series of board meetings where the directors could resolve the issues arising. He

- averred that he attended these meetings and that there was no consensus reached by the directors on the various issues arising.
- He submitted that the second defendant and some directors of CMC held a meeting on 21st February 2012, for which he had no notice, where they resolved to dissolve the Board and appoint an interim Board. He further submitted that an “interim Board” is not an entity known in law or recognized by the Company’s Memorandum and Articles of Association.
 - The plaintiff contended that the CMA had no legal right to appoint or nominate for appointment strangers to the Board of Directors of CMC since the power to appoint and remove directors is vested in the shareholders of CMC during an annual general meeting.
 - The plaintiff further stated that at the time of his purported removal from the Board and appointment thereto of the nominees of CMA, there were orders made in High Court Petition No. 216 of 2011 in which the court had directed that the status quo as regards the 1st defendant’s Board be maintained. He contended that the action to dissolve the previous board and appoint an interim board was an act in contempt of court. The changes in the Board were undertaken against an order issued by **Ngugi, J. in HCCC No. 216 of 2011** to maintain status quo. He cited the case of *CLARKE & OTHERS vs. CHADBURN & OTHERS [1985] 1 ALL ER 211* where it was held that an act done in willful disobedience of an injunction or court order was not only a contempt of court but also an illegal act which could not, therefore, affect any change in the rights and liabilities of others.

- He averred that, As a result of the unlawful acts and commissions of the defendants, he had suffered and stood to suffer extreme prejudice, loss and damage which extended to prejudicing his eligibility and chances of appointment to other Companies' Boards and Trustee positions.
- To rebut the plaintiff's allegations, the defendants submitted that CMC is a public company listed and trading at the Nairobi Securities Exchange and as such the 2nd respondent has an oversight role in so far as its operations are concerned.
- It was further contended that the Articles of the Company gave the Board powers to increase or reduce the number of directors and to fill up any vacancies in the membership of the Board. Further it had been the practice of the company to nominate and appoint directors through Board Resolutions.
- It was also submitted that the plaintiff was in attendance at the meeting where the motion to appoint an interim board was passed by the Board without any reservations. This was done in order to comply with the CMA's directive as a regulator of all public listed companies. The interim Board was to comprise of seven of the current Board members including two executive directors and three of the CMA's nominees. The members of the interim Board are to remain in place for twelve (12) months from 22nd February unless otherwise directed by the Authority, in order to ensure continuity in the affairs in CMCH and with a view to restoring stability to its affairs. In addition, It was submitted that during the meeting of 12th March 2012, the matter of the five non executive directors was put to the vote, since there was no consensus on the matter and the plaintiff was voted out of the interim board.

- It was further submitted that the CMA was well within its powers in appointing the interim Board under powers vested in it under section 11 as read together with Section 25 (a) of the Capital Markets Act. the Act empowers the CMA to take such measures as are necessary to safeguard the interests of investors in Capital Markets and such measures include the nomination of directors to be appointed as an interim Board of a public listed company where necessary. the 2nd defendant therefore acted within its mandate and the court ought not to interfere unless it is demonstrated that the 2nd defendant had exceeded its powers or had misdirected itself in fact or law. It was further submitted that the High Court had already ruled that the CMA had extensive powers to protect shareholders investments and restore public confidence in the case of *DRY ASSOCIATES LIMITED vs. CAPITAL MARKETS AUTHORITY & ANOTHER*, High Court Petition No. 328 of 2011 where the court decreed that: “CMA must have the flexibility within its regulations to deal with matters that may dent or diminish investor and public confidence in the Capital Markets.”
- It was also submitted that the plaintiff had been adversely mentioned in an audit report prepared after forensic investigations conducted by Pricewaterhousecoopers Limited dated 23rd January, 2012 and that the public interest regarding the issue of the plaintiff’s suitability to serve in the 1st defendant’s Board of Directors far outweighed any prejudice the plaintiff may stand to suffer arising from his removal. it was submitted that Where the defendant is a public authority performing duties to the public, one must look at the balance of convenience more widely and take into account the interests of the public in general to whom the duties are owed.” It was further submitted that the Plaintiff could adequately be compensated with damages.

- The CMA submitted that the formation of an interim board was necessary since forensic investigations conducted by Webber revealed, among other things, that the constant disagreements among the members of the Board of CMC Holdings had resulted in a dysfunctional Board and poor oversight by the Board in the affairs of the Company. The interim Board was appointed with a view to the appointment of an interim Board to run the affairs of the Company with a view to restoring the Company's financial and commercial viability as well as investor confidence in the Company.

3.2 The ruling of the court

- The court found that section 11 of the CMA Act was very elaborate and was not exhaustive as to the powers of the CMA. The court based its findings on section 11 (w) which confers the CMA with a power to “do all such acts as may be incidental or conducive to the attainment of the objectives of the Authority or the exercise of its powers under this Act.”
- The court also formed the view that the forensic investigations conducted by Webber established that there were various weaknesses in the Company's corporate governance structure and that the CMA was justified in appointing an interim Board to run the affairs of the Company so as to restore investor confidence.
- The court noted that the CMA did not recommend the removal of either Mr. Muthoka or Mr. Kivai and that the same had occurred *ipso facto* after the Board Members voted on the constitution of the interim Board. The court further noted that the Webber report had recommended that the aforementioned directors, who are also connected with AFS Ltd, be suspended from taking part in any of the business dealings and governance of CMC Holdings pending further

investigations of issues raised by Pricewaterhousecoopers. The court also found that the Plaintiff had sufficient notice of the business to be conducted at the various meetings. In light of the foregoing, the court was not satisfied that the plaintiff had demonstrated that his removal from the Board of Directors was done unlawfully. However, the court conceded that in light of CMC's Articles of Association, the removal of the two directors would have been irregular had the company not been a public listed company.

- The court stated that the Capital Markets Authority is the public watchdog in so far as the conduct of public listed companies is concerned and it is by law mandated and expected to take all necessary steps within the confines of its statutory mandate to protect the interests of investors in the companies' securities. It would have failed in its duties if it did not take the steps that it did in this particular case.
- The court declined to comment on the allegations that the actions of the company and CMA in appointing an interim board since the same were the subject of contempt proceedings that are pending before court in *HCCC No. 216 of 2011*.

4.0 DELIBERATIONS ON COOPER MOTORS CORPORATION (CMC) HOLDINGS

4.1. CAPITAL MARKETS AUTHORITY (CMA)

Mr. Kungu Gatabaki, Chairman of CMA accompanied by Messrs:- Stella Kilonzo, Chief Executive; Wyclife Shamiah , Director Market Operations; Rose Lumumba, Director Corporate Secretary, Abubakar Hassan, Senior Legal Officer- Forensic Investigations, David Warutere, Regulatory Framework, and Kendi Bariu, Surveillance, appeared before the

Committee on Friday 25th November 2011; 22nd March, 2012; and 29th May, 2012.

4.2.1 CAPITAL MARKETS AUTHORITY INTERVENTION IN CMC

CMA informed the Committee that:-

- a) CMC is a public company whose shares are quoted at the Nairobi Securities Exchange (NSE). Its main business is the selling motor vehicles. CMC has ten (10) Directors out of which two (2) are Executive. The major shareholders are Andy Forwarders Ltd, Kingsway Family Ltd, APA Insurance, Mr. Paul Kibe, and Mr. Charles Njonjo among others. Currently, the preliminary accounts of CMC (unaudited) indicate that the company is profitable. Most franchises have reassured CMA that they will continue doing business with CMC except the following:-
- b) Land Rover which is reviewing its business environment globally;
- c) Initial reports were that Standard Chartered Bank had withdrawn its credit facilities to CMC. However, CMA confirmed that after its intervention the company continues to enjoy credit facilities by CFC and KCB Banks. CMA also confirmed that the company has an overdraft with Standard Chartered Bank and is in the process of repaying it; and
- d) Deloitte & Touché have resigned as Auditors without giving clear reasons for resignation.
- e) CMA requires a declaration of intention by any shareholder who acquires more than 25% of a listed companies shareholding either directly, through his/her affiliate companies or close associates and family. Mr. Muthoka failed to declare his intention to either take over the company or apply for exemption when his cumulative shareholding in CMC surpassed the threshold set by the CMA. CMA stated that Mr. Muthoka, AFS and his close family cumulatively

owned 25.03% of the total shareholding at CMC Motors. CMA also informed the Committee that it had taken up the matter and would handle it appropriately.

- f) The frequent wrangles in the Board of Directors, rapid depreciation of CMC share value and constant negative media reports which were bound to negatively affect the price and dealings in the shares of the Company informed CMA's decision to suspend CMC shares from trading for 90 days to forensically investigate the matter and to further extend the suspension indefinitely. They also informed the CMA's move to carry out a forensic investigation into the affairs of the Company through Webber Wentzel so as to determine whether there was any truth in the allegations cited by the warring factions of the 1st defendant's Board of Directors.
- g) CMC awarded a contract to Pricewaterhousecoopers (PWHC) to investigate the matter and the contents of the report are being contested in court by one faction of the Directors and AFS. Consequently, CMA urgently procured Webber (a South African Company) with expertise in forensic accounting) to investigate the matter within nine weeks. CMA admitted that due to the urgency of the matter it did not follow the normal procurement procedure in appointing the forensic auditor.

The Terms of Reference for the investigation included:-

- Determining whether there was siphoning of money through offshore accounts;
- Determining whether there was improper disclosure of the company's financial position
- Determining whether there were any irregular transfers of the company's shares and insider trading by the directors of the company;

- Determining whether there was a conflict of interest in the awarding of contracts to Andy Freight Services Ltd by CMC considering the directorship of Mr. Muthoka in both CMC and AFS.
- h. Discussions between CMA and CMC Directors had been on-going with a view to resolving the issues facing CMC amicably. This culminated in CMA demanding through a letter that CMC should not hold an Extraordinary General Meeting (EGM) with a view to changing the membership of the company's Board. Some of CMC's majority shareholders insisted on holding the EGM. The CMA consequently went to court seeking orders to prohibit the shareholders from holding the EGM. The Court issued orders prohibiting the EGM and retained the current Board of Directors. In one of the subsequent meetings, it was resolved that an Interim Board of ten (10) members be constituted to streamline the firm. This Board was to be a precedent setting phenomena in the country and was to work for twelve (12) months. CMA nominated three (3) members while CMC nominated seven (7) members to the Interim Board. Mr. Muthoka then went to court challenging the formation of an interim Board on the ground that CMA and members of the interim board had flouted the conservatory orders issued by the court prohibiting any changes in the composition of the Board.
- i. CMA stopped the EGM to protect shareholders' interests, stabilize the market and instill good governance procedures at CMC. Once the investigations are complete and all the necessary structures put in place, the shareholders will decide whether or not to have the General Meeting, bearing the Court of Appeal verdict. CMA submitted that it has powers to stop EGM in order to ensure that all the shareholders, especially minority shareholders, have the

required information before electing the new directors. besides, the fifteen (15) month period provided by CMA Act within which election should be conducted had not elapsed in the case of CMC.

- j. CMA does not micromanage quoted companies but rather regulates them to ensure that they adhere to the corporate guidelines provided for in the CMA Act. The CMA has powers to suspend a company from trading in NSE and compel compliance with regulations in cases where a company is in breach.
- k. CMA confirmed that the Work Permit of the current Chief Executive of CMC is valid according to the documents presented to it and that CMA was not aware that the said permit had been acquired four days after denial in the first application on 26th May, 2011. CMA indicated that it was only interested in the validity of the permit and not the process of acquisition from the Ministry of Immigration and Registration of Persons. However, if the investigations reveal that the permit was acquired fraudulently, then CMA would advice the Board to take appropriate action. The CMA officers were categorical that the CMA cannot force the company to sack the Managing director if he is in possession of a valid work permit.
- l. CMA recognized that some publicly listed companies could be having Articles of Association which are not consistent with the CMA Act, and as such CMA is in a process of re-looking at them with a view of advising on their revision. This is because the CMA's powers are limited with regard to how far they can go in compelling a company to change its Articles of Association. In order to give CMA powers to effectively deal with dysfunctional Boards, CMA has proposed amendments to the CMA Act through its parent ministry, the Ministry of Finance, for introduction in Parliament.

4.1.2 AUDIT REPORTS

a) Pricewaterhousecoopers (PWC) Audit Report

CMA informed the Committee that:-

- (i) The audit report pointed out glaring inefficiencies in CMC with regard to corporate governance, the competence of external auditors, and the financial management of the firm. The management of CMA formed an ad hoc committee to analyze the contents of the report with a view to presenting its recommendations to the Board for adoption and implementation.
- (ii) The forensic investigations conducted by PWC revealed serious allegations of overcharging and overbilling that were made against Andy Forwarders Services Limited in respect of logistics services rendered by it. The PWC report also contained serious complaints against Mr. Muthoka. The complaints range from acting in conflict of interest, unjust enrichment of the plaintiff's company, Andy Forwarders Services Limited, at the expense of CMC Holdings, improper conferment of benefits on employees and generally failing to act in the best interests of the Company. All these complaints and/or allegations have not been determined or resolved.
- (iii) The PWC report was being contested in court by Andy Forwarders Services Limited.

b) Forensic Audit Report by Webber Wenzel

CMA informed the committee that investigations conducted by Webber revealed, among other things, that the constant disagreements among the members of the Board of the 1st defendant had resulted in a dysfunctional Board and poor oversight by the members of the Board in the affairs of the Company. The investigations further revealed various problems including poor corporate governance, poor internal audit and financial controls, non-

existence of procurement procedures, irregularities in procurement and sales operations and the creation of offshore bank accounts and trusts in which the Company's money was diverted and the creation of a fund to be used for the benefit of the Company's controlling Directors and Chief Executives in previous years.

c) The wrangles in CMC

CMA informed the Committee that the wrangles in CMC have dragged on for a long period due to:-

- i. A series of court cases that have been filed. Seven cases have been filed by various parties so far. CMA sought to consolidate all the cases but the court ruled against this prayer since the cases were between different parties and the orders sought are very varied.
- ii. Unwillingness of the CMC Directors to compromise and reach a consensus.
- iii. Delayed release of the forensic audit reports and the limited powers given to CMA by the CMA Act to disband the Boards of a listed company.

4.2 EVIDENCE BY ANDY FORWARDERS SERVICES LTD

Mr. Peter Muthoka, Chairman/Chief Executive Officer of AFS accompanied by Messrs: - Vincent Mwaniki, Finance Manager; Julius Wambua, General Manager; and Fred Ojiambo, Legal Representative, appeared before the Committee on 30th November, 2011.

The Committee was informed that:

- a) The problems of CMC started about three years ago when claims of mismanagement and misappropriation of funds were made. As a result of the above claims, the Board contracted an audit firm, KPMG in 2009 to investigate the matter. KPMG presented its draft report with findings

indicating that the claims were unfounded. Upon presentation of the final report in April 2011, one of the directors discredited it and as a result it was not adopted by the Board.

- b) In March 2011, Mr. Martin Foster was relieved of his duties as the Chief Executive Officer of CMC and a Caretaker Committee was appointed to oversee the recruitment of a new Chief Executive Officer. The Caretaker Committee established that most workers were underpaid and had stagnated at one Job Group for a long time. Consequently, the Caretaker Committee reviewed and adjusted their terms of service accordingly.
- c) Mr. William Lay (who was previously working at General Motors Ltd) was hired by the Board on 15th April, 2011 subject to his presentation of a valid Working Permit. He was unpopular with some of the Board Members such as Mr. Peter Muthoka who was of the view that Mr. William Lay had been sacked from General Motors Ltd and did not possess the requisite academic and professional qualifications. Mr. Peter Muthoka further maintained that since Mr. William Lay had failed to present his academic credentials, there was nothing to show that he was qualified for the job. However, Mr. William Lay was hired by the committee and was to report for duty on 1st June 2011 subject to obtaining a work permit.
- d) On 30th May, 2011 the Ministry of Immigration & Registration of Persons wrote to Mr. Peter Muthoka informing him that Mr. William Lay had been denied a work permit. Upon receipt of the above information on 30th May 2011, Mr. Muthoka, as the chairman of the Board, wrote to Mr. Lay informing him of the Ministry's position. Meanwhile, he drafted an appeal letter to the ministry on behalf of Mr. Lay only to be informed by Mr. Lay, via a text message, that the latter had obtained a work permit through his own connections. Mr. Muthoka informed the

committee that unconfirmed rumors indicate that Mr. Lay got the Work Permit through the intervention by the Office of the Prime Minister.

- e) The law is categorically clear that a work permit is only valid for a specific company within a specified period of time. Mr. Lay therefore had to apply for a new one after he ceased working for General Motors Ltd to enable him to work for CMC Limited.
- f) Before Mr. Lay's recruitment, Mr. Gerald Jones Muli from General Motors Ltd had been recruited for the position of Operations Officer with effect from 1st June, 2011. Despite the fact that Mr. Jones was recruited earlier than Mr. Lay, the former declined to confirm him to this position indicating that he had a Release Clause from General Motors Ltd forbidding him from employing any of its staff if he ever worked for a competitor.
- g) Mr. Lay demoted all the General Managers who had been promoted by the Caretaker Committee and ratified by the Board on the basis that he was tasked to restructure the staff development. This was a clear usurpation of the directives of the Board but a section of the directors sided with him. He promised to review the salaries of the staff but has failed to do so to the date of the representations made to the committee by Mr. Muthoka.
- h) On 8th September, 2011 Mr. Muthoka was ousted as the Chairman of the CMC Board during a meeting for which his removal was not an item that the agenda. Moreover, his removal was not the subject of any Board Paper yet it was a very serious matter. On 12th September 2011, Mr. Muthoka gave a notice to call for the EGM to fix the problems of the non-functional CMC Board.
- i) On 16th September, 2011 the CMA and CMC held a meeting to find an amicable solution to the problems affecting CMC during which Mr. Lay stated categorically that he was opposed to the chairmanship of Mr. Muthoka.

- j) There was always a clear separation of powers between the Chairman and the Chief Executive Officer of CMC up to the time when Mr. William Lay joined the company. Mr. Muthoka informed the committee that the latter has since made decisions that require the Board's approval single handedly.
- k) That AFS has challenged the forensic investigation report prepared by Pwc in the High Court on the grounds that:-
- i. The engagement of the Defendants to carry out a forensic investigation into matters affecting the business of CMC Group was without the approval and sanction of the Board of Directors of the CMC Group.
 - ii. The investigations were undertaken in a manner that was in violation of the Memorandum and Articles for Association for CMC Holdings and was therefore illegal and invalid and of no effect.
 - iii. Pwc failed, as required by law, to undertake the forensic investigation and to prepare the final report professionally with care, accuracy and diligence expected of a reasonably competent Forensic Auditor acting in accordance with the set forensic auditing standards
 - iv. Pwc made grave and unsubstantiated conclusions on the basis of an incomplete investigation, founded on speculation and the standards of which fell short of acceptable professional standards.
 - v. Pwc failed to adhere to the scope of the terms contained in the engagement letter.
 - vi. Pwc violated the principles of natural justice by condemning Mr. Muthoka unheard.
 - vii. The report was false in material particulars, reckless and baseless and its publication has led to the Plaintiffs immense loss and damage.

- viii. PWC owed the Plaintiffs a duty of care and were in breach of that duty by negligently preparing their report and publicizing findings and opinions that were inaccurate and highly injurious and prejudicial to both AFS and Mr. Muthoka. The case is currently pending before High Court.
- l) AFS Ltd has been doing business with CMC since 1996 and tenders to the former have been awarded competitively. despite charging high rates The company provides value added benefits to CMC due to the following:-
- i. AFS offers a competitive advantage in that it is the only service provider that specializes in automotives. Its clients include; General Motors, TATA Africa Holdings Ltd, D.T. Dobie (K) Ltd, Marshalls E.A Ltd and Urysia.
 - ii. AFS has the strongest network of global forwarders among logistics service providers hence high efficiency in the supply chain.
 - iii. AFS has placed and developed Implant staff within CMC premises to ensure timely flow of documentation and effective communication.
 - iv. AFS is ISO 9001:2008 Certified thus giving CMC the required assurance on the quality of the Company's processes.

4.3 COOPER MOTORS CORPORATION (CMC) HOLDINGS

4.3.1 EVIDENCE BY CMC CHAIRMAN, MR. JOEL KIBE

Mr. Joel Kibe, Chairman of CMC accompanied by Mr. Iseme Kamau, Legal Representative, appeared before the Committee on 13th December, 2011 and informed the Committee that:-

- a) The major problem affecting CMC is attributed to the conflicting interests of the former Chairman, Mr. Peter Muthoka who used his

directorships in both CMC and AFS to enrich himself through overcharging CMC for logistical services.

- b) Andy Forwarders Ltd had been in business with the CMC for the last 17 years without a valid contract. The contract that was in place did not specify any rates and was therefore a conduit to defraud CMC through arbitrary prices.
- c) Pewin Ltd is contracted as an agent to penetrate those market niches the sales department of CMC cannot reach and is paid a 6% commission.
- d) There were allegations that the former management (Mr. Martin Foster together with his Finance Manager) had misappropriated funds through accounts falsification and offshore accounts. This culminated in the exit of the Finance Manager and Martin Foster. As a result, the Board contracted KPMG to carry out investigations on those allegations and the final report by KPMG was presented to the Board in April 2011 but was not adopted.
- e) When Mr. Martin Foster left CMC in March 2011, a Caretaker Committee comprising of Mr. Peter Muthoka and Mr. Paul Ndung'u was appointed to run the affairs of the company and recruit the new Chief Executive Officer. In executing its mandate, the Caretaker Committee interviewed and hired Mr. William Lay, who was working as an expatriate at General Motors Ltd, to be the new CEO with effect from 1st June, 2011. The appointment of Mr. Lay was subject to his obtaining a valid Work Permit. Mr. Muthoka simultaneously recruited an Operations Manager from the General Motors without the knowledge of Mr. Paul Ndung'u.
- f) Mr. William Lay was denied a work permit by the Ministry of Immigration and Registration of Persons vide a letter dated 26th May, 2011 and received at CMC on 30th May, 2011. Upon getting a rejection

communication, Mr. Peter Muthoka appealed to the Minister, who rescinded the earlier decision on 31st May, 2011.

- g) At a Board meeting held on 8th September 2011, Mr. Peter Muthoka was ousted as the chairman of CMC on the grounds of conflict of interest and was replaced by Mr. Joel Kibe.
- h) The Board subsequently resolved to contract PWC to carry out independent investigation on the dealings of Andy Forwarders Ltd and CMC. Aggrieved by the said resolution, Andy Forwarders Ltd. requisitioned an EGM on 21st November 2011 to reconstitute CMC's Board of Directors by removing Directors who Mr. Muthoka perceived as being hostile against him at the Board meeting held on 8th September 2011.
- i) Since CMC is a quoted company, CMA, while acting in the interests of the shareholders of CMC, summoned the CMC Directors and directed them not to hold any EGM until all the investigations are completed. The CMA also sanctioned another independent investigation into the matter.
- j) On 26th October 2011, Andy Forwarders Ltd. filed a constitutional petition in the High Court seeking to be allowed to hold the EGM. The matter was heard on 9th November 2011 and a ruling delivered against Andy Forwarders on 16th November 2011. Andy Forwarders has since appealed the ruling.
- k) Efforts by the current Chairman of CMC to reach out to the former Chairman with a view to resolving the inherent problems at CMC have remained futile.

4.3.2 EVIDENCE BY CMC GROUP MANAGING DIRECTOR, MR. WILLIAM LAY

Mr. William Lay, Group Managing Director appeared before the Committee on 15th December, 2011 and informed the Committee that:-

- a) He was recruited to be CMC's Group Managing Director by the Caretaker Committee comprising of Mr. Peter Muthoka and Mr. Paul Ndung'u. This done with the Committee's full knowledge that he had a Release Clause from General Motors barring him from employing any staff from the General Motors if he wished to qualify for pension.
- b) He has a wealth of unparalleled regional experience in the industry having worked at the General Motors for 37 years out of which he did 21 years in Kenya.
- c) He holds a Bachelors of Arts degree in Business Administration from ALMA College in USA but does not have the original documents since they were destroyed by floods in the 1980s. He undertook to get the certified copies from college and present them before the Committee in January 2012.
- d) Upon signing the employment contract with CMC, he applied for a Work Permit from the Ministry of Immigration and Registration of Persons, which was rejected and information communicated to the chairman of CMC in a letter dated 26th May, 2011. However, this decision was overturned on 31st May 2011 when the then CMC Chairman appealed to the Minister.
- e) His relationship with Mr. Peter Muthoka started to strain when he refused to confirm the employment of Mr. Jones Muli as the Operations Officer. He refused to do this since Mr. Muli was an employee of General Motors and employing Mr. Muli would have been against the Release Clause that he had with the General Motors.
- f) While executing his duties, he discovered that only 63 members of staff, all allied to Andy Forwarders Ltd, had been promoted by the Caretaker Committee. In an effort to treat all the employees fairly, he reversed the promotions and decided to review the terms of service for all the employees. This was another source of conflict with Mr. Muthoka.

- g) He discovered from the Company's books of accounts that there were many operational weakness in CMC, one of which was exorbitant cost of logistical services provided by AFS (a company belonging to Mr. Peter Muthoka). A closer scrutiny at the existing contract between AFS and CMC indicated that it was devoid of specific rates. He submitted that AFS provided similar services to General Motors at a much lower rate.
- h) During the Board meeting held on 8th September 2011, the Board ousted Mr. Peter Muthoka as the Chairman and contracted PWC to independently investigate CMC's dealings with AFS with a view to determining the extent to which the company had been defrauded. The investigation was to cover the alleged falsification of accounts during Mr. Martin Foster's tenure. Most of these anomalies, especially with regard to dealings with AFS, could not be exposed by Pwc since Mr. Muthoka was directly involved in drawing their Terms of Reference.
- i) Aggrieved by the said resolution, AFS requisitioned an EGM on 21st November 2011 to reconstitute CMC's Board of Directors by removing Directors who Mr. Muthoka perceived as being most vocal against him at the board meeting held on 8th September 2011.
- j) Since CMC is a quoted company, CMA summoned the directors and directed them not to hold any EGM until all the investigations are completed. The CMA also sanctioned another independent investigation into the matter.
- k) On 26th October 2011, Andy Forwarders filed a constitutional petition in the High Court seeking to be allowed to hold the EGM. The matter was heard on 9th November 2011 and a ruling delivered against Andy Forwarders Ltd. on 16th November 2011. Andy Forwarders Ltd appealed the ruling and the matter was to be heard in January 2012.
- l) Pewin Ltd as an agent was introduced to Mr. William Lay by the Caretaker Committee and was required to negotiate and execute sales contracts to the advantage of the CMC. 6% commission was agreed

- upon negotiation; Mr. Lay submitted that this is relatively cheap as compared to other industry players. The contract that was entered with Pewin Ltd on 1st June, 2011 was later varied through a management decision since such variation was not subject to the Board's approval.
- m) Mr. Lay confirmed that Captain Masinde worked together with him at General Motors as the Director of Security. Mr. Masinde was however relieved of his duties when investigations confirmed that he was using General Motors staff in his private security firm at the company's cost. Realizing the implications of being sacked, he pleaded to be allowed to resign from the Company.
 - n) In term of salary and emoluments, Mr. Lay submitted that he earns less than what he used to earn at General Motors but could however not substantiate this assertion.
 - o) Regarding relocation of certain franchises to Sameer Park at a cost of Kshs. 250 million, he submitted that the decision was approved unanimously by the board. He further submitted that it was only the luxury cars that were to be relocated there.

4.4 EVIDENCE BY THE MINISTER FOR IMMIGRATION AND REGISTRATION OF PERSONS

Hon. Gerald Otieno Kajwan'g, EGH, M.P, Minister for Immigration and Registration of Person appeared before the Committee on 15th and 20th December, 2011 and informed the Committee that:-

- a) Mr. William Lay, the current Group Managing Director of the CMC, applied for a Work Permit, as an expatriate, to work in CMC but was rejected on grounds that the job could be done by a Kenyan and the information was communicated to the then Chairman of CMC via a letter dated 26th May, 2011.

- b) On 30th May 2011, the then Chairman of CMC Mr. Peter Muthoka appealed to the Minister on behalf of Mr. William Lay on grounds that Mr. Lay had been headhunted from General Motors and had already signed a contract with CMC with effect from 1st June 2011. This meant that the company could be sued if it breached that contract. On 31st May 2011, the Minister rescinded the earlier decision and granted Mr. William a work permit.
- c) Subsequent to the meeting with the Committee on 15th December, 2011, the Minister relooked the initial Work Permit application for Mr. William Lay and considered the numerous pieces of information submitted by various shareholders of CMC. In his analysis of the whole scenario and considering the national interest, the Minister revoked the work permit of Mr. William Lay with effect from 20th December, 2011. He therefore instructed the Director of Immigration in the Ministry to implement the revocation.
- d) He confirmed that Mr. Peter Muthoka did not submit any appeal on behalf of Mr. William Lay upon rejection.

4.5 EVIDENCE BY CAPTAIN (RTD) CHARLES MASINDE

Captain (Rtd.) Charles Masinde appeared before the Committee on 30th November, 2011 and informed the Committee that:-

- a) He had previously worked with Mr. William Lay at General Motors between 1989 and 1998 in the Sales Department where Mr. Lay was his immediate boss. He submitted that Mr. Lay was sacked by General Motors due to a series of audit queries and that Mr. Lay sacked him without reason.
- b) He described Mr. William Lay as follows:-
- A man whose self interest surpassed professionalism and integrity. He also submitted that Mr. Lay rarely signed

documents so that he had an option of backtracking on his earlier actions.

- One of the longest serving expatriates in Kenya yet he did not possess the requisite academic qualification.
 - Who acquired management skills through experience since his grandfather and father were in the same business line.
 - Liked making capital investments.
- c) He confirmed that he had never met Mr. Peter Muthoka before and therefore he was not in a position to know the relationship between Mr. William Lay and Mr. Peter Muthoka.

5.0 COMMITTEE'S OBSERVATIONS

The Ccommittee observed that:-

5.1 CMC management

- a) The current and former Chief Executive Officers of CMC should be included in the forensic investigation with respect to their credibility and background information.
- b) Based on Mr. Muthoka's presentation, the Committee noted that the current Chief Executive Officer of CMC has assumed alot of powers that extend to reversing the Board decisions especially with regard to the revision of employee's remuneration.
- c) The demotions of all the members of staff amounted to breach of contract and was insensitive which could cost the company a lot of money if the affected employees went to court to seek compensation.
- d) The circumstances under which Mr. William Lay was issued with a Work Permit within a day after rejection raises integrity questions. The initial application to the Ministry of Immigration and Registration of Persons for grant of a Work Permit to Mr. Lay was rejected by the

Minister and notification of that rejection (No 341890 dated 26th May 2011) was received by CMC on 30th May 2011. On the following day (i.e 31st May 2011) Mr. Lay was granted a Work Permit, even though the Minister had not received any appeal against such rejection by CMC. Equally, the circumstances under which Mr. William Lay was hired without the requisite academic qualifications raises integrity questions. The Committee was concerned that Mr. William Lay could neither provide his academic and professional qualifications nor collaborate his educational qualifications with his work experience over his 37 years of service. It would therefore appear that in his application for a work permit, Mr. Lay misled the Ministry of Immigration and Registration of Persons about his educational and professional qualifications probably leading to the rejection of the application for a Work Permit in the first place. The Committee also wondered how Mr. William Lay was allowed to sign an employment contract before presentation of his qualifications and credentials for evaluation.

- e) The contract offer to Mr. Lay was subject to him being granted a valid work permit by the Ministry of Immigration and Registration of Persons. This is the normal procedure when employing expatriates; employment is conditional on a work permit being granted. Therefore the assertion by the Minister that had Mr. Lays' employment contract been cancelled following rejection of the Work Permit, CMC could have been sued for breach of contract is not correct. Accordingly, the reason given for reinstating Mr. Lay's Work Permit is not legally and procedurally sound.
- f) The Committee was concerned about the manner in which the Minister in charge of immigration handled the issue of Mr. William Lay's work permit.

- g) Even though Mr. Lay personally gave an undertaking to furnish the Committee with his academic transcripts in January 2012, Mr. Lay was yet to transmit the same to the Committee at the time of its deliberations in August 2012.
- h) Andy Forwarders Services Limited (“AFS”) (of which Mr. Muthoka is a director) had provided logistics services to CMC from as far back as 1996, well before Mr. Muthoka became a director of CMC in 2006. During that period, the level of fees for the logistics services provided to CMC was negotiated and agreed from time to time between AFS and CMC and recorded in a schedule of rates signed on behalf of each party. When a formal logistics contract was entered into between the parties on 10th June, 2010, the same procedure was followed. A draft of the contract was reviewed and commented upon by the then CEO of CMC, Martin Foster. The agreement provided that a schedule of rates for the services would be agreed between the parties from time to time (as had been the case over the years). The Committee was informed that the reason for such arrangement is that clearing and freight rates keep on changing from time to time depending on several factors, like fuel increases or adjustments; airline and shipping line charges; bunker adjustment factors (BAF) and also currency adjustments factors (CAF) among several other factors beyond the control of the contracting parties. The Committee was provided with documentary evidence comprising of schedules of rates signed between AFS and CMC. The documents included exchange of correspondence between AFS and CMC officials showing that the rates were negotiated and agreed by both parties before the schedules were signed, again by both parties.
- i) The Committee noted that under the International Financial Reporting Standards (IFRS) additional disclosures are required where an audit is

undertaken in respect of transactions between related parties. The object of such disclosures is to ensure that related party transactions are adequately disclosed and that the affected transactions do not contain misstatements which could materially affect the financial statements of the related parties. The Committee observed that prior to 2005, PWC (which was subsequently contracted by the CMC management to undertake a forensic audit of the logistics contract between AFS and CMC) was the auditor of CMC. After 2005, Deloitte and Touche were appointed CMC's auditors. The Committee further noted that in the period of 17 years during which AFS provided logistics services to CMC, neither of the two international auditing firms ever issued a qualification to the CMC financial statements or raised a management letter point on the basis of the relationship between AFS and CMC.

- j) Serious allegations were made by Captain (Rtd.) Charles Masinde against Mr. William Lay which were not rebutted by Mr. Lay through provision of academic credentials. They require further investigations by the Ministry of Immigration and Registration of Persons.

5.2 Capital Markets Authority

- a) The powers of CMA are not limited with regard to the actions it can take to regulate the governance of a publicly listed company in order to protect investor's interests. However, there is need to expressly provide for the CMA's powers to oust dysfunctional boards and to take similar measures in overcoming governance problems at publicly listed companies. This is important so that the CMA is free to take any necessary and urgent action without fear that the same would be delayed by court action.
- b) That the CMA has already forwarded some proposed amendments to its parent ministry, the Ministry of Finance and that the same have

been finalized and are currently awaiting stakeholder input before introduction to Parliament. Therefore, there is need to expedite the amendments to the CMA Act and possibly the Companies Act.

- c) The Committee noted that CMA was not aware of the exact position of CMC's credit facilities in order to recommend a suitable re-organization/restructuring business model as it had done previously in case of Uchumi. The Committee therefore urges CMA to explore a suitable business model that can save CMC from going under.
- d) While appreciating the importance of CMA's suspension of CMC from the trading at the NSE and delaying the EGM, the Committee was concerned with the slow pace at which the matter was being handled and the increasing number of suits being filed in court. This has the effect of further eroding the value of the firm. The Committee therefore urged the CMA to expedite the processing of the audit reports in its possession and, draw a clear implementation road map. Although the suspension of CMC from trading was meant to allow CMA to conduct an investigation into the alleged misappropriation by some directors, the trading remains suspended at the time of doing this report even after the audit was finalized and a report issued in January.

5.3 The forensic Reports

The Committee observed that the forensic report by PWC contained many disclaimers and hardly provided any conclusive findings. The Committee also noted that the Webber Wentzel report had expressed reservations on the reliance which can be placed on the PWC report due to its many disclaimers and numerous calls for further investigations. This is

contained on page 38 and 39.of the Webber Wentzel report which reads as follows:-

“114.3 PWC do however go on to report that “on the basis (they) came across evidence pointing to collusion and/or undue influence, (they) recommend that further investigations are undertaken.....

114.4 the statement in 114.3 above is open ended and makes any decision on the conduct of AFS/PWM and his on-going role as a director of CMCH difficult due to uncertainty of the actual findings and evidence.

115 the report is written in the passive tense and includes many references to “it appears”. It is not clear whether this implies that PwC is unsure of the facts or whether PWC is being cautious in its findings, in the absence of hard facts...

121. The PWC report neither condemns nor exonerates PWM and alludes to evidence pointing to collusion and undue influence. In our opinion, this is insufficient for the CMA to suspend or disqualify PWM as a director until further investigation. PWM’s on-going appointment as a director is an issue which falls to be dealt with by the company itself”

The committee further noted that the PWC Report has been challenged in court and that there was a possibility that the court could expunge the same. Due to the foregoing, the Committee was of the view that reliance should not be placed on the Forensic Report prepared by PWC. The Committee also expressed further concerns on the reliability of the PWC report for the following reasons:-

- (i) The investigation was commissioned by the CMC management who were the accusers of AFS and therefore partisan. The investigation should have been commissioned by CMA to avoid the perception of bias and undue influence.

- (ii) It is not clear why CMA specifically excluded investigation of the Andy Forwarders logistics contract from the terms of reference of the Webber Wentzel investigation given the fact that the logistics contract was at the centre of the dispute between the directors of CMC.
- (iii) CMA appears not to have taken any action in connection with the Pewin contract which attracted an adverse mention in the Webber Wentzel report. For the sake of fairness and even handedness amongst the players in the CMC dispute, the Committee considers and recommends that appropriate investigations be commenced on the allegations made in respect of that contract. In particular, it was mentioned in the Webber Wentzel report (page 79) that the Pewin contract “was flawed” and was signed by Mr. Lay on the first day when he reported for work at CMC without Board approval. It was also a finding of the Webber Wentzel report that the GFD signed the contract against the wishes of a member of the caretaker committee, Mr. P W Muthoka.

5.4 The Ministry of Immigration

- a) The Committee was displeased with the manner in which the issue of Mr. Lay’s work permit was handled. The Ministry declined to award him a work permit and notified CMC of its decline through a notice dated 26th May 2011 which was received by CMC ON 30th May 2011. The Ministry then surprisingly awarded him a work permit a day later after receipt of the refusal notice by CMC. Thereafter the Minister revoked the work permit he had issued after just a few months via his interoffice Memo dated 20th December 2011 which he presented to this committee and confirmed his revocation.

- b) The Committee further notes that the work being done by the Chief Executive officer could be undertaken by a Kenyan and that the Chief Executive officer, Mr. Lay was unable to furnish the Committee with any certificates to prove his academic or professional qualifications.
- c) The Committee observed that it was not clear whether Mr. Lay had a valid work permit and whether he qualified to be issued with a work permit.

6.0 COMMITTEE'S RECOMMENDATIONS

1. That prior to suspending the trading of share in any listed company, CMA should carry out preliminary investigations and give the company in question an opportunity to make submissions to the CMA in order to protect investor's interests. In the event of suspension of trading in shares of a listed company, CMA should at the time of suspension impose conditions for the lifting of suspension to enable the company be aware of the action it should take in order for the suspension to be lifted. This shall be fair administrative action as set out at Article 47 of the new Constitution of Kenya which states as follows:

"Fair administrative action

47. (1) Every person has the right to administrative action that is expeditious, efficient, lawful, reasonable and procedurally fair.
- (2) If a right or fundamental freedom of a person has been or is likely to be adversely affected by administrative action, the person has the right to be given written reasons for the action.
- (3) Parliament shall enact legislation to give effect to the rights in clause (1) and that legislation shall—

- (a) provide for the review of administrative action by a court or, if appropriate, an independent and impartial tribunal; and
 - (b) promote efficient administration.”
- 2. CMA and the Director of Public Prosecutions should launch further investigations to establish whether the past and present Directors and management of CMC have committed any criminal offence.
- 3. The Shareholders of CMC associated with Andy Freight Forwarders Ltd should not be prohibited from being members of CMC’s Board of Directors until and unless they are implicated in the outcome of further investigations as this may infringe on their rights under the Companies Act.
- 4. CMA should take appropriate measures to ensure that CMC is operating in accordance with the principles of good governance and that shareholders interests are protected.
- 5. The law and regulations in place give CMA wide regulatory powers in respect of listed companies. CMA should continue to prudently exercise the powers granted to it in order to ensure the Capital Markets operate within the law and guidelines set out as well as protect investor’s interest.
- 6. The powers granted to CMA under the law have not anticipated all situations in which its intervention is required such as in this case where the Board of Directors has become dysfunctional. The law therefore needs to be reviewed in order to grant the CMA additional powers to intervene and protect investor interests in circumstances where a listed company is experiencing poor corporate governance. The trading rules of the Nairobi Securities tock Exchange should be

reviewed to introduce the concept of “closed periods” to better control the trading activities of directors of public listed companies in Kenya.

7. The Executive should fast track the introduction of the two Bills relating to the regulatory powers of CMA in Parliament.
8. The committee agrees with the assessment given by the Minister for immigration and Registration of Persons that the work performed by Mr. William Lay can be done by a Kenyan and recommends that Mr. Lay’s work permit be cancelled immediately, in the interest of the Kenyan public, unless there is a compelling reason not to do so.
9. The Departmental Committee on Administration and National Security should comprehensively investigate the manner in which work permits are issued to foreigners generally to establish whether the law is being flouted in awarding work permits.