FORTIS HEALTHCARE: REPEAT OF SATYAM?

We are seeing a repeat of what happened at Satyam and UB Group, at Fortis. Fortis recently admitted having '*deployed*' funds of Rs. 473 Crore with companies (that became promoter owned companies) by terming them as '*secured short-term investments in normal course of treasury operations*". This involved,

- no notification to stock exchanges either at the time of deploying these funds or when the entities became promoter entities,
- not seeking mandatory shareholder approval by routing the funds through a subsidiary, and
- possible violation of Indian Accounting Standards by classifying loans and advances to related parties (these promoter entities) as cash and equivalents.

Fortis even hasn't yet published its Q2 and Q3 results giving an absurd rationale of the Board being busy with other issues at hand. This has also triggered SEBI to institute an investigation for which it has asked Fortis to furnish information by 26th February 2018.

This article discusses this in detail and also studies Fortis' past actions to find that its frequent restructurings and frequent directors' resignations has eroded investors' trust as well as wealth. Fortis doesn't seem to be a stranger to utilizing company funds to fund promoters' own business interests.

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On 9th February 2018, Fortis Healthcare Limited ("Fortis") notified to the stock exchanges that, *"Fortis Hospitals Limited, a wholly-owned subsidiary of Fortis has deployed funds in secured short-term investments with companies in normal course of treasury operations. These entities as of the quarter ended 31st December 2017 have become part of the promoter group due to a shareholding change in those entities. Subsequently, the same loans have been recognized as Related Party Transactions in compliance with necessary regulatory requirements. Those loans are adequately secured, and the repayment has since commenced. The total value of the loans mentioned above amounts to approx. Rs. 473 Crore."*

Through other stock exchange notifications, the company also stated that the Q2 and Q3 results are not yet tabled due the Board being 'busy' in discussing acquisition of certain Religare Health Trust's assets and that the results were to be taken up in the Board meeting on 13th February 2018. The company held a Board meeting on 13th February 2018 but the Board still couldn't finalize the quarterly results and sought an extension till 28th February 2018.

We learn the following from these disclosures:

- Fortis has advanced its own cash to fund promoters' personal business interests without informing the shareholders. This is similar to what happened at UB Group.
- The company has skirted seeking public shareholders approval for a contentious related party transaction by routing the transaction through a subsidiary.
- The company has also possibly violated Indian Accounting Standards by classifying loans and advances to related parties as cash and equivalents. This is similar to what happened at Satyam.
- The rationale provided by the Board for delaying publishing of quarterly results is absurd and warrants a thorough regulatory investigation.

Skirting Shareholder Approval

Section 186 of the Companies Act, 2013 requires companies to mandatorily seek shareholders' approval to make inter-corporate investments and advances. However, for advances to wholly-owned subsidiaries, only a Board approval is required. If Fortis had made these advances directly to the promoter entities, it would have required minority shareholders' approval through a special resolution and there was a high probability that the resolution could have been defeated. However, by routing the advances through Fortis Hospitals Ltd, a wholly-owned subsidiary, Fortis didn't bother seeking shareholders' approval and also didn't have to even make a public disclosure about the transaction. Although the 2017 annual report of Fortis mentions a related party transaction with the subsidiary, there are no details till today of the ultimate beneficiaries. The link to the subsidiary's financial statements in the company's website throws up the statements of another subsidiary namely Fortis Hospotel Limited.

Possible Violation of Indian Accounting Standards

The company stated that it 'deployed' funds in secured short-term investments with promoter entities in normal course of treasury operations. This should be shown as current loans and advances on the assets side of the balance sheet. However, the consolidated balance sheet of Fortis shows a cash & equivalents amount of Rs. 544 Crore in 2017 compared to Rs. 142 Crore in 2016. Has the company classified the advances of Rs. 473 Crore as cash & equivalents? If yes, shouldn't this be considered as a violation of the Indian Accounting Standards?

Statutory Auditors' Responsibility – Reporting of Fraud

SEBI (LODR) Regulations require quarterly financial results to be published within 45 days of the quarter ending date. The company, in its notification dated 9th February 2018, stated that financial results for quarters ended 30th September 2017 and 31st December 2017 are under the limited review of auditors. The statutory auditors Deloitte Haskins & Sells have a responsibility to the shareholders and should have reported to the regulator the reason for not signing off on the Q2 statements. The auditors should also have flagged off the entry of advances to promoter entities as cash & equivalents in the consolidated balance sheet of Fortis. Section 143(12) of the Companies Act, 2013 states, "*if an auditor of a company (…) has reason to believe that an offence involving fraud is being or has been committed against the company by officers or employees of the company, he shall immediately report the matter to the Central Government within such time and in such manner as may be prescribed*". On basis of Section 143, isn't it the responsibility of Deloitte to report this fraud to the Central Government?

Utilizing Company's Cash to Fund Promoter's Personal Businesses

The funds of Rs. 473 Crore advanced to these promoter entities are cash in the books of Fortis. This transaction, made through a subsidiary, ensured that the company's cash is transferred to promoters' business without informing shareholders. However, this is not the first time that concerns of utilization of Fortis Healthcare's cash for promoters' own uses have surfaced. These concerns were raised even in 2011, brief facts of which are:

- In 2010, Fortis Mauritius, 100% subsidiary of Fortis acquired 25% in Parkway Holdings Singapore
- Fortis raised $100mn through FCCBs. In the same month it gave Rs.395 Crore loan to Fortis Mauritius
- In second round, RHC Healthcare submitted bid to increase Fortis Group shareholding in Parkway Holdings
- RHC Healthcare was 49% owned by Fortis Mauritius and 51% by Fortis Promoters
- Gradually, the promoters came to own 100% of shareholding in RHC Healthcare
- RHC Healthcare then underwent name changes twice to finally become Fortis Healthcare International ("Fortis International")
- During 2010-11, Fortis promoters bought 6 overseas assets through Fortis International
- As per Fortis Healthcare, Fortis International paid $580mn for the acquisition
- In 2011, Fortis acquired Fortis International for $665mn
- Here, a question is what happened to the loan of Rs.395 Crore given to Fortis Mauritius?
- Fortis International's annual returns for FY2011 showed a pending loan of $121mn from a related company
- Was this amount the loan given by Fortis to Fortis Mauritius and then possibly by Fortis Mauritius to RHC Healthcare to fund the second-round bid for shares of Parkway Holdings?
- If this loan was indeed out of Fortis Healthcare's FCCB proceeds of $100mn, it was a clear case of FCCB funds being diverted to fund promoters' private businesses
- Also, Fortis International was paying only 4.4% interest on that loan while Fortis was paying 5% interest on FCCBs

There were many other concerns that shrouded this transaction. These were:

- Promoters bought 51% stake in RHC Healthcare, changed its name twice and then sold their 100% stake in the company to Fortis Healthcare in less than a year

- Fortis International acquired these 6 overseas assets for $580mn. In less than a year, Fortis acquired Fortis International for $665mn. Why a premium of $85mn was paid to the promoters for holding these assets for less than a year?
- The valuation of Fortis International was questioned as all the 6 assets were not uniformly valued. While some assets were valued at market price, others were valued at book value
- Why did the company engage only one valuer when FEMA required two independent valuers' opinions in such foreign acquisitions?

Frequent Restructurings – Running Fortis or Playing Lego?

Frequent restructurings create confusion and sometimes, are catalyst to destruction of shareholders' wealth in any company. A look at the recent history of Fortis will show that its promoters love restructurings and have treated the company like a game of Lego.

Given below is a list of some of the acquisitions and restructurings by Fortis since 2010:

- December 2009: Addition of 175 bed hospital in Bhiwani, Haryana. Renamed as Fortis MK Hospital and will be managed by Fortis under an Operations and Management (O&M) arrangement
- February 2010: Announcement of 200 bed Greenfield project in Ludhiana and addition of 100 bed hospital in Kangra, Himachal Pradesh
- March 2010: Fortis Mauritius, a 100% subsidiary, acquires 23.9% stake in Parkway Holdings Ltd, Singapore from TPG Capital. Deal size was estimated at USD685.3mn
- May 2010: Raises USD100mn through FCCBs. Issues 22.3mn shares to GIC Singapore. Both fundraisings done to finance acquisitions. Religare Capital markets (a related party) was the book manager and advisor in both these fundraisings
- July 2010: Promoter entity RHC Healthcare bids with Fortis to acquire Parkway Holdings Ltd for USD3.2bn
- July 2010: Fortis divests entire stake in Parkway Holdings Ltd to Khazanah Nasional with a profit
- December 2010: Addition of 100 bed OP Jindal Hospital in Raigarh, Chhattisgarh under an Operations and Management (O&M) arrangement
- December 2010: Addition of 150 bed Vivekanand Hospital and Research Centre in Moradabad, UP. Renamed as Fortis Vivekanand Hospital and managed by Fortis under an Operations and Management (O&M) arrangement
- January 2011: Name changed from Fortis Healthcare Ltd to Fortis Healthcare (India) Ltd
- January 2011: Addition of 100 bed Lifeline Hospital in Alwar, Rajasthan
- May 2011: Acquisition of 86% stake in Super Religare Laboratories (SRL)
- September 2011: Name reverted from Fortis Healthcare (India) Ltd to Fortis Healthcare Ltd
- November 2011: Acquisition of and merger with promoter Entity Fortis Healthcare International Pte, Singapore at USD665mn. This is the same company under the name of RHC Healthcare which had bid with Fortis to acquire Parkway Holdings in July 2010

- January 2012: Fortis completes acquisition of promoter entity Fortis Healthcare International for USD665mn
- February 2012: Fortis Singapore, a subsidiary, acquired 85% stake in RadLink-Asia Pte Ltd, Singapore for SGD62.9mn
- June 2012: IFC and NYLIM Jacob Ballas India invest Rs. 370 Crore in SRL through convertible preference shares. Post conversion, Fortis will hold 55-56% stake in SRL
- October 2012: Religare Health Trust (RHT) raises SGD511mn and lists on the Singapore Exchange. Fortis continues to hold 28% stake in RHT. RHT's initial portfolio included 11 clinical establishments, 4 greenfield establishments and 2 hospitals
- May 2013: Dental Corporation Holdings, Australia, which was acquired as a result of acquisition of promoter entity Fortis Healthcare International, sold off to Bupa for AUD270mn
- August 2013: Fortis Hoan My Medical Corporation, VOF PE Holding2 Limited and Swindon Limited, which was acquired as a result of acquisition of promoter entity Fortis Healthcare International, sold off to Viva Holdings Vietnam for USD80mn
- October 2013: Quality Healthcare Hong Kong (held by Fortis Healthcare International) is sold off to Bupa for USD355mn
- February 2014: Board approval received for:
  - Division of the business of its hospital located at Mohali, Punjab into two separate business verticals i.e. clinical establishment division and medical services division;
  - Execution of a business transfer agreement with Escorts Heart and Super Specialty Hospital Limited ("EHSSHL"), a subsidiary of Religare Health Trust, for sale of the Mohali Clinical Establishment to EHSSHL;
  - Execution of a deed of sale with EHSSHL for the sale of its immovable plant and machinery at the Mohali Clinical Establishment; and
  - Execution of a hospital and medical services agreement with EHSSHL whereby EHSSHL shall provide Clinical Establishment Services in respect of the Mohali Clinical Establishment and the Company shall operate and manage the Mohali Clinical Establishment and provide medical and healthcare services, including in-patient services and emergency services
- March 2014: Board approval received for purchase of operations of Fortis Hospital, Shalimar Bagh by the Company from its subsidiary, Fortis Hospitals Limited on slump sale
- April 2015: Sale of Fortis Surgical Hospital (held by Fortis Healthcare International) to Concord Medical Services (International) Pte Ltd for SGD55mn
- March 2015: Sale of entire stake in RadLink-Asia Pte Limited, Singapore for SGD111mn to Fullerton Healthcare Group
- September 2015: Board approves structural re-arrangement of Kangra hospital
- February 2016: The Trustee Manager of RHT is acquired for USD14.9mn
- October 2016: The Board states that 100% subsidiary Fortis Hospitals Limited (FHsL) has agreed to acquire 4,01,769 Compulsory Convertible Preference Shares from International Hospitals Limited (IHL) issued by Escort Heart Institute & Research Centre Limited (EHIRCL) to IHL at a consideration of upto Rs. 360 Crores. After the said acquisition

holding of the Company (direct and indirect) in EHIRCL shall increase from 83.27% to 100%
- October 2016: Repurchase of 51% economic interest in Fortis Hospotel Ltd from RHT
- July 2016: Promoter company Fortis Healthcare Holdings Private Limited transfers its complete shareholding in Hiranandani Healthcare Private Limited, a subsidiary company to Fortis Healthcare Limited for Rs. 61 Crore
- July 2016: Fortis Healthcare Holdings Private Limited and RHC Holding Private Limited, promoter companies transfer their complete shareholding in Fortis HealthStaff Limited to Escorts Heart Institute and Research Centre Limited, both being subsidiary companies
- July 2016: Fortis Healthcare Holdings Private Limited, a promoter company has today transferred its complete shareholding in Fortis Emergency Services Limited, an associate company to Fortis Hospitals Limited
- March 2017: Shareholder approval sought for a scheme of arrangement involving:
    - Transfer of hospital business undertaking of Fortis Malar Hospitals to Fortis
    - Transfer of diagnostics business of Fortis to Fortis Malar Hospitals
    - Amalgamation of SRL into Fortis Malar Hospitals
- August 2017: Sale of entire 79.43% stake in Lalitha Healthcare Private Limited (LHPL) to promoters of LHPL
- November 2017: Execution of a term sheet containing an exclusivity arrangement, in relation to the proposed acquisition of the equity and financial securities, under RHT Health Trust for a combined enterprise value of approx. Rs. 4,650 Crore (including RHT Debt of approx. Rs. 1,152 Crore) from the wholly-owned subsidiaries of RHT

High ID Turnover – Without Proper Rationale

There has been a high Independent Directors turnover in Fortis Board and none of them were accompanied with a proper and logical explanation. As can be seen below, there have been cases of Directors resignations in the past year only and some of these directors resigned almost immediately after announcement/ conclusion of a restructuring by the company. Examples in 2017 are given below:

Date	Name	Type	Reason Provided	Major Event
14 Nov	Shraddha Suri Marwah	ID	Personal reason	Same day: Execution of term sheet for acquisition of certain assets of RHT
4 Aug	Sunil Godhwani	NED	Non-attendance	-
12 Apr	Ravi Mehrotra	NED	Pre-occupation	27 March: Scheme of Arrangement between Fortis, SRL and Fortis Malar Hospital
11 Apr	Lynette Hepburn Brown	ID	Personal reason. Due to frequent long travel.	

Also, the company announced Lt. Gen. Tejinder Singh Shergill as its new Independent Director w.e.f. 12th February 2018. The disclosure to stock exchanges nowhere stated that he already serves as an Independent Director of SRL Limited, which is a subsidiary of Fortis.

Rinse and Repeat at Religare Enterprises

The issue of diversion of funds from the company is not limited to Fortis alone. The auditors of promoter group's Religare Enterprises ("Religare") have also qualified its Q3 financial statements for similar issues. As per their limited review report, "*Recently, Company has forwarded inspection reports from RBI on the financial position of Religare Finvest Ltd as on March 31, 2016 and March 31, 2017, raising various concerns particularly additional material NPA provisioning (Rs. 798 Crores), diminution in value of investments (Rs. 15 Crores), resultant negative adjustments in net worth, restriction on expansion of credit/ investment portfolios, increase in corporate loan book against RBI directions* ***including some cases of movement of funds from intermediary borrowing companies to group companies of Religare Finvest Ltd*** *(further corroborated by our review procedures during the year (i.e. further* ***funds have been given during the year to such intermediary borrowing companies to the extent of Rs. 525 Crores) besides continuing weakness of internal control****, seeking clarity on roll over of fixed deposits lying with a Bank.* ***These may have penal consequences from regulators (including RBI)*** *and would then impact the carrying value of investments of the company in Religare Finvest Ltd. Considering the above, there are indicators on the material impairment of carrying value of investments of the company in its subsidiary Religare Finvest Ltd.* ***Extensive review is being conducted****.*"

In addition, the auditors have qualified the statements stating, "The company is registered as ND-SI-CIC under Section 451A of RBI Act, 1934 and primarily holding investments in various group companies. Management has informed us that impairment study is yet to be concluded with respect to investments held by the company in its major subsidiary, Religare Finvest Ltd constituting more than 75% (aggregating to Rs. 2900 Crores) of the total investments as on December 31, 2017.

The auditors also state, "*Attention is invited to note no.5 (b) of the standalone unaudited financial results referred to in this report in relation to put option exercised by non-resident shareholders of Religare Finvest Ltd on the company (amount involved Rs. 525 Crores approx. as per Hon'ble Delhi High Court order dated 5th Jan 2018). Pending litigation in the Hon'ble Delhi High Court, its potential impact due to probable impairment on the increased shareholding of the Company in Religare Finvest Ltd and cash outflows of the company is yet to be considered.*"

These statements by the auditors makes it clear that the modus operandi of Religare been the same as of Fortis in the matter of movement of funds to Group companies. Instead of advancing loans themselves, both Religare as well as Fortis have routed the funds through subsidiaries; Fortis through Fortis Hospitals Ltd and Religare through Religare Finvest Ltd. This has helped them avoid seeking shareholder approval. Also, Religare has tried to keep these irregularities under radar by not conducting any impairment study on Religare Finvest Ltd.

SEBI Investigation Instituted

On 17th February, the Company reported to stock exchanges that SEBI has instituted an investigation on the matter and has asked Fortis to furnish information and documents by 26th February. We opine that this investigation should not only be limited to Fortis but also look into the irregularities at Religare as well.

End Note

The issue of transferring funds to a wholly owned subsidiary which in turns lends to promoter entities, in order to skirt the shareholder approval requirement, seems to be a blatant fraud. Much like the Satyam cash, the cash and cash equivalents on the books of the company seem to be non-existent. The company's subsidiary has conveniently given the loans to related parties without seeking shareholder approval and regulatory filings. SEBI has instituted an investigation and take it to a logical conclusion on the basis of Companies Act and LODR Regulations. The statutory auditor has a responsibility to the shareholders and should have reported to the regulator the reason for not signing off on the Q2 statements.

Investors of Fortis and Religare are hoping for the true financial picture to come out and also hope that the companies, without the promoters, take steps to improve governance.

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