

To:

Directors of Tata Sons Ltd.

**CONFIDENTIAL**

I was shocked beyond words at the happenings at the board meeting of October 24, 2016. Apart from the invalidity and illegality of the business that was conducted, I have to say that the Board of Directors has not covered itself with glory. To "replace" your Chairman without so much as a word of explanation and without affording him an opportunity of defending himself, in a summary manner must be unique in the annals of corporate history. The suddenness of the action, and the lack of explanation has led to all manner of speculation and has done my reputation and the reputation of the Tata Group immeasurable harm.

At the outset, I have to say that I have great respect for the Tata Group and the thousands of employees who are working hard despite the challenges. I am writing this letter to the Board to emphasise the total lack of corporate governance and to point out the failure on the part of the directors to discharge the fiduciary duty owed to stakeholders of Tata Sons and of the group companies. All of this does not augur well for the future of the Group. All that is said here is well known to many among you, but I would like to put in one place my journey as Chairman of Tata Sons. It is important to emphasise the enormity of what has transpired in the Group and what corrective action is to be taken. Each of you is already in receipt of and familiar with

the Strategy 2025 document that I presented to you, and in which I had articulated our growth strategy for the future.

In 2011, after some exploration by a search committee, I was approached by both Ratan Tata and Lord Bhattacharya individually to be a candidate for the position. I politely declined. I had myself built a business which I would continue to run. However, as the search process progressed and the committee was unable to find a suitable candidate, I was asked to reconsider. After consulting my family and in the broader interests of the Tata Group, I took courage to overcome my initial reluctance and agreed to consider the position.

Prior to my appointment, I was assured that I would be given a free hand. The previous Chairman was to step back and be available for advice and guidance as and when needed. After my appointment, the Articles of Association were modified, changing the rules of engagement between the Trusts, the Board of Tata Sons, the Chairman, and the operating companies. Inappropriate interpretation indeed followed, and as elaborated below, it severely constrained the ability of the group to engineer the necessary turnaround.

I am not sure if the individual board members and the trustees truly appreciated the extent of the problems I had inherited. I cannot blame them, for I myself, as a non-executive director, did not have a clear grasp of the gravity of the issues involved. Without meaning to air a laundry list, let me outline some of the major challenges faced at the time of my entry.

As is public knowledge, the foreign acquisition strategy, with the exceptions of JLR and Tetley, had left a large debt overhang. The European steel business faced potential impairments in excess of USD 10 billion, only some of which has been taken as of date. Many foreign properties of IHCL and holdings in Orient Hotels have been sold at a loss. The onerous terms of the lease for Pierre in New York are such that it would make it a challenge to exit. Tata Chemicals still needs tough decisions about its UK and Kenya operations.

IHCL, beyond flawed international strategy, had acquired the Searock property at a highly inflated price and housed in an off balance sheet structure. In the process of unravelling this legacy, IHCL has had to write down nearly its entire networth over the past three years. This impairs its ability to pay dividends.

Tata Capital had a book that required significant clean up on account of bad loans to the infrastructure sector. The loan to Siva was under the strong advice of Executive Trustee Venkataraman, which has since turned into a non-performing asset. All of this resulted in Tata Capital having to recognize an abnormal size of NPAs.

Of all the companies in the portfolio, the telecom business has been continuously haemorrhaging. If we were to exit this business *via* fire sale or shut down, the cost would be USD 4-5 billion. This is in addition to any payout to DoCoMo of at least a billion plus dollars. The original structure of the DoCoMo transaction raises several questions about its appropriateness from a commercial or prudential perspective within the then prevailing Indian legal framework. In light of all of this, our strategy over the past three years has been to increase the EBITDA from Rs. 400 crores to Rs. 2,500 crores, in the hope of being a potential player in consolidation of the industry.

Tata Power aggressively bid for the Mundra project based on low-priced Indonesian coal. As regulations changed, the losses in 2013-14 alone amounted to Rs. 1,500 crores. Given that Mundra constitutes Rs. 18,000 crores of capital employed (40% of the overall company's capital employed), this substantially depresses the return on capital for Tata Power as well as carries the risk of considerable future impairment.

An even more challenging situation arose in Tata Motors, both on the commercial and passenger vehicles. Before 2013, in order to shore up sales and market share, Tata Motors Finance extended credit with lax risk assessment. As a result, the NPAs mounted to being in excess of Rs. 4,000 crores. Historically, the company had employed aggressive accounting to capitalize substantial proportion of the product development expenses, creating a future liability. Beyond this, the Nano product development concept called for a car below Rs. 1 lakh, but the costs were always above this. This product has consistently lost money, peaking at Rs. 1,000 crores. As there is no line of sight to profitability for the Nano, any turnaround strategy for the company requires to shut it down. Emotional reasons alone have kept us away from this crucial decision. Another challenge in shutting down Nano is that it would stop the supply of the Nano gliders to an entity that makes electric cars and in which Mr. Tata has a stake.

On the performance of the portfolio, as you are aware from my presentations to you in the recent past, if we look at the aggregate data between 2011 and 2015 and limit the analysis largely to the legacy hotspots (IHCL, Tata Motors PV, Tata Steel Europe, Tata Power Mundra, and Teleservices), it will show that the capital employed in those companies has risen from Rs. 132,000 crores to Rs. 196,000 crores (due to operational losses, interest and capex). This figure is close to the networth of the group which is at Rs. 174,000 crores. A realistic assessment of the fair value these businesses could potentially result in a write down over time of about Rs. 118,000 crores.

In the face of the above challenges, I had to take many tough decisions with sensitive care to the group's reputation as well as containing panic amidst internal and external stakeholders. Despite bad press, impairments were taken to clean the books but substantial exposure remains. Dividends were reduced (e.g., Tata Motors, IHCL) to conserve cash for needed investments in

the teeth of shareholder fury. Apart from hotels, the group made several exits in the fertilizer business, UK steel operations, and of course in smaller companies such as the logistics company, DIESL. I had to ease out hangers-on who are prone to flaunt their proximity to power. On the more positive side, Kalinganagar, the largest domestic capital investment of the group was completed overcoming significant obstacles that had left the project in doubt previously.

Early in my tenure, our foray into the aviation sector began when Mr Tata ushered me into his office and handed me a report on Air Asia by Bain & Co. He had concluded negotiations to partner with Air Asia and wanted the proposal tabled at the forthcoming Tata Sons board meeting. My pushback was hard but futile. However, I was able to extract a promise of no debt to be raised at the level of the JV as well as limiting Tata Sons investment to 30% of the USD 30 million equity. A few months later, I was surprised to be confronted with a similar situation requiring me to execute a *fait accompli* JV with Singapore Airlines. Without the benefit of time and experience to fully evaluate the proposal, I had to accept that Tata Sons would take a 51% stake in a USD 100 million joint venture. The passion for the airlines sector has led Mr Tata to continue his involvement with the strategy of the two airlines. It is on his advice that the Tata Sons board has increased the capital infusion in the sector at multiple levels of the initial commitment.

Board members and trustees are also aware that in the case of Air Asia, ethical concerns have been raised with respect to certain transactions as well as the overall prevailing culture within the organization. A recent forensic investigation revealed fraudulent transactions of Rs. 22 crores involving non-existent parties in India and Singapore. Executive Trustee, Mr. Venkatraman, who is on the board of Air Asia and also a shareholder in the company, considered these transactions as non-material and did not encourage further study. It was only at the insistence of the independent directors, one of whom immediately submitted his resignation, that the board decided to belatedly file a first information report.

Despite all of the above, during my term, the operating cash flows of the group have grown at 31% compounded per annum. The Tata Group valuation from 2013 to 2016 increased by 14.9% per annum in rupee terms as against the BSE Sensex annual increase of 10.4% over the same period. The Tata Sons networth has increased from approximately Rs. 26,000 crores to Rs. 42,000 crores, after considering the impairments. This has significantly strengthened our balance sheet, enhancing our ability to absorb further shocks from restructuring in the companies

To come back to the amendments in the Articles of Association, as feared, the inappropriate implementation created a flux in the decision-making process. I have often presented to the trustees, before and after Tata Sons board meetings. This created alternative power centres without any accountability or formal responsibility, invalidating the very governance role of the Tata Sons board and the Chairman, resulting in dysfunctional governance. The trust-

nominated directors, who I would assume would use their own independent judgment and discharge their fiduciary duties, were reduced to mere postmen. As an example, once, the trust directors (Nitin Nohria and Vijay Singh) had to leave a Tata Sons board meeting in progress for almost an hour, keeping the rest of the Board waiting, in order to obtain instructions from Mr. Tata. Such a work pattern has also created the added risk of contravening insider trading regulations and exposed the Trust, apart from exposing the trustees to potential tax liabilities. These circumstances forced me to circulate a note on corporate governance in order to clarify the distinct roles of Tata Trusts, Tata Sons Board, and the Boards of the operating companies.

I cannot believe that I was removed on grounds of non-performance. As you are aware, the Nomination and Remuneration Committee comprising Vijay Singh, Farida Khambata and Ronnen Sen, independent directors (two of whom have voted for my removal now), had only recently lauded and commended my performance.

In keeping with Tata Group values, to engage employees and have a favourable impact on the communities we operate in, we launched a volunteering programme, challenging group employees to volunteer a million hours in 2015 and the result was volunteering of 1.2 million hours, making it one of the top ten global volunteering programmes.

I hope you do realize the predicament that I found myself in. Being pushed into the position of a “lame duck” Chairman, my desire was to create an institutional framework for effective future governance of the group. I believe I had to be true to myself and the best interests of the organization. While I would be lying if I said I am not disappointed, I have a sense of pride and dignity intact in the efforts I have taken to professionalise and institutionalise, regardless of the outcome of effort, I now witness.

Since the developments at the Board Meeting were purported to have been initiated at the instance of the Trusts, I am copying the Trustees.

Sincerely,

Cyrus

(Cyrus P Mistry)

**C.C. Trustees of Tata Trusts**