Contemporary Corporate Governance analysis recognizes that the essential core of a corporation consists of three interrelated elements – Strategy, Structure and Practices. The Corporate Governance framework, discussed in chapter 2 and 3 involves all three and emphasizes the importance of their appropriate alignment, both internal and external, to the successful performance of the company. This chapter is a bridge between the theoretical analysis presented in the Part 1 and the empirical analysis that follow in the next 2 chapters. This chapter introduces the history and evolution of ITC Limited, where the research has been carried out and identifies Corporate Governance issues that have been critical for the selected divisions. It also brings out the problems that the company faced in balancing the diverse interests of its stakeholders – Employees, Farmers, Indian Shareholders, Parent Company and the Government. This chapter also illustrates the development of professional approach and forward looking ability of the company at a time when the history of the country itself was changing dramatically.

5. 1 Introduction

ITC is one of India’s foremost private sector companies with a market capitalization of over US$10 billion and a turnover of US$3 billion. Forbes magazine has rated it amongst world’s leading companies. Among India’s private sector corporations, ITC ranks third in pre-tax profits. ITC has a diversified presence in cigarettes, hotels, paperboards and specialty papers, packaging, agri-business, branded apparel, packaged foods and confectionary, greeting cards and other FMCG products. ITC is rapidly gaining market share even in its new businesses of branded ready-made garments, greeting cards, packaged foods and confectionary, while it is an outstanding market leader in its traditional businesses of cigarettes, hotels, paperboards, packaging and agri-exports. ITC is considered to be nationalistic to the core as one of India’s most valuable and respected corporations, which contributes substantially to the country’s revenues, employment, exports and socio-economic development. ITC’s strength emanates
from its corporate strategy that aims at creating multiple drivers of growth anchored on its
time-tested core competencies: large distribution reach, superior brand-building capabilities,
effective supply chain management and acknowledged service skills in hotel business. In the
not too distant future, ITC’s strategic forays into new businesses are likely to get it a
significant share of these emerging high-growth Indian markets. For instance, ITC which has
3.5 lakh tonnes capacity in paper and paperboard in its four production units including its 1
lakh tonnes of Elemental Chlorine-Free (ECF) paper for food packaging, has announced in
August 2005 its plan to invest Rs. 2500 crores during the next 5 years to enhance its
production of ECF by two lakh tonnes, which will increase the company’s total capacity to
5.5 lakh tonnes in the segment. Likewise, the company, encouraged by the tremendous
response to its new food products such as “Ashirwad” brand atta and Sunfeast brand biscuits,
achieved more than 100 per cent growth in turnover in this fast-growing segment. Against a
modest turnover of 400 crores in 2004 the ITC Foods increased the turnover to more than Rs.
1200 crore by the end of the financial year 2011.

ITC continuously endeavors to enhance its wealth generating capabilities in a globalizing
environment to consistently reward its 1.50 lakhs shareholders, fulfill the aspirations of its
stakeholders and meet societal expectations. ITC employs over 20,000 people at more than
60 locations across India.

5.2 History and Evolution
The story of Imperial Tobacco Company of India Limited (currently ITC Limited),
extraordinary though it may sound, starts long before the company was established, or even
thought of. It starts not in India, but in the United States of America and the United Kingdom.
The formation of its parent company BAT was formed in the year 1902, by merging of two
companies, Imperial Tobacco Company (of Great Britain and Ireland), and American
Tobacco Company (ATC) to stop the self-damaging exercise among them. Buck Duke
(James Buchanan Duke; the Founder of ATC) became the first Director of the company with
his company holding a majority of 67% shares of BAT. The real story started much before in
the year 1890, when Duke captured Ogdens of Liverpool and started a tobacco war in Britain.
Imperial Tobacco took the war in turn to the markets in America. This led to price-cutting by
both the giants of tobacco business. Huge Price cutting and discounts led to shrinking of
bottom lines of both the companies and as compromise they finally came to agree that they
shall not encroach each other’s domestic market and that they shall not fight in other foreign markets. Indeed, formation of BAT was an outcome of these developments and this new entity was to market cigarette products outside UK and USA.

BAT entered the Indian market in 1906; and the seed of BAT’s presence in India, once sown grew rapidly. Within five years of entering in India, its operations had expanded to include the manufacture of cigarettes, the procurement and processing of tobacco and the setting up of a full-fledged selling organization. This last was the Imperial Tobacco Company of India Limited, which came into being on 24th August 1910. In this study we study this company, which was destined in the course of its century to be buffeted, bruised and finally burnished by the winds of many challenges and changes.

When BAT decided to exploit the market opportunity in India, it perceived its operations in the country to be rather like a three legged stool, with the three legs representing Manufacture, Raw material procurement, and Sales respectively. Indeed, the first step, BAT took in this three pronged advance towards the Indian market was the establishment of a factory, and in November 1905, it incorporated a new company in England to undertake this venture (Basu, 1984).

This was Peninsular Tobacco Company, which BAT owned to all intents and purpose through its shareholding of 70 percent. However, an in due course BAT’s share in Peninsular was bought over by Imperial Tobacco Company in India and the London incorporated Peninsular Tobacco company itself would be wound up and its assets were acquired by Peninsular Tobacco Company In India.

The Imperial’s main thrust at the start was to promote sales both of imported cigarettes and those manufactured at company’s factor in Monghyr. It was the first factory of the company, which was set up in 1907. In the year 1910, duties on imported tobacco were enhanced appreciably causing an enormous fall in imports in India. This has provided stimulus to indigenous manufacture of cigarettes. Recognizing that the Peninsular Tobacco factory at Monghyr, then producing 750 million cigarettes a year, would not be able to cope with the additional demand, the company set plans to establish another factory.

The Bangalore factory was established in 15th July 1912, sprawling over thirty seven acres which were purchased from civil and military station in what then were fields on the outskirts of the city. Today, Bangalore factory is part of the largest cigarette making complex in the
country. Apart from the factory, the complex also has the only machine development unit to be attached to a cigarette factory in India. By 1990 the factory achieved a benchmark of processing 5500 Kg of tobacco each hour and 50 million cigarettes were manufactured daily comprising of premium brands of ITC’s cigarettes.

By 1924, Peninsular Tobacco Company, with a unit in Monghyr and another in Bangalore, was ready to set up another factory. It seemed logical to locate this factory in northern India where the volume of sales was growing faster than anywhere else at that stage. Saharanpur, which is situated in Kolkata and Mumbai railway line, which is widely connected up till west Punjab, was an obvious choice. This Factory was set up in May 1926.

It was at this stage that BAT decided prudently to set a separate company to handle the procurement and purchase tobacco in India and actively encourage farmers. Increasing demand for cigarettes coupled with heightened duties had already prompted the decision to establish the Bangalore and Saharanpur factories. A subsequent greater quantity of tobacco was needed to carry uninterrupted production at these factories. It was becoming evident that a full-fledged company would be needed to handle leaf requirements and to this end a new company was floated in July 1912 called Indian Leaf Tobacco Development Company. The ownership of this company was batted backwards and forwards before it finally became a division of ITC Limited in 1975. The hallmark of this company was to discover more promising tobacco growing area in the south India. The company had opened buying depots at 3 places of Guntur district namely Parchur, Nambur and Chilakaluripet.

With the ready market for their lead and middle man being eliminated, the farmers began to derive definite benefit immediately but it was in 1922 that the fortunes of the entire farmer community took a giant step forward. This was the year in which the company decided that it would build a tobacco re-drying factory at Chirala. The Chirala factory had become an important milestone in the annals of the company. Though its operations were simple, expansion at this factory was rapid. Apart from grading and re-drying the leaf, hundreds of people were employed in ‘stripping operations’ at a daily rate. Within few years, the workforce who was initially mixed but latter had women, increased from about 500 to 6000. Till 1984, when the factory was closed on the advent of mechanization, about 1500 women and 500 men who were employed in chirala factory came from marginalized community.

In spite of enlightened self-interest, the ILTD improved matters and their method of tackling the problem was to revolutionize the tobacco production in the country. It was the method
that was to bring relative prosperity to the Indian farmer, to help them become independent and secure, and it resulted in the establishment of an enviable and enduring relationship between ILTD and the farmers. The payments to farmers were made in cash which involved the transport and disbursement of large sums of money. The fact that ILTD came to have such good standing with the people in whose territory it worked was in large part due to the inherent ability of the managers to get on with the local population.

ITC Limited acquired its fourth cigarette manufacturing factory at Kiddorepore during 1935 from Carreras India. This was part of the larger reorganization strategy of BAT to streamline its investments in India.

ITC's had setup Packaging & Printing Business in 1925 as a strategic backward integration for ITC's Cigarettes business. The first factory was Started in Monghyr and later on a second establishment was found in Tiruvottur in Tamil Nadu. Today ITC Limited has become India's most sophisticated packaging house.

The political and economic scenario of the country has changed after Indian Independence in 1947. The Government legislations to that requiring Multinational Corporations to dilute their equity has led to first disinvestment in ITC during 1954 wherein firstly Rs 1 crore worth of shares was offered to Indian Public. This in itself did not seriously affect BAT’s position, but it did give the company an indication of the things to come. With the enactment of FERA in 1973, the BAT’s shareholding has further declined to below 40% in the company. By 1980s, the Indian Government through the shares held by various State run Financial Institutions had become the single largest shareholder in ITC Limited.

This gradual process of disinvestment has changed the priorities of the company. The dependence of the company on the manufacture and sale of cigarettes had to be reduced through diversification. The company prioritized to identify projects for new businesses which would fit within the framework of the government’s planning policies and would yield large and stable foreign exchange earnings.

However, the choice of suitable diversification project was in fact a difficult one. Many considerations have to be taken into account, prime amongst them the attitude of government, which at that stage was distinctly un-sympathetic. In the wake of business interests the ITC Limited Board of Directors found themselves involved in a tricky balancing act between the national interests and those of major shareholders. BAT was not interested in investing in
ventures such as paper or cement nor was ITC in a position to do so because any such major project would have involved a large capital investment, coupled with long gestation period. Finally, the need to intensify export promotion and focus on foreign exchange earnings led ITC to opt for three areas of diversification. These were Tourism sector where the intention was to set up a chain of hotels, in the field of general exports which would include various miscellaneous products and marine foods.

ITC Limited took a plunge in 1971 with the export of marine products and achieved good earnings in the first year. However, the company went into trouble due to absence of physical checking of inventories and perishable nature of marine products, which increased operating costs beyond the limits of viability. These factors had unfortunately led to the closure of the foods division in 1979. However, ITC Limited had experimented with varying degrees of success in the export of cut tobacco, paper and paper products, surgical dressings, insulators, hand tools, handicrafts, leather goods and garments.

Likewise, one other product in the ITC’s list of general exports needs mention, due to the sense of social responsibility which provided greater motivation than foreign exchange earnings. ITC promoted carpet manufacturing company called Triveni handlooms limited with its headquarters at Kanpur for export customers. The carpets were woven traditionally and were of coarse quality that did not command much of a market. Yet the weavers were undoubtedly talented. ITC decided that this was a worthy support. Though the promotion was small it constituted as one of ITC’s success stories. Within a short span of 12 months the project had become successful with turnover of 80 lakhs. However, the experiment was short lived due to host of reasons like, quality considerations, credit problems and fluctuation of international currencies.

In 1975, the Company launched its Hotels business with the acquisition of a hotel in Chennai which was rechristened 'ITC-Welcomgroup Hotel Chola' (now renamed as My Fortune, Chennai). The objective of ITC's entry into the hotels business was rooted in the concept of creating value for the nation. ITC chose the Hotels business for its potential to earn high levels of foreign exchange, create tourism infrastructure and generate large scale direct and indirect employment. Since then ITC’s Hotels business has grown to occupy a position of Leadership, with over 100 owned and managed properties spread across India under four brands namely, ITC Hotels - Luxury Collection, Welcom Hotels, Fortune Hotels and Welcom Heritage.
The Government’s desire that companies like ITC should both participate in core industries and develop backward areas led to ITC’s involvement with another major project, that of the manufacture of paper and board. In 1979, ITC entered the Paperboards business by promoting ITC Bhadrachalam Paperboards Limited. However, ITC was hesitant to make such an enterprise a division of the Company for fear of the impact it would have on its balance sheet. So it took the alternative route of promoting a separate company in which it held a substantial shareholding. The factory was erected within a matter of twenty-seven months, a record in itself. With ecology being a prime concern, great attention was paid to the environment. Effluents were meticulously treated before being discharged into the Godavari river and pollutants were trapped before fumes were released into the air. Continuing afforestation programmes were taken in hand including those in partnership with neighborhood farmers who had fallow land. Having aware of their own needs, the project also initiated a cyclical operation of tree support which ensured a continuing supply of the right quality of pulp wood to the factory without affecting the balance of nature. The combination of a modern plant, professional management and a committed workforce achieved Bhadrachalam Paperboards productivity levels that were extraordinary in the paper industry, even judged by international standards.

The Bhadrachalam Paperboards amalgamated with the Company with effect from March 13, 2002 and became a Division of the company named Bhadrachalam Paperboards Division. In November 2002, this division merged with the Company’s Tribeni Tissues Division to form the Paperboards & Specialty Papers Division. ITC's paperboards' technology, productivity, quality and manufacturing processes are comparable to the best in the world. It has also made an immense contribution to the development of Sarapaka, an economically backward village in the state of Andhra Pradesh. It is directly involved in education, environmental protection and community development. In 2004, ITC acquired the paperboard manufacturing facility of BILT Industrial Packaging Co. Ltd (BIPCO), near Coimbatore, Tamil Nadu. The Kovai Unit allowed ITC to improve customer service with reduced lead time and a wider product range.

In 1985, ITC set up Surya Tobacco Co. in Nepal as an Indo-Nepal and British joint venture. In August 2002, Surya Tobacco became a subsidiary of ITC Limited and its name was changed to Surya Nepal Private Limited. In 2004, the company diversified into manufacturing and export of garments.
In 1990, ITC acquired Tribeni Tissues Limited, a Specialty paper manufacturing company and a major supplier of tissue paper to the cigarette industry. The merged entity was named the Tribeni Tissues Division (TTD). To harness strategic and operational synergies, TTD was merged with the Bhadrachalam Paperboards Division to form the Paperboards & Specialty Papers Division in November 2002.

The 90s were challenging years for the company. The company had decided that diversification into new businesses was not only desirable but necessary. The Board of Directors had identified various diversification opportunities whilst enhancing the business and meeting national priorities. The company had decided to continue its strong hold on the core sector, such as cigarettes, paper boards, Hotels, whilst using competencies to grow in the other sectors like power, aviation, FMCG and oil seeds and exporting of commodities.

As part of diversification strategy, the company moved into castor and oil seeds industry, where the company had experience in agricultural commodity from seed to processed product through fruitful collaborations with farmers combined with its expertise in marketing and distribution. The company had started a sunflower oil project to conserve foreign exchange through reduction of imports. ITC set up ITC Agro Tech, to supply high quality hybrid seeds and provided meteorological data, to finally bought back the sunflower oil seed from the farmers' doorstep. ITC Agro Tech had achieved its target of becoming India's largest producer of branded edible oil in the private sector by 1993. In the same year, ITC and Zeneca Seeds of UK set up a joint venture company to develop a superior range of hybrid seeds suitable to growing conditions in India.

By 1995, a series of proposed diversification schemes into power sector, aviation, FMCG sector were discussed. However, the company had formally shelved its plan to diversify into unrelated areas like power and food. This was due to an open conflict with its foreign shareholders, BAT Industries of the UK. The parent company demanded that the ITC Ltd should plan to focus on its core competencies for future growth.

ITC therefore decided to focus more on its cigarettes, leaf tobacco, hotels, packaging and paper divisions in the coming years. The board accepted the company's plans to invest Rs1,900 crore by 2000 for its future plans. The ITC Agro Tech divested 51.4 percent stake in the ConAgra foods of the US.
During 1990, by leveraging the agri-sourcing competency, ITC set up the Agri Business Division for export of agri-commodities which is currently India's largest exporters. ITC's unique and now widely acknowledged E-Choupal initiative began in 2000 with soya farmers in Madhya Pradesh. Now it extends to 10 states covering over 4 million farmers. Also, through the 'Choupal Pradarshan Khet' initiative, the agri services vertical has been focusing on improving productivity of crops while deepening relationship with the farming community.

ITC launched line of premium range of notebooks under brand Paperkraft in 2002. To augment its offering and to reach a wider student population, the ‘Classmate’ range of notebooks was launched in 2003. Classmate over the years has grown to become India's largest notebook brand and has also increased its portfolio to occupy a greater share of a student’s school bag.

ITC also entered the Lifestyle Retailing business with the Wills Sport range of international quality relaxed wear for men and women in the year 2000.

In 2000, ITC spun off its information technology business into a wholly owned subsidiary, ITC InfoTech India Limited, to more aggressively pursue emerging opportunities in this area. Today ITC InfoTech is one of India's fastest growing global IT and IT-enabled services companies and has established itself as a key player in offshore outsourcing, providing outsourced IT solutions and services to leading global customers across key focus verticals - Banking Financial Services & Insurance (BFSI), Consumer Packaged Goods (CPG), Retail, Manufacturing, Engineering Services, Media & Entertainment, Travel, Hospitality, Life Sciences and Transportation & Logistics.

ITC's foray into the Foods business is an outstanding example of successfully blending multiple internal competencies to create a new driver of business growth. It began in August 2001 with the introduction of 'Kitchens of India' ready-to-eat Indian gourmet dishes. In 2002, ITC entered the confectionery and 2003 witnessed the introduction of Sunfeast as the Company entered the biscuits segment. ITC entered the fast growing branded snacks category with Bingo! in 2007. In just over a decade, the Foods business has grown to a significant size under seven distinctive brands, with an enviable distribution reach, a rapidly growing market share and a solid market standing.
In 2002, ITC’s philosophy to enhance the competitiveness of the entire value chain found yet another expression in the Safety Matches initiative. ITC now markets popular safety matches brands like iKno, Mangaldeep and Aim.

ITC’s foray into the marketing of Agarbattis (incense sticks) in 2003 marked the manifestation of its partnership with the cottage sector. Today, Mangaldeep is a highly established national brand and is available across a range of fragrances.

ITC entered the Personal Care Business in 2005. In seven years, the Personal Care portfolio has grown under 'Essenza Di Wills', 'Fiama Di Wills', 'Vivel' and 'Superia' brands which have received encouraging consumer response and are also being progressively extended nationally.

Thus, today ITC Limited is not just a tobacco company, but it is well known for read-to-eat foods, biscuits, atta, hotels, agri exports, speciality paper and others. The diversification in the 'FMCG and others' category has gathered pace and ITC earns 50% of revenues from these non-tobacco businesses. It is competing with the major and veteran players like Pepsico, Haldirams, Hindustan Unilever Limited, MTR, Nestle, in this segment.

The above history of the company describes diversification strategy of the company and how it has reduced the presence of cigarette business in public eye, taking much interest in fresh ventures and achievements as a corporate citizen. A clear rebranding by the company has taken the Wills brand’s association much beyond cigarettes, so that the equality built over the decades due to ITC’s dominance in the cigarette market is reaped by other products like apparel. Alongside, businesses such as hotels, packing and paperboards, which were initially separate companies, have now become divisions of ITC, and grown in size and scale too. The paper, paperboards and packaging business, which was once a struggling subsidiary, is today a thriving division accounting for a sixth of ITC's revenues.

5.3 ITC’s Vision and Mission

The vision of the company is well captured in its corporate positioning statement: “Enduring value for the shareholder, for the Nation”. Vision of the company is to “Sustain ITC's position as one of India's most valuable corporations through world class performance, creating growing value for the Indian economy and the Company's stakeholders”. The company would like to achieve its Vision by its Mission to "To enhance the wealth
generating capability of the enterprise in a globalizing environment, delivering superior and sustainable stakeholder value”.

- **Core Values**

ITC has adopted certain Core values that would enable the company to be a customer-focused, high-performance organisation which creates value for all its stakeholders. They are as follows

- **Trusteeship**

As professionally managed company the ITC is conscious to redeem the "trust" of all its stakeholders by adding value all the time.

- **Customer Focus**

To deliver to the customer his/her needs in terms of value, quality and satisfaction.

- **Respect for People**

To give respect and value people in all respects and uphold humanness and human dignity.

- **Excellence**

To do what is right, do it well and win.

- **Innovation**

For better processes, products, services and management practices.

- **Nation Orientation**

Being aware of its responsibility to generate economic value for the Nation. In pursuit of business goals the company adheres to compliance with applicable laws and regulations at all levels.

**5.4 ITC’s Corporate Strategies**

ITC is a board-managed professional company, committed to creating enduring value for the shareholder and for the nation. It has a rich organisational culture rooted in its core values of respect for people and belief in empowerment. Its philosophy of all-round value creation is backed by strong corporate governance policies and systems.
ITC’s corporate strategies are as follows:

- Create multiple drivers of growth by developing a portfolio of world class businesses that best matches organisational capability with opportunities in domestic and export markets.
- Continue to focus on the chosen portfolio of FMCG, Hotels, Paper, Paperboards & Packaging, Agri Business and Information Technology.
- Benchmark the health of each business comprehensively across the criteria of Market Standing, Profitability and Internal Vitality.
- Ensure that each of its businesses is world class and internationally competitive.
- Enhance the competitive power of the portfolio through synergies derived by blending the diverse skills and capabilities residing in ITC’s various businesses.
- Create distributed leadership within the organisation by nurturing talented and focused top management teams for each of the businesses.
- Continuously strengthen and refine Corporate Governance processes and systems to catalyse the entrepreneurial energies of management by striking the golden balance between executive freedom and the need for effective control and accountability.

5.5 Shareholding Pattern

The first disinvestment of 6 percent of BAT’s equity holding in ITC took place in 1954 when Rs. 1 crore worth of shares were offered to the Indian public. This in itself did not seriously affect BAT’s position but it did give the company a taste of things to come, and there was a growing conviction that this disinvestment was only a beginning. But in any case, BAT probably recognised as the largest single shareholder still had control over the company. Though the Indian shareholding had increased substantially, it was dispersed over a large number of individual shareholders, each having a small shareholding. No one had a large enough block of shares to cause any anxiety. This continued to be true until financial institutions entered the picture.

In 1958, the newly created state run insurance companies, namely General Insurance Company and Life Insurance Corporation of India thought ITC a good investment, thereby acquired a shareholding of 1,51,100 shares by buying from the open market. By 1968, this figure had risen to 1,90,000 shares. The GIC, including its constituent units, and the Unit Trust of India had also begun to buy some shares.
The ITC Ltd further proceeded to dilute its equity, by offering Rs. 3.79 crore worth of shares at a premium of Rs. 3 per share, thereby increasing Indian shareholding from 6.6 percent to 25 percent. As a consequence the Life Insurance Corporation (LIC), Unit Trust of India (UTI), General Insurance Company (GIC) and ICICI Ltd received a firm allotment of shares worth of 1.66 crore. By 1973, LIC, GIC and UTI had once again increased their shareholding through market operations. The presence of financial institutions had taken significant dimension in 1974, when BAT planned to dis invest in order to increase the Indian shareholding to 40 percent. The government institutions have acquired Rs. 2.80 crore worth of shares that were divested by the foreign shareholders. This has led to board level changes in the company, wherein LIC, Industrial Finance Corporation of India and Industrial Development Bank of India had nominated Non-executive directors to safeguard their interests. These developments, indeed, made the parent company to appoint a non-executive director to the ITC Ltd board, to keep itself abreast of developments and protect its investments in a more systematic manner.

Today, the largest single shareholder is, as it happened, not BAT but the Government of India through the shares held by the Indian financial institutions. Their acquisition of shares in ITC has been a gradual process that started in a limited way with the first disinvestment in 1954, as referred earlier. The company thus, not only diluted its foreign shareholding ahead of legislative/political pressure, but had also entered new areas of business which were in line with the governmental thinking. However, in 2002, the parent company-BAT had attempted to increase its shareholding in ITC Ltd by acquiring the shares which UTI had in the company. Their efforts were not been successful as other financial institutions objected to this move.

The table no. 5.1 illustrates the Shareholding Pattern of ITC ltd. for the period of 10 years from 2002 to 2011. As can be seen from the table, the highest shareholders were Banks, Financial Institutions, Insurance Companies and Mutual Funds followed by Overseas Corporate bodies. The table enables to understand the stylized models of Corporate Governance proposed by Tan (1999), of shareholding pattern which is based on Insider model.
Table No. 5.1: Shareholding Pattern in ITC Ltd

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Years</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2002</td>
</tr>
<tr>
<td>UTI</td>
<td>11.79</td>
</tr>
<tr>
<td>Middleton Investment Co. Ltd.</td>
<td>4.4</td>
</tr>
<tr>
<td>Citibank, New York</td>
<td>4.35</td>
</tr>
<tr>
<td>New India Assurance Co. Ltd.</td>
<td>2.99</td>
</tr>
<tr>
<td>Oriental Insurance Company Ltd.</td>
<td>2.46</td>
</tr>
<tr>
<td>General Insurance Corp. India Ltd.</td>
<td>2.22</td>
</tr>
<tr>
<td>National Insurance Comp. Ltd</td>
<td>2.03</td>
</tr>
<tr>
<td>Rothmans Intl. Ltd</td>
<td>1.4</td>
</tr>
<tr>
<td>ICICI Prudential Life Insurance Ltd.</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: adopted from annual financial reports of the company from 2002-2011

5.5.1 Insider-based Model of corporate governance

Insider-based system of Corporate Governance does not have an active market for corporate control where in the entire Governance is vested with Promoters, Large Shareholders, Financial Institutions and Commercial Banks. This model can be best illustrated in figure 5.1.

The outsider-based model can be considered to address issues stemming from disenfranchisement of corporate ownership and executive domination of the board. These models have developed in different social and commercial environments. Large block of shareholders usually assume a more active management role in these models of Corporate Governance. This model often directly facilitates production efficiency and harmonizes the interests of a wider range of stakeholders including employees of the company. Human capital and the employees investment in developing firm specific resource, are considered to
be given due importance in this model. This stylized model is prevalent in Japan and Germany.

The above discussion of the various models in their stylized forms is not meant to be exhaustive. For instance Corporate Governance models of the vibrant business corporations set up in South East Asian countries, China and India may constitute another distinct model. However, they are not well understood and there are few systematic studies of these Corporate Governance forms. Rather, the purpose of examining the above stylized models is to show the diversity of practices, objectives and underlying philosophies.

5.6 Segmental Growth: A Description

ITC, have posted stellar performance during 2003 - 2011, with an impressive top line growth and high quality earnings reflecting the robustness of its corporate strategy of creating multiple drivers of growth. This performance is particularly noteworthy when viewed against the backdrop of the extremely challenging business context, namely, the steep increase in excise duties and arbitrary increases in VAT on cigarettes, brand building and incubation costs of the new FMCG businesses, the impact of the significant investments made in augmenting distribution infrastructure and the gestation costs of the large investments in the Hotels business.

In 2011, the net turnover of Rs. 21167.58 crores grew by 16.6% primarily driven by 23.1% growth in the non- cigarette FMCG businesses, 22.9% growth in Agri business and 17.6% growth in the Hotels segment. Given these positive fundamentals, the Company has been rapidly scaling-up its new FMCG businesses comprising Branded Packaged Foods, Personal Care Products, Education and Stationery Products, Lifestyle Retailing, Safety Matches and Incense Sticks (Agarbattis) with Segment Revenues growing at an impressive compound
annual growth rate of 35% during the last 5 years. The table 5.2 illustrates the 10 years of financial information at ITC Limited.

Table 5.2: 10 years at Glance

<table>
<thead>
<tr>
<th>Year Ending 31st March</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Income</td>
<td>11176.47</td>
<td>12027.92</td>
<td>13542.39</td>
<td>16447.51</td>
<td>19557.14</td>
<td>21878.74</td>
<td>23593.64</td>
<td>26814.32</td>
<td>31399.1</td>
</tr>
<tr>
<td>Excise Duties</td>
<td>5141.1</td>
<td>5332.6</td>
<td>5667.1</td>
<td>6370.9</td>
<td>7056.3</td>
<td>7320.3</td>
<td>7446.7</td>
<td>8046.3</td>
<td>9360.3</td>
</tr>
<tr>
<td>Net Income</td>
<td>6035.3</td>
<td>6995.2</td>
<td>7875.2</td>
<td>10076.6</td>
<td>12500.78</td>
<td>14558.43</td>
<td>16146.85</td>
<td>18767.93</td>
<td>22038.8</td>
</tr>
<tr>
<td>Operational &amp; Admin Exp</td>
<td>3712</td>
<td>4109.8</td>
<td>4846.8</td>
<td>6463.1</td>
<td>8207.8</td>
<td>9543.5</td>
<td>10753.38</td>
<td>12079.16</td>
<td>14046.27</td>
</tr>
<tr>
<td>PBDIT</td>
<td>2323.7</td>
<td>2585.4</td>
<td>3028.3</td>
<td>3613.4</td>
<td>4292.9</td>
<td>5014.8</td>
<td>5393.4</td>
<td>6688.7</td>
<td>7992.5</td>
</tr>
<tr>
<td>Depreciation</td>
<td>237.34</td>
<td>241.62</td>
<td>312.87</td>
<td>332.34</td>
<td>362.92</td>
<td>438.46</td>
<td>549.41</td>
<td>608.71</td>
<td>655.99</td>
</tr>
<tr>
<td>PBIT</td>
<td>2086.0</td>
<td>2343.8</td>
<td>2715.5</td>
<td>3281.1</td>
<td>3929.9</td>
<td>4576.3</td>
<td>4844.0</td>
<td>6080.0</td>
<td>7336.5</td>
</tr>
<tr>
<td>Interest</td>
<td>29.84</td>
<td>24.79</td>
<td>42.43</td>
<td>11.93</td>
<td>3.28</td>
<td>4.61</td>
<td>18.32</td>
<td>64.75</td>
<td>68.38</td>
</tr>
<tr>
<td>PBT</td>
<td>2056.1</td>
<td>2319.0</td>
<td>2673.0</td>
<td>3269.1</td>
<td>3926.7</td>
<td>4571.7</td>
<td>4825.7</td>
<td>6015.3</td>
<td>7268.1</td>
</tr>
<tr>
<td>TAX</td>
<td>684.84</td>
<td>726.21</td>
<td>836</td>
<td>988.82</td>
<td>1226.7</td>
<td>1451.6</td>
<td>1562.1</td>
<td>1954.3</td>
<td>2280.5</td>
</tr>
<tr>
<td>PAT</td>
<td>1371.3</td>
<td>1592.8</td>
<td>1837.0</td>
<td>2280.3</td>
<td>2699.9</td>
<td>3120.1</td>
<td>3263.5</td>
<td>4061</td>
<td>4987.6</td>
</tr>
</tbody>
</table>

Dividends

| Ordinary Dividend     | 418.84   | 558.83   | 882.97   | 1134.7   | 1364.5   | 1543.1   | 1633.8   | 4452.3   | 4002.0   |
| Special Dividend      | 2448.7   | 8        | 1483.9   | 2        |          |          |          |          |          |

The table 5.3 describes the revenues generated in the key segments of ITC’s operations. From the above table it can be seen that agri products and paper boards and paper are major revenue generators for ITC apart from cigarettes during the study period.
<table>
<thead>
<tr>
<th>Items</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cigarettes</td>
<td>60,865</td>
<td>63,415</td>
<td>65,387</td>
<td>69,998</td>
<td>75,894</td>
<td>81,265</td>
<td>80,723</td>
<td>78,370</td>
<td>84,040</td>
<td>81,723</td>
</tr>
<tr>
<td></td>
<td>(8013.58)</td>
<td>(8756.82)</td>
<td>(9223.60)</td>
<td>(9996.39)</td>
<td>(11,322.80)</td>
<td>(12,824.42)</td>
<td>(13815)</td>
<td>(15100)</td>
<td>(17277)</td>
<td>(19821)</td>
</tr>
<tr>
<td>Smoking tobacco</td>
<td>71 (6.9)</td>
<td>75 (6.78)</td>
<td>77 (6.44)</td>
<td>73 (5.94)</td>
<td>93 (6.64)</td>
<td>164 (9.09)</td>
<td>195 (9.7 )</td>
<td>297 (13.7)</td>
<td>54 (4.31)</td>
<td>27 (4.5)</td>
</tr>
<tr>
<td>Unmanufactured tobacco</td>
<td>20,531</td>
<td>25,721</td>
<td>35,012</td>
<td>35,932</td>
<td>45,714</td>
<td>49,691</td>
<td>62,028</td>
<td>63,642</td>
<td>85,242</td>
<td>75,812</td>
</tr>
<tr>
<td></td>
<td>(194.04)</td>
<td>(232.90)</td>
<td>(259.30)</td>
<td>(273.76)</td>
<td>(356.31)</td>
<td>(422.34)</td>
<td>(511.40)</td>
<td>(782)</td>
<td>(1442.5)</td>
<td>(1291.4)</td>
</tr>
<tr>
<td>Printed materials</td>
<td>4,063</td>
<td>3,672</td>
<td>5,892</td>
<td>7,939</td>
<td>7,725</td>
<td>11,361</td>
<td>19,300</td>
<td>22,525</td>
<td>23,831</td>
<td>26,076</td>
</tr>
<tr>
<td></td>
<td>(45.3)</td>
<td>(44.1)</td>
<td>(59.05)</td>
<td>(75.93)</td>
<td>(74.06)</td>
<td>(111.5)</td>
<td>(163.19)</td>
<td>(207)</td>
<td>(236.17)</td>
<td>(297.91)</td>
</tr>
<tr>
<td>Agri Products</td>
<td>6,51,613</td>
<td>11,45,960</td>
<td>6,11,641</td>
<td>5,40,486</td>
<td>10,82,811</td>
<td>24,08,203</td>
<td>8,49,639</td>
<td>46,3150</td>
<td>275951</td>
<td>4,36,126</td>
</tr>
<tr>
<td></td>
<td>(773.54)</td>
<td>(1039.8)</td>
<td>(1024.28)</td>
<td>(936.36)</td>
<td>(1569.59)</td>
<td>(2238.01)</td>
<td>(2423)</td>
<td>(2169.6)</td>
<td>(2300.7)</td>
<td>(2771.7)</td>
</tr>
<tr>
<td>Paper Boards and Paper</td>
<td>1,82,649</td>
<td>1,75,220</td>
<td>1,69,582</td>
<td>2,36,920</td>
<td>2,90,109</td>
<td>3,01,196</td>
<td>3,29,423</td>
<td>3,66,474</td>
<td>4,31,885</td>
<td>4,26,478</td>
</tr>
<tr>
<td></td>
<td>(509.1)</td>
<td>(530.43)</td>
<td>(554.64)</td>
<td>(765.88)</td>
<td>(938.37)</td>
<td>(1016.4)</td>
<td>(1255.3)</td>
<td>(1512.3)</td>
<td>(1808.5)</td>
<td>(2017.67)</td>
</tr>
<tr>
<td>Hotels</td>
<td>160.28</td>
<td>192</td>
<td>254.49</td>
<td>573.02</td>
<td>777.8</td>
<td>978.7</td>
<td>1,093</td>
<td>1014.5</td>
<td>904.9</td>
<td>1067.9</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>24</td>
<td>110.5</td>
<td>83,461</td>
<td>2,07,547</td>
<td>3,44,745</td>
<td>4,98,376</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>(450.93)</td>
<td>(590.26)</td>
<td>(1,044.86)</td>
<td>(1,769.22)</td>
<td>(1,878.5)</td>
<td>(1,187.1)</td>
<td>(1,156.57)</td>
<td>(1,477.23)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 5.3 Segmental Reporting in Crores
5.7 ITC Ltd: A Prologue to Multi-Divisional Structure

Since organization structure is an important part of basic framework of management of enterprise, experiments in organization design have been a feature of the evolution of management thinking and practice. As enterprises encounter changing environments and adopt different strategies for achieving growth and improving performance, they tend to review and modify the structure and processes of the organization. Traditionally, ITC Ltd has been a single product organization and created separate companies for implementing diversified projects. However, as the company became large and operated in multi-product, multi-market situations, the limitations of functional structure and Holding-form of enterprise became more glaring and then product based divisional structure was adopted.

Before dealing with the specific issues, it may be appropriate to briefly explain the concept of Divisional Structure. In a seminal work published in 1965, Alfred Chandler pointed out that ‘structure follows strategy’ and ‘growth without structural adjustments can lead to economic inefficiency’. He also observed that usually there was time lag between a new strategy and the adoption of a new structure. Chandler (1965) opined that different strategies call for different structural changes. For instance, the strategy of vertical integration or expansion can be managed by strengthening the functional structure but the strategy of diversification into new products or new geographical areas requires multi-divisional structure. Chandler’s work inspired many researchers to explore the relationship between strategy, structure and performance. Many studies were conducted in United States, Britain, France, Germany and Japan, where in the divisional structure found widespread organisational scenario. Maheshwari (1985); also noted that the divisional structure has received importance as an organisational alternative in 1980s as several Indian companies had set up product based and location based divisions. However, he noted that many of these attempts were half hearted and failed to produce satisfactory results.

The case of ITC Ltd; is nevertheless, different from many others. The company followed the Multi-Divisional Structure to create product based autonomous divisions, with a focus on strategic diversification into new products and new geographical areas. Logically, the company had retained certain staff functions as corporate functions to provide advice/service to all the divisions. The corporate headquarter exercises control over the divisional operations on behalf of the top management.
As a Multi-divisional company, the ITC Ltd, further, balances the terms of sales volume and profit across the divisions. Generally, if one division accounts for a large proportion of the company’s turnover and exercise influence over corporate decisions it is detrimental to other divisions. The company stroked a perfect balance, though 55% or more of a company’s business currently located in a single division, the India Tobacco Division.

Evidently, divisionalization implicates decentralization of power; accountability for performance and a large degree of autonomy for the division. The ITC Ltd’s divisional structure is thus, characterized by a small and compact corporate office where the members of the top management are less concerned with day to day operations and are more involved in planning and ensuring future performance and facilitating the achievement of agreed performance by the divisions. The divisional decisions which may have influence beyond the divisional boundaries however, involve consultation and approval at the corporate management.

Further, ITC’s success of the divisional structure relates to the selection of the divisional management teams. These teams are accountable for the business performance of the division and possess perspective skills appropriate for growth. It is recognized that to be effective, an organization structure must be liked by appropriate support systems for planning, budgeting, performance, interview, control, information etc. Thus, a divisional budget is an essential prerequisite of a divisional structure. In the absence of such a budget it is difficult to ensure accountability for performance of the division.

The multi-divisional structure at ITC overcomes the problems of accountability, coordination and also strengthens relationships between various divisions and between the divisions and the corporate head office. These divisions are guided by clear norms and procedures in respect of (1) product/market boundaries; (2) management and utilization of common resources and facilities; and (3) determination of transfer price where services and products of one division are used as inputs by another division.

Thus, with autonomous divisions operating effectively in their respective spheres, the need for cooperation between divisions is also high at ITC Ltd. The table 5.4 and the figure 5.2 illustrates that while each division was not only effective, anything which required contribution from more than one division has also been considered. Typically, the loyalty to one’s division tends to transcend the corporate loyalty in case of ITC Ltd.
Figure 5.1 The organization Structure of ITC Limited
Table 5.4: Primary segment information (business segments)  
(Rs. in Crores)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>FMCG-Cigarette</td>
<td>802</td>
<td>676</td>
<td>923</td>
<td>1000</td>
<td>1132</td>
<td>1289</td>
<td>1362</td>
<td>1531</td>
<td>172</td>
<td>196</td>
<td>222</td>
</tr>
<tr>
<td>FMCG-Others</td>
<td>21.1</td>
<td>0.43</td>
<td>108.4</td>
<td>0.73</td>
<td>303.5</td>
<td>562.1</td>
<td>1011.</td>
<td>1701.</td>
<td>2506.</td>
<td>3020.</td>
<td>4.04</td>
</tr>
<tr>
<td>Hotels</td>
<td>160</td>
<td>0.28</td>
<td>192.0</td>
<td>1.32</td>
<td>254.4</td>
<td>578.0</td>
<td>777.8</td>
<td>978.7</td>
<td>1099.</td>
<td>1014.</td>
<td>5.16</td>
</tr>
<tr>
<td>Agri business</td>
<td>967.75</td>
<td>180.0</td>
<td>1272.95</td>
<td>385.39</td>
<td>1283.72</td>
<td>423.03</td>
<td>1220.7</td>
<td>559.37</td>
<td>1954.87</td>
<td>728.77</td>
<td>2719.97</td>
</tr>
<tr>
<td>Paperboards, paper and packing</td>
<td>609.52</td>
<td>361.57</td>
<td>687.37</td>
<td>475.47</td>
<td>740.95</td>
<td>512.35</td>
<td>991.17</td>
<td>574.14</td>
<td>1150.23</td>
<td>745.58</td>
<td>1271.62</td>
</tr>
<tr>
<td>Segment Total</td>
<td>984.6</td>
<td>544.0</td>
<td>847.6</td>
<td>1191.</td>
<td>1336.</td>
<td>1136.</td>
<td>1940.</td>
<td>1810.</td>
<td>2135.</td>
<td>2713.</td>
<td>2734.3</td>
</tr>
</tbody>
</table>

Source: CMIE Database
5.8 The study Area: Divisions taken for Study

It can be understood from the foregoing analysis that the present case – ITC Ltd is undoubtedly complex and a largely diversified business conglomerate. However, studying such a diversified conglomerate requires abundant resources and time. So the present study aims to study corporate governance practices of the ITC, with a focus on core business of the company. The study had selected cigarette manufacturing from FMCG segment, Paper boards and specialty from paper board and packing business, commodity marketing and leaf tobacco exporting from agribusiness. This strategic identification is not only for functional purposes of the study but in reality these divisions are historically old in terms of existence and known for their relationships with stakeholder groups from long time.

Thus, India Tobacco Division (ITD), Paperboards and Specialty Paper Division (PSPD), Agri Business Division (ABD) and Indian Leaf Tobacco Development Division (ILTD) have been selected among several other divisions of ITC ltd. These divisions are widely known for efficiency in operations and contributions to the total profits of the company. According to the recent estimates these four divisions contributes more than 70% of the profits to the case company.

The above divisions have headquarters in Bangalore, Hyderabad, and Guntur respectively, while their operations are not confined to headquarters alone, but found in distant and numerous locations. ITD has its manufacturing units in Mounghyr, Saharanpur, Bangalore, Kolkata (Kiddorepor), Hosur etc. In the same way PSPD operations are located in Badrachalam, Bollaram, Kovai and Tribeni. Similarly ILTD have processing plants at Chirala and Anaparthi, whereas ABD have enormous presence in Madhya Pradesh, Uttar Pradesh, Andhra Pradesh, Karnataka, Rajasthan etc. say in 11 states as of now. The field sites for the present study are limited to Bangalore cigarette factory for ITD, Badrachalam unit of PSPD, Chirala Unit of ILTD and Bhopal (MP) operations of ABD have been selected for carrying out filed work and collecting primary date regarding stakeholder relations.

These locations have been playing significant role in terms of turnover and profitability of the ITC Limited. Nevertheless, these locations are specific with regards to their history and operations. For instance ITD’s bangalore cigarette unit was started in 1912 and is unique in terms of its employees management practices. IR systems are essentially based on productivity bargaining and mutual agreements between management and workers. Alongside, this unit has witnessed widespread Trade Union Movement and faced turbulent
time during 1980’s. The unit also underwent several changes especially during the time of changing physical location of the unit from Cox Town to Devanahalli. Likewise ITC-PSPD’s division was the first unit commissioned by ITC in 1979. This unit marks the beginning of a new chapter in ITC’s move from core tobacco to non-core business. The unit has undergone numerous challenges from its inception of being located in interior tribal area of Andhra Pradesh. The unit has remarkable production capacity of 5 paper machines and its state of art environmentally friendly technologies.

In the similar way, ITC-ILTD’s Chirala unit marks the beginning of ITC’s venturing into Southern India. This unit was established in 1922 and today it is the largest leaf tobacco sourcing, processing and exporting line operating by the ITC-ILTD. The establishment of this unit in a way reflects ITC’s social concerns and the unit is unique in terms of its linkages with diverse stakeholder groups say customers, suppliers and community. While ITC-IBD operations at Bhopal (MP) depicts its foray into a large scale commodity marketing and IDB’s Bhopal operations was increasingly significant in the way the firm established linkages with farmers on the basis of information and communication technologies. ITC’s E-Choupal Movement was first initiated in MP with the launch of an internet portal Soya choupal which enabled farmers to know the necessary information regarding crops, pesticide use, weather forecast, prevailing prices in local, national and international mandis on the basis of the data disseminated through ITC’s Internet Portal – Soya Choupal. Today, E-Choupal gained wide spread attention by the National Government, National and International business schools and more importantly paved the way for rural marketing and the way towards bottom of the pyramid.

Thus, the field sites selected for the present research study are instrumental and intrinsic (Stake, 2003) for the case company’s growth, profitability, performance and linkage with stakeholder groups. They are instrumental because they provide insights in to the ground realities of functional integration with the diverse stakeholders and also play a supportive role for understanding the larger issues of corporate governance. These empirical findings facilitates for in depth understanding of the corporate governance practices of ITC Ltd in its contexts and situations at the bottom level where the case is as a complex entity operating with number of stakeholder groups like employees, customers, suppliers, local community, physical environment and regulatory bodies. The case may be here seen as typical because choice of such a case will enable advance understanding of top down / top management
process called corporate governance and its efficiency in integrating the issues with sheer operations at the bottom level.

The present study thus, intrinsically examines the nature of stakeholder relations / practices at the divisional level to facilitate a better understanding of the corporate governance policy of particular case. The purpose of the present study is not to understand abstract construction or generic phenomena but to describe and explain the intrinsic value of these relationships vis a vis corporate governance practice to the particular case company.

5.9 Conclusion

Thus, ITC Ltd has grown to its present status of one of India’s premier companies with a multi-product portfolio from a single product in the initial years. ITC’s businesses are as vast as they are different, from tobacco to hotels, from paper to foods, from high end retailing to international commodity trading. These businesses differ in their vary nature, the manner of their evolution and methods of their operations.

Nevertheless, ITC, like any other Indian corporate has been highly influenced by economic liberalization, globalization and the wide challenges and opportunities they have opened. To adopt themselves to a market situation replete with risks and to attract larger investments, the ITC have adopted transparent, open and internationally best practices in governance.

Many would agree that ITC has achieved significant milestones – some of them very prestigious indeed, through its strict adherence to excellence in every one of its operations. Today, about half of its net revenues of Rs. 18,000 crore comes from cigarettes, and the other half from hotels, paper boards, infotech, agri-business and now increasingly, foods and personal care. The company has pioneered social initiatives; though most of them are related to its industrial pursuits, but it has gone much beyond to espouse the causes of the underprivileged and the rural poor.

As every company has its history, the ITC too had a tragic past. Excise Evasion Case, Financial Irregularities, Tussle with Parent company on excessive diversification and the turbulence within the company for control were certain acts of commission and omission within the organisation which never came to the knowledge of ITC’s stakeholders and general public until the BAT-ITC spat and the company’s FERA violations came to limelight in 1996. All these have been an important learning experience for ITC Limited. It exposed the potential consequences of resolving internally, externally relevant issues on governance
aspects, and it revealed the need for a proactive approach. Most importantly, these controversies made ITC acutely aware that it is operating in the global environment, where the issues of good governance, board practices and internal controls are given utmost priority. The next chapter elaborates these issues at length.