CHAPTER 1

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INTRODUCTION

1.1 MEANING AND IMPORTANCE OF DEBT STRUCTURING

CORPORATE DEBT RESTRUCTURING

Subsequent to the Asian currency crisis which severely crippled the financial system in most Asian countries, the magnitude of Non Performing Assets (NPAs) in Asian financial institutions was brought to light. Driven by the need to proactively tackle the soaring NPA levels the respective Governments embarked upon a program of substantial reform.

Some of the more recent and aggressive steps to resolve NPAs have been taken by Taiwan. Taiwanese financial institutions have been encouraged to merge (though with limited success) and form bank based AMCs through the recent introduction of Financial Holding Company Act and Financial Institution Mergers Act. Alongside the Ministry of Finance has followed a carrot and stick policy of specifying the required NPA ratios for banks (5% by end 2003), while also providing flexibility in modes of NPA asset resolution and a conducive regulatory and tax environment. Deferred loss write-off provisions have been instituted to provide breathing space for lenders to absorb NPA write-offs. While it is too early to comment on the success of the NPA resolution process in Taiwan, the early signs are encouraging.

Most Asian countries adopted "Out of Court"

1 DBOD No. BP - 68 / 21.04.132 / 2002-03 Dated 05-02-03
restructuring mechanisms to minimize court intervention and speed up restructuring of potentially viable entities. However, this process has yielded mixed results. In Korea for example, while most Chaebols and Corporate entities entered into workout arrangements this often did not lead to far reaching restructuring of these entities. While debt restructuring was generally implemented quickly, delays were witnessed in asset reduction programs and improvement in operating performance was slower and lower than expected. In Thailand similarly, majority of restructuring arrangements have typically involved extension of grace periods or concessional arrangements and it is widely held that genuine restructuring has not taken place.

Internationally, restructuring of NPAs often involves significant operational restructuring in addition to financial restructuring.

The operational restructuring measures typically include the following areas:

- Revenue enhancement
- Cost reduction
- Process improvement
- Working Capital Management
- Sales of redundant / surplus assets

Based on the experience in other countries like the U.K., Thailand, Korea, etc. of putting in place institutional mechanism for restructuring of corporate debt and need for a similar mechanism in India, a Corporate Debt Restructuring System was evolved, and detailed guidelines
were issued by Reserve Bank of India (RBI) August 23, 2001 for implementation by banks. Based on the recommendations made by the Working Group to make the operations of the Corporate Debt Restructuring (CDR) mechanism more efficient, the announcement made by the Finance Minister in the Union Budget 2002-03, and consultations with the Government, the guidelines of Corporate Debt Restructuring system have since been revised and detailed hereunder for implementation by banks / Financial Institutions.

The RBI has instituted the Corporate Debt Restructuring (CDR) mechanism for resolution of NPAs of viable entities facing financial difficulties. The CDR mechanism instituted in India is broadly along the lines of similar systems in the U.K., Thailand, Korea and Malaysia. The objective of the CDR mechanism has been to ensure timely and transparent restructuring of corporate debt outside the purview of the Board for Industrial and Financial Reconstruction (BIFR), DRTs or other legal proceedings. The framework is intended to preserve viable corporates affected by certain internal / external factors and minimize losses to creditors / other stakeholders through an orderly and coordinated restructuring programme.

As on 31st March'03, 60 cases worth Rs. 44,369 crores has been referred to the CDR, of which 29 cases worth Rs. 29,167 crores have been approved for restructuring.

2 E.T. 12-05-2003
WHAT IS CORPORATE DEBT RESTRUCTURING?

Corporate Debt Restructuring (CDR) aims to ensure a timely and transparent mechanism:-

a. For restructuring of the corporate debts of the **viable** corporate entities (not being a "willful defaulter") affected by internal or external factors; and

- It is a press report that Reserve Bank of India is actively considered to allow restructuring of debts even of willful defaulters provided *inter-alia*
- The money was diverted only to the Companies in the business group;
- Borrower gives a firm commitment to bring back the diverted funds;
- The unit should be viable; and
- The promoters make necessary efforts to revive the unit.

b. **Outside** the preview of BIFR, DRT, and other legal proceedings, for the benefit of all concerned; however, in case an account is suit filed by an institutional lender / bank is a signatory of the ICA, then, such suit filed cases can also be covered by CDR process provided 75% or more of secured institutional lenders / Banks have voted in favour of invoking the CDR process.

Thus approach in Corporate Debt Restructuring inculcates
Pro active attitude of institutional lenders / Banks to the Company passing through transient of financial natures;

A more considered decision through interaction of all the majority of institutional lenders / Banks to take a view on the Company's future.

Sharing the “pain” with all the creditors / lenders without diluting seniority of claims of individual institutional lender

**CDR MECHANISM IN INDIA**

There are occasions when corporates find themselves in financial difficulties because of factors beyond their control and also due to certain internal reasons. For the revival of such corporates as well as for the safety of the money lent by the banks and financial institutions, timely support through restructuring of genuine cases is called for. However, delay in agreement amongst different lending institutions often comes in the way of such endeavors. The Corporate Debt Restructuring (CDR) Mechanism is a voluntary non-statutory system based on Debtor-Creditor Agreement (DCA) and Inter-Creditor Agreement (ICA) and the principle of approvals by super-majority of 75% creditors (by value) which makes it binding on the remaining 25% to fall in line with the majority decision. The CDR Mechanism covers only multiple banking accounts, syndication / consortium accounts, where all banks and institutions together have an outstanding aggregate exposure of Rs.200 million and above. It covers all categories of assets in the books of member-creditors classified in terms of RBI's prudential asset classification.
standards. Even cases filed in Debt Recovery Tribunals / Board for Industrial and Financial Reconstruction / and other suit-filed cases are eligible for restructuring under CDR. The cases of restructuring of standard and sub-standard class of assets are covered in Category-I, while cases of doubtful assets are covered under Category-II.

Reference to CDR Mechanism may be triggered by: · Any or more of the creditors having minimum 20% share in either working capital or term finance, or · By the concerned corporate, if supported by a bank/FI having minimum 20% share as above.

It may be emphasized here that, in no case, the requests of any corporate indulging in willful default, fraud or misfeasance, even in a single bank, can be considered for restructuring under CDR System.

The objective of the Corporate Debt Restructuring (CDR) framework is to ensure timely and transparent mechanism for restructuring the corporate debt of viable entities facing problems, outside the purview of BIFR, DRT and other legal proceedings, for the benefit of all concerned.

The sick enterprises will became techno and economically viable and start production, and will start profit. Ultimately the banks and financial institutions’ NPAs will sadistically be reduced and Banks will become healthier. More job opportunity will be created GDP will be increased and the thus there will be Country’s Economics Growth and National Goal will be achieved.
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The Banks & Financial institutions should ensure that CDR is not used as deferment of NPAs in the books, there should be physical reduction of NPAs.

To make the CDR more effective

i) The promoters must bring the Share of Funds before the banks and institutions bring their share.

ii) The product should be changed if there is no demand for it; for example if there is no demand for Scooters then it should be changed to motorbike or composite textile changed to yarn.

iii) The management is changed and Concurrent Auditors from the Institution be appointed to monitor the account.

1.2 NEED FOR DEBT RESTRUCTURING

WHY IS CORPORATE DEBT RESTRUCTURING THOUGHT OF?\(^3\)

Inspite of their best efforts and intentions, sometimes, corporates find themselves in financial difficulties because of factors beyond their control and also due to certain internal reasons. For the revival of such corporates as well as for the safety of the money lent to them by the Banks / Financial Institutions, timely support through debt restructuring in genuine cases is devised in the form of Corporate Debt Restructuring to avoid, *inter-alia*, and delay

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\(^3\) RBI Circular
in suitable agreement among the lending institutions for such endeavor. In particular, the framework will aim at preserving viable corporates that are affected by certain internal and external factors, and minimize the losses to the creditors & other stakeholders through an orderly and coordinated restructuring programme.

a. Minimize losses to institutional lenders / Banks on account of avoidable failures on part of the Company;
b. Pre-empt the liquidation of the Company;
c. Prevent failures to attempts of majority of institutional lenders / banks to restructure the Company merely because of abortive attempts by minority institutional lenders / banks.

Restructuring may envisage, inter-alia, any more or all of the following:

**WITHIN THE BORROWER’S SCOPE**
A. Management restructuring, such as,
   - Board-basing of the board of directors
   - Inducting of qualified & experienced executives.
   - Management controls through monitoring committee.

**WITHIN THE LENDER’S SCOPE**
In view of the reappraised cash flow generation, any of the following may be considered.

1. Rescheduling : Pattern of debt service obligations may be changed, e.g., from equated
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- Change management.
  - B. Modernization
    - b. Not exceeding the existing outstanding exposure.
  - C. Diversification
  - D. Expansion
    - c. Without changing the nature and quantum of existing credit facilities, and,
    - d. Without sanctioning any fresh / new credit facility and / or additional limit whether within or exceeding the existing outstanding exposure.
  - E. Business Process Reengineering
  - F. Mergers and take-over's.
  - G. Leasing of plant.

installments schedule or to descending schedule subject to;

- a. Retaining the existing repayment period.
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H. Re-engineering the marketing

I. Other Support measures.

- Disposal of assets
- Retrenchment
- Retraining & redeployment
- Relief from Government / Tax & other authorities.

2. Rephasement: Rescheduling without observing the above said condition number (A-a);

3. Reconstruction: Rephasement with observance of the above said condition number (A-b) only. Also it may envisage renegotiation of the existing terms & conditions including concessional rate of interest retrospectively/ prospectively and / or full or partial waiver / sacrifice of already booked interest etc.

4. Restructuring: Reconstruction without observance of the above said conditions number (A-a to A-d)
Corporates, in spite of their best efforts and intentions, sometimes find themselves in financial difficulty because of factors beyond their control and also due to certain internal reasons. For the revival of the corporates as well as for the safety of the money lent by the Banks and FIs, timely support through restructuring in genuine cases is called for. However, delay in agreement amongst different leading institutions often comes in the way of such endeavors.

Based on the experience in other countries like the U.K., Thailand, Korea, etc., of putting in place institutional mechanism for restructuring of Corporate Debt Restructuring System was evolved, and detailed guidelines were issued by RBI (Reserve Bank of India) August 23, 2001 for implementation by Banks. Based on the recommendations made by the Working Group to make the operations of the CDR mechanism more efficient, the announcement made by the Finance Minister in the Union Budget 2002–2003, and consultations with the Government, the guidelines of Corporate Debt Restructuring System have since been revised and detailed hereunder for implementation by Banks / FIs.

1.3

ROLE OF RESERVE BANK OF INDIA

Pursuant to the announcement made by the Financial Minister in the Union Budget 2002–2003, a working group was constituted under the Chairmanship of Shri Vepa Kamesam, Deputy Governor, Reserve Bank of India. The Group’s recommendations have since been considered and CDR
mechanism has been revised, w.e.f. 05-02-2003⁵

Corporate Debt Restructuring is conceived by RBI⁶. The roll-model of Corporate Debt Restructuring emanated from U.K., where Bank of England took first initiative in working on the similar CDR process. Thereafter, it was successfully implemented in Thailand, South Korea, etc.

The Reserve Bank of India has instituted the Corporate Debt Restructuring (CDR) mechanism for resolution of NPAs of viable entities facing financial difficulties. The Corporate Debt Restructuring mechanism instituted in India is broadly along the lines of similar system in the U.K. Thailand, Korea and Malaysia. The objective of the CDR mechanism has been to ensure timely the transparent restructuring of Corporate Debt outside the purview of the Board for Industrial and Financial Reconstruction (BIFR), DRTs or other legal proceedings. The framework is intended to preserve viable corporates affected by certain internal / external factors and minimize losses to creditors / other stakeholders through on orderly and coordinated restructuring programme.

AS on 31st March’ 03, 60 cases worth Rs.44,369/- has been referred to the Corporate Debt Restructuring, of which 29 cases worth Rs.29,167/- crores have been approved for restructuring.

REVISION IN CORE GUIDELINES:

⁵ DBOD No. BP.BC.68/21.04.132/2002-03 dated 05-02-2003
THE Reserve Bank of India proposes to widen the scope of Corporate Debt Restructuring (CDR) and make it more efficient. Under the changes proposed today by the RBI to the existing guidelines, the Corporate Debt Restructuring scheme will be extended to corporates on whom banks and financial institutions have an outstanding exposure of Rs 10 crore as against Rs 20 crore currently. This could bring a larger number of sick units under the ambit of CDR. A corporate coming under the scheme would require the support of 60 per cent of creditors by number in addition to the support of 75 per cent of creditors by value.

This is being done with a view to make the decision-making process more equitable, the Reserve Bank of India said.

"This is expected to give smaller lenders a say in the debt restructuring exercise. Until now, larger lenders have been enjoying greater influence in such exercises. To improve the efficiency of the Corporate Debt Restructuring scheme, it is proposed to link the restoration of asset classification prevailing on the date of reference to Corporate Debt Restructuring cell to implementation of package within three months from the date of approval of the package. This explained a banker, means that if a CDR scheme is not implemented within three months of its date of approval, the advantages of classification of the assets would not be available to the borrower."

The RBI has also proposed one-time settlement as a part of

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7 RBI Master Circular
9 Risk Based Requirement
10 Capital Adequacy Assets Quality, Management Aspects, Earnings, Liquidity & System
the CDR scheme to make the exit option more flexible. This has fetched a positive response from bankers.

A Special Group under the Chairmanship of Smt. S. Gopinath, Deputy Governor, Reserve Bank of India has undertaken a review of the Scheme recently and suggested certain changes / improvements in the existing Scheme for enhancing its scope and to make it more efficient. Based on the recommendations made by the Special Group amendments proposed to the guidelines on Corporate Debt Restructuring are furnished. The major modifications proposed in the existing Corporate Debt Restructuring Scheme relate to

a. Extension of scheme to corporate entities on whom banks and institutions have an outstanding exposure of Rs.10 crore or more

b. Requirement of support of 60% of creditors by number in addition to the support of 75% of creditors by value with a view to make the decision making process more equitable.

c. Linking the restoration of asset classification prevailing on the date of reference to Corporate Debt Restructuring Cell to implementation of package within three months from the date of approval of the package.

d. Restricting the regulatory concession in asset classification and provisioning requirement to the first restructuring where the package also has to meet certain norms relating to turnaround period and minimum sacrifice and funds infusion by promoters.

e. Convergence in the methodology for computation of economic sacrifice among Banks and Financial Institutions.

f. Regulatory treatment of non-SLR instruments acquired while funding interest or in lieu of outstanding principal and
valuation of such instruments.

g. Limiting RBI's role to providing broad guidelines for the Corporate Debt Restructuring System

h. Enhancing balance sheet disclosures.

i. Pro-rata sharing of additional finance requirement

j. Including OTS as a part of the CDR Scheme to make the exit option more flexible and

k. Discretion to the core group in dealing with willful defaulters in certain cases.

The Reserve Bank of India had undertaken a review of the working of the Corporate Debt Restructuring mechanism in the month of August 2004 and a Special Group was constituted in September 2004 with Smt. S. Gopinath, Deputy Governor, RBI as Chairperson to review and suggest changes / improvements, if any, in the CDR mechanism. Based on the recommendations of the Special Group, Corporate Debt Restructuring guidelines have been further revised. The changes to the existing guidelines are as under:

a. The Reserve Bank of India would not be a member of the Corporate Debt Restructuring Standing Forum and Core Group. Its role will be confined to providing broad guidelines.

b. The Forum, while laying down the policies and guidelines, should also set out the critical parameters for restructuring (i.e. maximum period for a unit to become viable under a restructuring package, minimum level of promoters' sacrifice, etc.) to be followed by the Corporate Debt Restructuring Empowered Group and Corporate Debt Restructuring Cell for debt restructuring.
CDR system is common for all banks. All financial institutions and banks should participate in the system in their own interest. CDR system in the country will have a three-tier structure.

- CDR Standing Forum and its Core Group.
- CDR Empowered Group
- CDR Cell

Reserve Bank of India by their circular that Price water house Coopers (PWC), a firm of consultants based in London, were engaged to undertake a review of the current regulatory and supervisory regime and prepare the blue print for the transition to a more sophisticated system of the RBS incorporating international best practices. A discussion paper on the Move towards Risk Based Supervision of banks has been prepared by RBI summarizing the recommendations of the Consultants.

RBI has further advised that the introduction of the RBS would require the banks to put in place an efficient risk management architecture, adopt risk focused internal audit, strengthen the management information system and set-up compliance units. The banks would also be required to address HRD issues like manpower planning, selection and deployment of the staff and their training in risk management and risk based audit. RBI has observed that the change management is a key element in RBS and the banks should have clearly defined standards of corporate governance, well documented policies and efficient practices in place so as to clearly demarcate the lines of responsibility and accountability to align them to meet
the requirements of RBS.

The RBS approach essentially entails the allocation of supervisory resources and paying supervisory attention in accordance with the risk profile of each institution. The approach is expected to optimize utilization of supervisory resources and minimize the impact of crisis situation in the financial system. The RBS process essentially involves continuous monitoring and evaluation of the risk profiles of the supervised institutions in relation to their business strategy and exposures. This assessment will be facilitated by the construction of a Risk matrix for each institution.

The key components of the risk profile document would be the following:

- CAMELS\(^\text{10}\) rating with trends
- Narrative description of key risk features captured under each CAMELS component
- Summary of key business risks including volatility of trends in key business risk factors
- Monitor able action plan and bank's progress to date
- Strength, Weaknesses, Opportunities, Threats (SWOT) analysis
- Sensitivity analysis

RBI would undertake a formal assessment of the risk profile of each bank on a regular basis. The period between assessments would vary depending on the materiality of the risk profile of a bank, with an average period of one year. However, more frequent assessments would be resorted to for higher risk
banks and less frequent assessment for lower risk banks.

1.4 **ROLE OF COMMERCIAL BANKS AND FINANCIAL INSTITUTIONS**

The restructuring guidelines for Corporate Debt Restructuring and for advances with funded exposure of & above Rs.10 Lacs are briefed out as under:

<table>
<thead>
<tr>
<th>No.</th>
<th>Corporate Debt Restructuring</th>
<th>Restructuring Guidelines</th>
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</thead>
<tbody>
<tr>
<td>1.</td>
<td>The foremost purpose is slippage prevention.</td>
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<tr>
<td>2.</td>
<td>Only feasible &amp; viable manufacturing or industrial units are eligible.</td>
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</table>

**Note:**

As trading involves only buying and selling of commodities and the problem associated with manufacturing units such as bottleneck in commercial production, time and cost escalation etc. are not applicable to them, these guidelines should not be applied to restructuring / rescheduling of credit facilities extended to traders.

3. Generally, only Standard or Sub-standard accounts are covered; however, even doubtful accounts may also be considered if 75% or more of the institutional lenders satisfy upon viability and consent to.

4. Generally the cases outside BIFR / Only Standard or Sub-standard accounts are covered.

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DRT or Courts are to be considered; however, on case-specific merits, such cases may also be considered.

5. Only Corporate Accounts to be covered

6. There has to be more one institutional lender.

7. Minimum exposure of the banking system to the unit should not be less than Rs.20 crore.

8. A voluntary mechanism.

9. The debts being restructured should be fully secured, if some portion is unsecured, it should be fully provided for;

**Note:**
While assessing the extent of security cover available to the credit facilities, which are being restructured / reschedule collateral security, would also be reckoned, provided such collateral is a tangible security properly charged to the Bank and is not in the intangible form like guarantee etc. of the promoter / others.
10. The borrower must not be willful defaulter or involved in fraud or misfeasance*  
*(bonafide reckless act detrimental to the interest of stakeholders in the unit.)

11. CDR mechanism can be invoked by any institutional lender(s) having minimum value wise exposure of 20% [or the borrower himself backed by such institutional lender(s)]  
It is to be initiated by the interested Bank(s) on its / their own.

12. Enforceability of Corporate Debt Restructuring from ICA and DCA and the super majority concept is abided.  
Enforceability is derived out of bilateral agreement / understanding between the Bank(s) and the borrower.

13. CDR envisages a stand still clause.  
Such clauses are not required because it is a case of individual Bank’s domain.

14. Additional finance, if sanctioned on case – specific merits, qualify for being classified as Standard irrespective of the current classification of the account and shall be governed by usual IRAC – norms.

15. IRAC – norms continue to apply;  
No such comfort is provided for.
favourably, than, the asset classification existing at the time of making reference by the lender to the CDR cell, is restored though no write back of provisioning is permitted.

The Indian banking scene has witnessed progressive deregulation, institution of prudential norm and an emulation of international supervisory best practices. The supervisory processes have also concomitantly evolved and have acquired a certain level of robustness and sophistication with the adoption of the CAMELS / CALCS approach to supervisory risk assessments and rating. The tightening of exposure and prudential norms and enhancement in disclosure standards in phases over a period of time have more closely aligned the Indian banking system to international best practices. Reserve Bank of India (RBI) has been constantly endeavoring to enhance the sophistication and efficiency levels of its supervisory processes.

The central plank for RBS IS an accurate risk profiling for each bank. The risk profile would be a document, which would contain various kinds of financial and non-financial risks faced by a banking institution. The risk assessment would entail the identification of financial activities in which a bank has chosen to engage and the determination of the types and quantities of risks to which these activities expose the banking institution. The type of risk that banking institution face individually or in combination include, but are not limited to, credit, market, liquidity, operational, legal and reputational risks. The quantity
of risks associated with a given activity may be assessed by the volume of assets and the off balance sheet items that the activity represents or the portion of revenue derived from that activity. Activities that are 'new to an institution or for which exposure is non readily quantifiable may also represent high risk to an institution that would also be evaluated and included in the risk profile document. The risk profile will also be designed to provide a systematic assessment from the supervisor's perspective of the adequacy and effectiveness of the bank's organisation, management and controls. The main risk profiling device at present is the CAMELS rating based on on-site inspection, which in course of time will be derived from off-site returns and other information. CAMELS rating would continue to be the core of risk profile compilation, but the successive ratings would be used to reflect trends in contrast to being used as a static annual indicator of risk.

The risk profile of each bank will draw upon a wide range of sources of information, besides CAMELS rating, such as, off-site surveillance and monitoring (OS MaS) data, market intelligence reports, ad-hoc data from external and internal auditors, information from other domestic and overseas supervisors, on-site findings, sanctions applied etc. The data inputs would be assessed for its significance and quality before being fed into the risk profile. All outliers i.e. banks which fall outside the normal distribution based on characteristics such as profitability, new business activity, balance sheet growth etc. would be identified on the basis of a two-tailed test (i.e. too good or too bad) and investigated on a regular basis. The risk profile would be constantly updated.
The key components of the risk profile document would be the following:

- CAMELS rating with trends
- Narrative description of key risk features captured under each CAMELS component
- Summary of key business risks including volatility of trends in key business risk factors
- Monitorable action plan and bank’s progress to date
- Strength, Weaknesses, Opportunities, Threats (SWOT) analysis
- Sensitivity analysis

RBI would undertake a formal assessment of the risk profile of each bank on a regular basis. The period between assessments would vary depending on the materiality of the risk profile of a bank, with an average period of one year. However, more frequent assessments would be resorted to for higher risk banks and less frequent assessment for lower risk banks.

The risk assessment of individual banks would be performed in advance of on-site supervisory activities. The risk assessment process would highlight both the strengths and vulnerabilities of an institution and would provide a foundation from which to determine the procedures to be conducted during the inspection. The current full-scope on-site inspections, which are carried out annually cover a substantive asset evaluation. The inspections under the new approach would be "largely systems based rather than laying emphasis on underlying transactions and asset valuations. The inspection would target identified high-risk areas from the supervisory perspective and
would focus on the effectiveness of mechanism in capturing, measuring, monitoring and controlling various risks. The inspection procedure would continue to include transaction testing and evaluation the extent of which will depend on the materiality of an activity and the integrity of the risk management system and the control process.

**1.5 COOPERATION OF CORPORATE BORROWERS**

Most Asian countries adopted “Out of Court” restructuring mechanisms to minimize court intervention and speed up restructuring of potentially viable entities. However, this process has yielded mixed results. In Korea for example, while most Chaebols and Corporate entities entered into workout arrangements this often did not lead to far reaching restructuring of these entities. While debt restructuring was generally implemented quickly, delays were witnessed in asset reduction programs and improvement in operating performance was slower and lower than expected. In Thailand similarly, majority of restructuring arrangements have typically involved extension of grace periods or concessional arrangements and it is widely held that genuine restructuring has not taken place.

Internationally, restructuring of NPAs often involves significant operational restructuring in addition to financial restructuring.

Typically, lenders set up a working group including their representatives as well as those of the borrowers. Usually, an independent consultant / financial advisor is engaged to advice on possible operational restructuring measures. The working
group adopts a brainstorming approach to identify possible improvement areas, which could include, inter alia:

Cost rationalization, e.g., through rationalization of workforce, closure of unviable units, product line rationalization, centralization of cash and accounting control, outsourcing, process automation, etc.

Improvement in sales though reorganization of sales force compensation packages, investment in new products, development of new markets, customer loyalty programmes.

Working capital management by negotiating deferrals with suppliers, identifying alternative sources of supply, tightening of recovery processes from debtors.

Identification of surplus / redundant assets could include identification of non-core business, surplus machinery and equipment, non core patents and trademarks.

Identification of profitable areas of operation and redoubling of efforts in those areas, backed up with additional funding if necessary.

For each of the improvement measures identified, the following analysis is carried out:

- Savings / effect on EBIT and EBIDTA
- Effects on cash flow.
- Related cost (e.g. one time cost of a VRS).

Once the restructuring measures have been agreed by
stakeholders, a complete restructuring plan is prepared which takes into account all the agreed restructuring measures. This includes establishment of a timetable and assignment of responsibilities. Usually, lenders will also establish a protocol for monitoring of progress on the operational restructuring measures. This would typically involve the appointment of an independent monitoring agency.

**CASE STUDY**

**Kinetic Engineering Limited (KEL)**

**RESTRUCTURING SCHEME**

1. **Cut-off date** - September 30, 2004

a. **Waiver**: all liquidated damages / further interest and penal interest payable from October 01, 2004 till March 31, 2006).

   a) **Appropriation of receipts to be made in the following order:**
      - interest dues outstanding as on cut-off date.
      - interest payments as envisaged under this scheme.
      - Principal outstanding as on cut-off date.

b. **Option of Quarterly / monthly interest payment**: At the option of the lender, the Company shall pay interest at monthly rests at an adjusted rate such that the annualized yield of proposed monthly rate is equal to the annualized yield of quarterly rate.

c. **Funding of Interest**: Rs. 84 million (approx.) of interest dues (for the, period 01.10.2004 to 31.03.06) to be funded @ 8.50
% p.a. payable quarterly (8.38% payable monthly) plus applicable interest tax or other, statutory levy, if any and would be repayable in 20 equal quarterly installments starting from June 30, 2006 or 60 equal monthly installments starting from April 30, 2006.

d. **Principal Outstanding of Secured Term Debt:** From the cut-off date, principal outstanding of secured debt of approximately Rs. 954 million (including proposed corporate loan- Rs. 250 million converted unsecured loan of Bank of Baroda or Rs. 150 million and Funded interest loan of approximately Rs. 84 million) shall be restructured as follows:

1. **Interest:** The principal shall carry interest rate of 8.50% p.a. payable quarterly (equivalent to 8.38% p.a. payable monthly) plus applicable interest tax or other statutory levy, if any, on the last day of each month. The first interest payment date would June, 30, 2006 in case of quarterly interest payment and April 30, 2006 in case or monthly interest payment.

2. **Repayment:** Term Loan will be repayable in 20 equal quarterly installments starting June 30, 2006 (FY 2007) and ending March 31, 2011 (FY 2011) or 60 equal monthly installments starting April, 30, 2006.

b) **Principal Outstanding of Unsecured Term Debt** of Rs. 150 million shall be restructured as follows:

i) **Interest:** The principal shall carry interest rate of 8.50% p.a. payable quarterly (equivalent to 8.38% p.a. payable
monthly) plus applicable interest tax or other statutory levy, if any, on the last day of each month. The first interest payment date would be June 30, 2006 in case of quarterly interest payment and April 30, 2006, in case of monthly interest payment.

ii) **Repayment** : Term Loan will be repayable in 20 equal quarterly installments starting June 30, 2006 (FY 2007) and ending March 31, 2011 (FY 2011) or 60 equal monthly installments starting April 30, 2006.

**Working Capital Assistance:** Working capital bankers will reduce the interest rates on fund-based limits to 8.50% p.a. payable monthly which would be subject to annual reset. The banks shall release the working capital limits (both fund based and non-fund based) in accordance with the assessment done by the lead bank. The lead bank, SBI has assessed the fund based requirements of the company with MPBF of Rs. 470 million, after taking into account additional funding of Rs. 250 million.

**Additional funding** by way of Corporate Loan of Rs.250 million would be shared in proportion of total sanctioned limits or working capital / outstanding limits or term loans & short term loan of respective banks as on cut-off date. Interest and repayment shall be as under:

**Interest:** The principal shall carry interest rate of 8.50% p.a. payable quarterly (equivalent to 8.38%, p.a. payable monthly) plus applicable interest tax or other statutory levy, if any, on the last day of each month. There would be no
interest funding applicable for proposed corporate loan. First interest payment date would be June 30, 2006 in case of quarterly interest payment and April 30, 2006 in case of monthly interest payment.

**Repayment:** Corporate Loan will be repayable in 20 equal quarterly installments starting June 30, 2006 (FY 2007) and ending March 31, 2011 (Financial Year 2011) or 60 equal monthly installments starting April 30, 2006.

Company to arrange funds in case SICOM (non-CDR lender) does not take up its share in Corporate Loan

**Security:**

**Term Loans:** The restructured term debt aggregating Rs. 954 million (including Corporate Loan of Rs. 250 million, converted unsecured Loan of Bank of Baroda aggregating Rs 150 million and Funded Interest Term Loan of approximately Rs. 84 million) would be secured as follows:

A first pari passu charge on all the Company's fixed assets, both present and future, in such form and manner as may be required by term Lender. The term lenders shall provide No-Objection Certificates and cede pari passu charge as contemplated in this package.

A second pari-passu charge on all the Company's current assets; both present and future, in such form and manner as may be required by such term lenders.
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**Working Capital:** The security for the working capital assistance would be as follows:

A first pari-passu charge on all the Company's current and future, in such form and manner as may be required by W. C. Banks

A second pari-passu charge on all the company's fixed assets, both present and future, in such form and manner as may be required by W. C. Banks.

**Additional Security:** The promoters shall secure the outstanding debt of lender forming part or CDR package by way of personal guarantee of promoters / directors, viz. Shri A. H. Firodia and Smt. S. F. Motwani and pledge of entire promoters shareholding in KEL as additional security on or before September 30, 2005.

**Unsecured loans by subsidiaries:** The outstanding debt of Kinetic Motor Company Ltd. (KMCL) having an outstanding of Rs. 90.4 million as on September 30, 2004, will be repaid on 24 equal quarterly installments commencing from June 30, 2006. The outstanding debt of JHS Taigene having an outstanding of Rs. 10.00 million will be repaid in 4 equal quarterly installments commencing from June 30, 2005.

**Conditions:**

The promoters would convert unsecured loans to the extent of Rs.150 million on or before March 31, 2006 as per regulatory norms.
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The promoters' debt and ICD from Group companies would be subordinated to the restructured debt of lenders and interest rate on promoters ICDs shall be nil interest rate on ICD from Group Companies shall be 5% p.a. payable quarterly. There will be no repayment on Promoters' ICD till the maturity of loans from lenders. The increase in rate of interest on ICDs may be considered by Monitoring Committee (MC) after analysing performance of company under the CDR package after which MC may recommend the same to the CDR Empowered Group (EG).

During the tenure of restructured loan, KEL would not furnish corporate guarantee to any group company without prior approval of lenders.

The company shall seek prior approval or the CDR Empowered Group of tenders before making any investment / providing loans and advances to group / subsidiary companies or divestment of any of its units or divestments of investments.

The lenders would constitute a Monitoring Committee (MC), to monitor to restructuring scheme and the performance of the Company on a regular basis. The Company shall undertake to provide all information as and when required by the Monitoring Committee, all costs, charges and expenses for convening the Monitoring Committee shall be incurred, paid by the company.
The lenders shall convey no-objection to the sale of R. & D: and tool room asset from Kinetic Engineering Ltd. to group companies along with approval of CDR scheme.

The Company shall finalize its annual budget in consultation with MC.

The company shall not escrow its future cash flows receivables subsidies of the company or create charge or lien or interest thereon or whatsoever nature except with the prior approval of lenders.

The Company shall take prior written approval of lenders for incurring any capital expenditure in excess of Rs.50 million in any particular year.

The Company shall not undertake any new project or expansion or make any investment; or take assets on lease or any divestment or sale without the prior approval of lenders.

The Company shall not pay any dividend on the equity shares without the prior written approval of lenders.

If required, the lenders shall have the right to appoint / retain a concurrent auditor to oversee and monitor this restructuring scheme and carry out a concurrent audit or the accounts of the Company. All costs, charges and expenses of the concurrent auditor shall be incurred, met, paid by the Company. The concurrent auditor would
continue for duration as is satisfactory to lenders. The appointment of concurrent auditor would be effective from April, 2005.

If required, the lenders reserve the right to stipulate Trust and Retention Account (TRA) mechanism to contral the cash flows of the company.

In the event of default to a lender, lender shall have the right to convert all defaulted amounts into equity at par. The Company shall undertake to increase its authorized share capital so as to ensure that lender(s) have the option to convert such defaulted amounts into equity.

If required, the Company shall broad base its Board of Directors & audit sub committee and strengthen its management set-up in consultation with and to the satisfaction of the lenders. The company shall not induct any person who is a director on the Board of a company which has been identified as a willful defaulter and in case such a person is found to be on the Board of the company, it would take expeditious steps for removal or the person from its Board.
The Company shall vest in the lenders the right of recompense in respect of the waivers / sacrifices undertaken by them.

In case the cash flows of the Company so warrant, the lenders at their description will have the right to accelerate the repayments of their facilities / renegotiate the terms of restructuring.

The company shall furnish a copy of the Fixed Assets Register to the lenders as at the end of every financial year, duly certified by the Statutory Auditor.

The lenders reserve the right to sell, assign, and securities the loan assets or cash flows to any third party.

The company shall have an option to prepay the loans without prepayment premium, in one or more tranches, anytime during the currency of the loan.

The lenders reserve the right to cancel, suspend, reduce or modify, including withdrawal with retrospective effect, all or any of the reliefs and concessions and / or amend or vary the terms and conditions thereof, in the event of default by Company.

The company / promoters shall give an undertaking
that in the event of any shortfall in the cash flows envisaged in the CDR projections, the company / promoters shall bring in the required funds without recourse to the lenders.

The company shall obtain approval of all FIs/ Banks / Debenture holders for the proposed restructuring package.

In the event of any default / breach / violation of any of the terms and conditions this package, the lenders have the right to revoke the restructuring package.
RESEARCH METHODOLOGY

Research Methodology is a very systematically solve the research problem. It may be understood as a science of studying how research is done scientifically. In it we study the various steps that are generally adopted by a researcher to know not only the research methods / techniques but also in methodology.

Research is an academic activity and as such the term should be used in a technical sense. According to Clyford Woody research comprises defining the redefining problems, formulating hypothesis or suggested solutions, collecting organizing and evaluating data, making deductions and reaching conclusions and at least carefully testing the conclusions to determine weather they fit the formulating hypothesis.

Research Process

Before embarking on the details of Research Methodology and techniques it seems appropriate to present a brief overview of the research process. Research process consists of serious of action or steps necessary to effectively carryout research and the desire sequencing of these steps. However the following order concerning various steps provides a useful procedural guidline regarding the research process:-

1. **Formulating The Research Problem:**
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There are two types of research problems viz. those relate to states of nature and those which relates to relationship between variables. At the very outset the research must single out the problem he wants to study i.e. he must decide the general area of interest or aspect of a subject matter that he would like inquire into.

In the present thesis the researcher wants to study the impact of Corporate Debt Restructuring (CDR) in India.

2. Extensive Literature Survey:

At this juncture the researcher should undertake extensive literature survey connected with the problem. For this purpose the abstracting and indexing journals and published or unpublished bibliographies are the first place to go to Academic journals, conference proceedings, government reports, books etc. must be tapped depending on the nature of the problem.

3. Development of Working Hypothesis

After extensive literature survey, researcher should state in clear terms the working hypothesis or hypothesis, working hypothesis is tentative assumption made in order to draw out and test its logical or empirical consequence. As such the manner in which the research hypothesis are developed is particularly important since they provide the focal point for research.

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4. **Preparing the Research Design**

The research problem having been formulated in clear cut terms and researcher will be required to prepare a research design i.e. he will have to state the conceptual structural within which research would be conducted the preparation of such design facilitates research to be as efficient as possible yielding maximal information.

5. **Determining Sample Design**

All the terms under consideration in any field of enquiry constitute a ‘universe’ or ‘population’ in known as a census inquiry. The researcher must decide the way of selecting a sample or what is popularly known as the sample design. In other words a sample design is a definite plan determined before any data are actually collected for obtaining a sample from a given population. The sample design to be used must be decided by a researcher taking into consideration the nature of inquiry and other related factors.

In the present thesis the components of Research Design are:

a. The Population to be studied.

b. Sample Unit
c. Sample Size.

d. Research Instruments.

**Population to be studied:**
Population to be studied is Corporate Debt Restructuring (CDR) in India.

**Sample Unit**
Who is to be Surveyed. Here the researcher defines the target population. Politicians, Economists, Academicians, Businessman and Bankers.

**The qualifying criteria for target sampling**
The researcher has collected data through Random Sampling.

**Sample Size**
To draw meaningful consequence only 20 people (Politicians, Economics, Academicians, Businessman and Bankers) from 4 metro cities is randomly selected (20x4 = 80 sample size)

**Research Instruments**
Research Instruments include the various tools which is researcher uses data and analyse the data to draw certain conclusions.

**Questionnaire** : Data is collected through questioner: Secondary Data is collected through
magazines, journals, newspapers, books, Circulars, Notifications etc.

6. **Collecting the Data**

In dealing with any real life problem it is often found that data at hand are adequate and hence it becomes necessary to collect data that are appropriate. There are several ways of collecting the appropriate data which differ considerably in context of money, costs, time and other resources at the disposal of the researcher.

**Sources of Data:**

After preparing the details of information required in investigation the researcher will find sources from where the information can be extracted. The sources available for gathering data are:

*Primary Data:*

Primary Data is the data which is collected afresh and for the first time and in original in character.

*Secondary Data:*

Secondary Data refers to the information that already exists somewhere having been collected for another purpose.

In the present thesis the data collected is both of primary and secondary nature. The method of primary data collection is
only through questionnaire. Apart from help of journals, magazines, books previous literature current news etc. is taken.

7. **Execution of the Project:**

Execution of the project is a very important step in the research process. If the execution of the project proceeds on correct lines the data to be collected would be adequate and dependable. The researcher should see that the project is executed in a systematic manner and in time.

8. **Analysis of Data**

After the data have been collected the researcher turns to the tasks of analyzing of them. The analysis of data requires a number of closely related operation such as establishment of categories and application of these categories to raw data through coding tabulation and then drawing statistical inferences.

9. **Preparation of the Report or Thesis:**

Finally the researcher has to prepare the report of what has been done by him.

10. **Limitations**

    a. To study the impact of Corporate Debt Restructuring (CDR) in India is such a vast subject that it becomes difficult to cover every aspect of it.

    b. Time and money are major constraints while doing the research.