

Debt Resolution under RBI Framework

Guiding Principles and Perspectives

Objective



Premise of Restructuring and a typical restructuring scheme

Synopsis of 6th August, 2020 RBI guidelines

Benefits under recent RBI guidelines and possible resolution approach

Comparison of Restructuring guidelines - 6th August, 2020 & 7th June, 2019

Resolution Option Analysis

Opportunities for Chartered Accountants

Premise of Restructuring – Critical Factors



Inadequacy of normal cash flows

- Are normal cash flows sufficient to service entire debt on current terms?

Uncertain extraneous factors

- Would sudden external factors (like COVID) impair operations in short to medium term?

Working capital

- Is current WC intact or eroded beyond any meaningful correction in future?

Adequacy of resolution measures

- Are current resolution measures and reliefs, sufficient to address liquidity problems?

Alternate options to resolve

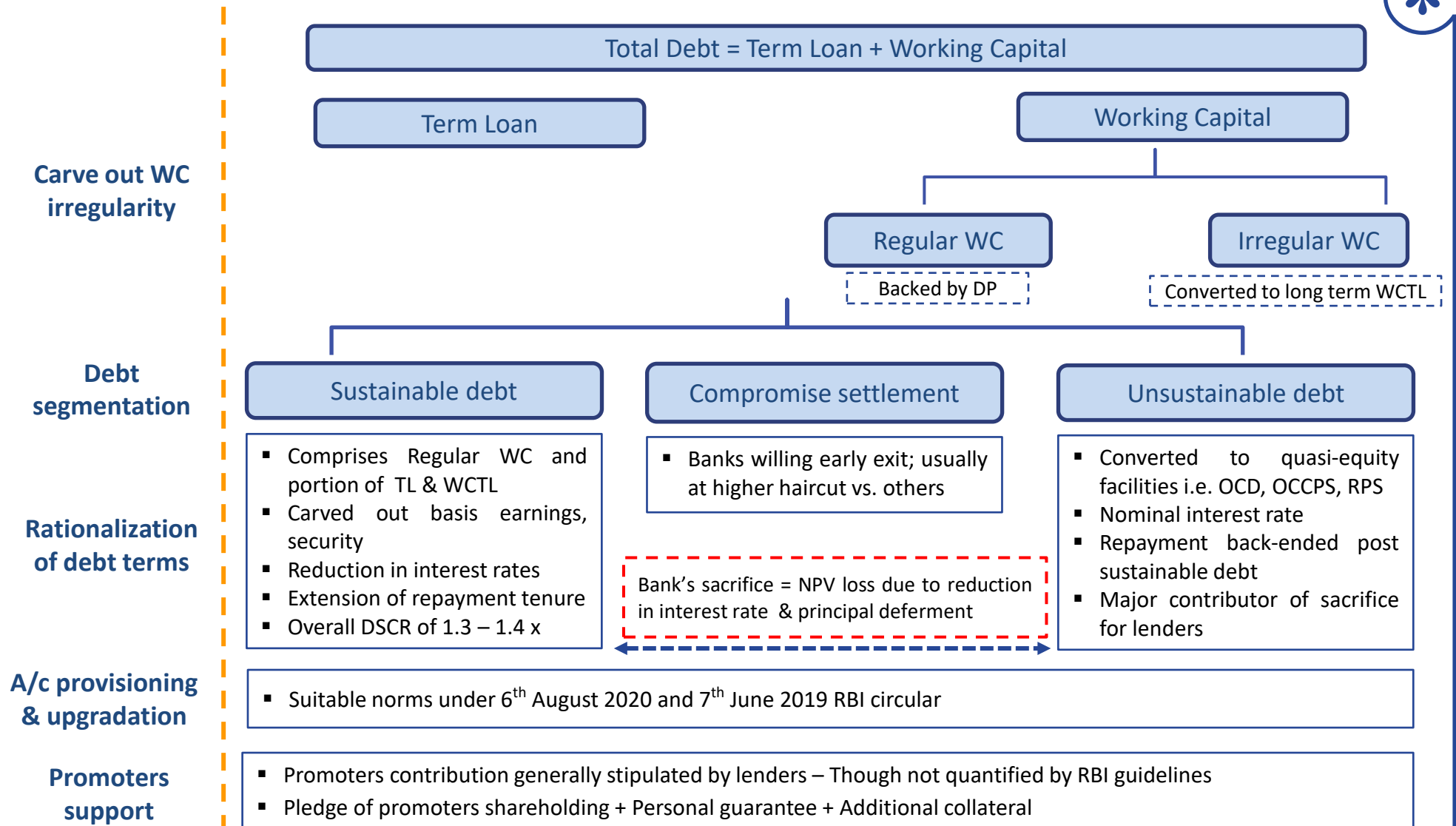
- Are there alternate sources like unavailed limits, new funding, equity, non-core asset sale, liquidation of investment, etc to address long term liquidity problems?

Group companies support

- Are some group companies strong enough to sustain & support stressed cos in the group, without draining their own resources and growth avenues?

Various guiding factors to be sensitised at company and group level

Typical Restructuring Scheme



Concessions "Ask" may vary based on guidelines and type of Resolution sought



Synopsis of 6th August, 2020 RBI guidelines

Resolution of Personal Loans



Applicability	<ul style="list-style-type: none">▪ Resolution of personal loans sanctioned to individual borrowers by LIs<ul style="list-style-type: none">○ Personal loans consist of (a) consumer credit, (b) education loan, (c) loans given for creation/enhancement of immovable assets (e.g., housing, etc.), and (d) loans given for investment in financial assets (shares, debentures, etc.)▪ Credit facilities provided by LIs to their own personnel/staff not eligible
Eligibility	<ul style="list-style-type: none">▪ Borrower accounts classified as Standard, but not in default for more than 30 days with the LI as on March 1, 2020▪ Eligible borrowers' accounts should continue to be classified as Standard till the Date of Invocation* of resolution under this framework
Invocation Date & Implementation	<ul style="list-style-type: none">▪ Invocation Date: Should not be later than December 31, 2020▪ Implementation Period: Within 90 days from Date of Invocation
Resolution Plan Features	<ul style="list-style-type: none">▪ To include rescheduling of payments, conversion of any interest accrued, or to be accrued, into another credit facility, or, granting of moratorium (maximum of two years)▪ Moratorium period, if granted, to be effective immediately upon implementation of resolution plan and would lead to overall tenor of loan to be modified commensurately
Implementation Conditions	<ul style="list-style-type: none">▪ Completion of all documentation & creation/perfection of security▪ Revised terms of conditions of loans duly reflected in books of lending institutions▪ Borrower not in default with the lending institution as per revised terms

**Date of Invocation (for Personal Loans): Date on which both the borrower and LI have agreed to proceed with a resolution plan under this framework.*

Note: Any resolution plan implemented in breach of the above stipulated timeline shall be fully governed by the Prudential Framework, or the relevant instructions as applicable to specific category of lending institutions where the Prudential Framework is not applicable.

RBI 6th August Framework Corporates – Key Aspects (1/2)



Eligibility

- Borrower accounts **classified as Standard**, but **not in default for more than 30 days** with any Lending Institution (“LI”) as on March 1, 2020
- Account should **continue to remain standard till the date of invocation**
- Resolution for other accounts to be done as per June 7, 2019 circular

Invocation Date & Implementation

- **Invocation Date:** Resolution may be invoked **not later than December 31, 2020**
 - **For Sole LI:** Date on which **both the borrower & LI agree** to proceed with resolution plan
 - **Multiple LIs :** LIs representing **75% by value** of total outstanding (FB & NFB) & **60% by number** agree to invoke
- **Implementation:** **Within 180 days** from the date of invocation

Signing of ICA

- Required to be **signed by all LIs within 30 days** from date of invocation – Consequences for LI not signing ICA discussed subsequently
- Invocation to **lapse in case LIs representing 75% by value & 60% by number do not sign ICA within 30 days** from invocation; process can’t be invoked again
- Lenders other than the LIs as per this circular may also sign ICA
- ICA to contain **dispute redressal mechanism** and suitable **mechanism for information sharing**

Expert Committee

- RBI shall constitute an Expert Committee which shall recommend:
 - List of financial parameters to be factored into assumptions for each resolution plan
 - Sector specific benchmark ranges for such parameters
 - Parameters shall cover aspects related to leverage, liquidity, debt serviceability, etc
- For accounts with **aggregate exposure >= Rs. 1500 Crs:** Expert Committee shall do **vetting of the resolution plans** with only purpose to verify that all the processes have been followed

RBI 6th August Framework Corporates – Key Aspects (2/2)



General Guidelines

- On any timelines breach, the resolution process ceases to apply immediately
- **Compromise settlement to be excluded** from this framework
- Additional funding as Resolution plan permitted **even if no renegotiation of existing debt**
- **Extension of loan tenor should not be more than 2 years** (with/without moratorium)
- Resolution plan to adhere financial parameters to be notified by RBI
- For **aggregate exposures >= Rs. 100 Crs, ICE from one CRA required**

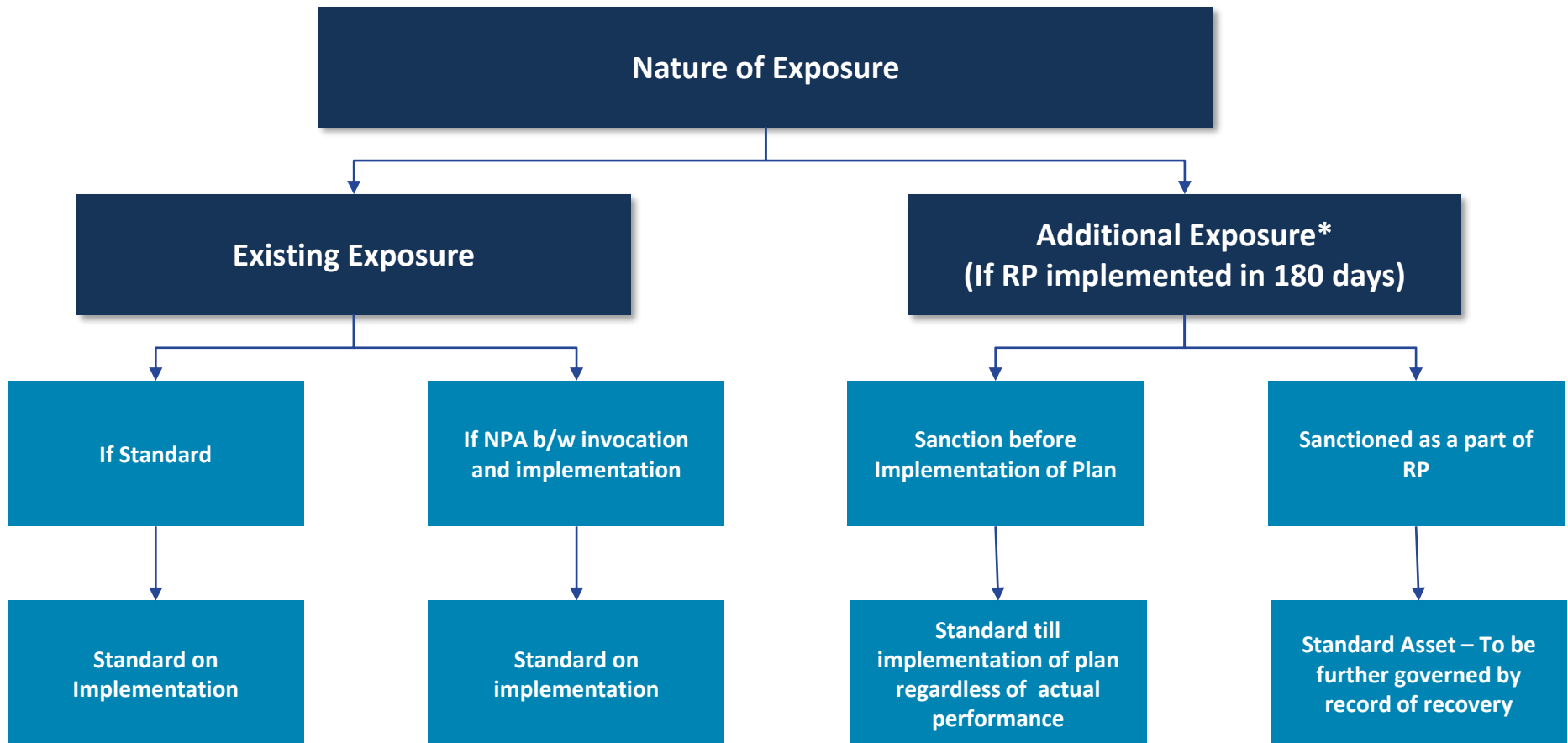
Conversion of Loans into Securities & Valuation

- **Loan conversion to equity / other marketable non convertible debt securities** permitted
- Amortization and coupon of such debt securities to be in line with residual debt terms
- Valuation of such converted equity shall be as per June 7, 2019 circular
- Valuation of debt securities shall be as per Master Circular for Investments dated Jul 1, 2015 or other relevant instructions as applicable
- **Valuation of converted debt into other securities to be collectively valued at Re. 1**

Escrow Mechanism

- Escrow account to be in place to route entire cash inflows/outflows of the borrower including fresh disbursement as per plan
- Formal agreement with escrow manager detailing duties and responsibilities of escrow manager to be entered
- Contractual empowerment to Escrow manager with proper enforcement mechanism to ensure disbursement commitment of LIS

Asset Classification Norms

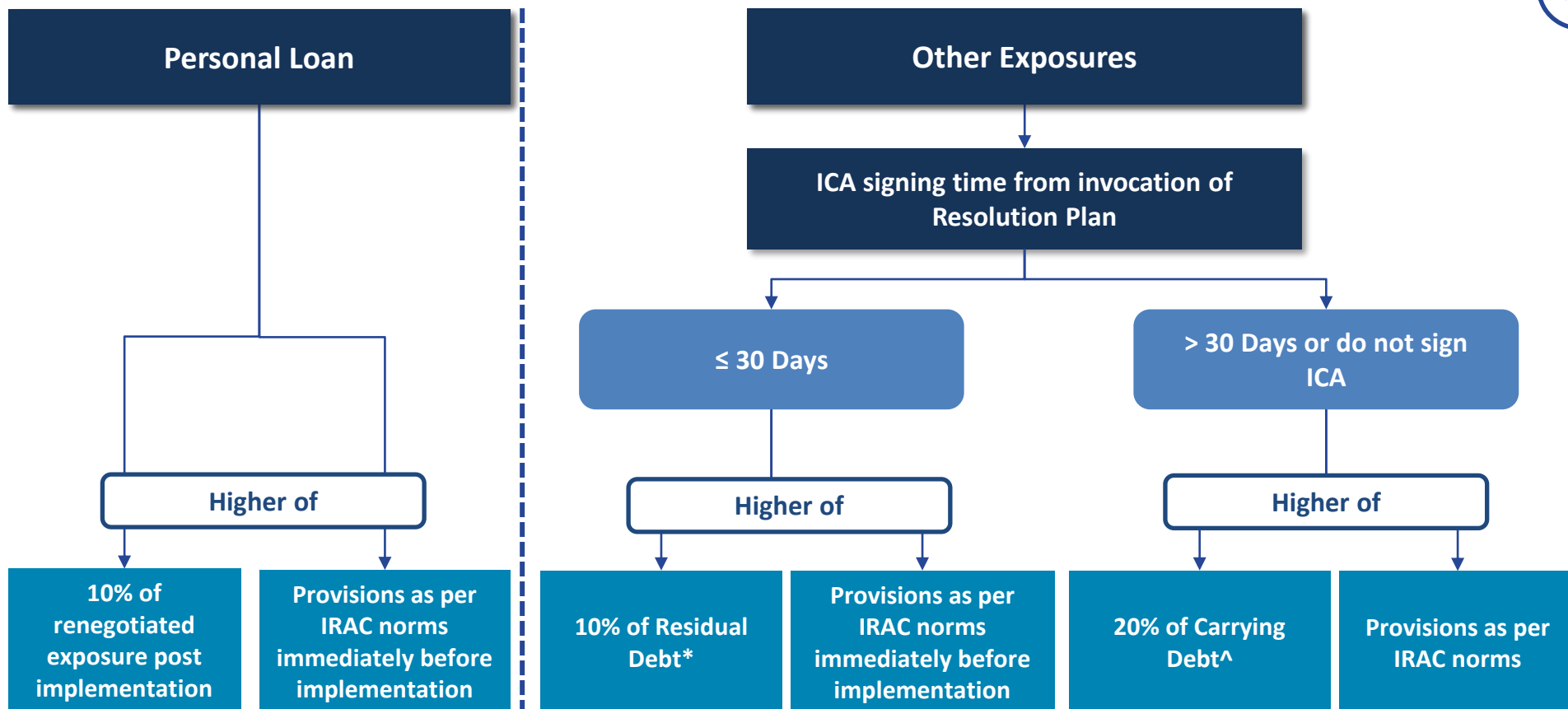


* In case non implementation of plan within stipulated timelines asset classification of additional finance worse of:

- Actual Performance
- Classification of all other credit facilities

RP: Resolution Plan

Provisioning Norms



Additional Provisions - Reversal

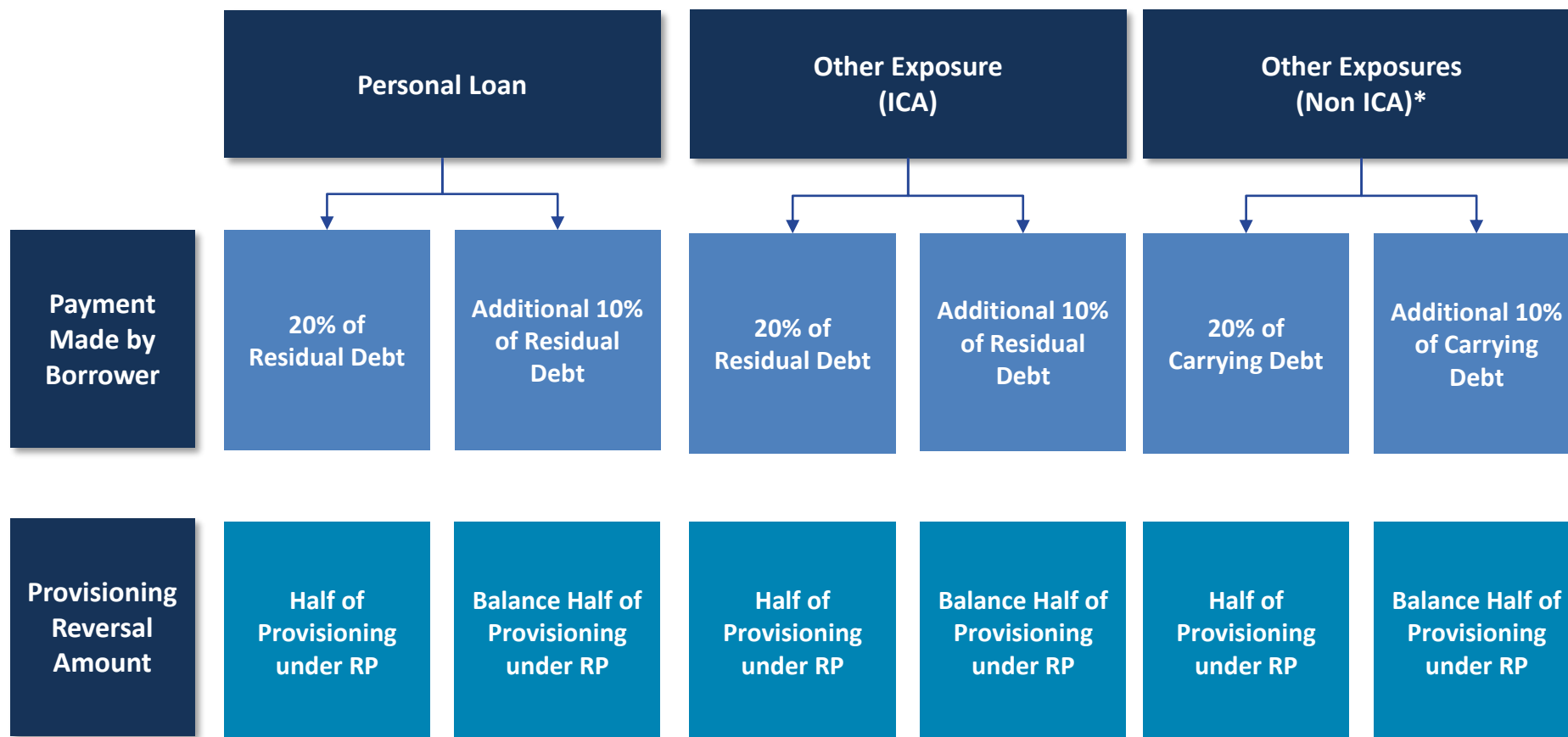
- Additional provisions maintained by LIs under April 17, 2020 Circular, to the extent not reversed – may be utilized for meeting provisioning requirements in all cases under this facility
- Any additional provisions maintained in terms of Paragraph 17 of Prudential Framework, wherever applicable may be reversed at the time of invocation of the resolution plan
 - If plan not implemented within 180 days from invocation, provisions as per the Prudential Framework will be maintained – as if resolution process never invoked under this window

*Total debt, Including debt securities issued as part of resolution plan, held by the ICA signatories post-implementation of the plan.

^ Debt on their books as on 30th day post invocation.

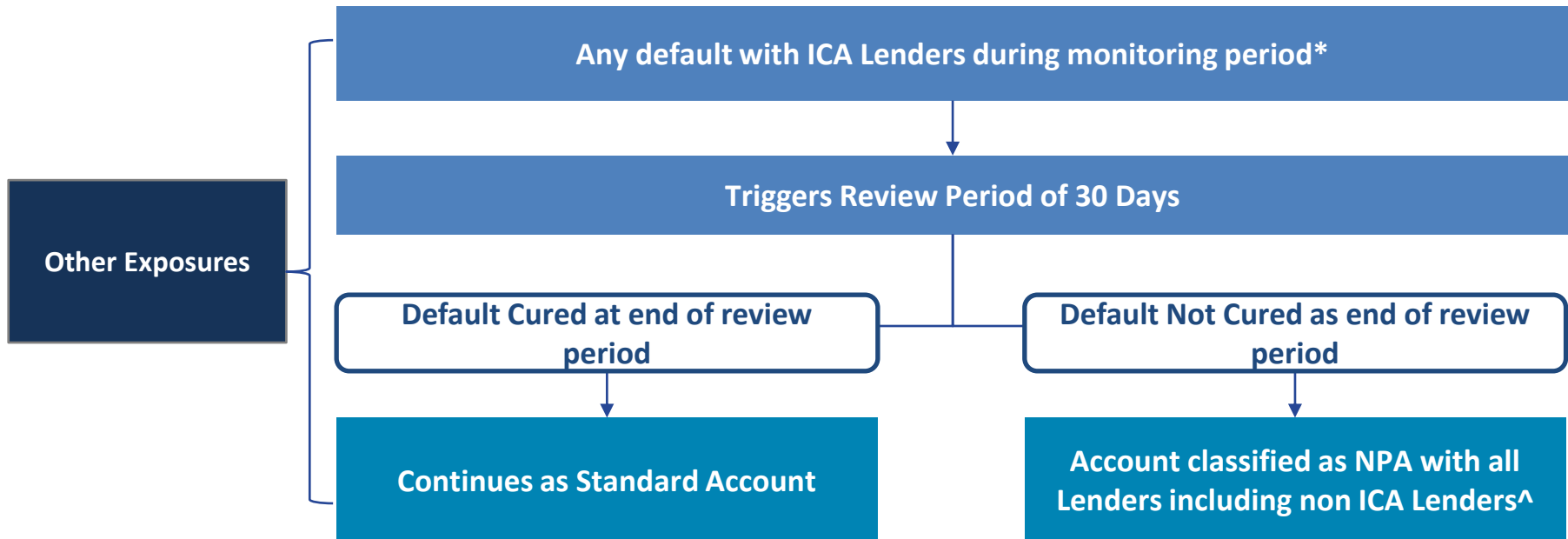


Reversal of Provisioning



*Reversal of provisioning subject to the required IRAC provisions being maintained.

Asset Classification Post Implementation



Personal Loans

- After implementation of resolution plan in terms of this facility, the subsequent asset classification will be governed by criteria laid out in Master Circular dated July 1, 2015 or other relevant instructions as applicable to specific category of LIs.

^Account to be classified as NPA from the date earlier of :

- *Date of implementation of RP*
- *Date of classification as NPA before implementation of RP*

**Monitoring Period - Period starting from the date of implementation of the RP till the borrower pays 10% of the residual debt, subject to a minimum of one year from the commencement of the first payment of interest or principal (whichever is later) on the credit facility with longest period of moratorium.*

Disclosures & Credit Reporting



Disclosure & Reporting

- Quarterly statements (at minimum) in prescribed Format A) in Financials statements for quarter ended March 2021 to September 2021
- Half Yearly disclosures in Format B commencing Sep 2021 till earlier of :
 - All exposures under RP fully extinguished
 - Completely slips into NPA
- Annual Disclosure mandatory
- Where RP implemented, credit reporting will reflect “restructured” status of account if RP involves renegotiation that would be classified as restructuring under Prudential Framework



Benefits under 6th August Circular

Resolution Approach under 6th August Framework



Company's Situation	Low Impacted	Impacted; can manage with Cashgap funding	Impacted; needs greater support
Indicators	<ul style="list-style-type: none"> Temporary Slowdown Moderate to Good financials 	<ul style="list-style-type: none"> Limited DP impact Moderately leveraged Healthy security cover Existing debt serviceable on current terms 	<ul style="list-style-type: none"> WC depleted High leverage Moderate security cover Existing debt terms rationalization; with limited sacrifice for bank
Feasible Solution	<ul style="list-style-type: none"> No additional support needed 	<ul style="list-style-type: none"> Corporate Loan 	<ul style="list-style-type: none"> Restructuring under 6th August, 2020

Suitable resolution may be adopted based on company specific cashflow situation
 Any delay would aggravate CF position – However maximum relief under proposed guidelines is 2 year
 If current measures seem inadequate, alternate resolution under 7th June, 2019 framework

Benefits under the Package



Liquidity relief	<ul style="list-style-type: none">• Interim Holding of Operations• Extension of Repayments• Rationalization of debt terms - with minimum sacrifice for lenders
Additional Funding	<ul style="list-style-type: none">• Addl. funding permitted to address CF mismatch even if no renegotiation of existing debt• However it may be subject to adequate collateral and comfortable financial ratios
Critical processes curtailed	<ul style="list-style-type: none">• Forensic can be avoided; but comfort to be given to bank through low sacrifice• Credit rating limited to one agency• ICA signing expedited through various deterrents for non-abiding lenders
Timeline bound resolution	<ul style="list-style-type: none">• Invocation to be done within specific timelines (before 31st Dec,2020)• Critical time-consuming processes (Forensic, ICA, Rating) curtailed enabling faster resolution• Resolution Plan to be implemented within 180 days of invocation
Bank Perspective	<ul style="list-style-type: none">• Asset classification to remain standard• Lower Provisioning requirement
Doability	<ul style="list-style-type: none">• Greater acceptability for resolution due to regulatory push and COVID factor

Comparison of Restructuring Guidelines – 6th Aug, 2020 vs. 7th Jun, 2019



Particulars	6 th August, 2020	7 th June, 2019
Applicability	'SMA-0' on 1 st March, 2020 and 'Standard' on invocation date	All accounts
Forensic Audit	May not be required citing COVID and if minimum sacrifice for lenders	Insisted
RP Ratings from CRA	1 rating	1 rating (debt <500 Cr) 2 ratings (debt >500 Cr)
Account post restructuring	Standard	NPA
Time bound resolution	Achievable due to less processes	Delayed
Financial parameters	Stringent parameters, if stipulated, may pose challenge	No pre-set parameters; but are guided by a viable resolution plan
ICA adherence by lenders	Disincentives for non-abiding lenders	No such deterrent
Extension of Loan Tenure	Max. 2 years	Guided by Resolution plan
Provisioning	Limited prov. may be acceptable by banks	Higher provisioning may be accepted, basis the viability of plan

Restructuring under 7th June circular, proposes a 'Practical' solution - Despite some challenges therein, it can be attempted in high stressed companies, where 6th August circular may not provide a 'Feasible' resolution

Resolution Options Analysis



Resolution option	Corporate Loan	Restructuring - 6 th Aug'20	Restructuring - 7 th June'19
Cash Flows Mismatch	Low to moderate	Moderate	High
Tenure extension required for existing debt	No	~2 years	Longer timeframe
Rationalization of debt terms	No	Yes	Yes
Unsustainable Debt	Nil	Marginal	High (~30-40%)
Leverage ratios	Low	Moderate	High
Security Cover	High	Moderate	Low
WC mismatch	Low to moderate (manageable with addl. funding)	Addressable with 2 year extension	High

'One-size-fits-all' may not work - Company Specific Resolution Approach should be worked out



Opportunities for Chartered Accountants

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CA fraternity has a significant role in successful restructuring under the RBI framework:

Advisory

- Guidance on the framework specifics with advisory services
- Evaluation and option analysis
- Advising on pros & cons to individual lenders looking to invoke the circular
- Advising clients about their rights under the circular in case of breach in timelines & recourse available

Documentation & Compliances

- Helping clients with compliance of sector specific financial parameters (expected to be submitted by the Expert Committee in coming week)
- Preparation of resolution plan after assessing industry parameters & client specific challenges
- Aiding individuals in completing necessary documentation – including execution of necessary agreements with lenders & ensuring accuracy of terms agreed

Filings, Monitoring & Certifications

- Regulatory and statutory filings
- Stock Audit; Concurrent Audit; & Forensic Audit
- Extension in ASM services by account monitoring & escrow account management
- Aiding in certifications that may be required by clients like
 - i. Net worth certificates
 - ii. Standard Account certificate
 - iii. Valuation certificates etc.



Glad to interact further on this

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