The Role of the Chief Restructuring Officer

By: Tommy M. Onich CTP

As Published in The Commercial Lending Review

Most organizations move along a continuum. Diametrical opposites, the end points of this continuum reflect a very different internal state of affairs.

At one end is the custodial environment, which is relatively stable and resource rich. The organization is profitable with growing revenues as reflected in both margins and market share. This provides access to additional capital if required. Information provided to management is timely, relevant and reliable. It is used by a competent and stable management team.

In these circumstances, there are no threats from creditors. And there are no other threats that represent a clear and present danger.

At the other end of the continuum is distress or crisis, which is a harsh, unforgiving, ambiguous and urgent environment. Losses are likely, with numerous threats from a variety of stakeholders. All important financial indicators – such as sales, margins and market share-are in decline. Often this is masked by reported financial data, which has lost its relevance. In the worst cases, financial data is scarcely being produced. All resources are scarce and the ability to raise capital is seriously impaired. It is impossible for existing management to cope given the enormous demands upon all resources. In fact managers may be taking actions that reinforce the status quo or make the situation worse.

There are many points between the ends of this continuum. The position of the organization may vacillate, dramatically change direction or temporarily stall. While some movement is inevitable, an irreversible decline is not. Often there is an inflection point, a point where there can be a reversal of fortune.

Predictably, businesses at each of these two end points require vastly different management skills, which are unlikely to be possessed by a single individual. In fact, the skills, techniques and methods to be applied are frequently antithetical.

What It Takes to Start a Turnaround

For companies in crisis, reversal depends upon two things, perception and action. Key stakeholders must first perceive that the company may be at a crossroads or at least is facing difficulty. Denial is strong and it is important to understand that only a few warning signs can indicate a malaise with both depth and breadth. (See" The Warning signs of Financial Distress by Tommy M.Onich CTP, Commercial Lending Review, January2007 pg 46).To start a turnaround, management must first be aware of the necessity for a reversal of fortune. Next, managers must embrace the need for additional management support and expertise.

It is unlikely that existing or custodial management will be capable of recovery. Factors that preclude this are time constraints, lack of objectivity and a lack of specific skills.

The appointment of a chief restructuring officer (CRO) gives the entity access to the specific skills necessary for recovery. Often this is a temporary position that is occupied by an individual from outside the organization. This achieves two things. First it provides the organization with clarity of perspective. Second, it provides an implacable force for change that is unencumbered by corporate politics. The CRO will possess one qualification that is essential: He or she will have previously participated in successful recoveries or reorganizations.

Where Does a Restructuring Officer Begin?

The first duty of the CRO is to assist with a fundamental decision. Should the organization attempt to reverse its position? Or must the organization seek other alternatives to recover shareholder value? The process of answering this question also provides key information necessary in forming a turnaround plan.

Under even the best-case scenario, this crucial process is difficult. The worst case is akin to chaos and usually includes a liquidity crisis, multiple threats and seriously flawed financial information. Time is tight and, in the face of failure, a second chance is unlikely. Time determines the tactics of the CRO, who faces a number of challenges simultaneously. These include cash management and an assessment of threats to the organization.

- **Cash management.** Cash is the lifeblood of any organization. First and foremost, the goal is to strictly control disbursement. It is also to husband all resources and seek additional sources of capital from any source. This pursuit must be ruthless in its intent to find additional resources. It must also be flexible in looking at all options unfettered by habit, tradition or emotion.

- **Threats.** Current threats against the organization can originate from many different sources. The most significant threats usually originate from the company's creditors, with secured lenders having primacy.

- It is important that nothing be taken for granted and the secured lenders themselves confirm their latest position. This includes any letters of demand, forbearance or default. In addition all loan documentation from origination should be inventoried and cross checked with lenders. An inventory and review of all outstanding or pending litigation will encompass claims of unsecured creditors including third party claims. It also includes such threats as environmental or human resource issues. Each case must be clearly documented with current information from counsel or source. A central file should be created to consolidate results of this review with key dates and timelines. Above all the goal is to avoid precipitous action from any source. Even a relatively small event, such as a nominal judgment can trigger a downward spiral.

Addressing cash management and conducting a threat assessment help to ensure the short-term survival of the organization. Concurrently, the CRO must seek information that will answer the fundamental question: Should the business seek to reverse its fortunes or not? This question is framed by three other questions:

- Is there a core business that is profitable or nearly so?

- Are there cash resources necessary to support a turnaround?

- Is management competent to provide effective implementation?

The tactics employed to manage cash in the short term will have already provided significant information relevant to these questions. Of necessity, the information gathering will have begun with short-term projections or pro formas. This process will have yielded valuable information with respect to the viability of the core business. The immediate quest for capital may find sources from improved internal efficiencies, the divestiture of redundant assets, new equity or new debt including debtor in possession (DIP) financing. In aggregate, the opening moves of the CRO (defined as cash management and threat assessment) will also yield significant insight into management's capability to meet the requirements of a turnaround.

Given that time is of the essence the decision to attempt recovery or seek other alternatives is made very quickly. The decision process concurrently sets the stage for a plan of recovery. Then the CRO will assist management as an architect of recovery and act as a resolute force for change.

Tommy M.Onich CTP is the president of TCMI with offices in the United States and Canada he can be reached at tonich@turnaroundinternational.com