

## Turnarounds & Workouts

### Spring 2011

#### General Purpose of the **TWO** Course

The **TWO** course is intended for those desiring a deeper understanding of the problems of effecting turnarounds (restructurings, involving less serious treatment, Figure 1) and workouts (resuscitations, which may require notification of next-of-kin, Figure 2) than is available in other courses that briefly treat these matters. The intent is to make the course of relevance to those planning to work in marketing, operations, general management, smaller enterprises, and new ventures as well as those wishing to associate with workout specialists, as illustrated in Figure 3.

The course is *not* intended to qualify participants as experts in the legal and tax niceties, both of which are important but which require counsel from professionals current with the latest developments and rulings. Neither is the course designed to help identify undervalued turnaround opportunities. Although valuation is an element in determining how a restructured company's value may be distributed, this course will focus more on topics such as causes of trouble (and, by implication, warning signs), what can be done to protect and restore a company's health, and dealing with the aggrieved financial sources that are inevitably but unwillingly involved. It is *not* a course in vulture finance.

The complexity of major turnarounds and workouts requires that the course material deal primarily with smaller companies and exclusively with U.S. companies. A basic understanding of the legal and tax environment is critical in effectively resolving a turnaround or workout situation. Painful experience has shown how difficult it is to convey this information for the United States, a familiar jurisdiction, let alone to attempt to convey it for other national jurisdictions in which the rules are dramatically different.

As presently structured, the course will perhaps concentrate more heavily than it should on financial matters, particularly dealing with creditors, reflecting their importance in the process, the instructor's experience, and available material. Nevertheless, the financial focus will be diffused among a variety of financial issues rather than concentrated on valuation. Inevitably, however, as befits a finance course, lower-order numerical analysis will creep into the picture, an aspect that should be considered by those who find these techniques a challenge or boring.

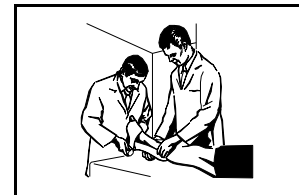


Fig. 1 Turnaround



Fig. 2 Workout



Fig. 3 Workout Specialist

There are no prerequisites for the course. Despite its general-management orientation, however, the course is officially counted as a finance elective. Be sure to include this course in calculating the number of finance electives you take so that you do not unintentionally exceed the maximum you can count toward your degree.\*

The course consists of eight straightforward case discussions, two periods for a workout negotiation activity and report on the outcome, four outside speakers, and a take-home final examination. The course grade will be equally weighted between class participation and the final exam, with the full range of grades from DP to F being available as earned.

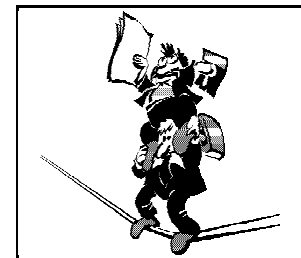
Grading for class participation is based on the quantity and quality of what individuals contribute to the class. Although absences from a regular class are not counted against a participant, it is usually hard for a member of the course to contribute constructively to the discussion if the individual is not present. Furthermore, it is sensible to let me know if you have to miss class so I can indicate what you need to do in order not to be put at a disadvantage in subsequent classes. You should be sure to attend classes conducted by the guests because they will often be covering material that is essential to other classes and even to the final exam. Those who participate in discussion with the guest speakers receive the same credit for that participation they would receive during a regular case discussion.

### Topics Covered

The brief length of the course does not permit lingering on any topic very long. The course will try to tie together the various elements and parties involved in a workout and their roles. These topics include the operating problems of taking over a distressed firm, red flags to watch for, fundamentals of the bankruptcy law and process, perspectives of various players, and working out a deal that is acceptable to all concerned. The course schedule, which follows, associates topics, material, and class meetings.

### The Speakers

The speakers have been selected because they well represent the various important specialties (such as illustrated in Figure 4) that are usually required to bring about a successful turnaround. In several instances, they will have been involved in the cases we are discussing. They will assume that you have prepared whatever advanced material they have asked you to study. *Please do not embarrass the school by coming to a speaker's session unprepared or by behavior (such as answering your cell phone or texting during class) that would adversely reflect on the quality of the student body.*



**Fig. 4** Overhead Specialist

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\* If you should exceed the limit, you will have a workout experience as you attempt to persuade the faculty you should be granted a degree despite the oversight and misunderstanding all around. There will be an interminable and inconclusive discussion at the May faculty meeting about whose fault the error was, resulting in punishment of the innocent, rewards for the guilty, and honors for the uninvolved.

### The Workout Negotiation

The last two class periods, May 5 and 6, are allocated to a workout exercise. The cases for this activity will be distributed at a later date. No class will be held on May 5, but you should reserve that period to use for the negotiation. Otherwise, it will be difficult to schedule a meeting for the eight to twelve participants. During the last class session on May 6, the teams will reveal the resolutions they have agreed to (or their ending positions).

Each team will be divided among creditors, management, and investors. Within each team, specific roles will be assigned and briefed. Teams must therefore consist of at least four individuals but not more than six. Those who wish to form their own groups may submit their names in teams of four to six by April 22, 2011. Those who have not submitted names by the deadline will be assigned randomly (including being assigned to existing short-staffed teams) so that the total constitutes an even number of properly sized groups. You will be reminded again about the voluntary formation of groups. After the teams have been settled, the individual roles will be distributed.

### Sundry Notes

Please scan technical note, *Corporate Bankruptcy* (UVA-F-0490), included in your course book, as soon as possible. A grasp of at least the rudiments of who stands where in the process is helpful even in several of the early cases. In addition, a few copies of *Financial Turnarounds: Preserving Value* are in the library on reserve for the course. You may find it useful to scan Chapters 2 (the executive summary), 4, and 5 as well as pages 18-25.

Considering the time, effort, opportunity cost, and even out-of-pocket expense the guest speakers (or Darden) will be incurring in order to be with the class, it would be rude for a course participant to cut any of those classes. Absences reflect very poorly on Darden; in the current competitive educational environment we need all the good reputation we can get. *Your participation during guest presentations does count when the format permits,\** and your absence could adversely affect the assessment of your performance. If you have an unavoidable problem, please let me know in advance in order to minimize damage. The relevant dates are:

Wednesday, April 6  
Friday, April 8  
Thursday, April 14  
Wednesday, April 20  
Wednesday, April 27  
Thursday, April 28

There are few, if any, occasions for which elaborate numerical development is required. *Therefore, computers will be closed during class unless otherwise announced.* Class preparation should be completed and printed out as necessary in advance of class.

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\* In fact, it is usually easier to provide accurate credit for class participation when a guest is presenting.

## **Turnarounds & Workouts** *Spring 2011*

### *Assignments*

\*By the end of the second week, you should have read: *Corporate Bankruptcy* (UVA-F-0490)

**Thursday, March 31**      ♦To Be or Not To Be

Case: *PROSitis, Inc.* (UVA-F-1099)

**Friday, April 1**      ♦Taking Charge

Case: *The Company Store (A)* (UVA-F-0994)

**Wednesday, April 6**      ♦How Are We Doing?

Case: *To be announced*

Guest: Mr. H. B. Turner, former CEO of Ardshiel, will conduct the class.

**Thursday, April 7**      ♦Indica of Distress

Case: *Sherwood Sound Systems, Inc.* (UVA-F-1248)

Scan: "Attention to Seven Warning Signs Can Keep Companies Out of Trouble," by C. Charles Bahr, III

**Friday, April 8**      ♦The Accountant's Perspective

Guest: Mr. Seymour Jones, Visiting Lecturer at the Darden School and Professor of Accounting at New York University; formerly Partner, Coopers & Lybrand with responsibility for the firm's practice in emerging businesses and troubled companies.

**Wednesday, April 13**      ♦Dealing with Adverse Industry Developments

Case: *SWC Corporation (A)* (UVA-F-0977)

Scan: *How Not to Go Bankrupt in the First Place*, by C. Charles Bahr, III.

**Thursday, April 14**      ♦Effecting Turnarounds

Guest: Mr. Henry B. Schacht, Senior Advisor, Warburg Pincus, and formerly CEO of Cummins Engine and Lucent Technologies.

**Wednesday, April 20**      ♦And Now What?

Guest: Mr. David Steadman, Visiting Lecturer and Principal, Atlantic Management Associates, Inc.

**Thursday, April 21**      ♦Introduction to Unidimensional Problems

Case: *To be announced*

**Friday, April 22**      ♦Introduction to Multidimensional Problems

Case: *Desmond Distribution, Inc. (A)* (UVA-F-1249)

**Wednesday, April 27**      ♦The Bankruptcy Law and Process

Guest: Michael A. Policano

Mr. Policano spent 25 years advising major stakeholders, such as Morgan Stanley, in financially troubled situations, such as Enron and Xerox. He is currently an adjunct professor at Villanova, where he teaches Crisis Leadership in the MBA program. He is author of “Excuse Me, Aren’t You in Charge?”

Read: If you have not yet completed reading *Corporate Bankruptcy* (UVA-F-0490), you should take this opportunity to finish it before the course goes further. “Damage Control for Bank Capital,” by Paul H. Hunn, up to the “Cash Flow” heading on page 5. (You are of course welcome to scan the rest of the article.)

Ref: The excerpt on United States’ bankruptcy procedures from “Solving the Insoluble,” *International Financial Law Review*, June 1990, pp. 50-62, is provided as reference you may wish to scan for reinforcement after Mr. McDonagh’s talk.

**Thursday, April 28**      ♦Resolving a Multidimensional Problem

Case: *Waverly Corporation* (UVA-F-1327) (Mr. Policano will conduct the discussion)

**Wednesday, May 4**      ♦When the Vultures Begin to Circle

Case: *Medici Internet Systems, Inc.* (UVA-F-1329)

This case was the final exam in the Spring of 2001. The question was:

What should Mr. Magnifico do to resolve the problems that have arisen with the Guelf merger and the “1999-1” investors’ plan to exercise their warrants? If you decide he should threaten to resign, indicate the minimum terms acceptable for him to withdraw his threat.

**Thursday, May 5**      ◆Reserved for Negotiations

Case: *Tempo National Bank (UVA-F-0732)*

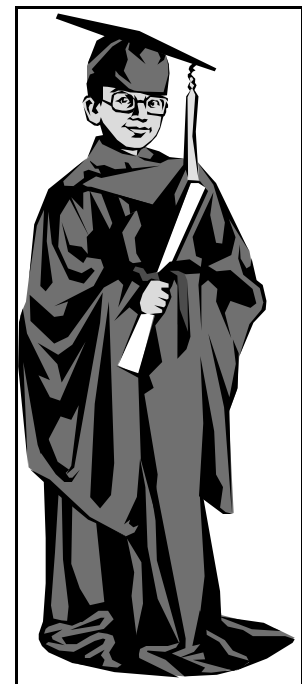
You should reserve this period to accomplish the negotiations case. (See introductory memorandum. Further instructions and material will be distributed separately.)

**Friday, May 6**      ◆Report on results of negotiations.

**Tuesday, May 10**      ◆4:00 p.m., take-home examination distributed to your mailbox

**Thursday, May 12**      ◆4:30 p.m., examination due at Ms. Shelton's office, FOB-265

**Sunday, May 22**      See Figure 1



**Fig. 1** Restructured Assets, Somewhat Reduced in Size but with Higher Income Potential, Ready for Reissue to the Public with a Challenging Capital Structure