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# Analysis of the Restructuring of Bad Credit Agreements in Conventional Banks

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## ABSTRACT

Credit restructuring is a crucial mechanism in the banking sector designed to protect the interests of both creditors and debtors who are experiencing financial distress. In essence, restructuring serves as a remedial policy aimed at preventing loans from deteriorating into non-performing status while preserving the continuity of viable businesses. Rather than immediately enforcing collateral execution or initiating legal proceedings, banks may modify the original loan agreement to restore the borrower's repayment capacity. This process typically involves adjusting credit terms through interest rate reductions, extension of loan maturities, rescheduling of installment payments, conversion of short-term obligations into longer-term facilities, or, in certain cases, partial principal reduction. These measures are intended to realign debt obligations with the borrower's current cash flow conditions. In Indonesia, regulatory frameworks established by the Financial Services Authority (OJK) and Bank Indonesia provide a strong legal and prudential basis to ensure that restructuring is conducted transparently, objectively, and in accordance with sound risk management principles. For creditors, restructuring minimizes potential losses, preserves asset quality, and prevents a sharp increase in non-performing loans that could weaken capital adequacy. For debtors, it offers financial relief, protects business sustainability, and helps maintain employment and economic productivity. Although risks such as moral hazard, repeated default, and legal disputes may arise, effective supervision, fair mediation, and continuous performance evaluation can mitigate these challenges. When implemented prudently, credit restructuring becomes a strategic instrument for safeguarding financial system stability, particularly during periods of economic uncertainty or crisis.

**Keywords:** Restructuring, Credit Agreements, Banking.

## I. Introduction



Banks occupy a pivotal position in modern financial systems as institutions that mobilize savings and channel them into productive investments. In Indonesia, as stipulated in Article 1 of Law No. 10 of 1998 (amending Law No. 7 of 1992 on Banking), a bank is defined as a business entity that collects funds from the public in the form of deposits and redistributes them in the form of credit or other financial instruments to improve public welfare. This statutory mandate reflects the broader economic function of banking institutions as catalysts of regional and national development. By facilitating credit intermediation, banks contribute to capital formation, entrepreneurship, and economic growth. Empirical evidence consistently demonstrates that efficient financial intermediation strengthens economic resilience and enhances macroeconomic stability (Beck, 2018; Demirgüç-Kunt, Pedraza, & Ruiz-Ortega, 2021). In recent years, the banking industry has undergone rapid structural transformation, characterized by intensified competition, digital innovation, and regulatory evolution. The expansion of both conventional and Islamic banking institutions in Indonesia has heightened competitive pressures, compelling banks to innovate continuously in credit products, deposit schemes, and digital financial services. Digitalization, fintech integration, and data-driven risk management have become central to strategic differentiation (Vives, 2019; Thakor, 2020). While such innovation enhances efficiency and customer outreach, it also introduces new dimensions of credit risk, particularly in highly competitive lending markets where risk appetite may increase. Credit provision remains the core business of conventional banks. Lending activities generate the majority of banking income but simultaneously expose banks to default risk. The sustainability of banking operations is therefore highly contingent upon the quality of loan portfolios. Non-performing loans (NPLs) represent one of the most critical threats to banking stability, as they erode profitability, impair capital adequacy, and constrain future lending capacity (Klein, 2017; Ahamed & Mallick, 2019). Elevated NPL ratios can trigger systemic vulnerabilities, particularly in emerging markets where financial systems may be less diversified and more susceptible to external shocks (International Monetary Fund [IMF], 2022).

The global economic disruptions triggered by the COVID-19 pandemic further amplified concerns regarding credit quality. Lockdowns, supply chain disruptions, and declining business revenues significantly affected borrowers' repayment capacity, leading to a surge in distressed loans across jurisdictions (World Bank, 2021). In response, regulators worldwide introduced extraordinary policy measures, including loan restructuring programs, payment moratoria, and regulatory forbearance, to prevent a sharp escalation of NPLs and preserve financial stability (BIS, 2021; Demirgüç-Kunt et al., 2021). These developments underscore the strategic importance of credit restructuring as a mechanism for mitigating credit risk while maintaining banking sector resilience. Credit restructuring refers to the modification of loan terms granted to borrowers experiencing financial difficulty but deemed to have viable business prospects. Restructuring mechanisms may include interest rate reductions, loan maturity extensions, installment rescheduling, partial principal forgiveness, or debt conversion to equity. The objective is not merely to delay recognition of losses, but to restore the borrower's repayment capacity and prevent further deterioration of asset quality. When implemented prudently, restructuring can reduce default probability, preserve banking relationships, and support economic recovery (Agarwal, Amromin, Ben-David, Chomsisengphet, & Piskorski, 2017; IMF, 2022). However, credit restructuring also presents regulatory and ethical challenges. Improper or excessive restructuring may lead to "evergreening," whereby banks repeatedly roll over distressed loans to avoid classifying them as non-performing. Such practices can obscure the true financial condition of banks and delay necessary corrective actions (Klein, 2017). Consequently, regulatory frameworks emphasize the importance of transparency, accurate loan classification, and adequate provisioning to ensure that restructuring does

not undermine prudential standards (BIS, 2021). In Indonesia, the Financial Services Authority (OJK) has issued guidelines governing credit restructuring, particularly during periods of economic distress, to balance financial stability with sound risk management.

From a theoretical perspective, credit restructuring can be examined through the lens of risk management and financial intermediation theory. Banks operate under asymmetric information conditions, where borrowers possess superior knowledge regarding their financial condition and business prospects. Effective restructuring therefore requires comprehensive credit assessment, monitoring, and renegotiation mechanisms to mitigate moral hazard and adverse selection (Thakor, 2020). Moreover, relationship banking theory suggests that long-term interactions between banks and borrowers can facilitate efficient renegotiation, as accumulated information reduces uncertainty and transaction costs (Beck, 2018). In highly competitive banking environments, institutions often engage in aggressive lending strategies to expand market share. Lower interest rates, simplified credit approval processes, and higher credit ceilings may attract customers but simultaneously increase exposure to credit risk. Empirical studies indicate that intensified competition can weaken lending standards and contribute to future loan deterioration if not accompanied by robust risk governance (Ahamed & Mallick, 2019; Vives, 2019). Therefore, the management of non-performing loans through restructuring becomes a critical component of sustainable banking strategy. The Indonesian banking sector provides a particularly relevant context for examining credit restructuring. As an emerging economy with a growing middle class and expanding micro, small, and medium enterprise (MSME) sector, Indonesia relies heavily on bank financing to support economic activities. MSMEs, while vital for employment and innovation, are also more vulnerable to economic shocks and liquidity constraints (World Bank, 2021). Consequently, restructuring policies targeting MSME loans have been instrumental in preventing widespread defaults during economic downturns. Nevertheless, questions remain regarding the long-term implications of such policies on asset quality, profitability, and moral hazard.

Furthermore, the increasing integration of digital technologies in credit assessment—such as alternative data analytics and machine learning—has altered the landscape of credit risk management. While digital tools enhance predictive accuracy and operational efficiency, they do not eliminate the fundamental uncertainty associated with borrower behavior (Thakor, 2020). Thus, when credit distress occurs, banks must still rely on qualitative judgment, negotiation capacity, and regulatory compliance in executing restructuring strategies. Given these dynamics, analyzing the restructuring of non-performing credit agreements in conventional banks is both theoretically and practically significant. First, it contributes to the literature on credit risk mitigation by exploring how contractual renegotiation can function as a strategic response to borrower distress. Second, it provides insights into the balance between financial stability objectives and prudential risk management. Third, it informs policymakers and banking practitioners regarding best practices in implementing restructuring mechanisms without compromising transparency and accountability. This study therefore seeks to examine the legal, economic, and managerial dimensions of restructuring non-performing credit agreements in conventional banking institutions. By integrating regulatory analysis with contemporary risk management perspectives, the research aims to elucidate how restructuring policies can simultaneously safeguard bank solvency and support debtor recovery. In doing so, it responds to recent calls in the literature for more nuanced understanding of post-crisis credit management strategies in emerging markets (IMF, 2022; World Bank, 2021). In conclusion, as banking systems confront evolving economic uncertainties, credit restructuring emerges as a strategic instrument situated at the intersection of law, finance, and risk governance. While it offers a pathway to mitigate credit deterioration and sustain

economic activity, its effectiveness depends on rigorous assessment, transparent implementation, and strong regulatory oversight. A comprehensive analysis of restructuring practices in conventional banks is therefore indispensable for advancing both academic discourse and policy formulation in the contemporary financial landscape.

## II. Literature Review and Hypothesis Development

### 2.1. General Overview of Credit

#### 2.1.1. Definition and Conceptual Foundations of Credit

The concept of credit originates from the Latin word *credere*, meaning trust or belief. In its most fundamental sense, credit embodies a relationship built upon confidence—confidence that resources transferred today will be returned in the future under agreed conditions. This notion of trust forms the institutional backbone of modern financial systems. Without trust, financial contracts would be unenforceable, transaction costs would escalate, and economic exchange would become inefficient (Guiso, Sapienza, & Zingales, 2004). Thus, credit is not merely a financial mechanism but also a social construct embedded in legal, institutional, and governance frameworks. In modern banking, credit reflects a legally binding contractual relationship in which a lender provides funds to a borrower based on the expectation of future repayment with compensation, usually in the form of interest. This intertemporal exchange involves risk pricing, contractual enforcement, and monitoring mechanisms. According to Diamond (1984), financial intermediaries play a critical role in delegated monitoring, reducing agency costs between savers and borrowers. The existence of formal loan agreements ensures clarity regarding rights and obligations, including principal amount, maturity, repayment structure, and default consequences.

This trust-based foundation constitutes the core mechanism of financial intermediation. Banks collect funds from surplus units—primarily households—and channel them to deficit units such as firms and entrepreneurs. Through this intermediation process, banks reduce transaction costs, diversify risks, and allocate capital efficiently (Levine, 2005). Empirical evidence consistently shows that well-developed financial systems are positively associated with long-term economic growth and capital accumulation (Beck, 2018; King & Levine, 1993). By facilitating productive investment, credit supports innovation, employment generation, and structural transformation in both advanced and emerging economies. From a legal standpoint, Indonesian Banking Law No. 7 of 1992 as amended by Law No. 10 of 1998 defines credit as the provision of money or equivalent claims based on a loan agreement requiring repayment within a specified period with interest or other compensation. This definition highlights the contractual, economic, and risk-bearing dimensions of lending. The legal enforceability of credit agreements strengthens creditor rights, which in turn influences lending volume and financial stability (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1998). In financial theory, credit is considered the primary asset-generating activity of commercial banks and the main source of profitability (Thakor, 2020). Loans typically constitute the largest component of bank assets, and interest income remains the dominant revenue stream in traditional banking models. The structure and quality of loan portfolios significantly determine financial performance indicators such as return on assets and return on equity (Athanasoglou, Brissimis, & Delis, 2008). Consequently, credit management becomes central to maintaining both profitability and solvency.

However, credit activities inherently expose banks to credit risk, defined as the probability that a borrower will fail to meet contractual obligations. Credit risk arises due to asymmetric information, macroeconomic volatility, and borrower-specific factors. Stiglitz and Weiss (1981) demonstrated that imperfect information in credit markets may lead to adverse selection and credit rationing, even when borrowers are willing to pay higher interest rates. Such inefficiencies highlight the importance of robust screening and monitoring systems. Credit risk remains the most significant source of banking instability globally (Ahamed & Mallick, 2019). Historical financial crises frequently originate from excessive credit expansion followed by asset quality deterioration. Research shows that rapid credit growth often precedes banking crises, particularly when accompanied by weak regulatory oversight (Schularick & Taylor, 2012). When loan performance deteriorates, non-performing loans (NPLs) increase, eroding bank capital and constraining future lending capacity. High levels of non-performing loans weaken capital buffers and reduce banks' intermediation capacity (IMF, 2022). Persistent NPL problems may lead to a "credit crunch," limiting access to financing for productive sectors and slowing economic recovery (Bernanke & Gertler, 1989). In emerging markets, where banks serve as the primary financial intermediaries, elevated credit risk may create systemic vulnerabilities and macroeconomic instability (Rajan & Zingales, 1998).

The relationship between competition and risk-taking in banking further complicates credit management. While competition can enhance efficiency and lower borrowing costs, it may also incentivize banks to assume greater risk to maintain profitability (Vives, 2019). Empirical studies indicate that excessive competitive pressures can weaken lending standards and increase portfolio risk if governance mechanisms are insufficient (Boyd & De Nicolo, 2005). Therefore, regulatory supervision and internal risk controls are critical in balancing growth and stability. Prudent credit analysis remains fundamental to banking sustainability. Traditional credit evaluation frameworks such as the 5C principles—character, capacity, capital, collateral, and conditions—are complemented by quantitative risk models, stress testing, and portfolio diversification strategies. Modern regulatory standards, including capital adequacy frameworks under Basel accords, emphasize risk-based supervision and capital buffers to absorb unexpected losses (BIS, 2021). Ultimately, credit serves as both an engine of economic development and a potential source of financial fragility. When managed prudently, credit stimulates investment, supports entrepreneurship, and fosters inclusive growth. However, when risk governance fails, excessive lending may culminate in systemic crises. As Minsky (1986) argued, financial systems are inherently prone to instability when credit expansion becomes detached from underlying economic fundamentals. Therefore, sustaining trust—the essence of *credere*—requires sound governance, prudent regulation, and disciplined risk management practices.

### 2.1.2. Credit Analysis and Risk Assessment

Before granting credit, banks conduct comprehensive assessments to evaluate borrower feasibility and repayment capacity. This process aims to mitigate asymmetric information and reduce moral hazard. Relationship banking theory suggests that accumulated borrower information enhances monitoring efficiency and facilitates renegotiation in times of distress (Beck, 2018). Empirical evidence indicates that weak underwriting standards and aggressive competition increase the likelihood of future NPL accumulation (Ahamed & Mallick, 2019). Furthermore, macroeconomic shocks significantly influence credit performance. The COVID-19 pandemic, for example, severely disrupted borrower cash flows and heightened credit risk across banking systems worldwide (Demirgüç-Kunt, Pedraza, & Ruiz-

Ortega, 2021). External shocks such as economic downturns or global crises may impair even well-assessed loans. During systemic crises, governments and regulators often introduce extraordinary measures to prevent widespread defaults and maintain financial stability (BIS, 2021). In this context, credit restructuring emerges as a strategic instrument for mitigating loan deterioration while preserving economic continuity.

## 2.2. General Overview of Credit Restructuring

### 2.2.1. Definition and Objectives of Credit Restructuring

Credit restructuring refers to corrective measures undertaken by banks to modify loan agreements for borrowers experiencing financial distress but retaining viable long-term prospects. The primary objective is to restore repayment capacity while safeguarding the bank's financial interests. From a regulatory perspective, restructuring gained prominence during the COVID-19 crisis, when authorities worldwide introduced temporary forbearance frameworks to avoid a sudden surge in NPLs (BIS, 2021; IMF, 2022). Research demonstrates that timely restructuring can reduce default probability and improve recovery outcomes compared to immediate legal enforcement (Agarwal et al., 2017). The theoretical justification for restructuring is grounded in efficient renegotiation theory. When liquidation value is lower than continuation value, renegotiation maximizes joint surplus between creditor and debtor (Thakor, 2020). However, regulators caution against "evergreening," a practice in which banks repeatedly extend distressed loans to avoid recognizing losses, potentially masking systemic fragility (Klein, 2017). Thus, restructuring must be implemented transparently and accompanied by proper asset classification and provisioning to prevent regulatory arbitrage (IMF, 2022).

### 2.2.2. Distinction Between Credit Rescue and Legal Settlement

The resolution of non-performing loans can follow two main pathways: negotiated restructuring (credit rescue) or legal enforcement (credit settlement). Negotiated restructuring involves revising loan terms through mutual agreement, while legal enforcement entails court proceedings, arbitration, or collateral liquidation. Empirical studies suggest that negotiated restructuring is often more cost-efficient and time-effective than litigation, particularly in jurisdictions with slow judicial processes (IMF, 2022). Moreover, relationship-based renegotiation can preserve long-term banking relationships and reduce transaction costs (Beck, 2018). Nevertheless, restructuring must be based on rigorous viability assessment to avoid moral hazard. Evidence from crisis-period policies shows that targeted restructuring for viable borrowers contributes positively to financial stability, whereas indiscriminate forbearance may undermine asset transparency (Demirgüç-Kunt et al., 2021).

## 2.3. Forms of Credit Restructuring

Credit restructuring in conventional banking may take multiple forms, each with distinct financial implications:

- a. Interest Rate Reduction  
A reduction in interest rates decreases the borrower's periodic payment burden and may help restore short-term liquidity. This mechanism is commonly applied in cases of temporary cash-flow distress (BIS, 2021).
- b. Extension of Loan Maturity (Rescheduling)  
Extending the loan maturity period enables borrowers to spread repayment obligations over a longer time horizon, thereby improving debt sustainability and reducing immediate financial pressure (IMF, 2022).
- c. Reduction or Waiver of Interest Arrears  
The partial or full waiver of accrued interest can strengthen repayment incentives and improve overall recovery outcomes by making the outstanding obligation more manageable (Agarwal et al., 2017).
- d. Principal Reduction  
Although financially costly for banks, a reduction in the loan principal may generate higher net recovery compared to liquidation, particularly when the continuation value of the business exceeds the collateral value (Thakor, 2020).
- e. Additional Credit Facilities  
The provision of supplementary credit to financially viable firms may support business recovery and operational continuity, especially in the MSME sector, which is often disproportionately affected during economic downturns (World Bank, 2021).
- f. Debt-to-Equity Conversion  
Converting outstanding debt into equity can align incentives between banks and borrowers, particularly in corporate restructuring scenarios where long-term viability is anticipated (IMF, 2022).
- g. Collateral Takeover (Set-Off)  
The takeover of collateral assets may be executed through formal legal mechanisms. However, high transaction costs, legal complexity, and regulatory constraints often reduce its efficiency compared to negotiated restructuring arrangements (Klein, 2017).

#### 2.4. Eligibility Criteria for Credit Restructuring

The determination of borrower eligibility constitutes one of the most critical stages in the implementation of credit restructuring. Prudential banking regulations consistently emphasize that restructuring must not be applied indiscriminately but rather based on objective, transparent, and viability-oriented criteria. This requirement is rooted in the need to balance financial stability with risk discipline. While restructuring can serve as an effective mechanism for mitigating non-performing loans (NPLs), poorly targeted forbearance may generate moral hazard, distort asset quality reporting, and weaken long-term banking resilience (International Monetary Fund [IMF], 2022). Therefore, eligibility assessment operates as a gatekeeping function designed to ensure that restructuring supports economically viable borrowers rather than merely postponing inevitable default. One of the primary criteria for restructuring eligibility is the existence of genuine financial distress. Borrowers must demonstrate that their repayment difficulties arise from identifiable economic, operational, or external shocks rather than from chronic insolvency or deliberate non-compliance. Regulatory guidance issued

during systemic crises underscores that restructuring measures should target borrowers facing temporary liquidity constraints rather than structural unviability (Bank for International Settlements [BIS], 2021). The distinction between illiquidity and insolvency is fundamental: illiquid borrowers may recover under adjusted repayment terms, whereas insolvent borrowers lack sufficient underlying economic capacity to honor obligations even after modification. Empirical analyses of crisis-period interventions reveal that restructuring programs are most effective when focused on borrowers whose distress is shock-induced and reversible (Demirgüç-Kunt, Pedraza, & Ruiz-Ortega, 2021). In practical terms, genuine financial distress must be substantiated through verifiable documentation, including updated financial statements, income records, cash-flow projections, and evidence of revenue decline.

Banks frequently conduct site visits and independent verification procedures to ensure the reliability of submitted data. The requirement for demonstrable distress also mitigates adverse selection risks, preventing strategic default behavior in which borrowers seek restructuring despite having adequate repayment capacity. Research indicates that transparent eligibility screening significantly reduces opportunistic borrower behavior and enhances post-restructuring performance (Agarwal et al., 2017). Beyond temporary distress, banks must evaluate whether the borrower maintains positive business prospects. Viability assessment is forward-looking and involves analyzing long-term sustainability rather than merely current financial hardship. According to international financial stability assessments, restructuring is justified when continuation value exceeds liquidation value, meaning that maintaining the borrower's operations yields greater economic benefit than asset seizure and disposal (IMF, 2022). This viability principle aligns with efficient renegotiation theory, which posits that debt restructuring maximizes joint surplus when the borrower's business remains fundamentally productive (Thakor, 2020). The evaluation of business prospects typically involves assessing market position, competitive advantages, operational efficiency, and sectoral outlook. In emerging economies, small and medium-sized enterprises (SMEs) often experience temporary volatility but retain strong long-term growth potential. Studies show that targeted restructuring for viable SMEs contributes positively to economic recovery and employment preservation without substantially increasing systemic credit risk (World Bank, 2021). However, viability assessment must be grounded in realistic cash-flow projections and stress-testing scenarios. Overly optimistic assumptions may lead to repeated restructuring cycles, thereby eroding asset quality transparency. Another essential eligibility criterion concerns good faith and cooperative behavior. The restructuring process is inherently relational and relies heavily on transparent communication between creditor and debtor. Relationship banking literature highlights that information exchange and trust accumulation reduce monitoring costs and facilitate efficient renegotiation (Beck, 2018).

Debtors who proactively disclose financial conditions, comply with documentation requirements, and demonstrate willingness to adhere to revised payment schedules are more likely to succeed under restructuring arrangements. Conversely, lack of transparency increases moral hazard and undermines restructuring effectiveness. Regulatory authorities have cautioned against "evergreening" practices in which distressed borrowers exploit leniency without genuine repayment commitment (BIS, 2021). Empirical findings indicate that restructuring outcomes are significantly improved when banks incorporate behavioral assessments, including repayment history and responsiveness during negotiation phases (Demirgüç-Kunt et al., 2021). Thus, eligibility is not solely a financial calculation but also an evaluation of debtor integrity and engagement. Closely linked to viability and good faith is the requirement that restructuring demonstrably improves expected collectability relative to alternative enforcement mechanisms. From a prudential standpoint, restructuring should only be granted if

projected recovery under modified terms exceeds the anticipated recovery from collateral liquidation or legal proceedings. Comparative recovery analysis is therefore integral to eligibility determination. In jurisdictions with slow judicial processes or volatile collateral markets, restructuring may offer superior net present value outcomes compared to litigation (IMF, 2022). However, banks must quantify such projections using conservative assumptions to avoid overstating recovery potential. Improved collectability is often evaluated through discounted cash-flow models, collateral revaluation, and scenario-based stress testing. By integrating forward-looking risk assessment tools, banks can determine whether restructuring enhances asset quality classification prospects. Research on post-pandemic restructuring frameworks demonstrates that well-designed eligibility filters significantly reduced the long-term accumulation of hidden NPLs (BIS, 2021).

The emphasis on collectability improvement also aligns with prudential capital regulation principles, ensuring that restructuring does not compromise solvency standards. In addition to these core criteria, many regulatory frameworks require internal governance safeguards to ensure consistency and accountability in eligibility decisions. Credit committees, independent risk management units, and compliance oversight mechanisms typically review restructuring proposals. Strong governance structures prevent discretionary abuse and ensure alignment with regulatory expectations (Thakor, 2020). The integration of internal control systems further reinforces transparency and supports supervisory confidence. Empirical studies examining restructuring programs implemented during global crises suggest that targeted eligibility criteria contribute to macro-financial stability. For instance, evidence from pandemic-related interventions indicates that countries applying strict viability-based screening experienced lower subsequent NPL spikes compared to jurisdictions with broad, indiscriminate forbearance policies (Demirgüç-Kunt et al., 2021). This finding underscores the importance of eligibility discipline as a determinant of long-term financial system resilience. Ultimately, eligibility criteria serve as a balancing mechanism between debtor rehabilitation and banking prudence. By requiring demonstrable financial distress, positive business prospects, cooperative behavior, and improved collectability projections, banks ensure that restructuring remains a corrective instrument rather than a concealment strategy. Properly implemented eligibility assessment enhances transparency, mitigates moral hazard, and preserves capital adequacy. In this sense, eligibility criteria are not merely administrative prerequisites but foundational safeguards underpinning the legitimacy and sustainability of credit restructuring practices within conventional banking systems.

### III. Research Method

This study employs a qualitative research design aimed at comprehensively understanding the mechanism of restructuring non-performing credit agreements in conventional banks and its alignment with principles of justice within the Indonesian legal framework. A qualitative approach is considered appropriate because the phenomenon under examination involves legal interpretation, institutional discretion, contractual renegotiation, and the interaction between banks and debtors. These elements cannot be adequately captured through quantitative measurement, as they require contextual depth and interpretative analysis. The research therefore seeks to explore how restructuring practices are implemented in real settings, how decisions are formulated, and how fairness is perceived and operationalized in the restructuring process. Qualitative research emphasizes naturalistic inquiry, allowing the researcher to investigate phenomena within their actual institutional and social context. In the case of credit restructuring, the process does not merely concern financial calculations but also

involves legal compliance, negotiation dynamics, regulatory considerations, and ethical judgments. By directly engaging with the field, the researcher is able to observe how restructuring mechanisms function in practice, particularly in situations where debtors experience financial distress yet retain potential business viability. This approach enables a deeper understanding of how banks balance prudential risk management with equitable treatment of borrowers. The research adopts a descriptive qualitative orientation, focusing on systematically describing and analyzing the procedures, criteria, and legal implications of restructuring non-performing loans. Rather than testing hypotheses, the study seeks to provide a detailed account of how restructuring agreements are formed, what considerations guide decision-making, and how contractual modifications are justified within existing regulatory frameworks. The descriptive nature of the research allows for a structured exploration of restructuring practices while maintaining analytical depth.

Data collection is conducted through multiple qualitative techniques to ensure comprehensive coverage of the research problem. Primary data are obtained through in-depth, semi-structured interviews with relevant stakeholders, including bank officers involved in credit management and restructuring decisions, as well as legal practitioners familiar with banking dispute resolution. These interviews are designed to capture experiential insights regarding eligibility assessments, negotiation processes, risk evaluation, and perceptions of fairness. Where feasible, perspectives from debtors who have undergone restructuring are also considered to provide a balanced understanding of the contractual relationship. In addition to interviews, the study incorporates document analysis as a critical data source. Relevant documents include credit agreements, restructuring addenda, internal banking policies, and applicable financial regulations issued by the Financial Services Authority (OJK). The examination of these documents provides normative grounding for the analysis, enabling the researcher to compare formal regulatory standards with practical implementation. Observation, where accessible, further enriches the dataset by allowing the researcher to understand procedural practices in restructuring negotiations and administrative processes. To enhance the credibility of the findings, the research applies a triangulation strategy by cross-verifying information obtained from interviews, documents, and observations. This approach reduces the risk of subjective bias and strengthens interpretative reliability. The data analysis process follows an interactive qualitative model involving data reduction, thematic categorization, and interpretative synthesis.

Collected data are systematically organized into thematic clusters, such as forms of restructuring, legal justification, eligibility criteria, institutional constraints, and justice considerations. Patterns emerging from these themes are then analyzed in relation to contractual principles, prudential banking norms, and broader notions of fairness in financial relationships. The focus of this study is confined to restructuring practices in conventional banking institutions, particularly in cases involving non-performing loans. The analysis concentrates on the legal and procedural dimensions of restructuring, including modifications of interest rates, extension of loan tenors, reduction of arrears, principal adjustments, additional credit facilities, and debt-to-equity conversion. Special attention is given to how these mechanisms are structured in addendum agreements and how banks determine whether a debtor qualifies for restructuring based on financial distress and business viability assessments. The overarching objective of restructuring non-performing credit agreements is to provide a sustainable solution that enables debtors to fulfill their obligations under lighter and more realistic repayment schemes. Such measures may involve extended maturities, lower interest rates, installment adjustments, or other contractual modifications designed to restore repayment capacity. Importantly, restructuring does not function as debt elimination; rather, it constitutes a strategic

renegotiation mechanism aimed at preserving economic continuity while safeguarding the financial stability of the bank. From the banking perspective, restructuring seeks to minimize losses arising from non-performing status, maintain asset quality, and avoid the time and cost burdens associated with litigation or collateral liquidation. From the debtor's perspective, restructuring offers an opportunity for financial recovery and business continuity. Thus, the restructuring process embodies a negotiated balance between economic efficiency and contractual justice. Through this qualitative and contextual analysis, the study aims to contribute to a deeper understanding of how legal norms and financial practices interact in shaping fair and sustainable credit restructuring mechanisms within Indonesia's conventional banking sector.

#### IV. Result and Discussion

The empirical findings of this study are derived from field observations, in-depth interviews with bank officers, and document analysis of restructuring agreements and internal credit policies. The data indicate that credit restructuring in conventional banks is a selective and viability-based mechanism rather than an automatic entitlement for all non-performing borrowers. Only debtors who demonstrate good faith, cooperative behavior, and realistic business prospects are considered eligible for restructuring. This selectivity reflects the prudential nature of restructuring as a risk management instrument rather than a debt forgiveness policy. The findings reveal that restructuring is positioned by banks as a credit rescue mechanism aimed at preserving asset quality while simultaneously providing financially distressed borrowers with an opportunity for recovery. In practice, restructuring is preceded by a comprehensive assessment of the debtor's financial condition, operational viability, and collateral value. Banks emphasize that restructuring is not intended to eliminate debt obligations but to recalibrate contractual terms in accordance with the debtor's actual repayment capacity. The procedural implementation of credit restructuring generally begins with an initiation phase. This initiative may originate either from the bank, after identifying a loan as non-performing, or from the debtor, who submits a formal request for relief. In many observed cases, the bank first contacts the debtor through written notifications or telephone communication to discuss possible resolution pathways. At this stage, the bank typically offers two alternatives: liquidation of collateral or restructuring of the credit agreement. If the debtor opts for restructuring, a formal written application is required. Subsequently, the bank conducts a site visit to verify the debtor's business activities, financial condition, and collateral status. During this phase, negotiations take place regarding possible adjustments, including interest rate reductions, maturity extensions, partial waiver of arrears, or other forms of contractual modification.

The bank then performs a detailed financial and business feasibility analysis to determine whether the proposed restructuring scheme is capable of improving loan collectability. Following internal approval, the restructuring decision is formalized through an addendum to the original credit agreement. Supporting documentation—such as minutes of negotiation meetings, collateral revaluation reports, business assessment results, and site visit records—forms an integral part of the approval process. Once the restructuring agreement is executed, the bank proceeds to the monitoring phase, which involves periodic evaluation of the debtor's business performance and repayment compliance. From a contractual perspective, restructuring represents a dynamic modification of the credit relationship. The principal obligation remains intact, but its terms are adjusted to restore proportionality between the debtor's capacity and contractual burden. In this sense, restructuring reflects corrective justice within contractual relations, addressing imbalances caused by changing

economic circumstances while maintaining the binding force of agreements. However, the study also identifies several obstacles in the implementation of restructuring agreements. A significant portion of these challenges originates from the debtor side. Some debtors are difficult to contact, reluctant to provide transparent financial information, or inconsistent in fulfilling obligations after restructuring approval. In several cases, debtors resumed payment for a limited period—typically two or three months—before defaulting again. Such behavior increases the risk of repeated restructuring and potential moral hazard. Another recurring issue concerns discrepancies between the information provided by debtors and actual field conditions. In certain instances, documentation submitted by debtors did not accurately reflect real business operations or financial capacity. These inconsistencies complicate the bank's analytical process and may lead to suboptimal restructuring decisions. From the institutional perspective, banks also face structural constraints, particularly limitations in human resources for intensive post-restructuring monitoring. Effective supervision of business activities and financial flows requires significant administrative capacity. Due to staffing constraints, continuous monitoring of all restructured loans is often challenging, thereby increasing exposure to recurring credit risk.

To address these obstacles, banks implement several strategic measures. First, they prioritize communication-based approaches aimed at fostering cooperative relationships with debtors. By maintaining open dialogue, banks attempt to build mutual trust and encourage transparency. Second, during negotiation phases, banks emphasize a principle of balance, seeking to avoid both excessive leniency and excessive rigidity. The objective is to achieve an agreement that protects the bank's financial interest while remaining realistically manageable for the debtor. Furthermore, banks strengthen analytical procedures prior to approving restructuring. Field verification is conducted more rigorously to ensure the authenticity of business activities and financial statements. In some cases, third-party professionals may be engaged to assist in monitoring or evaluating debtor performance after restructuring. These strategies are designed to reduce the probability of repeated default and enhance the effectiveness of restructuring outcomes. Overall, the findings suggest that the success of credit restructuring depends on a combination of debtor viability, genuine repayment commitment, thorough financial analysis, and consistent monitoring. Restructuring is not merely an administrative adjustment but a negotiated legal mechanism requiring integrity, transparency, and mutual accountability. Its effectiveness is determined not only by contractual modification but also by the quality of institutional governance surrounding its implementation.

## V. Conclusion

This study concludes that the implementation of credit restructuring in resolving non-performing loans within conventional banks follows a structured and systematic process. The procedure encompasses initiation, negotiation, financial and business evaluation, internal decision-making, documentation through contractual addenda, and post-restructuring monitoring. Each stage plays a critical role in ensuring that restructuring enhances loan quality rather than merely postponing default. The challenges encountered in restructuring implementation arise predominantly from the debtor side, including lack of transparency, inconsistent repayment behavior, and unrealistic demands during negotiation. From the banking side, the primary constraint concerns limited human resources for comprehensive monitoring of restructured loans. These challenges underscore the inherent risk of moral hazard in restructuring practices if not accompanied by rigorous supervision. Strategic problem-solving

efforts focus on strengthening communication, applying balanced negotiation principles, improving financial due diligence, and enhancing monitoring mechanisms. Ultimately, credit restructuring functions as a sustainable resolution mechanism that enables debtors to fulfill their obligations under adjusted contractual terms without extinguishing their debt. When implemented prudently and proportionately, restructuring not only safeguards the financial stability of banks but also embodies principles of fairness and contractual justice within the creditor–debtor relationship.

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