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நீதி, திட்டமிடல் அமைச்சு
MINISTRY OF FINANCE & PLANNING

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 திகதி }
 Date } 14.07.2005

CONFIDENTIAL/IMPORTANT

Hon. K.C. Kamalasekera, P.C.
 Attorney General
 Attorney General's Department
 Colombo 12.

Dear Sir,

GOVERNMENT POSITION / PROPOSALS

Formulated by the Cabinet Appointed Negotiation Committee(CANC) for
 the Financial Re-structuring of Hotel Developers (Lanka) Ltd. (HDL)
and the Divestiture of GOSL Shareholdings, subject to Cabinet Approval

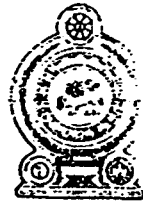
I attach herewith a letter dated 11th July 2005 addressed to Secretary to the Treasury by the Senior Advisor/ Senior DG, President's Office and Chairman CANC, enclosing the note dated 11th July 2005, setting out the Government position/proposals as approved by the CANC to be submitted to you with a view to finalize the settlement of the pending litigations as had been suggested by his lordship the Chief Justice to enable the expeditious disposal of the Government Shareholdings in HDL Ltd.

I would appreciate if these matters are finalized as early as possible to enable me to obtain Cabinet approval for settlement and to proceed with the divestiture of GOSL holdings in HDL.

Yours faithfully,

S.B. Divaratne
 Deputy Secretary to the Treasury

Copy to :- Mr Mano Tittawella, Senior Advisor/ Senior DG, President's Office,
 Chairman CANC.



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ஜனாதிபதி செயலகம் THE PRESIDENT'S OFFICE

11th July 2005

Dr. P.B. Jayasundera
Secretary to the Treasury
Ministry of Finance & Planning
Secretariat Building
Colombo 1

Dear Sir,

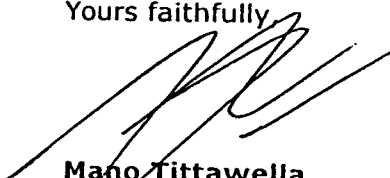
Hotel Developers (Lanka) Ltd. (HDL)

GOVERNMENT POSITION / PROPOSALS

**Formulated by the Cabinet Appointed Negotiation Committee for
the Financial Re-structuring of Hotel Developers (Lanka) Ltd. (HDL)
and the Divestiture of GOSL Shareholdings, *subject to Cabinet Approval***

I refer to the discussions had on 8.7.2005 with Her Excellency the President and the Hon. Minister of Finance with your participation, where the enclosed Government Position / Proposals, which had been formulated and approved by the CANC, were agreed upon to be submitted to the Hon. Attorney General, with a view to finalising the settlement of the pending litigations as had been suggested by His Lordship the Chief Justice to enable the expeditious disposal of the Government Shareholdings in Hotel Developers (Lanka) Ltd.

Yours faithfully,


Mano Tittawella
Snr. Advisor / Snr. DG, Presidents Office
Chairman, Cabinet Appointed Negotiation Committee

GOVERNMENT POSITION / PROPOSALS

Formulated by the Cabinet Appointed Negotiation Committee for
the Financial Re-structuring of Hotel Developers (Lanka) Ltd. (HDL)
and the Divestiture of GOSL Shareholdings, subject to Cabinet Approval

1. Draft Balance Sheet of HDL as at 30th June 2005 is as follows:

	Rs. Mn
Fixed Assets	2,139.2
Current Assets	744.6
Current Liabilities	<u>271.6</u>
	473.0

Net Assets	<u>2,612.2</u>
Share Capital	452.2
Reserves	860.7
(Accumulated Loss)	<u>(6,351.5)</u>
	(5,038.6)
Long Term Liabilities	<u>7,650.8</u>

Sources of Funds	<u>2,612.2</u>

2. The Land on which the Hilton Hotel stands had reverted from the UDA to be owned by the Government from 26th July 1999, as per the Surrender of Special Grant Instruments Nos. 673 & 674. Hence, HDL has no Lease of the Land on which the Hilton Hotel stands.

3. The following Loans due by HDL as at 30.6.2005 are proposed to be converted into Share Capital @ Rs 30/- per Share i.e. a Rs. 10/- Share, at a Premium of Rs. 20/-, after proposed Rebates given at 8. below:

	Rs.
Loans to Government	4,940,555,722
Balance Loans to Mitsui & Taisei (Jap. Yen. 2,611,392,610)	<u>2,386,551,716</u>
Total	<u>7,327,107,438</u>

Loans to Government comprises of Capital Rs. 2,991,482,954/- and Interest Rs. 1,949,072,768/-.

The debt to the Government has been defaulted by HDL: Interest defaulted from 1998 and Capital defaulted from 2001.

4. The present Loans due and in default to the Government by HDL are advances that had been made by the Government under the State Guarantees given to Mitsui & Taisei, to enable HDL to make payments to Mitsui & Taisei, and include interest thereon; Interest and Capital of which have been defaulted by HDL.

<u>Date of Loan</u>	<u>Capital</u>	<u>Rate of Interest</u>	<u>Interest</u>	<u>Default</u>
	Rs.	% p.a.	Rs.	
02.7.1997	288,567,633	12.50	451,834,732	Capital + Interest
12.7.1999	469,742,070	12.50	482,559,701	Capital + Interest
03.7.2000	464,427,826	12.50	372,486,197	Capital + Interest
29.6.2001	360,618,876	18.56	351,907,947	Interest
01.7.2002	446,803,874	12.50	189,368,048	Interest
04.7.2003	340,024,378	9.40	66,929,038	Interest
30.6.2004	395,658,959	8.59	33,987,105	Interest
30.6.2005	<u>225,639,338</u>	10.25*	-	
Total	<u>2,991,482,954</u>		<u>1,949,072,768</u>	

* To be confirmed

5. In addition to the above total debt of Rs. 7,327.1 Mn. there is a balance concessionary Loan to the Bank of Ceylon of Rs. 271.6 Mn. payable by 2013 at 2% p.a. concessionary interest and a Gratuity Provision of Rs. 52.1 Mn., making the total of Rs. 7,650.8 Mn. given at 1. above.
6. The above balance debt due to Mitsui & Taisei is after payment of the 10th Annual Instalment on 30.6.2005 amounting to Jap.Yen. 686,796,257 (Capital Jap. Yen. 522,278,522 + Interest Jap.Yen. 164,517,735) computed at 1 Jap. Yen. = Rs. -/9139 (as at 30.6.2005) giving a total of Rs. 627,663,099/-; of which Rs. 402,023,761/- was funded by HDL and the balance shortfall of Rs. 225,639,338/- paid by the Government.

After the above payment, the balance Loan payments due to Mitsui & Taisei are as follows:

<u>Date Payable</u>	<u>Capital</u> Jap.Yen
30.6.2006	522,278,522
30.6.2007	522,278,522
30.6.2008	522,278,522
30.6.2009	522,278,522
30.6.2010	<u>522,278,522</u>
Total	<u>2,611,392,610</u>

Converted at 1 Jap.Yen = Rs. -/9139 (as at 30.6.2005) the above Capital amounts to Rs. 2,386,551,716/- given at 3. above.

If paid in instalments as scheduled above the interest rate applicable is 5.25% p.a.

The Schedule of payments made to Mitsui & Taisei upto 30.6.2005 is as follows:

<u>Date</u>		<u>Jap. Yen</u>
27.03.1990	- Advance	312,000,000
29.10.1996	- At Settlement	2,000,000,000
	- <i>Delayed Interest</i>	138,082,192
15.11.1996	- 1 st Instalment	933,572,859
	- <i>Delayed Interest</i>	18,396,501
02.07.1997	- 2 nd Instalment	906,153,236
19.04.1999	- 3 rd Instalment	878,733,614
	- <i>Delayed Interest</i>	34,631,734
12.07.1999	- 4 th Instalment	851,313,991
03.07.2000	- 5 th Instalment	823,894,369
29.06.2001	- 6 th Instalment	796,474,747
01.07.2002	- 7 th Instalment	769,055,124
04.07.2003	- 8 th Instalment	741,635,502
30.06.2004	- 9 th Instalment	714,215,879
30.06.2005	- 10 th Instalment	<u>686,796,257</u>
	Total	<u>10,604,956,005</u>

Converted at 1 Jap. Yen = Rs. -/9139 (as at 30.6.2005) this would amount today to a value of Rs. 9,691,869,293/-

7. In the context of the Supreme Court Judgment delivered in December 2002 in the derivative action in law instituted in the right and interest of HDL and the Government by Nihal Sri Ameresekere, the above re-schedule Loans to Mitsui & Taisei are, after a write-off as at 30.6.1995 of Jap. Yen 17,586 Mn., then US \$ 207 Mn. / SL Rs. 10,200 Mn) (SL Rs. 16,071.8 Mn. as at 30.6.2005) from the total Claims as at 30.6.1995 made by Mitsui & Taisei under the State Guarantees and under and in terms of the Agreements entered into by HDL with Mitsui & Taisei.

The said write-off by Mitsui & Taisei had amounted to 63.3% of the total Claims made by them including penal interest, and had amounted to 55.4% of the total Claims made by them excluding penal interest.

After payment of Jap. Yen. 2,312 Mn. (then US \$ 27 Mn. / SL Rs. 1,341 Mn.) essentially out of funds accumulated in HDL due to interim injunctions obtained in the above Case by Nihal Sri Ameresekere, the balance of Jap. Yen. 7,834 Mn. (then US \$ 92 Mn. / SL Rs. 4,544 Mn.) had been re-scheduled from July 1995 to be paid over a period of 15-years, at a reduced rate of interest of 5.25% p.a., with a grace period of 1-year, repayment to be completed by 2010; whereas the original total Claims by Mitsui & Taisei had been fully payable by 1999, at an effective interest rate of 8.43% p.a. (7.95% p.a. applied quarterly) from 1984 (subsequently reduced to 6% p.a. from July 1989), under the State Guarantees given by the Government in 1984.

8. The following write-offs on the defaulted Loans to the Government and the balance Loans to Mitsui & Taisei are proposed:

	<u>Rs.</u>
Government - 16% on total	790,488,916
Mitsui & Taisei - 9.5% on original balance Re-scheduled Loan	<u>680,167,232</u>
Total	<u>1,470,656,148</u>

	Loans Rs.	Write-offs Rs.	Balances Rs.
Government	4,940,555,722	790,488,916	4,150,066,806
Mitsui & Taisei	<u>2,386,551,716</u>	<u>680,167,232</u>	<u>1,706,384,484</u>
Total	<u>7,327,107,438</u>	<u>1,470,656,148</u>	<u>5,856,451,290</u>

Debt conversion into Equity

	No. of Shares @ Rs. 30/-	Share Capital Rs.	Share Premium Account Rs.
Government	138,335,560	1,383,355,600	2,766,711,200
Mitsui & Taisei	<u>56,879,483</u>	<u>568,794,830</u>	<u>1,137,589,660</u>
Total	<u>195,215,043</u>	<u>1,952,150,430</u>	<u>3,904,300,860</u>

9. The above Debt Rebates and Conversion of debt into equity have been proposed on the basis of maintaining the Government's and Mitsui & Taisei's Share ownership percentages. Mitsui & Taisei Loan has been guaranteed by the Government.

In order to maintain the same percentage of 7.5% of Public Shareholdings, without erosion, particularly in the context that no Dividends had been declared since HDL's inception, it is proposed to issue Bonus Shares amounting to Rs.152,655,890/- only to the Public Shareholders on the basis of 4 ½ Bonus Shares of Rs. 10/- each, for each Share of Rs 10/- held; with the Government and Mitsui & Taisei waiving their right to Bonus Shares to prevent the erosion of the Public Shareholdings percentage.

10. On the above proposed conversion of Rebated Debt into Equity and the issue of Bonus Shares to the Public Shareholders, the present Share Structure of HDL would change as follows:

Present Share Structure

	No of Rs 10/- Shares	Rs.	%
Government	29,388,463	293,884,630	64.98
Mitsui & Taisei	12,445,325	124,453,250	27.52
Public Shareholders	<u>3,392,353</u>	<u>33,923,530</u>	<u>7.50</u>
Total	<u>45,226,141</u>	<u>452,261,410</u>	<u>100.00</u>

Share Structure after Conversion

	No of Rs.10/- Shares	Rs.	%
Government	167,724,023	1,677,240,230	65.59
Mitsui & Taisei	69,324,808	693,248,080	27.11
Public Shareholders	<u>18,657,942</u>	<u>186,579,420</u>	<u>7.30</u>
Total	<u>255,706,773</u>	<u>2,557,067,730</u>	<u>100.00</u>

11. The Authorized Share Capital of HDL is at present only Rs. 600 Mn. Hence, the Authorized Share Capital would need to be increased at an EGM.

The Articles of Association of HDL also would need to be amended at an EGM to remove the right to nominate Directors to HDL Board, and to remove the restrictive Articles giving certain rights to Mitsui & Taisei; so that Articles of Association of HDL would be that of a normal listed public company.

12. After the above proposed restructuring, HDL will be a 'Debt Free Company'; except for the balance Loan to the Bank of Ceylon of Rs. 271.6 Mn. payable by 2013 at 2% per annum concessionary interest, and a Gratuity Provision of Rs 52.1 Mn.
13. The estimated Draft Balance Sheet of HDL as at 30.6.2005, after the above proposed financial re-structuring, would be as follows :

	Rs. Mn
Fixed Assets (<i>Subject to Revaluation</i>)	2,139.2
Current Assets	744.6
Current Liabilities	<u>271.6</u>
	473.0
Net Assets	<u>2,612.2</u>
Share Capital	2,557.0
Share Premium Account	3,904.3
Reserves	860.7
<u>Less</u> : Bonus Share Issue to Public	<u>152.7</u> 708.0
(Accumulated Loss)	(6,351.5)
<u>Less</u> : Debt written off	<u>1,470.6</u> (4,880.9)
Long Term Liabilities	323.8
Sources of Funds	<u>2,612.2</u>

14. Lease Agreements in respect of the Land on which the Hotel stands need to be entered into with the Government on a 99-Year Lease basis, because since July 1999 the Government owns the Land and HDL has no lease of the Land.

Since consideration for part of the present Shareholdings held by the Government, amounting to Rs. 250.9 Mn., had been the capitalised lease value of the above Lands, the said part of the Government Shareholdings stood and stands 'as not paid for' since July 1999, in the context of the ownership of the Lands having reverted to the Government from the UDA in terms of the Surrender of Special Grant Instruments Nos. 673 and 674 in July 1999.

15. In terms of the Investment Agreement with the Government, Cornel & Co. Ltd., had been leased the above Land (1170.5 perches) by the UDA in 1984 for a 99-year period for a total lease consideration of Rs. 136.83 Mn., with Rs. 27.36 Mn. having been paid as a down payment, and the balance Rs. 109.47 Mn. having had to be paid free of interest in equal instalments over 33-years, after a grace period of 3-years, which instalment payments had been defaulted by Cornel & Co. Ltd., without any instalment being paid. The UDA consequently had instituted action, Case No. 16716/MR against Cornel & Co. Ltd. claiming damages for default.

In terms of the Investment Agreement with the Government, Cornel & Co. Ltd. had under-written the HDL Public Share Issue in 1984 on which there had been a shortfall of Rs. 85.7 Mn. Cornel & Co. Ltd. had failed to make such payment disregarding repeated requests made by the Government. In these circumstances, the Government had to pay Rs. 40 Mn. in March 1990 for 4 Mn. Shares of HDL to effect payment to Mitsui & Taisei.

Consequently, the Government increased its nominees on the HDL Board, from 2 to 6 out of a total of 11 Directors, thereby taking control of the management of HDL, for which unanimous Resolutions had been passed at an HDL EGM In December 1990, with Cornel & Co. Ltd., confirming that the Government was the owner of 65% Shareholding of HDL.

16. As per initial discussions had with Hilton International, they have in principle agreed to consider terms of a new Management Agreement, subject to their corporate approvals, whereby the Management Fees & Charges to Hilton International are endeavoured to be reduced by approx. 42%, with certain other benefits to HDL.
17. Heads of Terms of the new Management Agreement being considered with Hilton International, compared with the Terms of the present Management Agreement are as follows:

	Present	Proposed
Management Fees	25% of Gross Operating Profit (GOP), which is after deducting FF&E	2% of REVENUE as Base Fee + 7% of Adjusted Gross Operating Profit (AGOP) as Incentive Fees, only if it EXCEEDS Rs 400 Mn AGOP = GOP-RATES-INSURANCE
Group Services and Benefits	Approx. 7% of GOP	2% of Revenue
Term	Initial term expires on 31.12.2007, with the Option to extend the Operating Term by three (3) successive periods of 10 years each	The initial term is ten (10) years, with the Option to extend by two further five year periods with the mutual agreement of both parties
Furniture, Fittings and Equipment Reserve	US \$ 700,000/= per annum	The Reserve for FF&E will be fixed at 5% of the Gross
Early Termination	Not allowed	Allowed. No Compensation if the Hotel's Revpar in any two consecutive years does not exceed it's Competitors

		If the ownership of the hotel is sold, compensation is payable if the Contract is to be terminated.
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18. The Net Present Value (NPV) of HDL, on the basis of the above proposed financial re-structuring and the proposed new Management Agreement with Hilton International, has been reckoned as follows, on a potential 'earnings basis':

	<u>2 - Towers</u>		<u>3 - Towers</u>		
	NPV Rs.Mn.	Value per Rs.10/- Share Rs.	NPV Rs.Mn.	Value per Rs.10/- Share Rs.	
On 15-Year Earnings Basis	8,480	33/16	11,449	36/95*	35/00**
On 20-Year Earnings Basis	11,817	46/21	16,147	55/33*	53/37**

The Hotel is already structured and designed to afford an additional 3rd Tower of 200 Rooms on top of the Lobby, where a specific area has been earmarked, with 2 Lift wells already provided for. The potential Net Present Values for a 3-Tower operation would also have taken into account the additional investment, which would be required to complete the 3rd Tower. (*Reckoned as US \$ 20 Mn. / US \$ 25 Mn. ** for the above valuation.)

The above excludes the potential profitability from a new development of the valuable approximate 2 ½ Acre Land behind the Treasury, with a new Tower Complex of Luxury Rooms/Apartments, overlooking the Beira Lake and Sea.

The Chief Valuer is in the process of carrying out a Valuation.

19. In the context of the present 'amended' Architectural Plans filed with the UDA being irregular, the UDA has undertaken to do a Measured Drawing of the Hotel Buildings constructed; the UDA approved original Architectural Plans also not being available with the UDA.
20. After the above re-structuring the Shareholdings of HDL would be as follows:

Government

	<u>No. of Shares</u>	<u>%</u>
Present Shareholding	29,388,463	11.49
Conversion of Debt	<u>138,335,560</u>	<u>54.10</u>
Total Shareholding	<u>167,724,023</u>	<u>65.59</u>

Mitsui & Taisei

	<u>No. of Shares</u>	<u>%</u>
Present Shareholding	12,445,325	4.87
Conversion of Debt		
Guaranteed by the Government	<u>56,879,483</u>	<u>22.24</u>
Total Shareholding	<u>69,324,808</u>	<u>27.11</u>

Public Shareholders

	<u>No. of Shares</u>	<u>%</u>
Present Shareholding	3,392,353	1.33
Bonus Shares	<u>15,265,589</u>	<u>5.97</u>
Total Shareholding	<u>18,657,942</u>	<u>7.30</u>

It would be noted that 77.90% (i.e. Government 55.66% + Mitsui & Taisei 22.24% guaranteed by the Government) are Shareholdings of the Government on the basis of monies paid and the debt guaranteed to Mitsui & Taisei by the Government.

The HDL Shareholdings after the above financial re-structuring would be as follows:

	<u>%</u>	<u>No. of Shares</u>
Government - Payment made in Cash (<i>Original 4 Mn. + Debt Conversion</i>)	55.66%	142,335,560
Mitsui & Taisei - Debt to be paid by the Government	22.24%	56,879,483
Mitsui & Taisei original Shareholding	4.87%	12,445,325
<u>Shareholdings not paid for</u> (<i>Allotted for Land Lease now frustrated</i>) <u>to be cancelled</u>	9.81%	25,089,750
Equivalent Shareholding to be allotted to the Government for a 99-year Land Lease Balance Government Shareholdings, - Paid by Cornel & Co. Ltd.	0.12%	298,713
Public Shareholders	<u>7.30%</u>	<u>18,657,942</u>
	<u>100.00%</u>	<u>255,706,773</u>

21. Settlement of pending Litigations is proposed to be on the following lines to be entered into by way of an Addendum to the previous Agreements:
- i. To financially re-structure HDL converting long-term debt into equity and the issue of Bonus Shares to the public Shareholders, as proposed above; after increasing HDL's Authorised Share Capital.
 - ii. To amend the Articles of Association of HDL to be that of a normal listed Public Company, without provisions for nomination of Directors and any restrictive provisions.
 - iii. For HDL to enter into a Lease Agreement for the Land with the Government for the Allotment of new Shares, after cancelling the present Share Allotment; and after conversion of present Defaulted Debt into equity as above.
 - iv. Agreement to be reached by the Government with Mitsui & Taisei on the total payment to be made to them by the Government for their balance Debt guaranteed to be paid by the Government, proposed as above to be converted into Shares and for their present Shareholdings in HDL, after the Sale of the HDL Shareholdings; the State Guarantees continuing to be in force until the full agreed payment is made by a specified date.

- v. To thereafter combine the Shareholdings of the Government (65.47%) and Mitsui & Taisei (27.11%) – a total of 92.58%, and Offer for sale 60% Shareholding of HDL to the highest bidder on the Colombo Stock Exchange, *with an Offer Sale Document published.*
- vi. It is proposed that Cornel & Co. Ltd., be allocated 1½% i.e. 3,835,602 HDL Shares after above restructuring or paid Rs. 100,000,000/- in lieu in cash for initial costs incurred and promotional efforts, on the basis that all connected litigations / Appeals made in D.C. Cases Nos. 4392/Spl, 4447/Spl, 4413/Spl, 4414/Spl, 4785/Spl (+ Contempt Applications), 4791/Spl, 5095/Spl, 16832/MR and H.C (Civil) 1/98(2) are caused to be withdrawn / withdrawn, and the Claims in Reconvention made against Cornel & Co. Ltd., by HDL and Nihal Sri Ameresekere in the relevant Cases to be concurrently withdrawn, without costs. Case No. 16716/MR instituted by UDA against Cornel & Co. Ltd. to be withdrawn without costs.
- vii. Government to decide on an appropriate allocation of HDL Shares after above restructuring or a payment in lieu in cash, to be made by the Government to Comindtax Management Service Ltd., (now Consultants 21 Ltd.), for the endeavours and efforts in bringing about the write-off of Jap. Yen 17,586 Mn. (then US \$ 207 Mn. / SL Rs. 10,200 Mn.) benefiting the Government and HDL, and for the costs incurred since July 1995 in assistance rendered in defending the interests of the Government and HDL in the above litigations instituted / caused to be instituted by Cornel & Co. Ltd.; and HDL and Nihal Sri Ameresekere to withdraw Case No. 15322/MR and the Claim in Reconvention, respectively, without costs.
- The Supreme Court to decide on the Terms of Settlement in D.C. Cases Nos. 19849/MR and 21819/MR instituted by Nihal Sri Ameresekere against the then Deputy Minister of Finance, G.L. Peiris, in the interest of HDL.
- viii. HDL has incurred Legal Costs amounting to Rs. 17.8 Mn. to date on the above litigations.
- ix. 5% i.e. 12,785,339 Shares of HDL after above restructuring to be allocated to the present HDL employees (Approx. 950 Employees) on the basis of their service.
- x. The balance Shares of HDL to be sold on the Colombo Stock Exchange, as retail sales in small blocks, to realise the maximum sale proceeds possible for the Government.
22. Without the proposed financial re-structuring, HDL as per projections made, would continue to operate at cognisable Losses, accumulating an estimated Defaulted Debt to the Government of Rs. 9,300,000,000/- by 31.3.2010.
23. HDL's Losses for the last 7-Years had been as follows :

	Rs. Mn.
1999	(188.9)
2000	(291.5)
2001	(223.8)
2002	(288.0)
2003	(240.0)
2004	(248.6)
2005	(400.8)
	<u>(1,881.6)</u>

Loss for the quarter-ended 30.6.2005 is Rs. 19.5 Mn. with an exchange gain of Rs. 92.2 Mn.

24. If, Settlement of pending Litigations cannot be concluded, and the proposed Financial Restructuring on the lines given above not given effect to immediately; then there would be no other option, but to wind-up HDL, transferring the Hotel Building to the Government, which owns the Land, and the Government settling Mitsui & Taisei the balance Loans under the State Guarantees; and setting-off the value of the Hotel Buildings against the defaulted owings by HDL to the Government.
25. The foregoing has been set out without prejudice to the rights of the Government to take warranted action.

11.7.2005

OK.
[Signature]
11/7/05

OK. *[Signature]*
11/07/05

OK
[Signature]
11/07/05