The swift and silent restructuring of Singapore's Pacific International Lines

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On 31 March 2021, the world's 12th largest liner company and Southeast Asia's largest carrier Pacific International Lines (PIL) announced the completion of the US$600 million investment by Heliconia Capital Management. The investment, which has resulted in Heliconia obtaining a majority shareholding stake in the PIL group, marked the completion of PIL's US$3.3 billion debt restructuring which involved a combination of a US$1.1 billion scheme of arrangement as well as an out-of-court restructuring of the company's remaining debts.

Amidst the highly publicized ongoing restructuring efforts by Hyflux which have yet to successfully conclude despite years of discussions with creditors and the bleak prospects faced by creditors of the once mighty oil trader Hin Leong Trading, questions have been raised concerning the effectiveness of Singapore's restructuring regime and its updated legal toolkit which adopts several features of Chapter 11 of the United States Bankruptcy Code.

While detractors have taken aim at Singapore's new restructuring laws, citing the low rate of successful restructurings conducted since and the difficulties which remain unresolved, it is far too soon and simplistic to conclude that the new laws have not gone far enough. In this regard, the successful conclusion of PIL's restructuring efforts through its ambitious strategy of undertaking a "pre-negotiated" restructuring bears testament to the major shift in dynamics that the new laws have brought about in the restructuring space.

The PIL approach is reflective of how these "Chapter 11-style" provisions in Singapore's updated legal toolkit can be utilized to effect swift and elegant corporate rescues. The manner in which PIL's restructuring was carried out potentially serves as Singapore's blueprint today for restructurings of container shipping lines globally and large scale restructuring generally.

PIL's strategy for a pre-negotiated restructuring

It was no secret that PIL had been facing increasing pressure from the steep downturn in shipping demand over the past few years with various industry insiders pegging PIL as a potential takeover target by Cosco. Following the onset of the COVID-19 pandemic, PIL's difficulties were further exacerbated as governments worldwide implemented lockdowns which restricted trade flow and depressed global consumer demand, adversely impacting PIL's revenue streams.

While PIL could have followed the traditional restructuring route by commencing moratorium proceedings in Singapore without a comprehensive restructuring proposal in place, a different approach had to be conceptualised in light of the experience faced by Hanjin Shipping which was declared bankrupt in 2017.

Prior to its collapse, Hanjin Shipping had been the world's 7th largest containership company and had begun restructuring discussions with its creditors in April 2016. However, restructuring discussions subsequently hit a snag and resulted in the company's main lender withdrawing its support. A day after the withdrawal of support was announced, Hanjin Shipping filed proceedings in the Seoul Bankruptcy Court for the equivalent moratorium relief. However, instead of providing the company with the relief it needed, the court filing resulted in an immediate supply chain implosion which ultimately resulted in its demise as many of its vessels became stranded or were seized.

Drawing from the lessons of the Hanjin Shipping bankruptcy, the company took early action and adopted a bold legal strategy by embarking on a "pre-negotiated" restructuring process with the assistance of WongPartnership as its legal advisor, Evercore Asia (Singapore) as its investment banker to advise on its capital raising plans and AlixPartners as its operational consultant. This was an unusual move with a cocktail of sophisticated advisors as pre-negotiated restructurings, although fairly common in Chapter 11 proceedings, are not typically undertaken in Singapore.

However, it was necessary for the survival of the business that the deal proceed as expeditiously as in Chapter 11 restructurings.

Pioneering the pre-negotiated restructuring process in Singapore

Conceptually distinct from a “pre-packaged” scheme of arrangement or a “pre-pack” (which is where the debtor company solicits acceptances from all intended scheme creditors in respect of the full terms of the restructuring), a pre-negotiated restructuring is one where the key terms of the restructuring are negotiated with principal creditors before the filing of any court proceedings but votes are not actually solicited.

Only upon obtaining the agreement of a substantial group of creditors are court proceedings then commenced with the draft restructuring documentation having been prepared in substantially final form and with a request that the timelines for soliciting creditor approvals and court hearings proceed on an expedited timetable.

While “pre-packs” are specifically provided for under the Insolvency, Restructuring and Dissolution Act in Singapore and were undertaken by Hoe Leong Ltd and more recently, iFlix Pte Ltd, they are practical only in situations where the debtor has relatively few creditors and is not seeking to undertake a comprehensive restructuring of its business. In the case of PIL which needed to restructure debts owing to more than 50 creditors comprising, amongst others, bank lenders, financial lessors and bondholders which included retail investors, a “pre-pack” would not have been feasible.

The availability of the tools under the new restructuring regime helped shaped a successful pre-negotiated restructuring

Three key steps were crucial to the success of PIL’s pre-negotiated restructuring. The first was a consensual standstill on enforcement action which PIL only sought from its bank lenders. Given the highly competitive of the container shipping industry which demands service reliability, it was clear that PIL needed to continue its operations in order to preserve its business. However, with the increasing liquidity crunch, cash needed to be preserved and managed carefully. As such, a strategic decision was made to seek a consensual standstill and a principal and interest holiday from PIL’s bank lenders whilst continuing repayments to PIL’s trade suppliers and financial lessors who were situated in other jurisdictions.

On the face of it, seeking a principal and interest holiday from bank lenders whilst continuing repayment of other creditors was an unpopular proposal. However, two factors held the most sway. First, under the new restructuring provisions in Singapore allowing debtors to obtain an automatic moratorium upon filing a court application, PIL had the unilateral ability to bring to a halt any threatened enforcement action at any point in time by filing the necessary application with the Singapore courts. Having seen the commercial fallout from Hanjin Shipping’s public court filing, the irretrievable consequences that would follow should PIL be forced to file for court protection were clear. Second, any enforcement action taken by financial lessors situated in other jurisdictions such as vessel arrests would have a domino effect on the company’s business operations and that it would be nearly impossible for the company to recover from such actions.

As a result of the above two factors, PIL was able to obtain the standstill on a consensual basis, thus obtaining breathing room to work on the restructuring terms and avoiding the industry backlash that would have accompanied a court filing. In exchange for the consensual standstill, PIL provided the lenders the same informational safeguards that they would have obtained from the Singapore courts if a formal application had been filed on a voluntary and consensual basis.

The second key step undertaken was the strategic establishment of an informal steering committee who would have the ability to build momentum towards obtaining the necessary consents to implement the restructuring. This was done to facilitate restructuring negotiations and to ensure that the restructuring would have the support of a critical group of creditors. In particular, it was considered that as it would not be feasible to include a large number of unsecured creditors in the informal steering committee, the informal steering committee would at least hold in aggregate the necessary quantum of debts required to implement the restructuring through a cross-class cram down.

Compared to the previous requirement where the scheme company would need to obtain the approval of a majority in number of creditors representing 75% in value of the scheme creditors in every single class of creditors in order to obtain court sanction of the scheme, the cross-class cram down mechanism introduced by the new restructuring toolkit enables a scheme company to obtain the court's sanction of the scheme if at least one class of creditors approve of the scheme and if a majority in number of creditors representing 75% in value of the scheme creditors approve of the scheme as long as certain thresholds concerning the treatment of creditors under the scheme have been met.

The true impact of this new mechanism goes beyond lowering approval thresholds. In effect, being able to utilise this tool reduces the ability of creditor groups to take unreasonable holdout positions, allowing negotiations to progress more quickly and for value to be distributed more fairly under the restructuring plan.

Although as matters turned out, PIL did not have to utilise the cross class cramdown as the scheme of arrangement achieved overwhelming majority support from creditors voting in the unsecured class (which looked perilous for a while), the ability to utilise the cross-class cramdown allowed PIL to focus its efforts on developing a feasible restructuring proposal within a few months.

Finally, the lynch pin to the pre-negotiated restructuring was the US$112 million emergency credit facility which was extended to PIL by Heliconia to facilitate continued operations while the restructuring plan was negotiated.

Realistically, PIL could only able to obtain financing if the facility was backed by security. However, it did not have any unencumbered assets which it could use as security for the facility. Although the new restructuring toolkit allowed PIL to apply to court for an order that Heliconia be granted a priming lien over certain of its assets in relation to the emergency financing, this would have magnified unwanted publicity and potentially caused delays which would increase the risk of business failure. In the circumstances, PIL sought to persuade secured financial lenders who had an equity cushion to support the ECF on the basis that PIL could seek a court order to the same effect under the new restructuring regime.

Given the prospect of PIL being compelled to file for a moratorium to utilise those provisions, certain supportive lenders eventually agreed to enter into deeds of undertaking pursuant to which each of them would make payment of an agreed committed sum to Heliconia (which would in aggregate be equal to the new financing provided) in the event of the restructuring was not successful. While such sum would be payable upon the enforcement of their respective security, it was agreed that these lenders would retain the discretion to determine the enforcement timing and process In consideration of the undertakings, the participating lenders were granted the right to accelerated repayment of a certain sum calculated based on a percentage of their commitment amounts following the restructuring contemplated by PIL.

The advantages of such a structure were three-fold: First, as the facility was extended by a third party, the lenders did not have to extend fresh cash to PIL and could support the financing by simply sharing in the financial risk with the other participating financial lenders. Second, the arrangement effectively granted Heliconia a priming lien over the collateral held by those financial lenders but allowed the lenders to retain control over the enforcement strategy, thus allowing them to manage the risk of any shortfall arising from enforcement. Third, as the arrangement was done on a consensual basis where lenders could determine the amounts that they were prepared to commit based on their own assessment of their security position, an expedited approach could be taken, allowing PIL quick access to the funds it needed.

With these successful structures in place, PIL was able to engage with Heliconia, who were advised by global investment bank, Houlihan Lokey, on the terms of Heliconia's investment and formulate a restructuring plan that had the support of the informal steering committee.

Obtaining the Singapore court's approval of the pre-negotiated restructuring plan

As the entry of any company into court restructuring proceedings inevitably results in some reputational damage even with the best public relations and media strategy, one of the crucial

advantages of the pre-negotiated restructuring is the ability to request for the court proceedings to proceed on an expedited basis.

It was on this front that the Singapore court's efficiency and flexibility was exemplarily displayed, with the court proceedings relating to PIL's pre-negotiated restructuring concluding in slightly under 4 months – a duration almost unheard of in the context of large-scale Singapore restructurings.

Further, while the Singapore court recognized the necessity of moving expeditiously in the light of PIL's financial position, it took great pains to ensure that the rights of creditors were protected. For instance, although the nominee holders of bonds issued by PIL were entitled to attend and vote at the scheme meeting, the court adopted a flexible and creative approach by directing that the voting instructions of beneficial owners that were given to the nominees (who had the legal standing to cast the vote) were to be preserved. This way, the court could have regard to their wishes when PIL sought the court's sanction of the scheme.

This unprecedented direction, which allowed effective enfranchisement of the beneficial owners, recognized the economic reality of the beneficial owners' financial interest in the scheme notwithstanding the strict legal rights stipulated in the contracts. This practical and impactful measure displayed the careful balance adopted by the Singapore court to the rights of all stakeholders involved including PIL.

Why the new hybrid restructuring laws should not be written off just yet

The successful execution of PIL's "pre-negotiated" restructuring strategy evidences how Singapore's updated restructuring toolkit is shaping the mindset, discourse and playing field between a debtor and its creditors and PIL's restructuring plan which was completed swiftly and with minimal fanfare should be marked as a triumph of Singapore's hybrid restructuring regime.

Further, with the increasing adoption of selected Chapter 11-style provisions globally, PIL's pre-negotiated restructuring paves the way for similar containership liner restructuring deals internationally and for future complex and large-scale restructurings in similar hybrid restructuring regimes. In this regard, it is worth noting that while AlixPartners and Evercore have extensive experience in Chapter 11 restructurings, PIL's restructuring is both advisory firms' first foray into Singapore restructurings.

There remains many provisions in Singapore's new restructuring regime that have untapped potential for strategic and innovative use in restructurings, and it is exciting to see what further new ground can be broken with an enlarged ecosystem of advisors who can draw on their experience handling complex restructurings in other jurisdictions to advise debtors and creditors in Singapore restructurings.

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<u>Summary of the terms of PIL's restructuring deal:</u>

The Investment:
US$600 million was invested into the PIL group by Heliconia via a combination of debt and equity instruments, resulting in Heliconia acquiring a significant majority economic stake in PIL.

The Scheme of Arrangement:
PIL's scheme of arrangement restructured its secured and unsecured debts including fixed-rate bonds that were due in November 2020. The scheme of arrangement was approved by an overwhelming majority of creditors across all 4 classes voting at the scheme meeting on 1 February 2021 and sanctioned by the Singapore court on 3 March 2021.

<u>Secured debts:</u> PIL's previous secured debts have been reinstated to the extent of the agreed value of their security with the repayment of the reinstated secured debts re-profiled based on the PIL's available cash flows in accordance with a pre-agreed debt service waterfall arrangement.

Unsecured debts and undersecured claims: Previous unsecured debts and undersecured claims (being the difference in value between the secured debts and the agreed value of security) converted to perpetual bonds which have been issued by PIL with two options for, amongst others, varying combination of cash and non-cash (payment-in-kind) interest payments.

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