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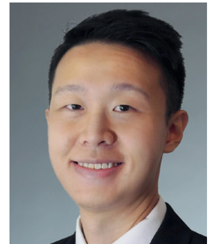
The restructuring of corporate bonds in Singapore



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Large-scale restructurings in modern times almost invariably involve bonds and other debt securities. In this article, we discuss the mechanisms and processes for restructuring bonds in Singapore, and highlight common legal and practical issues that arise in bond restructurings. This article should interest not only Singapore restructuring practitioners, but also international practitioners whose clients may want to leverage on the robust, efficient and well-developed Singapore regime to implement complex debt restructurings.

Introduction

The Singapore restructuring industry has seen a spike in the number of restructurings involving corporate bonds in 2020 and 2021. This development is unsurprising given the flourishing bonds market in Singapore which has grown steadily over the years, with the total outstanding corporate bonds reportedly rising 10.2% to SGD420bn as of December 31, 2019.[1] Where a company that has issued bonds in Singapore's capital markets seeks to restructure its bonds, it will need to consider a variety of legal issues in determining its approach.

Procedures for bond restructurings

Bonds are usually restructured in Singapore either by way of a:

(a) consent solicitation exercise; or

(b) scheme of arrangement.

A consent solicitation exercise involves restructuring the bonds by amending the terms of the bonds pursuant to the amendment and modification clauses set out in the bond documents. Typically, the approval of a supermajority of 66 2/3% or 75% of the bondholders would be required. A meeting of the bondholders is usually convened for them to consider and vote on the restructuring proposal.

A scheme of arrangement is a court-supervised restructuring plan that requires the approval of each class of creditors (by a majority in number and three-quarters in value) and the court.[2] A scheme of arrangement, once effective, binds all creditors including any dissenting creditors who voted against the scheme.

In broad terms, a typical scheme process involves circulating an explanatory statement to the scheme creditors, convening a scheme meeting (which requires the leave of the court), and thereafter applying for the court's approval of the scheme assuming the creditors have approved it at the scheme meeting. A "pre-pack" scheme of arrangement, which is an expedited procedure that does away with a scheme meeting, is also possible where the requisite majorities of creditors have pre-negotiated and agreed to the scheme terms.[3]

Choosing the right procedure

Choosing between a consent solicitation exercise and a scheme of arrangement is a critical decision in any bond restructuring, requiring an analysis of an interplay of strategic, legal and commercial considerations.

Getting a restructuring across the line

The analysis usually begins with an assessment of which procedure is more likely to meet the approval thresholds required to get the restructuring across the line.

The approval threshold for a consent

solicitation exercise may be lower than that for a scheme of arrangement. It is not unusual for a consent solicitation to require the approval of only 66 2/3% of bondholders, compared to the 75% value requirement for schemes.

Additionally, a scheme requires the approval of a majority *in number* of the scheme creditors (sometimes referred to as the "headcount test"). It can be challenging to meet the headcount test where the bonds are held by a dispersed and wide group of bondholders, especially for bonds issued to retail investors. The headcount test gives rise to other unique legal issues which are discussed later in this article.

For deal certainty, practitioners may therefore prefer consent solicitation exercises over schemes to avoid having to meet the headcount test. This could be particularly advantageous in a situation where a small number of key bondholders have entered lock-up arrangements and own enough bonds to carry the vote in a consent solicitation exercise.

Another relevant factor to be considered is the time required for the processes to be completed. As compared to a typical scheme of arrangement which would require the filing of at least two court applications (which may be contested by creditors who oppose the deal), consent solicitation exercises can typically be completed on a much quicker timeline.

However, there are strategic advantages to undertaking a bond restructuring through a scheme of arrangement. In complex restructurings with multiple creditor groups, a debtor company may want to encompass the bondholder group in a scheme together with the other creditor groups, in order to help sway the overall vote in its favour. If the bondholders are supportive, including them in the scheme can help the debtor company increase the pool of votes in favour of the scheme, making it more likely for the scheme to be passed.

We discussed a real-life example of these strategic calculations at play in our previous article in this publication in 2020, where a debtor company proposed a single scheme of arrangement for two sets of bonds to prevent a dissenting group of bondholders from vetoing a restructuring.[4]

"Supercharged" scheme of arrangement

The key advantage of a scheme of arrangement compared to a consent solicitation exercise is that the debtor company can access a suite of tools to help facilitate its restructuring. These tools were introduced in legislation as part of efforts to "supercharge" the scheme of arrangement regime in Singapore:

(a) moratorium protection against legal proceedings and enforcement action (including an automatic 30-day interim moratorium upon filing), which can be given extraterritorial *in personam* effect;[5]

(b) moratorium protection for related entities of the debtor company;[6]

(c) a super-priority rescue financing regime;[7]

(d) a cross-class "cram-down" mechanism allowing the court to sanction a scheme even if there are dissenting classes of creditors;[8] and

(e) an *ipso facto* regime that restricts the exercise of *ipso facto* contractual rights, such as termination of contracts on the basis of the debtor company's insolvency.[9]

These tools can be particularly helpful to a debtor who has not yet formulated a detailed restructuring proposal but whose bonds are about to fall due as they provide crucial breathing space to the debtor and help to preserve the debtor company's position while it carries out negotiations with its creditors. For these reasons, a debtor company may very well choose to undergo a scheme process even though it entails being placed under the supervision of the court.

International bond restructurings in Singapore

The Singapore scheme of arrangement process and its "supercharged" scheme tools can be utilised by foreign companies as long as they can show a "substantial connection" with Singapore.[10]

A "substantial connection" can be shown by, among other things, the company having a place of business or substantial assets in Singapore, the company being registered as a foreign company in Singapore, or the company having submitted to the jurisdiction of the Singapore court for one or more of its transaction disputes.

In 2020, the Singapore High Court held that having the company's securities traded on a Singapore exchange was a strong connecting factor, which on its own was sufficient to meet the jurisdictional test.[11] The debtor company in that case was able to obtain moratorium protection in Singapore even though it did not have substantial business activities or assets in Singapore and its bonds were governed by New York law. This decision helps to provide an important gateway for foreign debtors to access the Singapore restructuring regime, especially considering that the Singapore Exchange lists over 3,000 debt securities in issuances from 45 countries.[12]

Unique legal issues in bond schemes

A unique issue that arises in schemes of arrangement involving bonds is whether the ultimate beneficial owners of the bonds should be regarded as creditors for the purpose of the scheme, or whether the bonds trustee should be regarded as the only relevant creditor.

This peculiar issue arises where the bonds are held through global custodian arrangements. In such arrangements, the debtor company covenants to pay the bond debt to the trustee (not the ultimate beneficial owners) while the trustee holds the debtor's covenant on trust for the benefit of the ultimate beneficial owners of the bonds. Superficially, the trustee may be seen as the only 'true' creditor as it is the party with a direct monetary claim against the debtor company.[13]

However, there are situations in which the courts would recognise the ultimate beneficial owners of the bonds as *contingent* creditors of the debtor company, thereby giving them a right to vote directly on the scheme. This "contingent creditor analysis" was affirmed in 2018 in a thorough and lucid judgment of the Singapore High Court, following a detailed survey of cases in other common law jurisdictions.[14]

In order for the "contingent creditor analysis" to apply, the test is whether the bond documents entitle the ultimate beneficial owners to require definitive securities to be issued to them (e.g. upon an event of default), and thus to acquire direct rights against the debtor in respect of their interests in the bonds. In this regard, we have observed in practice that bond documents are not consistent across the board, and a careful scrutiny of the bond terms is required in each case to determine the extent to which the "contingent creditor analysis" applies.

Leaving aside the strict legal position, Singapore regulators have also (in at least one instance) required the debtor company to treat the ultimate beneficial owners as the creditors for the purpose of the scheme, even though the bond documents did not lend itself to such treatment. That restructuring involved debt securities purchased by many individual "mom-and-pop" retail investors which affected the dynamics of the restructuring and public perception.

These various issues discussed above have given rise to slightly different results in restructuring matters:

(a) Hyflux (2019) – a hybrid approach was applied, whereby sub-account holders whose debt securities were held through regulated entities (e.g. the Central Provident Fund, capital market services licensees, and banks) had direct votes (via proxy), while beneficial owners whose debt securities were held through sub-account holders had to vote through their sub-account holder.[15]

(b) Miclyn Express Offshore (2020) – beneficial owners of the bonds were treated as contingent creditors of the scheme companies and were allowed a direct vote on the scheme.[16]

(c) Pacific International Lines (2021) – the persons registered as bondholders with the

Central Depository ("CDP") (which provides clearing, settlement and depository services in the Singapore securities market) were entitled a direct vote.[17] The persons registered as bondholders with the CDP might not necessarily be the ultimate beneficial owners of the bonds, and could be custodians or nominees holding on behalf of such ultimate beneficial owners.

This has important practical implications for the calculation of votes on the putative scheme (and the prospects of getting the scheme passed):

(a) If the ultimate beneficial owners of the bonds are regarded as creditors, each one of them would be counted for the purpose of the headcount test, giving them a substantial influence in determining whether the scheme passes or not. Given that an issuer may not necessarily have visibility over who the ultimate beneficial owners of the bonds are (as the bonds could be held by nominees and banks on behalf of their clients whose identities are to be kept confidential), this increases the level of uncertainty involved in getting the scheme passed.

(b) If the trustee is regarded as the only creditor, the trustee has to split its vote into a vote for and a vote against the scheme based on the instructions of the ultimate beneficial owners (assuming their instructions are not unanimous). For the purpose of the headcount test, the trustee's votes for and against the scheme cancel each other out, which means its vote effectively has no influence on the headcount test.[18]

Practical aspects of bond restructurings[19]

Bond restructurings give rise to distinctive practical challenges, considering the sometimes-vast number of bondholders involved, particularly for retail bonds. One such challenge is coordination between the creditors and the debtor in conducting negotiations and information flow.

In the Singapore context, a practice has developed where the company takes the lead in commencing the process to form an ad-hoc committee for the relevant stakeholder constituency. An ad-hoc committee can serve to facilitate coordination, negotiations, and information exchange, between the stakeholder group and the debtor as well as with other creditor groups *inter se*, ultimately enabling the formulation of a restructuring plan with better prospects of success.

In bond restructurings, the formation of an ad-hoc committee comprising bondholders who hold a significant amount of bonds can be useful in generating momentum for obtaining the necessary approvals as well.

Townhall sessions are also a common feature of bond restructurings. These townhalls provide a platform for engaging with the bondholders, sharing information and explaining the restructuring proposal. Interestingly, due to the safe distancing restrictions in Singapore that were implemented in light of the COVID-19 pandemic, townhall sessions which previously took the form of large-scale physical meetings in Singapore are now taking place via video conferencing platforms which allows bondholders residing outside Singapore to participate as well.

It is also commonplace for the debtor company to seek the support of investor advocate groups such as the Securities Investors Association (Singapore) and to get buy-in from regulators such as the Singapore Exchange at key milestones of the restructuring process.

Conclusion

As outlined in this article, bond restructurings in Singapore give rise to important strategic, legal and commercial considerations. With the growing bond market, the size and complexity of cross-border bond restructurings in Singapore will likely continue in an upward trajectory. Practitioners will therefore increasingly be required to deftly navigate the complex terrain of nuances unique to such restructurings in Singapore.

Notes:

[1] Singapore Corporate Debt Market Development 2020 by the Monetary Authority of Singapore (accessible at https://www.mas.gov.sg/-/media/MAS/News-and-Publications/Surveys/Debts/Singapore-Corporate-Debt-Market-Development-2020.pdf).

[2] Section 210 of the Companies Act (Cap. 50) ("Companies Act").

[3] Section 71 of the Insolvency, Restructuring and Dissolution Act 2018 (Act 40 of 2018) ("IRDA").

[4] Smitha Menon and Clayton Chong, "*The emergence of a debt restructuring regime for corporate groups in Singapore*", International Insolvency & Restructuring Report 2020/21 at pages 65 to 68 (accessible at https://www.iiiglobal.org/sites/default/files/media/International%20Insolvency%20%26%20Restructuring%20Report%202020-21%20e-book.pdf).

[5] Section 64 of the IRDA.

[6] Section 65 of the IRDA.

[7] Section 67 of the IRDA.

[8] Section 70 of the IRDA.

[9] Section 440 of the IRDA.

[10] Section 63(3) read with section 246(1)(d) and (2) of the IRDA.

[11] *Re PT MNC Investama TBK* [2020] SGHC 149.

[12] https://www.sgx.com/fixed-income.

[13] *Re Swiber Holdings Ltd* [2018] 5 SLR 1358 at [33].

[14] *Re Swiber Holdings Ltd* [2018] 5 SLR 1358 at [37] to [41], [45].

[15] Orders of Court granted on February 21, 2019 by the High Court of the Republic of Singapore, HC/ORC 1515/2019 (Hyflux Ltd), HC/ORC 1512/2019 (Hyflux Engineering Pte Ltd), HC/ORC 1516/2019 (Hyflux Membrane Manufacturing (S) Pte Ltd), HC/ORC 1527/2019 (Hydrochem (S) Pte Ltd).

[16] Orders of Court granted on March 16, 2020 by the High Court of the Republic of Singapore, HC/ORC 1983/2020 (MEO Finance Company Limited), HC/ORC 1988/2020 (Miclyn Express Offshore Pte Ltd) and HC/ORC 1989/2020 (Miclyn Express Offshore Limited).

[17] Order of Court granted on January 28, 2021 by the General Division of the High Court of the Republic of Singapore, HC/ORC 531/2021 (Pacific International Lines (Private) Limited). A direction was made by the Court for the scheme manager to preserve the instructions of the beneficial owners received by the nominees for the Court's consideration at the scheme sanction stage. This left open the possibility that if the beneficial owners' votes did not meet the threshold for the headcount test, the Court might have exercised its discretion not to approve the scheme.

[18] *Re Swiber Holdings Ltd* [2018] 5 SLR 1358 at [69] to [72].

[19] For a more detailed discussion on the practical aspects of bond restructurings, see Smitha Menon, Clayton Chong and Muhammed Ismail Noordin, 'Singapore' in The Art of the Ad Hoc (Morris, Peck and Van de Graff eds, 2nd ed, 2020), pages 151-162 (accessible at https://www.wongpartnership.com/upload/medias/KnowledgeInsight/document/14125/GlobalRestructuringReviewTheArtoftheAdHocEdition2-SingaporeChapter.pdf).

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