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SINO-OCEAN'S RESTRUCTURING: REINFORCING THE USE OF PARALLEL RESTRUCTURING PROCEEDINGS

On 3 February 2025, the High Court sanctioned a restructuring plan proposed by Sino-Ocean Group Holding Limited ("**Sino-Ocean**") despite opposition from a bondholder aggrieved by the fact that the plan provided for existing shareholders to retain more than 50% of the Group's equity. The sanction hearing took place over three days, with the decision providing important guidance on the scope and extent of the cross-class cram down mechanism and Court's approach to fairness. The restructuring also provides another example of parallel processes being used by a Hong Kong debtor to restructure their English and Hong Kong law obligations.

Sino-Ocean Group's capital structure will be familiar to anyone following the ongoing restructuring efforts of Chinese property developers, sparked by regulatory changes leading to the 2021 default of Evergrande Group. Sino-Ocean is incorporated in Hong Kong and listed on the Hong Kong Stock Exchange. The majority of its assets are indirectly held and are located in the PRC, with the governing law of the debt subject to restructuring a mixture of English and Hong Kong law. The company faced financial difficulties amid a downturn in China's property sector, leading to defaults on offshore bonds in 2023 and eventually presentation of a winding-up petition in Hong Kong in June 2024. To address approximately US$6 billion in offshore debt, Sino-Ocean proposed a dual-track restructuring involving an English restructuring plan (the "**Plan**") with a parallel Hong Kong scheme of arrangement (the "**Hong Kong Scheme**") promulgated by its subsidiary, Sino-Ocean Land (Hong Kong) Limited.

KEY FEATURES OF THE PLAN

Commercial terms: The proposed restructuring involved the conversion of Sino-Ocean's existing unsecured liabilities into new secured debt instruments, mandatory convertible bonds and perpetual securities. Existing state-owned shareholders, China Life Insurance Group Co and Dajia Insurance Group Co, would retain a minimum 15% stake each, ensuring Sino-Ocean's status as a state-owned enterprise (SOE). This was argued to be critical for the company's ongoing viability and access to favourable financing terms.

Key issues

- The English Court sanctioned the Plan proposed by Sino-Ocean despite opposition from a bondholder, reaffirming its willingness to use the cross-class cram down mechanism.
- A relevant alternative must be a concrete, identifiable scenario, not a hypothetical possibility.
- Variation in creditors' recourse and restructuring terms justified placing *pari passu* creditors in separate classes.
- Another example of parallel processes being used to implement international restructurings.
- Maintaining the company's state-owned status justified the favourable treatment of shareholders as it directly and positively impacted creditor recoveries.

Class composition: The Plan categorised creditors into four distinct classes:

- **Class A**: Approximately US$2.05 billion in syndicated loan agreements governed by Hong Kong law.
- **Class B**: Approximately US$1.986 billion across four series of notes governed by English law.
- **Class C**: Approximately US$1.293 billion across two series of notes governed by English law.
- **Class D**: Approximately US$652 million in subordinated perpetual securities governed by English law.

The creditors in Classes A, B and C all ranked *pari passu* as against Sino-Ocean, but had differing recourse to other co-obligors within the group, which in the relevant alternative would result in different recoveries. Based on that assessment, those creditors were offered different rights through the Plan, which in turn justified the separate classes. The creditors in Class D were subordinated and therefore their rights were clearly distinct from those of the other creditors. The class composition was one of the elements challenged by the dissenting creditor. At the convening hearing the Court rejected the dissenting creditor's arguments but indicated that there may be fairness issues as to what they were being offered, which would be considered at the sanction hearing.

Voting Outcomes: The Plan was approved by over 75% in value of Class A and Class C creditors but was not approved by the requisite majorities of Class B and Class D creditors. The Court was therefore invited to sanction the Plan using the cross-class cram down mechanism under section 901G CA 2006 (the "**cross-class cram down**") under which a plan can only be imposed on a dissenting class if (A) no member of the dissenting class would be worse off under the plan than they would be in the *relevant alternative* and (B) at least one in-the-money creditor class voted in favour of the plan.

Parallel proceedings: Both Hong Kong and England recognise "the rule in *Gibbs"* (which dictates that foreign proceedings cannot discharge a debt governed by English or Hong Kong law, respectively), which means that for the restructuring to have the desired effect, Sino-Ocean's debts had to be compromised by parallel English and Hong Kong processes. The Hong Kong Scheme relates only to Hong Kong governed debt, which forms Class A debt. This was not the first time a Hong Kong company used an English Plan in parallel with a Hong Kong scheme, with the Hong Kong Airlines 2022 restructuring paving the way for this practice.

KEY TAKEAWAYS FROM THE COURT'S DECISION

The Court sanctioned the Plan, utilising the cross-class cram-down powers, thereby binding dissenting creditor classes to the restructuring terms. The sanction decision hinged on satisfying the following cross-class cram down conditions:

- **Condition A (the "no worse off" test):** The court was satisfied that none of the members of the dissenting classes (Classes B and D) would be worse off under the Plan than in the relevant alternative, which was identified as an insolvent liquidation of Sino-Ocean. The Court rejected the opposing creditor's argument that a fairer plan could emerge as the relevant alternative if the Plan were not sanctioned. In doing so, the Court took into account the fact that:
  - the opposing creditor had not identified a relevant alternative – the vague idea that parties might agree another plan is insufficient; and

- on evidence, Class A creditors would not have supported the proposed alternative and there would have been little incentive for shareholders to agree to an alternative proposal.

- **Condition B (the "economic interest" test):** The opposing creditor argued that this condition was manipulated by artificial creation of a "cramming class" of creditors:
  - In respect of **Class A**, the dissenting creditor argued that its inclusion in the Plan was unnecessary and unjustified and its inclusion as cramming class "entirely unprecedented" given the intended compromise of Class A pursuant to the parallel Hong Kong Scheme. The Court rejected these arguments, noting that the proposed reorganisation, taken as a whole, affects all classes (including Class A) – to deny the ability to use the Plan to compromise Class A would "deny companies that were operating internationally the ability to deal holistically with the different classes of their creditors" and therefore deny the will of Parliament. The Court appeared to have particular regard to the adverse effects of the relevant alternative on Class A and the fact that they were still being substantially impaired by the plan.
  - In respect of **Class C**, the dissenting creditor argued that the votes of a significant creditor within that class should be disregarded given their affiliation with one of the shareholders, with such creditor's vote most likely motivated by an extraneous interest. The Court rejected this argument noting both (i) evidence of the relevant creditor's apparent independence from the relevant shareholder, and (ii) that, even if they were not independent, the existence of other rational bases on which such creditor could approve the plan.

Conditions A and B having been satisfied, it was left to the Court to decide whether to exercise its discretion to sanction the Plan and in doing so it considered the following questions:

- **Was there a "blot" on the Plan?** The dissenting creditor raised a technical objection to the Plan, arguing that a shareholder class should have been included in the Plan given their rights were significantly affected by the Plan due to the issuance of new shares diluting existing equity holdings. The Court noted that this point should have been raised at the convening hearing (rather than sanction hearing), but was nevertheless satisfied that in the current case it was not necessary to join the shareholders in the Plan given that at the time of the hearing they had already voted and chosen to approve the issue of the convertible bonds. This case was distinguished from an earlier English case (Re Hurricane Energy Plc [2021] EWHC 1418) where shareholders were being deprived of an ability to veto a non-pre-emptive issue of shares.
- **Is it "fair" to sanction the Plan?** The opposing creditor's key commercial objection to the Plan was that it was too generous to shareholders who did not provide any new money and whose equity, even though significantly diluted, would still amount to approximately 53.8% post-implementation. The Court acknowledged that, compared to the relevant alternative, the value which the shareholders derive from the Plan was "disproportionate". However, this departure from the *pari passu* principle was considered justifiable on the basis that retaining the SOE shareholders was crucial to Sino-Ocean's future viability and based upon

the valuation had a direct and positive impact on the consideration to be received by all the Plan creditors.

PRACTICAL IMPLICATIONS

Cross-class cram down: The judgment reinforces the court's willingness to use the cross-class cram down mechanism to sanction restructuring plans. Whilst it is important that the creation of a "cramming class" is not wholly artificial, the mere fact that the creditors in that class would also be compromised through a parallel proceeding (and such creditors could avoid the cram down by not submitting to English jurisdiction) does not amount to such artificiality, provided the relevant creditors submit to the jurisdiction of the Court (e.g. by voting in the Plan). It also follows previous case law, serving as a reminder that it did not preclude a class from being the cramming class if the entirety of the class had voted in favour, or had pre-agreed to support the Plan.

Treatment of *pari passu* creditors: On the facts of the case, the inclusion of *pari passu* creditors within different creditor classes was justifiable given differences in consideration offered to creditors, which in turn was commercially justifiable since it was aimed at aligning their returns with those in the relevant alternative. This is a good reminder that the Court will consider the classification of stakeholders, based on existing rights and priorities, and also the rights allocated in the restructuring process, "rights in and rights out".

Relevant alternative: The Court relied heavily on expert evidence to determine the relevant alternative and the likely outcomes for creditors under different scenarios. The definition requires a particular alternative to be identified – there must be at least prospects of it being implemented and it must be specified in sufficient detail to allow assessment of its effects on creditors – which means that a vague idea that an alternative plan may emerge is not sufficient for the purpose of identifying a relevant alternative.

Treatment of shareholders: The court accepted Sino-Ocean's argument that retaining significant shareholdings for SOE shareholders would benefit the company by maintaining its status as an SOE, which would positively impact the valuation of the Plan consideration. In doing so, the Court again placed heavy reliance on submitted expert evidence. However, the Court required undertakings from the SOE shareholders (and a corresponding undertaking from Sino-Ocean to use all reasonable endeavours to enforce the shareholder undertaking) to retain their shares for a minimum period of two years to ensure the perceived benefits of the Plan.

Wider implications: The Sino-Ocean restructuring plan decision highlights the flexibility and robustness of the Part 26A restructuring plan framework and the English Court's willingness to facilitate complex cross-border restructurings even when involving foreign entities and parallel proceedings in other jurisdictions. This decision may serve as a precedent for other Chinese developers and international companies considering English restructuring plans to address offshore debt obligations.

NEXT STEPS

The Hong Kong scheme of arrangement is inter-conditional with the English restructuring plan, meaning both must be sanctioned for the restructuring to take full effect. The Hong Kong scheme was approved by the scheme creditors (Class A under the Plan) at the scheme meeting in November 2024 and the sanction hearing was adjourned to 19 February pending the English court's decision on sanctioning of the Plan.

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