



Recent Developments in Insolvency in Japan



Bingham McCutchen LLP
Shinichiro Abe

I. Overview of the Recent Japanese Insolvency Laws

- Reorganization cases:
 - Civil Rehabilitation Law (“CRL”)
 - Corporate Reorganization Law (“Reorg. Law”)
- Liquidation cases:
 - Bankruptcy Law



A. The Civil Rehabilitation Law



- Established in 1999
- Effective from April 2000
- Replaced the Composition Law, which was established in 1922



CRL

- Debtor-in-possession type procedure
- Advantages: Swift procedure, low cost.
- Disadvantages: Secured creditors are not bound.



Purpose of CRL

- Ease of rehabilitation for medium to small sized companies
 - 99.7% of Japanese companies are small to medium sized
 - 80% of Japanese employees work at small to medium sized companies



Differences from Former Composition Law

- ◆ Can file earlier
- ◆ Rehabilitation plan not required at time of filing
- ◆ Protection against abuse of rehabilitation procedures
- ◆ Increased oversight of debtor
- ◆ Ability to hold directors, officers, and shareholders accountable for misconduct

Number of Filings (All Japan)

Year	Number	Description
1999	231	Under the Composition Law
2000	662	Under the CLA (From April)
2001	1,110	
2002	1,093	
2003	941	

Tokyo District Court Filings

Year	Number	Stock Corporations (public corporations and closely held corporations)	Listed Corporations (stock corporations listed on the Tokyo Stock Exchange)
2000	170	153	5
2001	359	262	6
2002	394	284	13



Issues under the CRL



One issue under the CRL is the increased number of filing companies that (a) do not succeed in getting a plan confirmed or (b) do not successfully execute their confirmed plans. This is likely due to the simplified filing requirements under the CRL.



B. The Corporate Reorganization Law



- Established in 1952
- Reformed in 2002
- Effective from April 2003
- Only for stock companies, especially big companies



Reorg. Law



- Appointment of trustee
- Advantages: All creditors are bound.
- Disadvantages: Replace of executives (even though law allows former officers and directors to remain).

Main Purpose of Reforming the Reorg. Law

- “Main banks,” which obtain majority debts (often over 60% of exposure) of a given company and are actively involved in monitoring the business, can no longer lead and manage workouts for distressed companies after the bubble era, due to a lack of financial resources and increased risk of liability.
- Listed companies were reluctant to file under the former Reorg. Law because of burdensome procedures. Listed companies used to prefer filing under the CRL for that reason (e.g., Sogo).



Results of Reorg. Law Reform



- ◆ Simplified and shortened procedure
- ◆ Increased involvement of creditors
- ◆ Increased options for revitalizing distressed companies



C. Bankruptcy Law

- Established in 1922
- Expected reform in 2004

Number of Filings (All Japan)

Year	Number	Description
1994	40,802	Just after the “Bubble Era” (approx. 1985-1992)
2001	164,521	
2002	220,322	
2003	253,957	

Tokyo District Court Filings

Year	Number	Stock Corporation	Description
1989	824	145	During the Bubble Era
1994	3,858	462	Just after the Bubble Era
2001	16,585	2,106	
2002	22,317	2,797	
2003	12,045	1,324	From Jan. to June



Purpose of Expected Reform



- ◆ Lower standards for proof of claims
- ◆ Transparency with regard to creditors
- ◆ Expediency
- ◆ Conformity of law and practice
- ◆ Increased flexibility with regard to secured assets



II. Guidelines Regarding Out of Court Workouts

In 2001, Japan issued guidelines regarding out of court workouts for multi-financial creditors, which follow the London approach and the Insol International “Global Approach to Multi-Creditor Workouts.”



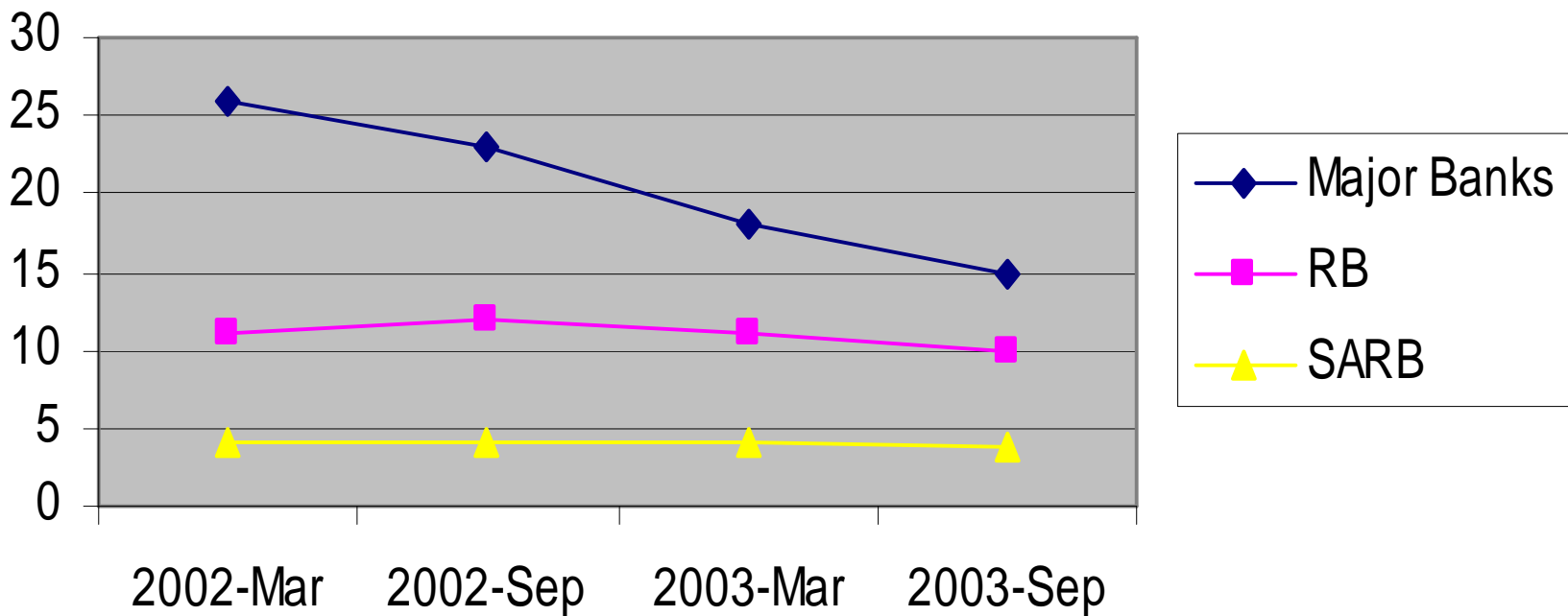
III. Recent NPL Problems in Japan



A. Statistics

Balance of Non-and Poor-Performing Loans among Major Banks

(Trillion Yen)

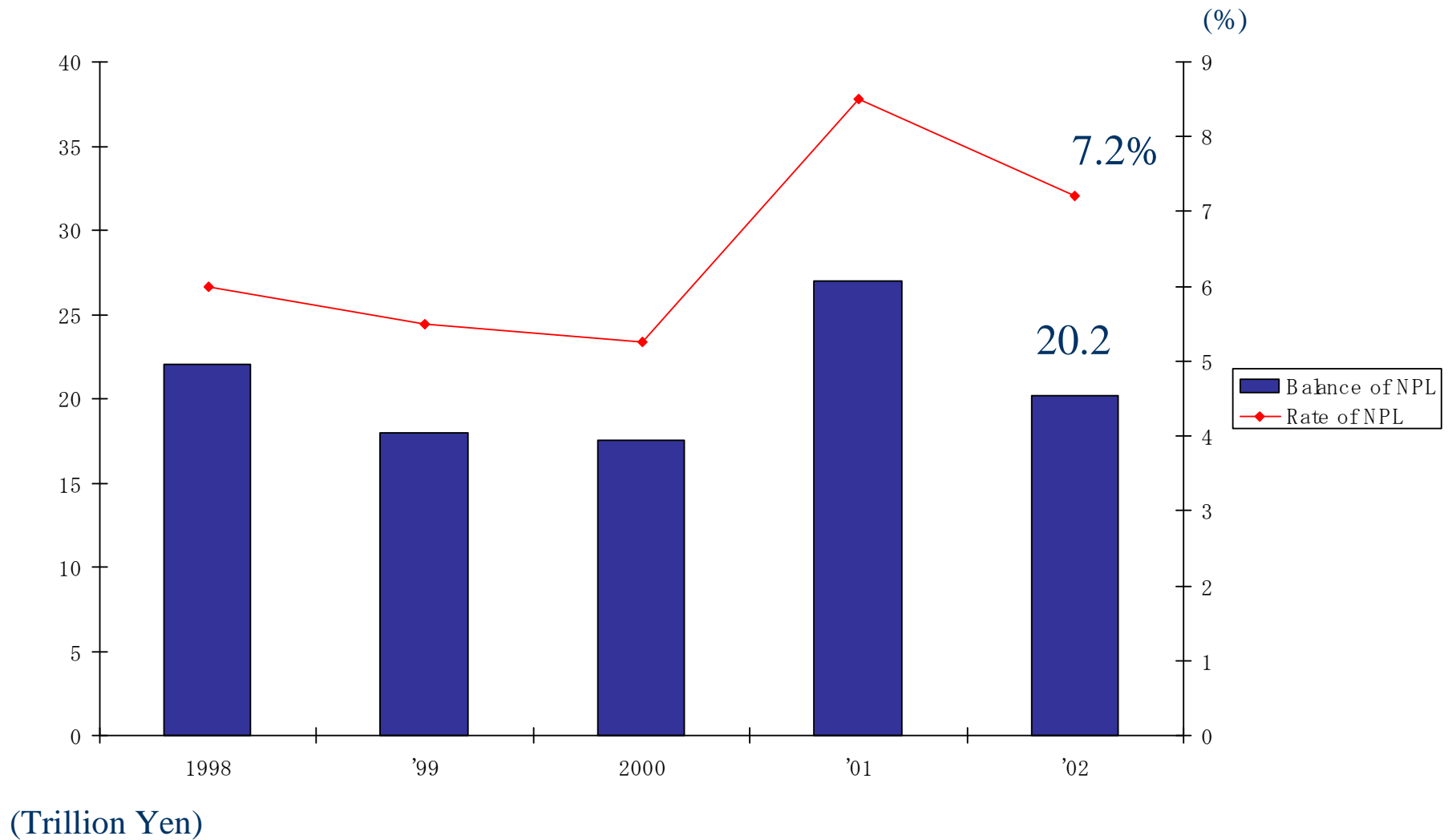


RB-Regional Banks

SARB-2nd Association of Regional Banks

Balance and Rate of Non- and Poor-Performing Loans among Major Banks

(From White Paper on the Economy and Public Finance 2003)



Disposal of NPLs among the Major Banks Bankrupt and “*De facto*” Bankrupt and Doubtful

from Presentation on Distressed Investing in Japan, Moore Strategic Value

Partners Japan, LLC

<u>Sep., 2000</u>	<u>Mar., 2001</u>	<u>Sep., 2001</u>	<u>Mar., 2002</u>	<u>Sep.,</u>
2002				
				(Trillion Yen)
12.7	8.3	6.6	4.7	3.4
(Newly Emerged)	3.4	2.6	1.9	1.2
	(Newly Emerged)	3.0	2.0	1.4
		(Newly Emerged)	6.9	4.3
			(Newly Emerged)	2.0
Balance				
12.7	11.7	12.2	15.4	12.3

B. Japan's Solution: Public Sector

- (1) The Industrial Revitalization Corporation in Japan (IRCJ), created by the government in 2003.
 - The IRCJ's goal is to reduce NPLs by half (approximately 4%) before March 2005
 - The IRCJ can raise money guaranteed by the government up to 10 trillion yen (approximately \$9 billion) to purchase loans and infuse new money into the distressed company.



B. Japan's Solution: Public Sector



- The IRCJ can also establish a restructuring plan with the debtor and main bank.
- Application to the the IRCJ is voluntary. As of April 2004, the IRCJ was involved in 13 restructuring plans.



B. Japan's Solution: Public Sector



(2) The Resolution and Collection Corporation (RCC), created by the government in 1999.

The RCC:

- buys assets from bankrupt financial institutions
- buys NPLs from healthy financial institutions
- manages and collects the above debts
- (recently) reorganizes debtors, usually small companies

C. Japan's Solution: Private Sector

(1) New subsidiaries

- Created by major banks, often funded by U.S. firms such as Goldman Sachs and Merrill Lynch.
- Serve similar function to IRCJ: taking over NPLs from their parent banks, acting as financial advisors for distressed companies, infusing new money into distressed companies, revitalizing companies by supplying or recommending TMs

C. Japan's Solution: Private Sector

(2) Servicer Companies

- Serve similar function to RCC
- As of December 2003, 82 companies were licensed as servicer companies.

(3) Corporate Recovery Funds

- Buy NPLs of and/or infuse equity into distressed companies, then turn them around