

Recent Developments of Restructuring Schemes and Practices in the US, the UK, Germany and France: Comparative Study

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Summary

Since the beginning of the 21st century, schemes and practices for rapid restructuring of ailing enterprises at early stages have been reformed to large extent in various countries including the United States of America, the United Kingdom, Germany, France and Japan.

In the **United States**, Chapter 11 of Bankruptcy Code has been the most useful tool to reorganize troubled companies since its enactment in 1978 (as amended in 2005 most recently) and a pre-negotiated or pre-arranged Chapter 11 case is now very popular in that a debtor and major financial creditors negotiate on the draft reorganization plan and agree upon the plan in advance of the filing of petition for the Chapter 11 in order to conclude the case as soon as possible. Moreover, soon after opening the case, the debtor company may sell its on-going business with its assets or transfer it to a new owner as a means of Section 363 sale combined with or without stalking horse bidding; the new owner who purchased the debtor's business and business assets – which are free and clear from any encumbrance – starts its operation without intervention by a court, US Trustee, creditors and other former stakeholders. This can be seen in the recent GM case in 2009.

In the **United Kingdom** (England and Wales), successive law reforms regarding business reorganization have been made since the beginning of this century to accelerate business restructuring. Most recently, pre-pack administration cases in which a debtor company and its major creditors negotiate on a proposed draft reorganization plan that seeks to find a prospective buyer prior to appointment of an administrator is becoming popular. The administrator, who is a licensed insolvency practitioner, may conclude and execute a contract to sell the debtor's business and its assets to the buyer soon after appointment made by the board of directors of the debtor company without court-involved insolvency proceedings.

In **Germany**, the Insolvency Plan proceedings for reorganization of troubled corporations provided in Insolvency Law of 1994 (which became effective in 1999) has been rarely used due to various reasons. Federal Government publicized the draft Law named "Law to Further Accelerate Company Reorganization" on August 2010, and the

draft law is expected to be adopted and become law by the end of 2011. The draft law is going to facilitate self-administration proceedings and an appointment of an administrator recommended by a debtor and creditors. These reforms may be useful for filing of a prepackaged plan at an earlier stage. The draft law also enable to change and impair shareholders' rights in insolvency plan proceedings and is expected to be helpful for debt equity swaps which should be conducted out of insolvency proceedings so far.

In **France**, a special administration (*mandataire ad hoc*) and a conciliation proceeding, in which an administrator or conciliator appointed by a commercial court consults and discusses with a debtor and its creditors about how to prevent bankruptcy, have been widely used since law reforms made in 1994 and 1984 respectively. In addition to these proceedings, reformed Commercial Code of 2005 created a safeguard proceeding. Upon application of a debtor company, a commercial court appoints a judicial administrator to administer the proceeding. When the proceeding is undertaken, any collection efforts by creditors are stayed by moratorium. The debtor and the administrator jointly draft a reorganization plan and it can be accepted if creditors who hold more than 75% of debts in value of all classes of creditors. Once the accepted plan is approved by the commercial court, the plan becomes effective. More than one class of creditors may be organized: a class consisted of trade creditors or financial creditors. The Reformed Commercial Code that was enacted in 2010 and will be effective after March 2011 provides for an accelerated financial safeguard proceeding which is to affect financial creditors only by means of debts forgiveness and debt equity swaps without impairing trade creditors' rights.

In **Japan**, Guidelines for Out of Court Multi-Financial Creditors Workout, a gentlemen's rule, was established in 2001. Reformed Industrial Revitalization Law of 2007 provides for Business Reorganization scheme by Alternative Dispute Resolution proceeding (BRADR) – a tool for the workout to restructure troubled business companies. Japanese Association of Turnaround Professionals, an organization licensed by Minister of Justice and Minister of Economy, Industry and Trade, manages the proceeding. Unanimous consent by creditors is required for reorganization plan to be accepted in BRADR. Many cases are resolved by BRADA. For more detail on the Japanese workout, please refer to “Takagi, *Out of Court Workout based on the Guidelines and the Alternative Dispute Resolution Scheme for Business Reorganization in Japan*, International Corporate Rescue ,Vol.6 Issue 1, page 14 (2009)”.

The United States of America

Chapter 11

Chapter 11 is the most debtor-friendly corporate reorganization proceedings all over the world. A Debtor in Possession (DIP) will not be deprived of its rights to operate business and dispose of assets even after commencement of the case. A debtor's filing of the petition for Chapter 11 with a court itself constitutes an order for relief upon commencing the case without any court order and every collection efforts by creditors are stayed automatically. Claims on loan made by DIP finances after opening a case are protected by super-priority and priming liens. Due to DIP system in nature and no court-opening requirements such as insolvency, Chapter 11 may not be an insolvency procedure according to the definition provided in EU Insolvency Regulation.

Even solvent and profitable companies avail themselves of Chapter 11 to limit possible huge amounts of future damage claim caused by asbestos and alleged defective chemical products. When Braniff International Airlines filed for Chapter 11 in early 1980s, passengers with air tickets rushed airline counters complaining their inconvenience. However, when all major airlines except American Airlines filed for Chapter 11 to reject and revise onerous collective bargaining agreements several years ago, no one stormed check-in counters then. In the United States, Chapter 11 is not stigma any more.

Prearranged Chapter 11 vs. Freefall Chapter 11

The Section 1126(b) of US Bankruptcy Code provides for a "prepackaged plan" of Chapter 11 in which a debtor proposes a plan with a disclosure statement that includes sufficient information. In a prepackaged plan or pre-pack, if requisite majority of creditors accept the plan before commencement of a case, then the court approves the accepted plan soon after the filing of a petition for the case. The prepackaged plan is very convenient and speedy proceeding in theory. But pre-pack has been rarely used because the disclosure statement must include sufficient and adequate information that can meet requirements provided in blue sky laws. On the one hand, listed companies must file the draft plan and disclosure statement with Securities and Exchange Commission, which can often entail time-consuming inspection prior to voting by creditors; on the other hand, unlisted companies' dissenting minority creditors may file an objection as to adequacy of information included in those statements after commencement of a prepackaged plan, which once again takes time for court-hearing

procedures. Thus, the prepackaged plan is not considered as the best candidate to facilitate the Chapter 11 proceedings in reality.

Meanwhile, prearranged plan is popular in larger cases. In a prearranged plan case, a debtor discusses with unofficial creditors committee consisting of major creditors on a proposed draft reorganization plan. Upon obtaining consents of majority of creditors, the debtor and creditors enter into **lockup agreements** in which creditors agree to vote for the plan at a time when a court approves disclosure statements. A prearranged plan makes it possible for those involved to exit from cumbersome, time-consuming court-involved Chapter 11 proceedings within shorter time period in stark contrast to freefall Chapter 11 cases that could cause possible deterioration of enterprise value of the debtor corporation.

Section 363 sale

Another useful tool to expedite Chapter 11 proceedings is Section 363 sale. The Section 363(b) of US Bankruptcy Code provides that after notice and hearing, a debtor may sell, other than in ordinary course of business, property of the estate including the debtor's business and business assets free and clear from any encumbrance. A transfer of a "good" company with its assets to New GM is a typical Section 363 sale. Negotiating with major stakeholders before filing a petition for Chapter 11, GM sold its good business and assets to New GM and the sale was consummated within seventy days after the petition. American and Canadian Governments as well as other major stakeholders made a credit-bidding to obtain shares of the New GM, as can be seen in debt-equity swap deals. Secured creditors who had liens on the assets sold got paid in full in cash. The bankruptcy and appellate courts cooperated together for speedy proceedings, rendering their decisions and judgments within limited period. A sale under provisions included in a plan may be conducted after acceptance and approval of the proposed plan at a later stage of reorganization case. One advantage of Section 363 sale is that a debtor's business can be sold at an earlier stage of Chapter 11, which will arrive at a higher sales price and thus prevent deterioration of enterprise value. A Section 363 sale was criticized as a *sub rosa plan* in a way that size of a pie to be shared by stakeholders may be fixed in advance and/or without drafting and voting procedures of the plan in place. A fair evaluation of enterprise value and equitable bidding procedures may be critical to withstand any criticisms arising. In many cases, stalking horse biddings can be combined with Section 363 sale. For these cases, it happens that no equity value might be left for unsecured creditors and equity holders.

Stalking horse bidding

In Section 363 sale cases, filing a petition to open the cases takes place at an early stage and stalking horse bidding procedures were widely utilized. Most stalking-horse bidding procedures are taken in the following manner: A debtor retains a financial advisor to find a possible buyer after conducting due diligence to appraise the debtor's business and its business assets; a buyer-candidate proposes a purchase price with other contractual terms including **break-up fees**; After negotiations, the debtor and the candidate (a stalking horse) conclude a stalking horse agreement which will become effective upon a court approval; The debtor files a petition for Chapter 11 with a court and seeks the court approval of the stalking horse agreement; While the stalking horse keeps the business of the debtor company running in effort to minimize deterioration of enterprise value, public auction procedures will also be conducted to solicit prospective buyers willing to pay more than the stalking horse believes the debtor's business and its assets deserve. If and when another prospective buyer bids a far higher price with better contractual terms and its proposed amount is sufficient to pay for the break-up fee or any expenses incurred by the stalking horse and higher than **initial or subsequent overbid amounts** provided in the stalking horse agreement, the bidder replaces the stalking horse and takes over the debtor's business and its related assets

According to Frazier's research ⁽¹⁾, break-up or topping fees of the proposed purchase price range from 1.25% to 5% with an average of 2.7%. The percentage tends to be smaller in bigger cases. Usually the amount of **expense reimbursement** will be capped at the designated level and range from 0.1 to 5.6% with an average of 1.65%, according to the research findings. Consequently, the sum of break-up fee and expense reimbursement will range from 1.5% to 7% with an average of 3.85%. The reason to cap the amount of the expense reimbursement is to prevent the stalking horse from enjoying excessive amounts to be reimbursed.

(1) Frazier, *A Comparison Shopping Guide for 363 Sales*, American Bankruptcy Institute (2009)

The United Kingdom

The pertinent corporate reorganization proceedings in the United Kingdom (England and Wales) are governed by Insolvency Act of 1986, Insolvency Act of 2000, Enterprise Act of 2002 and Companies Act of 2006. Especially, Enterprise Act of 2002 changed reorganization practices dramatically in that a debtor or a floating charger holder is

entitled to undertake out-of-court administration without opening insolvency proceedings by appointing an **Insolvency Practitioner (IP)** as an administrator. One of the most distinguished features of British business restructuring system is the engagement of IP who is licensed by Insolvency Service, a governmental agency.

Company Voluntary Arrangement vs. Scheme of Arrangement

Company Voluntary Arrangement (**CVA**) may be conducted either in or out of insolvency proceedings. When a court appoints an IP as an administrator and commences administration proceedings, they enter into insolvency proceedings and a CVA may be conducted in the administration proceedings. However, majority of CVAs are handled without insolvency proceedings.

A board of directors of a debtor corporation appoints an IP as a nominee and drafts a plan assisted by the nominee. The plan may provide for financial restructuring by means of partial debt forgiveness (haircut), rescheduling of repayment dates, debt equity swap, etc. Unlike Scheme of Arrangement (**SA**), CVA cannot change secured rights. The nominee files the plan including the report that assesses fairness and feasibility of the draft with a court. After obtaining a court approval, the debtor company convenes meetings comprising unsecured creditors and shareholders. The plan will be accepted if more than 75% of creditors in value and 10% of shareholders in face value agree upon it. The accepted plan becomes binding against dissenting minority creditors and shareholders (cram-down). Commencement of CVA itself does not constitute “stay” of any collection efforts made by creditors. However, small companies are not obliged to pay for matured debt within twenty eight days following the commencement of CVA. Unlike SA, CVA requires only one-time court approval for convening a meeting of creditors and shareholders. Additionally, a court does not approve the accepted plan in CVA.

Scheme of Arrangement (**SA**) can also be conducted either in or out-of-insolvency proceedings. In SA, a debtor company must file a petition seeking for permission to convene meetings of creditors and shareholders with a court in advance, as the debtor would do in CVA. Also more than one creditor meetings may be held in SA and creditors will be grouped into different classes according to similarity of rights. SA can change secured rights of creditors. The debtor company must provide stakeholders with sufficient information on fairness and feasibility of a proposed plan. The plan may provide for financial restructuring by means of partial debt forgiveness (haircut), rescheduling of repayment dates, debt equity swap, etc. The plan will be accepted if

more than 75% of each class of creditors in value and 75% of shareholders in face value agree upon the plan. Upon court approval, the plan becomes binding against dissenting minority creditors and shareholders. Commencement of SA itself does not constitute “stay” of any collection efforts made by creditors, as in the case of CVA.

In recent cases, courts decided that stakeholders are not entitled to vote against a plan when they find no equity value in business assets based upon deliberate evaluation of the proposed business or assets sale in the plan. In other words, shareholders have no equity value in debtor’s assets due to insolvency – debts exceeding assets of the debtor at a point in time. Namely, the debtor is able to sell its assets without involving these stakeholders even in out-of-an insolvency proceedings. In addition, unsecured creditors with no equity value in assets may not be entitled to oppose the proposed asset sales in and out-of-insolvency proceedings.

Again, in CVA proceedings, a court gets involved in the proceedings and approves meeting of creditors and shareholders at one time. In this regard, CVA is different from SA: A court takes two steps to approve stakeholders meetings in SA.

CVA is used more frequently than SA.

Administration

There are two types of “Administration” under Insolvency Act of 1986 and 2002: insolvency and non-insolvency proceedings. When a court admits that requirements for opening an insolvency case are met, an administrator is appointed and subsequently insolvency administration proceedings are undertaken. However, when a debtor company or a floating charge holder appoints an administrator (or an administrative receiver appointed by a floating charge holder, strictly speaking) without any court order, the proceedings will not be insolvency-related. There are much more non-insolvency administration proceedings than insolvency ones.

Both in and out of insolvency proceedings, commencement of administration constitutes an automatic stay and any collection efforts by creditors are prohibited. A debtor company is protected by a “**ring fence**” even in out of court administration. CVA and SA may be conducted without administration proceedings, but in case a debtor company needs to be protected by a ring fence, it commences an administration procedure and the board of directors of the debtor company appoints an administrator. Non-insolvency administration involves an administrator appointed by either a debtor company or a floating charge holder. Compared to an administrator appointed by a debtor company or a court, the one selected by a floating charge holder tends to sell off collateral assets at

liquidation value rather than on a going concern basis.

The Insolvency Act of 1986 made it possible to reorganize a distressed corporation, yet the biggest obstacle to open an administration for reorganization purposes was a floating charge holder's right to block the administration order of an administrative receiver – mostly a bank providing finance to a debtor company is the floating charge holder. According to Enterprise Act of 2002, it is still possible for a floating charge holder to appoint an administrator, but the holder is unable to prevent an administration order by the appointment when the charge is created after 2002. This has been one of the biggest changes in reorganization-related schemes in the UK since 1986, and removed the biggest obstacle which stymied commencement of insolvency administration proceedings for the purpose of reorganization.

When an administration order under insolvency proceedings is made, a court -appointed administrator runs a debtor's business and disposes of its assets by depriving incumbent managers of their rights. However, the administrator can ask managers to assist it to maintain the debtor's going-concern value and may retain a professional chief restructuring officer in case of need. Within eight weeks after an appointment, an administrator should propose how to reorganize the debtor's business or liquidate its assets for stakeholders and take steps towards preparing for CVA or SA draft plan.

According to European Union Insolvency Regulation, an insolvency proceeding commenced at the center of common interests (COMI) of one of EU member countries constitutes only one main proceeding all over the EU area and non main (secondary) proceedings may be commenced in other EU countries. And the EU regulation, an administration without any court order is not listed as an insolvency proceeding in the meaning of the Regulation. Therefore, if a debtor company wishes to commence a main proceeding which is effective in all EU countries, it has to apply for an administrator order of a court.

Pre-pack Administration

The UK pre-pack is a concept different from the one used in the US. Statement of Insolvency Practice (SIP) 16 – setting out basic principles and essential procedures with which insolvency practitioners are required to comply – was issued in November 2008 by the Insolvency Service for the Secretary of State for Business, Enterprise and Regulatory Reform. SIP 16 refers to “pre-packaged sale” where a purchaser and a seller of business assets enter into negotiation prior to appointment of an administrator and the administrator effectuates the pre-agreed sale immediately upon or shortly after his

or her appointment.

A key incentive for using a pre-pack is to save the value of business. Even a little sign of possible formal insolvency could significantly impair the debtor's business value. With a pre-pack administration the debtor's business can recover quickly and save expenses paid for professionals.

The pre-pack's disadvantages may include a lack of transparency in the process. Someone interested in acquiring the debtor's business can be left out of negotiation without any chance to participate in. The worst case may be the "phoenix" pre-pack case in which a current owner-manager is supposed to buy-back its over-indebted company at a low price by using a scheme where a new company as a shell purchaser can escape the burden of excessive debt, save its job, and inherit goodwill from the troubled entity. According to the report issued by the Insolvency Service, the number of pre-pack administration used in the first quarter of 2009 is 376 – accounting for almost 30% of 1311 administration cases for the same period.

Against this backdrop SIP 16 was issued for establishing fairness and ensuring integrity of the pre-pack and IPs who are qualified to be an administrator. Paragraph 8 of SIP 16 states: 'it is in the nature of a pre-packaged sale...that unsecured creditors are not given the opportunity to consider the sale of the business or assets before it take place. It is important, therefore, that they are provided with a detailed explanation and justification of why a pre-packaged sale was undertaken...'. To this end, Paragraph 9 sets out a list of 17 pieces of information which, subject to some exceptions, the administrator must disclose to creditors, including information about:

- terms of sale;
- marketing activities undertaken;
- alternative courses of action that the administrator considered, with an explanation of what their possible financial outcomes would have been;
- why it was not possible to trade the business and offer it for sale as a going during administration; and
- any connection between the purchaser and the directors or others involved in the company.

I carefully asked my fellow British practitioners why stalking horse bidding procedures are not common in the UK. They do not deem the stalking horse biddings to be necessarily helpful in the UK because they believe the pre-pack without any stalking horses should be good enough and no one is willing to pay more in cash immediately if

parties involved negotiate faithfully and agree upon value of the business after conducting due diligence.

It is fair to argue that the pre-pack administration scheme is widely used in the UK in effort to achieve quick revitalization of troubled business.

Germany

Insolvency proceedings and Insolvency plan

Insolvency Law (*Insolvenzordnung, InsO*) of 1994 has been effective since 1999. Managing directors and managing board members of a debtor company are obliged to file a petition for commencement of insolvency proceedings without undue delay, at the latest within three weeks after the date on which the debtor's liquidity dries up or the debtor becomes over-indebted. Managers of the debtor company are personally liable to creditors for damages increasing due to delay of the filing. Furthermore, non compliance with aforementioned obligations is a misdemeanor under Criminal law, which shall impose a prison term of up to three years or fine. Burdened by their duties, managers of debtor companies tend to file for insolvency proceedings at an early stage, rather than struggling to trade their business. After the filing of the debtor, a court appoints a provisional administrator and releases tentative orders to prevent possible creditors' collection activities. Managers of the debtor company are replaced by the provisional administrator and lose their rights to run the business and dispose of assets. The provisional administrator is able to continue the debtor's business when there is a chance of reorganization. However, most provisional liquidators are hesitant to restructure the troubled business due to the risk of being held personally liable for potential damages caused by trading the business of the debtor company. If a court judges that requirements for commencing proceedings are met, an insolvency proceeding is undertaken, yet the court does not specify reorganization or liquidation. The provisional administrator may be an administrator instead of provisional administrator after insolvency proceedings begin. At the first meeting of creditors, which will be held within six weeks (or this can be extended up to three months) after the onset of the case, the creditors determine whether they would reorganize or liquidate the business of the debtor company. The decision should be supported by a majority of creditors who refer to the administrator's report that assesses a chance of reorganization of the debtor's business. In fact, most German cases end up in liquidation. In Germany, out of 29,291 corporate insolvency cases filed in 2008, the

number of submitted insolvency plans with a liquidation option is 283.(1) When an insolvency plan proceeding is selected to reorganize the business of the debtor company, the administrator or the debtor should prepare the draft plan within a reasonable period. The plan will be accepted by the court if a majority of creditors agree in number and value of claims for each class. But stockholder rights cannot be changed by the insolvency plan. Because the insolvency plan alone is unable to achieve financial restructuring through debt equity swap (DES), a resolution of stockholder's meeting under company law is needed.

(1) Shultze & Braun, *Insolvency and Restructuring in Germany, Yearbook 2010*, 38,44, F.A.Z.-INSTITUT(2010)

Exceptional Self-Administration and Prepackaged Plan

A German court is able to order a self-administration under Insolvency Law in a business reorganization case. A court appoints a supervisor instead of an administrator when requirements such as approval by resolution of creditor's meetings are met. However, German courts are generally reluctant to order the self-administration and there have been four exceptional self-administration cases so far. A debtor is able to file a prepackaged plan, where the debtor and major creditors agree upon relevant terms before filing with the court in order to save time and money. In theory, if the court is positive about reorganization of the debtor company by means of self-administration and prepackaged plan, the procedures can be closed within six weeks after filing the petition at the latest, according to a German expert(1) . Another professional with whom I conducted an interview told me that in some self-administration cases chief restructuring officer (CRO) – a professional who specializes in business reorganization – is appointed by the board of directors to assist the management to turn around the business, draft an insolvency plan, and negotiate with major creditors at an early stage before filing the case.

(1) Braun, *Commentary on the German Insolvency Code*,426,IDW-Verlag(2006)

Draft Law to Further Accelerate Company Restructuring

Generally speaking, German judges are criticized as conservative to reorganize insolvent enterprises and German Insolvency Law is also negatively viewed as

creditor-friendly to stymie reorganization process. This is in sharp contrast to Anglo legal framework for business restructuring. According to the EU Insolvency Regulation, an insolvency proceeding that is commenced in one of its member states, where the center of main interest exists, is only one main proceeding applicable in EU countries. German legal consultants sometimes recommend that headquarters of some big German distressed corporations be relocated in London to take advantage of business restructuring schemes available in the UK, including Scheme of Arrangement and CVA. Considering potential unfavorable circumstances, German Ministry of Justice published the first draft law titled “Act to Further Accelerate Company Restructuring” (*Gesetz zur weiteren Erleichterung der Sanierung von Unternehmen*) for discussion in August 2010. Most German legal experts expect that the draft law will be adopted by the end of 2011.

Some of the characteristics in the draft law include choice of administrator, self-administration and pre-pack. Because a German court has discretionary authority to appoint administrators, creditors and a debtor are not sure about who will be an administrator. As mentioned above, a self-administration – where the incumbent management can continue the business and stay in his or her current position without being expelled – is available in the existing German Insolvency Law, but rarely approved by German courts. Even when major creditors and a debtor backed by CRO negotiate, agree upon a proposed draft reorganization plan, and find a prospective investor or purchaser before filing a petition for insolvency plan, an independent administrator appointed by a court can ignore the agreed plan. The efforts made by parties involved may wind up with nothing.

In contrast, under the draft law, the court should grant self-administration or appoint a candidate administrator, who is recommended by a majority of creditors in number and value, as an administrator, in general. The reformation facilitates to formulate a draft plan including proposed sale of business or capital injection by new investors. Major creditors, a debtor, and a candidate administrator agree upon the draft plan before filing a petition to open an insolvency proceeding, as can be seen in English pre-pack administration.

Another notable feature of the draft bill is cram-down of shareholder’s rights under insolvency plan. The draft law allows shareholder’s rights to be impaired under an insolvency plan that is accepted by a majority of shareholders in number and face value, as in the case of creditors. Upon court approval, the plan becomes effective and legally binding against dissenting minority shareholders. This enables capital restructuring such as debt equity swap.

France

What makes French schemes of business reorganization and insolvency unique would include *tribunaux de commerce* (commercial court) judge, a venerable business person (not a legal expert) who receives no remuneration in return for his or her services rather serves in an honorary status, *administrateur judiciaire* (judicial administrator), and *mandataires judiciaires a la liquidation des entreprises* (enterprise liquidator) who are professional lawyers (but not general private lawyers) specialized in insolvency-related cases and also licensed by French government. They are not private lawyers.

Special Agent and Conciliation proceedings

Both *Mandatarié ad hoc* (special agent) and conciliation proceedings are non-insolvency and out-of-court proceedings to prevent insolvency.

In a **special agent proceeding**, upon request of a debtor whose business is in distress but not in suspension of payment, a commercial court nominates a judicial administrator as a special agent who assists the debtor to negotiate with creditors for debt restructuring such as rescheduling or other avenues at an early stage. Behind the scenes, creditors and a debtor backed by the administrator enter into negotiation to hammer out terms and conditions in debt restructuring. No moratorium is available in the special agent proceeding.

At the request of a debtor whose business is already in distress or on the verge of bankruptcy within forty five days after suspension of payment, a commercial court may require **conciliation proceedings**, during which an enterprise liquidator or retired commercial court judge will be chosen as a conciliator to preside. These are not insolvency proceedings and the conciliation primarily takes place out of court. The proceedings should be closed within four months (or can be extended up to five months) after commencement. Backed by the conciliator as a mediator in the negotiation, a debtor and creditors may be able to reach agreements on debt restructuring. Creditors are not prohibited from collection, even though a conciliation process kicks off. A commercial court can suspend collection of creditors during the pendency of the conciliation proceedings (not in special agent proceedings) at the request of the

conciliator.

Safeguard

Inspired by Chapter 11 in the US, safeguard (*sauvegarde*) proceedings were created in the Commercial Code (Corporate Rescue Law) of 2005. The safeguard was later revamped in 2008 and 2010. Annex A of the European Union Insolvency Regulation includes the safeguard on the list of EU insolvency proceedings, which are effective across the region.

Upon request of a debtor whose business is in distress but not in suspension payments, a commercial court sets off a safeguard proceeding by appointing a judicial administrator as an administrator who assists and supervises the debtor company while the case is pending. In principle the debtor remains in possession of the business. The safeguard proceedings suspend collection of creditors while the case is pending. During a six month observation period (renewable for up to 18 months) the administrator and the debtor prepare a reorganization plan. Creditors are divided into two classes: financial and trade. Major trade creditors are those who hold more than 3% of the aggregate amount of trade payables owed by the debtor. Any party that acquires bank loans to the debtor company, such as investment funds playing on the secondary market, joins the class of financial institutions creditors (clarified by the revised law of 2008). A reorganization plan may include financial and operational restructuring such as waiver of debt, debt rescheduling, debt equity swap, replacement of managers, and partial or complete asset sale. The plan will be accepted if creditors of each class vote for it (50% in number and two third in value) and a court then approves it. The court has legislative authority to order extension of payment terms up to 10 years. However debt restructuring is not available and the debtor company's balance sheet will not be deleveraged. This may indicate that the extension of payment debt might hamper merger and acquisition of the debtor corporation. In light of this, I need to further delve into the issue

Accelerated financial safeguard

A proposed act to create "*sauvegarde financiere acceleree*" (accelerated financial safeguard) was enacted in October 2010 and became effective since March 2011. The accelerated financial safeguard is a French "pre-pack restructuring" where a debtor company and creditors of financial institutions and bondholders can accelerate the

process of restructuring without impairing trade payables and avoid destruction of enterprise value. In a preceding conciliation proceeding, a debtor and creditors enter into negotiation to agree upon reorganization plan. The debtor then applies for an accelerated safeguard with a commercial court. The conciliator submits a report that includes outcome of the conciliation and a chance of acceptance by creditors of financial institutions and bondholders who hold two third of the aggregate amount of claims in value for each class. The new law ensures that pre-initiation agreements continue to be binding. The court should validate the plan within one month after the financial creditors support the plan and the case is commenced. But the court can extend the deadline for one more month. The court approval can take less time than ordinary safeguard that usually requires six to twelve months for court approval. The plan may include such terms as rescheduling of payment dates, debt forgiveness, debt equity swap, and other capital restructuring that needs a resolution at stockholders meetings. A company with more than 150 employees or annual revenue of over 20 million Euros is eligible to apply for the accelerated financial safeguard proceeding.

Judicial Reorganization Proceedings

A Law of 1985 was revised and a subsequent Law of 1994 includes *redressment judiciaire* proceedings (judicial reorganization). The 1985 law put preserving jobs ahead of creditors' interest. In contrast, the 1994 law enforced creditors' rights vigorously. A commercial court first undertakes an insolvency proceeding as a judicial reorganization where a debtor company seeks to restructure its business. If the court decides that it is hard for the debtor to achieve reorganization after two months of observation period (renewable for up to eighteen months), then the case will be converted to *liquidation judiciaire* (judicial liquidation) proceedings. But the revised law of 1994 enabled a debtor company to apply for liquidation proceedings anytime it becomes crystal clear that the debtor is unable to continue reorganization. A debtor must apply for the judicial reorganization proceedings with a commercial court within forty five days after suspension of debt repayment except in the case of conciliation proceedings. A creditor, an employer and a public prosecutor are entitled to file for a judicial reorganization while a commercial-court judge can start the case at its own discretion (*ex officio*). Once the case is undertaken, the court appoints a supervisory judge (*juge commissaire*) who is another commercial-court judge, a judicial administrator, and controllers (*controleur*) representing creditors. Creditors' committees must be organized for big cases. The court may decide whether to confide management of the debtor's business to the judicial

administrator or require the current management team to ask for help from the administrator. There are two classes of creditors to be organized: one for banks and another for trade creditors. Backed by an administrator, a debtor prepares a plan for reorganization that must be accepted by each class of creditors (a majority of creditors in number holding more than two thirds of claims in value). The court then approves it. In liquidation proceedings, a court-appointed liquidator disposes of the debtor's assets under supervision of a supervisory judge. Contrary to what French law makers envisioned, insolvency cases in France mostly end up in liquidation.

Upon request from Ministry of Economy, Industry and Trade (MEIT), a team consisting of members including Ms. Akiko Nomura, Mr. Daisaku Kadomae, Mr. Kazuyuki Ukawa of Nomura Institute of Capital Markets Research and myself conducted a research on *Business Restructuring Related Matters in Foreign Countries* and subsequently submitted a report to the MEIT on February 4, 2011.

This article is not a summary of the report. The article reflects my personal understandings gained through the aforementioned research. I wrote this paper by referring to books, articles, papers and other materials, all of which were suggested and provided by many international friends of mine and during interviews with distinguished practitioners including Messrs James H.M. Sprayregen and Ryan B. Bennett of Kirkland & Ellis, The Honorable Chief Justice Arthur J. Gonzalez of United States Bankruptcy Court for Southern District of New York, Mr. Mark S. Cheri of Skadden, Arps, State, Meagher & Flom, Messrs Lewis Kruger, Andrew Denatale, Mark A. Speiser and Gabriel Sasson of Strook & Strook & Lavan, Mr. Richard Levin of Cravath, Swaine & Moore, Mr. Neil Cooper of Zolfo Cooper, Messrs Mark Frennessy and Crispin Daly of Orrick, Herrington & Sutcliffe, Messrs David Ereira and Paul Sidle of Linklaters, Dr. Eberhard Braun and Dr. Annerose Tashiro of Schultze & Braun, Ms. Isabelle Didier of Cabinet Isabelle Didier & Associates, Ms. Isabelle S. Monnerville of Smith Violet, Mr. Constantin Achillas of SNR Denton, Former Commercial Court Judge Mr. Bernard Soutumier. Once again, this article stands upon my own personal opinions, not these interviewees'. Special thanks to those respectable friends.