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Comparison of Japanese and American Bankruptcy Law

Brooke Schumm III*

I. INTRODUCTION

A. Overview

Japan has many fewer court-supervised insolvency proceedings than the United States. In Japan, a court may preclude a filing under the Corporate Reorganization Law based only on a brief pre-petition investigation, and thereby force the publicly-held corporation into a bankruptcy setting. The directors and officers may be individually liable for debts of the corporation without having signed personal guarantees. The Japanese martial and samurai traditions, and the consequent concern for family honor and pride, cause the Japanese to feel great shame and disgrace upon a failure such as a bankruptcy.¹ The bankruptcy laws reflect this disgrace in the lengthy period required for a fresh start.

The outline and direction of this article are arranged approximately in the order of provisions under the U.S. Bankruptcy Code.² The article focuses on Japanese

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A reader using this article would find the table of contents of Title 11 of the United States Code useful:

Chapter 1—General Provisions
Chapter 3—Case Administration

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reorganization proceedings, but necessarily discusses Japanese bankruptcy provisions at length. First, eligibility and types of proceedings are discussed. Second, commencement details and administrative provisions, including the "automatic stay" and assumption and rejection of leases and contracts are presented. Third, the debtor's duties and the handling of claims are reviewed. Fourth, liquidations are compared. Fifth, confirmation and reorganization are explored in detail. Last, a comparison of bankruptcy provisions for individuals concludes the article.

Japan has four major bodies of law that govern "bankruptcy court" practice: the Bankruptcy Law of Japan, the Corporate Reorganization Law, the Japanese Law on Composition, and the Japanese Law on Special Composition. The

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Subchapter I—Commencement of a Case
Subchapter II—Officers
Subchapter III—Administration
Subchapter IV—Administrative Powers

Chapter 5—Creditors, the Debtor and the Estate
Subchapter I—Creditors and Claims
Subchapter II—Debtor's Duties and Benefits
Subchapter III—The Estate

Chapter 7—Liquidation
Subchapter I—Officers and Administration
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Subchapter III—Stockbroker Liquidation
Subchapter IV—Commodity Broker Liquidation

Chapter 9—Adjustment of Debts of Municipality
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Chapter 11—Reorganization
Subchapter I—Officers and Administration
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Subchapter III—Postconfirmation Matters
Subchapter IV—Railroad Reorganization

Chapter 13—Adjustment of Debts of an Individual With Regular Income
Subchapter I—Officers, Administration and the Estate
Subchapter II—The Plan

Chapter 15—United States Trustees [repealed]
Subchapter I—General Provisions
Subchapter III—Case Administration
Subchapter VII—Liquidation
Subchapter XI—Reorganization
Subchapter XIII—Adjustment of Debts of an Individual With Regular Income

Throughout this article, "section" shall refer to a United States section of Title 11.

Bankruptcy Law is, in concept and objective, similar to Chapter 7, or “straight bankruptcy,” in the United States. The Japanese Corporate Reorganization Law corresponds to Chapter 11 of the U.S. Bankruptcy Code, but is restricted solely to publicly-held companies. In addition, the Japanese Civil Code and Commercial Code contain provisions that affect insolvency proceedings.


B. History of Japanese Insolvency Law

Prior to the Meiji Restoration in 1867, the only Japanese insolvency remedy was a custom of private settlement: kashi bunsan.

A conference was held with creditors, a solution was proposed, and the major-


Throughout the discussion, “article” refers to the Japanese section of law referenced immediately prior to the word “Art.”; Chapters 1, 3, 5, 7, 9, 11, 12 and 13 refer to United States law; and chapters numbered with Roman numerals refer to Japanese law.

In certain instances, the statute, as translated into English, does not have numbers describing the subparagraphs attached to the text immediately after the opening words “Article ——.” Therefore, this article refers to the subparagraph after the phrase “Article ——” as “Article ——(1)”, the following subparagraph as “Article ——(2)”, and so forth.
5. Bankruptcy Law, contents:
   - Book I Substantive Provisions
   - Book II Procedural Provisions
   - Book III Discharge and Rehabilitation
   - Book IV Penal Provisions

Corporate Reorganization Law, contents:

Chapter I General Provisions
Chapter II Commencement of Reorganization Proceedings
Chapter III Receiver and Investigation Commissioner
Chapter IV Reorganization Creditors, Reorganization Secured Creditors and Shareholders
Chapter V Meeting of Interested Persons
Chapter VI Proceedings After Commencement of Reorganization Proceedings
Chapter VII Terms of Reorganization Plan
Chapter VIII Approval or disapproval and Execution of Reorganization Plan
Chapter IX Discontinuance of Reorganization Proceedings
Chapter X Remuneration and Reward
Chapter XI Penal Provisions
ity decision bound any dissenters. The debtor still personally owed debts remaining after liquidation of his assets. Few assets beyond clothing and utensils were exempt from the creditors. In 1872, a liquidation approach modeled on French concepts was incorporated into the Japanese Commercial Code. The new law was applicable only to the merchant class.\(^6\)

In 1923, the Obligee's Composition Act, now known as the Bankruptcy Law, was enacted, using the German legal approach. It contained procedural, substantive, and discharge provisions and was applicable to all classes of business.\(^7\)

That Act, and the corporate rehabilitation provisions in the Commercial Code, proved inadequate to restore Japan's industry following World War II. A Corporate Reorganization Act was enacted at the suggestion of the U.S. Occupation Government. It included the expansion of the scope of insolvency laws to include 1) provisions to alter secured creditors' rights, 2) provisions explicitly adopting a fair and equitable concept of distribution, and 3) allowance of restructuring and transfer of corporate assets by a merger or creation of a new company.\(^8\) Provisions for pre-"ruling" investigators, interim receivers, and an 80% limit on necessary consents of secured creditors were added in 1967.\(^9\)

II. U.S. Chapter 1: Who Qualifies for Which Japanese Proceeding

United States Chapter 1 provides that any person including a corporation, a partnership, or an individual may be a debtor, except that a) a railroad may not be in a liquidation proceeding, and b) a bank or insurance company may not be a debtor at all under the Bankruptcy Code.\(^10\) Special U.S. Chapters exist for family farmers, and for individuals with smaller debts and a regular income.

Japanese debtors fall into the following categories: individuals, limited partnerships (Goshi-Kaisha), commercial partnerships (Gomei-Kaisha), "limited" companies (Kabushiki-Kaisha) and mutual companies (Sogo-Kaisha). Any person, including closely-held corporations, publicly-held corporations, individuals, associations, partnerships, limited partnerships, and sole proprietorships, can be adjudged bankrupt under the Bankruptcy Law. Only publicly-held Japanese corporations, that is, Kabushiki-Kaisha, are eligible for proceedings under the Corporate Reorganization Law.\(^11\) A Special Composition Law passed in 1946 covering war-torn financial institutions and "special account corporations" has fallen into disuse.\(^12\)

\(^6\) Matsuo §§ 7.01[1]-7.01[2] at 7-3 to 7-4.
\(^7\) Matsuo § 7.01[3] at 7-5.
\(^9\) Matsuo § 8.01[2][c] at 8-5 to 8-6.
\(^11\) Matsuo § 7.02[2][a] at 7-6, § 7.02[2][b][iii] at 7-8; Matsuo § 8.02[2][a][i] at 8-7 to 8-8; Bankr. Art. 133 at LU 31.
\(^12\) Spec. Comp. Art. 15 at LW 5–6.

A. Commencement Details

1. Petitioning procedure; which proceeding preempts

In Japan, an "application for adjudication of bankruptcy" or an "application for commencement of reorganization" initiates the court process.14 An adjudication of bankruptcy or a ruling for commencement of a reorganization proceeding is required to enter a proceeding, much as under the old U.S. Bankruptcy Act.15

If an application for reorganization is filed, the Japanese Court may suspend an already-under-way bankruptcy procedure or composition procedure.16 If a corporation is already in non-bankruptcy liquidation proceedings, two-thirds of shareholders must approve an application to commence reorganization proceedings.17

After an adjudication of bankruptcy, debtors cannot resort to the Composition Law (which permits the debtor to more rapidly accomplish a plan binding on its creditors and to continue to operate its business, as opposed to operation by a receiver or an administrator); they must resort to Chapter IX of Book II of the Bankruptcy Law to obtain a composition equivalent called "compulsory composition."18 A proceeding under the Composition Law and a compulsory composition under the Bankruptcy Law both act as a cross between a liquidating plan of reorganization and a straight liquidation. Either proceeding is useful for persons not otherwise eligible for the Corporate Reorganization Law of Japan.19

2. Eligibility for a proceeding20; cause-voluntary and involuntary petitions

Like U.S. law, Japanese law provides for both voluntary and involuntary applications to establish eligibility for a proceeding.21 In the United States, no cause is required for a voluntary application. A successful U.S. involuntary

15. Bankr. Art. 1 at LU 1; Reorg. Art. 2 at LZ 2.
17. Reorg Art. 31 at LZ 14; Matsuo § 8.02[2][a][ii] at 8-8.
19. The Special Composition Law, passed in 1946 to distribute losses caused by war indemnities, also preempts applications for commencement of composition or bankruptcy. Spec. Comp. Arts. 1, 3 at LW 1.
petition requires a showing of either suspension of payments generally for 120
days or insolvency. The most common criterion of eligibility for a proceeding
under Japanese law, known as a "cause of proceeding," is "suspension of pay-
ment" by a corporation or individual debtor.\textsuperscript{22} A negative asset/liability or bal-
ance sheet is also cause for voluntary petitions.\textsuperscript{23} For partnerships, inability to
perform obligations is the only criterion for an adjudication of bankruptcy while
the partnership continues to exist; individuals will be liable to satisfy the debts of
the partnership, so no balance sheet test is provided for.\textsuperscript{24}

Proof of the facts comprising the just-mentioned "causes" of bankruptcy must
be provided unless all of the directors, partners with liability, or liquidators file
the application to commence a proceeding.\textsuperscript{25} Proof of causes is not necessary,
however, if reorganization or composition is unsuccessful and the proceeding is
being "converted" to straight bankruptcy.\textsuperscript{26}

The Japanese equivalent to a U.S. involuntary petition can occur if creditors
having claims of $\frac{1}{10}$ of the capital or shareholders holding $\frac{1}{10}$ of the issued stock
of a corporation file an application to commence reorganization.\textsuperscript{27} Creditors filing
such an application must detail the amount and nature of their claims, as in the
United States.\textsuperscript{28}

A foreign corporation already in bankruptcy in its native country need not
prove causes of bankruptcy to file a proceeding in Japan.\textsuperscript{29} Section 304 of the
U.S. Bankruptcy Code has similar provisions for cases ancillary to pending
foreign proceedings. Section 304 contemplates that the trustee or the represen-
tative in a foreign proceeding will file a U.S. petition. The U.S. Bankruptcy
Court will assist such trustee or representative in the administration of assets in
the United States, taking into account various factors, including just treatment of
all creditors, prevention of preferential or fraudulent dispositions of property, and
comity.\textsuperscript{30}

3. Jurisdiction and venue\textsuperscript{31}

The Japanese court having initial jurisdiction is called a "District Court".\textsuperscript{32}
Jurisdiction and venue lie in the exclusive jurisdiction of the district court for the

\textsuperscript{22} Reorg. Arts. 30 at LZ 14, 33 at LZ 15, 38 at LZ 18–19; Bankr. Arts., 126(2), 127, 132 at LU
\textsuperscript{23} Reorg. Art. 30 at LZ 14; Bankr. Art. 126, 127 at LU 30.
\textsuperscript{24} Bankr. Art. 127(2) at LU 30.
\textsuperscript{25} Bankr. Art. 134 at LU 31.
\textsuperscript{26} Reorg. Art. 30(2) at LZ 14.
\textsuperscript{27} Reorg. Art. 33(2) at LZ 15; Bankr. Art. 132(2) at LU 31.
\textsuperscript{28} Bankr. Art. 137 at LU 32.
\textsuperscript{31} Reorg. Arts. 6, 7 at LZ 3; Bankr. Arts. 105–07 at LU 25–26; Comp. Art. 3 at LV 1, Spec.
Comp. Art. 14 at LW 5.
geographic area where the head office of the company or the debtor's residence is located.\textsuperscript{33} If the head office is located in a foreign country, venue is proper in the location of the principal place of business in Japan.\textsuperscript{34} Similar concepts apply to other entities. This is somewhat different than in the United States, where either the state of incorporation, the principal place of business, or the principal location of assets may be chosen as the proper venue of a bankruptcy proceeding, as well as the "residence" of a corporation or person.\textsuperscript{35}

4. Pre-case meeting with the court clerk—unique to Japanese proceedings

A Japanese custom not found in the United States is the pre-case meeting. In reorganization, the court generally conducts a "pre-hearing" on the application to determine if a filing will receive the adjudication desired.\textsuperscript{36} In Tokyo, ex parte contacts with the clerk are permitted. The Tokyo court clerk exercises great influence over the debtor's decision as to what type of proceeding best suits the dilemma at hand. The clerk may go so far as to have a meeting between the debtor and large creditors before proceeding to the judge with the petition for reorganization.\textsuperscript{37}

There is a variance in pre-case meeting practice among courts in different areas of Japan: the Osaka court clerk offers no advice but merely issues a standard form containing various options.\textsuperscript{38} Creditors are not initially called in Osaka. This is done to prevent self-help by creditors.\textsuperscript{39}

In Japan, the commencement of reorganization proceedings is accompanied by substantially more financial information than in the United States. Details about the affairs of the company, its assets and liabilities, and the names of its creditors must be immediately filed.\textsuperscript{40} If managers, directors, or individuals cannot properly report assets and liabilities of the estate, they are subject to severe criminal sanctions of imprisonment at hard labor and monetary fines.\textsuperscript{41}

These financial reporting requirements, which are timed earlier than in the United States, are designed to aid in finding a "sponsor" or "corporate angel." To avoid the risks of an insolvency proceeding for a weak company, a "pre-insolvency angel" is generally sought.\textsuperscript{42} Since, as will be shown later, the shareholders' interests are otherwise ignored or extinguished,\textsuperscript{43} some sort of merger

\textsuperscript{33} Reorg. Art. 6 at LZ 3; Bankr. Art. 105 at LU 25–26.
\textsuperscript{34} Id.
\textsuperscript{36} Matsuo § 8.02[1] at 8-7.
\textsuperscript{37} Id.
\textsuperscript{38} Id.
\textsuperscript{39} Id. at § 8.02[3][c] at 8-11.
\textsuperscript{40} Reorg. Art. 32 at LZ 14–15.
\textsuperscript{42} Matsuo § 8.03[1][a][c] at 8-16.
\textsuperscript{43} Reorg. Arts. 129(3) at LZ 61, 164(2) at LZ 78. See also supra note 36.
and voluntary work-out is often consummated, which enables shareholders to retain some equity interest. Because of this "corporate angel" approach, many pre-filing workouts result and thus, there are relatively fewer reorganization proceedings in Japan than in the United States.

5. Significant filing fees

The district court clerks issue the scale of charges. The fees for a bankruptcy or reorganization proceeding are substantial and are determined on a sliding scale. As in the United States, the court fees receive priority over all other creditors. If the fees cannot be paid up-front in a reorganization setting, the proposed debtor must resort to a bankruptcy. There is an immediate appeal available from the determination of fees in reorganization. If the fees are not available for bankruptcy, the court may dismiss the petition, or they may be advanced from the national treasury. In Osaka, the minimum fee for a corporation is five million Yen in cash. In Tokyo, the sliding scale is based on the company's paid-in capital and the costs can be as high as 10,000,000 Yen. The significant up-front fees deter filings with a marginal chance of success.

B. Proceedings Post-application but Before the Ruling for Commencement of Proceedings

The period between the filing of the application for commencement of the proceedings and the Japanese court's adjudication tends to be approximately two to three months. In the United States, the petition acts as an immediate order for relief, which order of relief is the United States equivalent of an adjudication or ruling for commencement and injunction against creditor action. In Tokyo, the largest obligees or creditors are called, and the court examines and interviews one or two of the top company executives. Generally the employee representatives are consulted.

The most significant points for the Court (and in Tokyo, the clerk, initially) to consider in granting a corporate reorganization ruling are profitability, likelihood

45. Reorg. Art. 34 at LZ 16; Matsuo § 8.02[2][c] at 8-10; Bankr. Art. 139 at LU 32; Comp. Art. 14 at LV 3.
46. Reorg. Art. 34 at LZ 16; Bankr. Arts 139-40 at LU 32.
47. Matsuo § 8.02[2][c] at 8-10.
49. Bankr. Art. 139(1), 140 at LU 32; cf. Comp Art. 19(1) at LV 4 (authorizing dismissal of application for the commencement of composition when there is no advance payment of costs).
50. Matsuo § 8.02[2][c] at 8-10.
51. Id. § 8.03[1][a] at 8-16.
of obtaining consent of a majority of the creditors to a plan of distribution, and
the assurance of a suitable trustee or "sponsor" for the company. A favorable
ruling after an application for commencement of reorganization is usually
granted because in the initial pre-case meeting, the clerk or court has advised the
debtor of its inclinations.

A corporate reorganization differs from commencement of composition in that
the latter automatically permits "debtor-in-possession" operation of the business,
meaning that the debtor continues to control the assets and finances of the
business under the supervision of the court. The receiver in a composition,
however, can make application to restrict the rights of management to manage the
company.

In Tokyo, a practicing attorney is appointed as an interim receiver of the
company's assets, and normally hires an accountant. By contrast, in the Osaka
court, the interim receiver is often an accountant. The interim receiver may also
be designated the receiver after the ruling for commencement.

The Japanese Court, upon the filing of an application for commencement of
reorganization, enters various preservation measures to prevent transfers out of
the company and to prevent dismemberment by creditors. A preservation ad-
ministrator may be appointed on application to the court or sua sponte by the
court to administer the preservation measures pending the ruling for commence-
ment. These preservation measures implement provisions similar to those of the
automatic stay in the United States. There may also be a court-appointed
overseer (supervisor) to supervise disposition of property by the interim receiver
prior to ruling for commencement.

C. Appeal of the Ruling for Commencement or Adjudication.

An appeal of the ruling or adjudication is theoretically possible, as in the
United States, but it is unlikely to be successful because after the ruling or
adjudication, default clauses are triggered or trade credit dries up, necessitating
the insolvency proceeding.

54. Matsuo § 8.03[1][a] at 8-16.
56. Matsuo § 8.02[3][c] at 8-11 to 8-12.
at LU 36.
61. Matsuo § 8.03[1][b] at 8-16 to 8-17; Reorg. Art. 50 at LZ 23-24, 28 U.S.C.A. § 158 (West
D. Notice of Proceedings

Upon adjudication of bankruptcy or a ruling for commencement of reorganization, public notice is immediately given.62 The notice contains more detailed information than a U.S. notice of first meeting.63 For individuals, the commencement of the case subjects them to the disgrace of a compulsory public notice in newspapers, and they may not depart from their dwelling place (meaning geographical area of residence) without the permission of the court.64

E. Post-ruling or Post-adjudication Proceedings

1. Officers and professionals

a. Reorganization

After a ruling for commencement of reorganization, a receiver is appointed by the court. The receiver may, after consultation with the agent and investigation commissioners (discussed below), make decisions for the debtor.65

A receiver may be a trust company, bank or other corporation, as well as an individual unlike in the United States, where the equivalent of a receiver (a trustee) is usually an individual.66 The receiver may appoint an operating “agent” for whose actions the receiver is responsible.67 This “agent” may well be the “angel” just mentioned. The receiver may also, with the permission of the Court, appoint a legal advisor.68 There can be multiple receivers among whom the court will divide appropriate duties.69

The court can appoint an investigation commissioner, who functions as a “creditor-selected examiner,” acting for all creditors.70 An investigation commissioner is held to the same standard of care as a receiver and must have similar qualifications.

Another professional is the agent commissioner, who may represent the interests of a subset of creditors and has a narrower scope of representation than an investigation commissioner. Reorganization unsecured creditors, reorganization

64. Bankr. Art. 147 at LU 33–34; see also Bankr. Art. 149 at LU 35; Matsuo § 7.04[5][b] at 7-18.
66. Reorg. Art. 95 at LZ 41. See supra note 56.
67. Reorg. Art. 98 at LZ 42.
68. Reorg. Art. 186 at LZ 86; Matsuo § 8.03[3][a] at 8-20.
70. Reorg. Art. 101 at LZ 43–44.
secured creditors, or shareholders, with permission of the court, either jointly or separately, may appoint one or several agent commissioners. 71

A receiver proposing a reorganization plan generally stays on to implement the plan once it is approved. 72 If a receiver departs from office, an accounting is required just as for a trustee in the United States. 73

There may also be a "trustee company" appointed pursuant to a resolution of debenture holders under the Secured Bonds Trust Law [of Japan]. This entity acts on behalf of all bondholders. 74

b. Bankruptcy

After an adjudication in bankruptcy, an administrator in bankruptcy is appointed by the court. He is the bankruptcy equivalent of a "receiver." In bankruptcy, the inspection commissioners are appointed at the first meeting of creditors. 75 They are the bankruptcy equivalent of the reorganization investigation commissioner. Inspection commissioners act as overseers on behalf of the creditors, who as a body may direct the inspection commissioners' actions or overrule the inspection commissioners' decisions. 76 The administrator in bankruptcy (trustee) must have consent of the inspection commissioners to dispose of certain assets and to make distributions. 77

73. Reorg. Art. 99 at LZ 43.
74. Reorg. Art. 161 at LZ 74.
75. Bankr. Arts. 7 at LU 2, 142 at LU 33, 170 at LU 39; Matsuo § 7.06[1] at 7-34 to 7-35 (also referred to as "superintendants").
77. Bankr. Art. 197 at LU 44–45:

Article 197. In order to do any of the following acts, the administrator in bankruptcy shall obtain consent of inspection commissioners; provided however, that this shall not apply to those acts mentioned under items (7) to (14) inclusive, of which value is not less than one hundred thousand yen:

(1) Voluntary sale of real rights on immovable property, Japanese vessels of which registration is required, and foreign vessels;
(2) Voluntary sale of mining right, fishery right, patent right, design right, right of utility model, copyrights, and neighboring right thereof;
(3) Assignment of business;
(4) Sale in block of merchandises;
(5) Obtaining loans;
(6) Approval of the renunciation of succession under the provisions of Article 9 paragraph 2, approval of the renunciation of testamentary gifts by a universal title under the provisions of Article 10, an renunciation of specific testamentary gifts under the provisions of Article 11 paragraph 1;
(7) Voluntary sale of movables;
(8) Assignment of obligations and of valuable instruments;
(9) Demand for performance under the provisions of Article 59 paragraph 1;
(10) Institution of an action;
c. General rules applicable to professionals

Both the administrator in bankruptcy and the receiver are charged with the duty of care of a good manager, with preserving the estate, and with managing the business and assets of the company.

Compensation for the above professionals is set by the court. The professionals appointed, much like in the United States, usually have prior experience in insolvency matters and practice in the area as a specialty.

In Japan, the investigation commissioner(s) and agent commissioners perform the oversight function of the U.S. creditors' committee and its counsel.\(^7^8\)

2. Meetings

Under Japanese law, the creditors exercise considerably more influence on a case than in the United States. There are three key meetings in reorganizations: (i) the "first meeting of persons concerned," much like the U.S. Section 341 "first meeting," (ii) the special day for investigation of reorganization claims and reorganization security rights,\(^7^9\) and (iii) the meeting of interested persons.\(^8^0\) The latter two meetings have no American counterparts.

In a reorganization, the court sets the date of the meeting of persons concerned and the date for investigation of claims and security rights. Public notice is given. The meeting of persons concerned must be held from one week to two months after the ruling for commencement. The claims investigation meeting is set two weeks to four months after the ruling for commencement of reorganization. This latter date must also be between one week and two months from the date of the first meeting.\(^8^1\)

The Japanese equivalent of an American "first meeting" in a bankruptcy occurs on application of the administrator or the inspection commissioners, on petition of one fifth of creditors in amount of claims, or by order of the Court. Public notice is given.\(^8^2\) The persons present at the initial meetings vote in proportion to the amount of liquidated claims that each holds.\(^8^3\) For claims and creditors that are indefinite, e.g. disputed or unliquidated, the court determines

\(\text{(11)}\) Agreement of compromise and of arbitration;

\(\text{(12)}\) Relinquishment of a right;

\(\text{(13)}\) Admittance of claims pertaining to the bankrupt estate, of the right to redeem; and of the right of separation;

\(\text{(14)}\) Redemption of the subject-matter of the right of separation.

\(^7^8\) 11 U.S.C. §§ 1102, 1103 (1982).


\(^8^1\) Bankr. Art. 176 at LU 39–40, Art. 177 at LU 40.

\(^8^2\) Reorg. Art. 113 at LZ 50–51; Bankr. Art. 182 at LU 41.
whether or not the right to vote may be exercised and on what amount of claim
the vote may be exercised.\textsuperscript{84}

In reorganizations, this early meeting is less critical because more profes-
sionals are involved to represent various interests throughout the proceeding. The
first meeting is used to determine the granting of allowances and to make deci-
sions regarding discontinuance of the business and how cash collateral is to be
handled.

The meeting for investigating claims and security rights is usually postpon-
e until parties to the case are in a position to agree formally on the amounts of all
claims.

The meeting of interested persons in reorganization follows the submission of
a draft plan of reorganization, and the special day for investigating claims.\textsuperscript{85} The
meeting of interested persons can be used to confirm a plan with the approval of
the Court. These latter two meetings are very important to the confirmation of a
plan.

\section*{F. The Japanese Analogies to the Section 361–365 Administrative
Powers and the Effects of Provisions of those Sections on Claims.}

\subsection*{1. Introduction}

The four substantive areas covered in sections 361 to 365 of the U.S. Bank-
ruptcy Code are: adequate protection; the automatic stay; the use, sale and lease
of property, including borrowing; and unexpired leases and executory contracts.

\textbf{2. Adequate protection and the automatic stay in Japan: "suspension of pro-
ceedings" and "preservation measures"}

The concept of adequate protection in the United States, in the form of pay-
ment or additional collateral, arises in the context of the prohibition of a secured
creditor from realizing on its claim. Absent a stay prohibiting secured creditor
action, adequate protection is not needed. The subject is best addressed in the
context of the automatic stay and its Japanese equivalent.

Just as in the United States, Japan has measures in all of its bankruptcy laws
that prohibit collection of pre-petition claims pending distribution through the
insolvency proceeding.

\textbf{a. Japanese law: preservation rights.}

Prior to the ruling for commencement of reorganization or adjudication of
bankruptcy, a set of remedies called preservation measures can be invoked by

\textsuperscript{84} Reorg. Art. 117 at LZ 51–52; Bankr. Art. 182 at LJ 41.
\textsuperscript{85} Matsuo § 8.03[b] at 8-20 to 8-21. Reorg. Art. 187 at LZ 86. Reorg. Arts. 192 at LZ 87, 200 at
leave of court only. In reorganization, they are common. The threshold to be met to obtain preservation measures appears higher and the scope more limited in bankruptcy than in reorganization.

The Court may order provisional attachment, provisional disposition or any other necessary measures for preservation of the estate. Preservation measures can also include a prohibition of payments, a prohibition of borrowing or a prohibition of disposal of assets. The preservation measures can be directed against the officers and directors of the debtor. The check clearing house can be ordered to stop refusing to perform transactions for a debtor even if "checks" have been dishonored. Normally, a company is disqualified from the check-clearing house if a check fails to be honored twice. Without this preservation measure, a company would effectively be forced to cease business. The clearing house is protected by a priority claim for common benefit.

b. Post-adjudication "suspension of proceedings" in Japan.

Upon the application for commencement of reorganization proceedings, the Japanese District Court may, and usually does, suspend the following: bankruptcy procedures, composition procedures, arrangement procedures, provisional or completed dispositions of company assets, auction sales, exercise of hypothecation rights, lawsuits, and procedures of administrative government agencies in connection with the company's assets.

Under the Japanese Bankruptcy Law, as under U.S. law, the effect of an adjudication of bankruptcy is to suspend execution, attachment, provisional disposition or enforcement of any type of hypothecation. These measures are effective until the case is closed. In contrast, however, to U.S. law, Japanese Bankruptcy Law does not have an automatic injunction against foreclosure. Accordingly, adequate protection is not normally needed in a bankruptcy setting in Japan. In Japan, if the right to foreclosure is not properly exercised, or is not exercised at all, it may be lost in a bankruptcy setting.

Although Japan has no explicit standards of adequate protection, pre-ruling suspension "of compulsory execution, of provisional attachment, of provisional disposition, or of auction sale . . . [may occur where there is no] likelihood of

88. Bankr. Arts. 95 at LUZ3 155 at LU 36; Matsuo § 7.03[3][b] at 7-13 to 7-14.
89. Reorg. Arts. 37, 39 at LZ 17–19; Bankr. Art. 155 at LU 36.
90. Reorg. Art. 72(1)(1), 72(1)(2), 72(2) at LZ 32–33.
95. Bankr. Art. 204 at LU 46.
inflicting unreasonable losses on the creditors..."96 Japan has no comparable timetable to the thirty day/sixty day preliminary hearing/final hearing rule on motions to lift the automatic stay, as found in the U.S.97

In addition, the Reorganization Law prohibits performance or actual payment by the Debtor to repay pre-petition claims, just as in U.S. Sections 362, 363, and 549.98 The practical exception to that rule is wages of company employees. These constitute claims for "common benefits," or priority claims.99

The exceptions to the suspension of proceedings for bankrupt individuals are in the area of Domestic Affairs Trial Law, and the management of property under matrimonial contract. Those matters are deemed to be under the "jurisdiction" of the Domestic Affairs Trial Law. That law, however, incorporates aspects of the Bankruptcy Law where a bankruptcy has been filed.100

In a Japanese bankruptcy, it does not appear that lawsuits are stayed—only the execution of judgment is stayed.101

Japanese law includes the concept of set-off. The law does not explicitly prohibit effecting set-offs subsequent to the commencement or adjudication of a proceeding. A set-off may be exercised "without resorting to the bankruptcy procedure."102 This is somewhat less clear in a reorganization context because a set-off could be deemed an act prejudicial to the estate and may therefore be voidable.103 Set-offs pursuant to cross-assignments of claims are prohibited as in the United States.104

A unique exception exists for a medium or small entrepreneur to the suspension of proceedings and the prohibition against pre-petition payments in reorganizations. If the debtor company is the main customer of such entrepreneur and it is feared that the entrepreneur would be seriously impeded in continuing his enterprise unless the reorganization claim held by him is paid, the court may, prior to the ruling to approve the reorganization plan, permit whole or partial payment of the claim, on application of the receiver or on the court's own motion.105

96. Reorg. Art. 37(1) at LZ 17–18.
100. Bankr. Art. 68 at LU 15.
101. Bankr. Arts. 47(7), 69, 70 at LU 9, 15–16. No provisions interrupting or staying lawsuits are present in the bankruptcy law such as exist in reorganization law; cf. Reorg. Art. 68 at LZ 31.
103. Reorg. Arts. 78(1), 78(2) at LZ 34–35; Reorg. Arts. 162–63 at LZ 74–77.
105. Reorg. Art. 112-2 at LZ 50. Matsuo § 8.01[2][c][ii] at 8-6, § 8.05[1] at 8-30 (noting that the receiver’s management must consider alleviating financial distress in small towns as a result of an employer company’s financial distress).
Because Japanese law is more creditor-oriented and the creditors can closely supervise a case, and because a foreclosure action may generally continue in the face of bankruptcy, the significant litigation which is now occurring over adequate protection issues in the United States is not as common in Japan. Such an orientation and the absence of the "automatic stay" in bankruptcy may have the effect of forcing consummation of liquidation proceedings in Japan more promptly.

c. Adjudication and taxes

The pre-ruling suspension of proceedings in reorganizations can include a suspension of tax delinquency collection. Suspension lasts for two months from the date of ruling of suspension or until the ruling for commencement of reorganization, whichever is earlier. After the ruling, such suspension continues for one year. There is no limit on the number of suspensions that may be invoked, but there is a compulsory review by the Court for each continued suspension. With respect to tax delinquency proceedings, there is no suspension of the proceeding itself during or because of the reorganization or bankruptcy. Collection measures in progress at the time of adjudication of bankruptcy are not suspended or stayed. In the United States, there is an automatic stay in all proceedings against collection and against administrative proceedings, but not against issuance of a deficiency notice.

3. Use, sale, and lease of property

Japanese law has less language than United States law about the use, sale and lease of property during an insolvency proceeding, but does require formal consent of professionals or court approval. In the United States, notice and an opportunity for hearing are required before use, sale or lease of property out of the ordinary course of business. The manner of handling money deposits and other valuables is be determined by the Japanese court. This is very similar to the restrictions on use of cash collateral in U.S. Section 363 and the provisions in U.S. Section 345 relating to deposits in appropriate depository institutions. In Japanese reorganizations, decisions on the use of cash collateral are made at the first meeting of creditors.

If the administrator in bankruptcy intends to sell property of certain kinds for a sum below a certain amount, the consent of the inspection commissioners is sufficient; absent that consent, permission of the court must be obtained.

106. Reorg. Art. 37(2), (3) at LZ 18.
107. Reorg. Art. 67(2), (3) at LZ 30.
110. Reorg. Art. 185 at LZ 86.
112. Reorg. Art. 188 at LZ 86.
other kinds of property, permission must be obtained from the court even with the
consent of the inspection commissioners. In general, there is no unilateral
authority for the administrator to dispose of property in the absence of a court
order authorizing disposition. A reorganization receiver must proceed in similar
fashion to obtain consents.

4. Unexpired leases

Unexpired leases and related claims under Japanese insolvency law are not
only governed by the Bankruptcy Law and Corporate Reorganization Law provi-
sions, but also by the Japanese Civil Code. Assumption is not explicitly avail-
able, but the debtor's interest in certain types of leases can be protected so long as
rent is kept current by the debtor. The practical result for all but short term
commercial leases is similar to the result under U.S. law and Section 365.

In the United States, the lessee may assume a lease in default if all defaults are
cured, actual damages are paid, and adequate assurance of future performance is
given. The lessee may also reject any lease, based on his business judgment. The
lessor in the United States may reject a lease, but the tenant, unless otherwise
applicable law permits eviction, may remain in the premises until the close of the
term under the lease. The lessee who is not in default may not be ejected in the
United States by a bankrupt landlord.

The Japanese trustee may terminate a non-residential, short-term lease on
behalf of a debtor lessee in accord with Article 617 of the Civil Code. No
damages may be claimed by the lessor.

With respect to the issue of assumption in Japan, the bankrupt lessee may fall
under special rules applicable to "emphyteusis" and "superficies." Emphyteusis
is defined as a long term or perpetual lease where rent is reserved from the
property. Superficies is defined as an alienation by lease of the earth's surface
for a dwelling place. For dwellings and residential tenants, Japanese law is
very protective. Either of those types of leases which are long-term and residen-
tial in character may be sold, re-leased, or assigned. The rules relating to termi-
nation in the Civil Code by the trustee on behalf of a lessee-debtor (or
"rejection," as American practitioners think of rejection) are not generally ap-
plied to land leases or residential leases; i.e., those leases are not subject to

113. Bankr. Arts. 197(7)-(14) at LU 45.
114. This is more implicit than explicit. There is no statutory authority for a receiver to petition the
court to sell an asset. However the receiver is to manage the assets, to appraise them and to file a
115. Matsuo § 7.05[6][c] at 7-30 at n. 46.
117. Minpo (Japanese Civil Code) [hereinafter "Civil Code"], Law No. 89 of 1896 and Law No. 9
of 1898, Art. 617.
119. Id. at 1288.
notices of termination by the administrator under Civil Code Article 621. Therefore, it appears that a bankrupt lessee can force a lessor to continue a lease if the lease relates to personal dwellings and long-term land leases. This preserves critical long-term leases for corporations in reorganization and prevents dislocation of individuals.

In Japan, the bankrupt lessor can only compel termination of leases under their terms. He appears to have limited ability to reject leases and relieve himself of obligations. The bankrupt lessor or his administrator cannot reject a lease with respect to personal dwellings, superficies or emphyteusis because of their sensitive, long-term character.

Upon a lessor's bankruptcy, "caution money," e.g., a security deposit, is treated as advance rental post-bankruptcy for the period of lease at the time of the adjudication of bankruptcy or for the next following period only. The lessee is thus relieved of rent to the extent of caution money during the initial post-reorganization lease period. Advance rental is treated in the same manner. The post-petition debt to the bankrupt landlord is thus set-off against the pre-petition obligation of the landlord to return the advance rent or caution money. Section 507(a)(5) is the only similar provision in the United States; it allows security deposits of consumer lessees to be set-off against the claim of lessors.

Damages related to breach of leases as a result of an insolvency proceeding are relatively low in Japan because leases can often be easily terminated with low damages in the case of a lessee or can be, and are, enforced with full payment. Under the Civil Code, which applies to leases in reorganization, there may not be a claim by a lessor for damages from termination. The Japanese landlord's remedy is to relet the premises, not to claim damages. The U.S. landlord's remedy is the larger of 15% of the remaining rent on the lease or three years' rent.

5. Bilateral and executory contracts

a. United States and Japanese standards

In the United States, an executory contract is defined as a contract in which future obligations are remaining on the part of both parties and failure to perform those obligations would be a material breach of the agreement. To assume a

120. Matsuo § 7.05[6][c] at 7-30 n. 46.
121. Civil Code Art. 617.
122. Matsuo § 7.05[6][c] at 7-30.
123. Matsuo § 7.05[6][c] at 7-30.
125. Civil Code Arts. 617, 621. The termination by at the administrator for a lesser must be pursuant to standard notice periods in Article 617: one year for land, three months for a building, one day for a room, and at the end of the harvest season for a lease of farmland.
127. 2 L. P. King, COLLIER ON_bankruptcy, ¶365.02 at 365-15 (15th ed. 1987 Supp.)
defaulted executory contract, the benefits must outweigh the burdens in the trustee's reasonable business judgment, all defaults must be promptly cured, actual damages must be paid and adequate assurances given of future performance. If the trustee desires to affirmatively reject an executory contract, the burdens must outweigh the benefits in the trustee's reasonable business judgment.128

Japanese insolvency law focuses on a broader class of contracts than executory contracts: bilateral contracts, which include executory contracts. A bilateral contract is defined as a contract under which at one time there were future obligations on the part of both parties, such that a failure to perform those obligations would be a material breach of the agreement.129 Thus, in Japan, any non-unilateral contract, even with complete performance by one party, is still a bilateral contract. In the United States, a contract fully performed by one side is no longer an executory contract, but simply gives rise to a claim for damages.130

The options of the Japanese receiver or administrator in bankruptcy are either to perform the obligations of the bankrupt and demand performance by the other party to the bilateral contract, or to rescind the contract and return the performance given by the other side.131 The U.S. concept of rejection of a bilateral contract for the sale of goods where the debtor actually has the goods is not a practical option in Japan. The Japanese non-bankrupt party to the rejected bilateral contract has the right to recover all property sold to the debtor still in the debtor's hands upon rescission or the right to assert a priority claim.132 In the United States, such a creditor has only an unsecured claim except for a limited right to reclaim goods delivered in the 10 days prior to the petition.

Japanese law does not specifically address the enforceability of "ipso facto clauses." They are invalid in the United States with a few exceptions.133 Ipso facto clauses are clauses that automatically terminate a contract in the event of bankruptcy. A party to a Japanese bilateral contract with a bankrupt may not refuse to perform its obligations on the grounds of monetary default and non-payment. This implicitly invalidates "ipso-facto" clauses.134 Overall, ipso facto clauses appear unenforceable in Japan in circumstances similar to where they are unenforceable in the United States.

130. See supra note 127.
131. Reorg. Art. 103(1) at LZ 45; Bankr. Art. 59 at LU12. However in bankruptcy a contract for a commodity with a publicly quoted price on which delivery is to occur part adjudication is deemed rescinded. Bankr. Art. 61(1) at LU 46.
132. Reorg. Art. 104(2) at LZ 46; Bankr. Art. 60(2) at LU 12-13.
134. Reorg. Art. 104-2(1) at LZ 46. However, if the receiver or administrator require performance, any unpaid amount under the contract is a claim for common benefit. Reorg. Art. 104(2) at LZ 46; Bankr. Art. 59(1) at LU 12.
If a defaulted contract is to be assumed in Japan, there does not appear to be an explicit concept of adequate assurance of future performance as there is in the United States.\textsuperscript{135} Defaults must be immediately cured in Japan, not merely promptly cured as in the United States. The affirmation of a Japanese contract gives rise to a claim for common benefits which is similar in concept to a priority claim under the U.S. Bankruptcy Code.\textsuperscript{136}

\textit{b. Pre-emptory Notice}

The Japanese Reorganization Law provides that the non-bankrupt party to a bilateral contract may give pre-emptory notice to the receiver to perform the contract. If the receiver fails to respond with a definite answer within thirty days, the receiver is deemed to waive the right of rescission of the contract. The contract then must be performed. The thirty day period can be extended.\textsuperscript{137}

In a Japanese bankruptcy, the non-bankrupt party to a bilateral agreement may give pre-emptory notice to the administrator in bankruptcy. Such notice must designate a reasonable period of time in which the administrator must respond as to whether he is rescinding the contract or demanding performance of obligations. In the absence of a definite answer within the given period, the contract is deemed rescinded.\textsuperscript{138}

\textit{c. Damages}

Upon rescission of a bilateral contract, the non-bankrupt party has a right to damages similar to that of a party to a rejected executory contract.\textsuperscript{139} If the contract is one with publicly-listed quotations, damages may be set by the difference between publicly listed quotations and the amounts to be paid under the contract.\textsuperscript{140}

\textit{d. Reclamation/redemption}

With respect to bilateral contracts, the most significant difference between Japanese and American law is in the area of reclamation, or redemption, as it is known in Japan. In a Japanese reorganization, where a bilateral contract exists, if the non-bankrupt party has rendered part performance, and if the receiver rescinds the contract, the performance rendered may be reclaimed by the creditor party to the bilateral contract. Also, if the property that was delivered to the debtor is still in existence at the time of rescission, then the property must be

\textsuperscript{136} 11 U.S.C. 502(b)(1) (1982), Reorg. Arts. 208(7) at LZ 94, 103(1) at LZ 45, 104-2(2) at LZ 46.
\textsuperscript{137} Reorg. Art. 103(2), (3) at LZ 45.
\textsuperscript{138} Bankr. Art. 59(2) at LU 12.
\textsuperscript{139} 11 U.S.C. § 502 (1982); Bankr. Art. 60(1) at LU 12; Reorg. Art. 104(1) at LZ 45–46.
\textsuperscript{140} See, e.g., Bankr. Art. 61(1) at LU 13, which applies generally to claims for rescission, Bankr. Art. 61(3) at LU 13, 60(1) at LU 12.
returned. In reorganization, if the property is not in existence, then the non-bankrupt party has a claim for common benefits (priority claim). Significantly, there is no ten day limit such as exists under Section 546 in the United States (which provides that a creditor can reclaim goods that exist so long as demand is made within 10 days of delivery to the debtor). The effect of these provisions is to grant substantial protections to trade creditors. These provisions also act as a practical limitation on the “avoiding powers” of the receiver or administrator in bankruptcy and a less detailed preference section is the result.

There is a provision in Japanese reorganization and bankruptcy law analogous to UCC Section 2-705 and Section 546 relative to in-transit liens. Goods in transit may be demanded if the trustee/buyer pays the obligations and demands the non-bankrupt party’s performance of its obligations under the rules relating to bilateral contracts.

e. Contracts for hire

Under the U.S. Bankruptcy Code, a contract for hire is an executory contract. If a contract for hire is actually a contract for personal services, i.e., a contract in which at least one party specifically relies on the skills of the other, the trustee or debtor-in-possession may not assume the contract, contrary to the general rule that executory contracts may be assumed.

In contrast, in Japan, if the debtor is a bankrupt building contractor (who cannot be in corporate reorganization), the receiver or administrator may purchase and provide to the debtor/contractor the necessary materials to complete the work and require that the contractor/bankrupt finish the job. If the work need not be specifically completed by the bankrupt, a third party can be nominated to carry out the work. In either case, whatever the bankrupt contractor would be entitled to receive for completing the work becomes an asset of the estate. The effect is that a receiver or administrator may compel assumption of what appears to be a personal services contract.

If the now-bankrupt debtor hired the contractor, then, under Japanese law, both the trustee and the contractor have a right to rescind the contract. Neither the trustee nor the contractor can make claims for services based on any contract in

141. Reorg. Art. 104(2) at LZ 46; Bankr. Art. 60(2) at LU 12–13.
142. Reorg. Art. 104(2) at LZ 46; Bankr. Art. 60(2) at LU 12–13.
146. Reorg. Art. 103(1) at LZ 45; Bankr. Arts. 59 at LU 12, 89 at LU21; Reorg. Art. 64 at LZ 28.
147. 11 U.S.C. § 365(a), 365(c) (1982).
148. Bankr. Art. 64(1) at LU 14; Matsuo § 7.05[6][d] at 7-31.
149. Bankr. Art. 64(2) at LU 14.
150. Matsuo § 7.05[6][d] at 7-31 n.47; Civil Code Art. 642.
which the debtor has hired the contractor. A claim for redemption of goods would be preserved.\(^{151}\)

In the United States, all wages or earnings of an individual debtor subsequent to the filing of a petition are explicitly excluded from the definition of property of the estate.\(^{152}\) A Japanese administrator may compel a debtor to perform a contract with the proceeds of the contract to be paid to the administrator.\(^{153}\) In the United States, the trustee in bankruptcy can only compel the performance of services to assist in the administration of the estate.\(^{154}\)

\(f.\) **Employment contracts**

Employment contracts cannot be assigned under Article 625 of the Civil Code of Japan.\(^{155}\) If an employer is adjudged bankrupt, either the employee, the receiver, or the administrator in bankruptcy can petition to terminate a contract regardless of the contract's term. Two weeks after such notice the contract is terminated.\(^{156}\) However, if the administrator in bankruptcy decides to terminate and to nullify the contract, there are certain additional requirements. The administrator or receiver must comply with the termination provisions of Japan's Labor Standards Act, which requires at least 30 days' notice or 30 days' compensation.\(^{157}\) If the receiver or administrator does not have the funds to pay thirty days' compensation either by maintaining employees on the payroll for thirty days or paying it directly, the Japanese Government will supply the necessary funds.\(^{158}\) In addition, there is no prohibition against an administrator or receiver paying prepetition wages during the proceeding.\(^{159}\)

\(g.\) **Collective bargaining agreements**

Both the United States and Japan accord labor and labor organizations a special place in the bankruptcy and reorganization scheme.\(^{160}\) In Japan, labor claims are often immediately paid in a reorganization proceeding to avoid disputes and large priority claims.\(^{161}\) The Corporate Reorganization Law specifically exempts labor contracts from the class called bilateral contracts.\(^{162}\) The notice provisions requir-
ing thirty days' pre-emptory notice to reject a bilateral contract exclude collective bargaining agreements.\(^{163}\)

Under Japanese Law, the labor union or other employee representative dealing with the debtor has standing to appear before the court and the court does consider the employees' positions.\(^{164}\) There is no right under Japanese law to reject a collective bargaining agreement as there is in the United States.\(^{165}\)

In the United States, under the 1984 Amendments to the Bankruptcy Code, the trustee or debtor-in-possession must make a proposal to modify the collective bargaining agreement to the authorized representative of employees covered by a collective bargaining agreement. The proposal must be limited to necessary modifications. Relevant information must be provided to evaluate the proposal.\(^{166}\) Further, the trustee must meet with the employees' authorized representative. Only if the authorized employee representative refuses to accept the proposal without good cause and if the balance of equities favors rejection of the agreement may the court approve an application for rejection of the collective bargaining agreement. Unilateral modification is prohibited unless various time periods have expired, various hearings have commenced and no ruling has been given by the Court.\(^{167}\) Because Japanese law does not permit any non-agreed-upon modification, there can be no unilateral modification.

Wage claims arising from rejection of the collective bargaining agreement in the United States are unsecured except to the extent that they are administrative claims or were incurred within ninety days prior to the petition and are less than $2,000 per employee.\(^{168}\) Retirement contribution claims are treated similarly in the United States, except the $2000 limit is calculated differently.\(^{169}\) In Japan, there is a six-month priority period for wage claimants.\(^{170}\) In addition, roughly six months' salary or one-third of the retirement claim directly due from the company is treated as claims for common benefits.\(^{171}\) This area is currently the subject of great controversy in the United States because of the LTV case (a major reorganization of a steel company and related subsidiaries) and recent temporary legislation.\(^{172}\) Cash bonds posted by company employees to ensure good behavior or to insure against theft are claims for common benefits in Japan.\(^{173}\) The struc-

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171. Reorg. Art. 119-2(2); *see also* Matsuo § 8.04(2)(a). *But see* Reorg. Art. 119-2(3) and Reorg. Art. 208(8).
ture of the Japanese statutes concerning bilateral contracts, damages and collective bargaining agreements is designed to afford trade creditors and employees strong protection.

Because Japanese banks often are shareholders in companies to which they lend and can foreclose on collateral more easily than in the U.S., and because of the propensity in Japanese reorganizations to find corporate sponsors or “angels,” the shareholders/lenders are not as poorly protected as might appear from the discussion of the rights of workers and trade creditors. Precipitous action by secured lenders that could extinguish shareholder interests is not common because often the largest shareholders are these same secured lenders. The result is that in a heavily secured estate, the secured lenders/shareholders have practical leverage because they can press foreclosure or withhold new capital as well as extinguish junior interests. However, trade creditors and unions have much statutory leverage as well. In a case with large unsecured assets, the trade creditors and unions have the upper hand.

IV. U.S. CHAPTER 5: CLAIMS, AVOIDANCE RIGHTS, AND SCOPE OF THE ESTATE

A. Claims

1. How a Japanese reorganization plan affects claims

Under the U.S. Bankruptcy Code, a claim amount is determined, a method of distribution on that claim is proposed, and further action to collect on the claim beyond the contemplated distribution in the plan is prohibited. The remainder due is discharged.

In a Japanese “straight” bankruptcy, a claim is allowed in the full amount and a dividend paid just as in the United States. In a Japanese reorganization, by contrast, the claims are adjusted in amount to a feasible level and then appropriate payment “in full” is made. As under U.S. law, the amount of the claim is determined without including interest accrued subsequent to commencement of the proceeding.

174. Matsuo § 8.03[1][a][c] at 8-16.
179. Reorg. Art. 211(1) (stating, “The reorganization plan shall stipulate the terms for modifying the rights of all or some of the reorganization creditors.”) at LZ 96; Reorg. Arts. 212 at LZ 96, 242(1) at LZ 112.
2. Types of claims

There are five general types of claims under Japanese insolvency law. First are secured claims. These are similar in nature to those under the U.S. law. Second are claims for common benefits in a reorganization matter or, as they are known in a bankruptcy, claims appertaining to bankruptcy. Under the U.S. law these are described as priority claims. Third are unsecured claims. In Japan, these may include future claims. Fourth are deferred claims which are generically referred to in the United States as subordinated claims. These include such items as penalties and interest. Fifth are the claims of shareholders, which are referred to as "interests" in the United States.

a. Secured claims

Secured claims are claims for which the claimant holds collateral belonging to the debtor. They are valued as of the time of the commencement of reorganization proceedings on a "going concern" basis. A secured creditor in Japan does not have the option, in lieu of treatment as a secured creditor to elect treatment in the class of unsecured claims with that claim to be secured by the collateral. Secured claims in the United States are evaluated on a projected use/going concern basis at the time of confirmation of a plan.

In Japan there is a limit, whether or not a claim is secured, on claims for interest, compensation for damages, or penalty money. That limit is one year after the commencement of the case on a secured claim. There is an exception to this rule on damages for a security right associated with debenture. The damages or penalty money (interest), even within that one year limit, do not count towards voting rights. No such limits exist in the United States.

181. Reorg. Arts. 159 at LZ 72; Bankr. Arts. 228 at LU 48, 258(2) at LU 54.
182. 11 U.S.C. § 506(a) (1982); Reorg. Arts. 159(1), at LZ 72, 156 at LZ 71; Bankr. Art. 228 at LU 48, 92 at LU 22, 96 at LU 23.
186. Reorg. Art. 159(3) at LZ 72; Bankr. Art. 258(2) at LU 54.
190. Bankr. Art. 289 at LU 60; Reorg. Art. 159(5), (6) at LZ 72.
b. Common benefits

Claims for common benefits include wages due and accrued within the last six months, retirement benefits due, funeral expenses, costs of litigation, and the expenses of the receiver or administrator in bankruptcy. There is also a special priority claim for monies deposited with a debtor company for savings. Many Japanese corporations have no retirement plan; rather, they strongly encourage employees to put money for retirement into these high-interest "company savings plans." While the United States has more limited priorities for employees and slightly different priority classes, the United States classes are similar in their nature and include employees, post-petition expenses, administrative fees, and consumer deposits.

Utilities must continue service, but their claims are given priority status pre- and post-filing. In the United States, pre-petition utility claims are unsecured, but the utility can require a deposit on post-petition services. Management costs and monies expended personally by managers to keep a company in business are also claims for common benefits: this is a contrast to the United States which has no such provision. Gap claims, i.e. claims arising in the period between the time of filing and the entry of the ruling for commencement, are paid in the same class as claims for common benefits. In the United States, gap claims have a lower priority of payment than administrative claims, even though they rank "above" unsecured claims.

Taxes due to governmental units are claims for common benefits in bankruptcy, but not in reorganization. In reorganization, such taxes are unsecured. There are some exceptions: withholding taxes, security transaction taxes, and taxes not yet due all are claims for common benefits. Tax claims are effectively accelerated upon adjudication of bankruptcy. A plan of reorganization can only postpone collection of taxes in Japan by paying tax claims over a period of up to three years. This is one-half the period available in the United States.

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197. Bankr. 47(1) at LU 9; Reorg. Art. 208(1) at LZ 93.
198. Bankr. Art. 47(4) at LU 9; Reorg. Art. 208(4) at LZ 93.
202. Reorg. Arts. 119-3 at LZ 53, 208(2), 208(5) at LZ 93; Matsuo § 8.04[2][c].
203. Reorg. Art. 208(1) at LZ 93.
209. Reorg. Art. 122(1) at LZ 55.
States.\textsuperscript{210} Interest on taxes is not payable during that three year period in Japan.\textsuperscript{211} Therefore, while the Japanese treatment is not precisely like that in the United States, both countries do grant tax claims special treatment.\textsuperscript{212}

c. Unsecured claims

The next class of claims is unsecured claims.\textsuperscript{213} This class may include unliquidated contingent claims.\textsuperscript{214} All claims are filed and determined as of the time of commencement of the case; accordingly, interest is not accrued or paid after the case begins on unsecured claims. As an alternative to estimation, a Japanese plan may provide that unliquidated claims will be paid as allowed.\textsuperscript{215} Reorganization Article 118(2) explicitly allows a plan to cover future claims.\textsuperscript{216} The explicit language dealing with future claims is not found in the U.S. Bankruptcy Code and normally “future” claims are not dealt with in reorganization plans in the United States.\textsuperscript{217} Late filed claims may be allowed, but if a special investigation meeting is needed, the late filer bears the costs.\textsuperscript{218}

d. Subordinated claims

Deferred reorganization claims are automatically subordinated in Japan. They include interest, damages and penalties accruing post-filing, and certain tax penalties. There are analogous provisions in the Japanese Bankruptcy Law.\textsuperscript{219}

e. Shareholder claims

Shareholders need not file a claim in a reorganization proceeding.\textsuperscript{220} Their interests are often ignored because they have no right to notice if the debtor is insolvent, and in any event are usually diluted or extinguished in a plan of reorganization.

3. Filing a claim

The receiver prepares a list of claims. They appear to be prima facie evidence of indebtedness, similar to U.S. Code Section 502.\textsuperscript{221} A creditor should file the Japanese equivalent of a proof of claim (a report of claim) if the receiver's list differs from the creditor's records. Appropriate evidentiary support must be

\textsuperscript{211} Reorg. Art. 121(1) at LZ 53.
\textsuperscript{213} Reorg. Art. 159(3) at LZ 72.
\textsuperscript{214} Reorg. Art. 117 at LZ 51–52.
\textsuperscript{215} Reorg. Arts. 159 at LZ 52, 215 at LZ 97, 218 at LZ 98.
\textsuperscript{216} Reorg. Art. 118(2) at LZ 52.
\textsuperscript{217} See, e.g. 11 U.S.C. §§ 101(4)(b), 502(c) (1982).
\textsuperscript{218} Reorg. Arts. 127(1) at LZ 59, 138 at LZ 64 140 at LZ 65, 121 at LZ 54, 159(4) at LZ 72.
\textsuperscript{219} Bankr. Art. 46 at LU 8.
\textsuperscript{221} Reorg. Arts. 129[3] at LZ 61, 164(2) at LZ 78, 180 at LZ 84.
given, such as invoices, contracts, notes, or statements of account. If priority is claimed, that must be noted on the report of claim.  

Secured creditors must also file a claim or their rights may be lost. In the United States, a secured creditor must file a claim only to protect rights to participate in plan distributions on the unsecured portion of the claim; the creditor need not do so to protect this property right in rem. In a Japanese bankruptcy, a person exercising the right of separation (similar to a security interest and the corresponding right to foreclose) must give notice as to what subject matter is being disposed of and the amount of claim which cannot be paid by such disposal. Failure to give such notice can result in the secured creditor being liable for any loss to the estate.

No claim may be filed after the closing of the meeting of persons interested, in which meeting the draft plan of reorganization has been examined.

The claims filing procedure is similar in a Japanese bankruptcy.

4. Priority of claims

The classification of creditors and their priority is set by statute as follows (in decreasing order of priority): reorganization secured creditors, reorganization creditors possessing claims which have a general preferential right or other priority rights; “general” reorganization rights (general unsecured); reorganization creditors possessing deferred claims; shareholders with preferential rights of distribution of the assets; and shareholders other than the shareholders mentioned under the preceding item. The claims are to be paid in that order of priority, although the absolute priority rule (the rule requiring that senior claims be paid first) is not stated explicitly in the statute. The absolute priority rule is established in the United States by case law. It is clear from the statutes, and from the following discussion concerning shareholders' rights, that such a rule does exist in Japan. The bankruptcy classifications and priority are the same.

5. Conclusion of claims allowance process

Generally, the claim filing process parallels that in the United States. What is different in Japan is the meeting mechanism under which the claims are allowed. Claims are finally and conclusively resolved at a meeting on the date of investigation of reorganization claims and reorganization security rights. A
meeting with dissension rarely occurs because settlements or litigation are normally concluded prior to the meeting. The receiver or a creditor may, however, object to a claim. If objection is raised by the receiver, the creditor may institute a lawsuit to have the claim "confirmed" (allowed). If a party other than the receiver objects, then that party must institute an action to object to the claim. If no objection is on file by the final meeting on the report of claims, the claim is conclusively determined and allowed.

In the United States, the filing of a claim is prima facie evidence of its validity. Any party may object, which creates a lawsuit (a "contested matter"). The burden of proof lies on the creditor to prove its claim. The practical procedure is not much different than that in Japan, except that there is no special meeting or date in the United States.

6. Shareholders' interests

Shareholders' rights often receive little attention in reorganization proceedings. Reorganization Article 129(3) states that shareholders shall not have the "right of vote" in the case where there exist the facts comprising causes of bankruptcy with respect to the company. Since one of those causes is insolvency, which often exists for companies in reorganization, the shareholders usually do not have the right to vote. Consequently, higher-ranking creditors can ignore the shareholders. Effectively, the shareholder interest is terminated. In the United States, shareholders rank last in priority, but they are entitled to vote on a plan and have standing to be heard with respect to a proposed plan.

In Japan, however, as stated above, the shareholders are often the lenders. They can dismember an estate by exercising rights of separation on secured assets if such actions are not stayed or if their demands as a class cannot be met. Thus, shareholders, if also the secured lenders, have a voice in a different context. Further, such lender/shareholders represent the best source of new funding, which can result in a higher long-term distribution to creditors. Thus, while there may be no right to vote, the shareholders' ability and incentive to find an "angel" or sponsor gives them a practical, if not theoretical, voice.

The major differences in treatment of claims between the United States and Japan, then, can be summarized as being: 1) in the area of secured claims: the requirement of filing a Japanese claim, and the Japanese limits on interest and penalties even if "oversecured", 2) the more generous grant of claims for com-

235. Reorg. Arts. 129(3) at LZ 61; Bankr. Arts. 126, 127 at LU 30, 137 at LU 32; Matsuo § 7.02[2][b] at 7-6.
mon benefits to Japanese employees, and 3) the inclusion of future claims in the class of Japanese unsecured creditors.

B. Sub-Chapter 3: Scope of the Estate and Rights of Avoidance

1. Scope of the estate

The Japanese bankruptcy administrator and the reorganization receiver are vested with broad rights to marshal the estate for the benefit of creditors. Because the Japanese receiver succeeds to all rights to manage the debtor public corporation and its property, the receiver’s powers and rights are equivalent to the broad rights set forth in the Japanese Bankruptcy Law, although there are no express provisions to that effect in the Corporate Reorganization Law. In the United States, the bankruptcy or reorganization estate consists of all legal and equitable interests of the debtor.

The significant limits on the scope of the Japanese estate are those set forth previously relative to partially performed bilateral contracts where property remains in the estate. In that situation, the creditor has the right to reclaim or “redeem” the property.

There is no specific “strong-arm” clause under Japanese Law such as the hypothetical lien creditor concept under 11 U.S.C. § 544(a). However, there are strong avoiding powers for unfair or preferential acts which can achieve the same results as the U.S. “strong-arm” clause.

2. Avoiding powers—preference and fraudulent transfer

Japanese law provides a number of avoidance powers to the officers in reorganization or bankruptcy. These powers are like those of the trustee in the United States except that in Japan, lack of knowledge may prevent the voidance of a particular preferential act. Japanese reorganization law provides that a receiver may void any act which gives unfair or preferential treatment to a creditor. “Unfair or preferential” means any act that caused one creditor to receive more under a plan than another creditor of the same class.

The District Court with jurisdiction over the insolvency proceeding has exclusive jurisdiction over any action for avoidance. The receiver or admin-
istrator has standing to press an action to avoid a transfer in Japan. The limitations period for prosecuting an action is the earlier of two years from the date of commencement of the proceeding or 20 years from the date of the act complained of. 245 Absent a fraudulent transfer, however, the effective limit is usually one year because knowledge of suspension of payment prior to one year before the application for commencement of reorganization does not make an act voidable. 246 Within that one-year period, knowledge of suspension of payment gives rise to the inference of knowledge of "prejudice." 247

The mechanical tests of U.S. Code Section 547 are similar in concept to Japanese law except they contain no knowledge element. 248 The first element in establishing a claim of unfair or preferential treatment in Japan is knowledge of the creditor and the debtor.

Any of the acts set forth below may be avoided in favor of the company's assets subsequent to the commencement of reorganization proceedings:

(1) Any act done by the company with the knowledge that it would prejudice [creditors]. . . . Provided, that this shall not apply in the case where the person benefited by the act did not know at the time of the act the fact that it would prejudice the reorganization creditors. . . . 249

Both knowledge of the debtor and the creditor is needed. The debtor's knowledge is inferred because it knows its own problems. The focus is on establishing the creditor's knowledge. This is easily accomplished, provided the act to be voided occurred within one year before the application, because the only requirement is knowledge of suspension of payment to the creditor. Before one year prior to the petition, such knowledge is not probative.

Japanese law allows for (a) voiding the transfer of a security interest, (b) voiding the extinction of an obligation, (c) voiding certain insider transfers, and (d) voiding certain acts after the suspension of payments, after the petition for bankruptcy, or within 30 days prior to the application for commencement. All of these acts are in the nature of a U.S. preferential transfer. 250

In addition, in a fraudulent transfer context, "gratuitous" acts, or a "non-gratuitous act assimilated to a gratuitous act, which the company has done subsequent to suspension of payment, etc. or within six months prior thereto,. . . ." may be set aside. There is no requirement of proof concerning knowledge for the avoidance of gratuitous acts, i.e., acts taken without consideration. 251 This is very similar to the concept in the United States that transfers without consideration

246. Reorg. Arts. 91 at LZ 39-40, 78(1) at LZ 34-35. See also Bankr. Arts. 84 at LU 20, 72 at LU 17.
247. Reorg. Art. 78(1) at LZ 34-35; Bankr. Art. 72(1) at LU 17.
249. Reorg. Art. 78 at LZ 34-35. See also, Bankr. Art. 72 at LU 17.
251. Reorg. Art. 78(1)(4) at LZ 36.
prior to bankruptcy are almost conclusively presumed voidable if the debtor was or would become insolvent.\textsuperscript{252}

The period in which a person acquiring a property interest (such as a lien for new consideration) can "perfect" that interest even with knowledge of financial difficulty and have the date of perfection relate back to the date of acquisition of the interest is 15 days in Japan.\textsuperscript{253}

The U.S. Section 550 subsequent-transferee concepts and the liability of a subsequent transferee to a trustee for a voided transfer are found in the Japanese concept of "sub-acquirers."\textsuperscript{254} Thus, transfers voidable as to a debtor can also be voided as to a sub-acquirer of rights.\textsuperscript{255} Again, knowledge of a sub-acquirer is very important—just as in the United States. There is a bona fide purchase concept to protect arms-length transfers for value.\textsuperscript{256} As in the United States, any avoided claim is preserved for the creditor upon payment or return to the estate of the voided payment or transfer.\textsuperscript{257}

3. Setoff

Rights of setoff are preserved in Japan as in U.S. Section 553.\textsuperscript{258} Cross assignment of claims against the debtor and debts owed to the debtor can be avoided either a) because of pre-petition prejudice to creditors if the party seeking setoff had knowledge of financial difficulty, or b) because the cross assignment occurred post-petition.\textsuperscript{259}

V. JAPANESE BANKRUPTCY AND LIQUIDATION; ADMINISTRATIVE DUTIES OF AN ADMINISTRATOR OR RECEIVER

A. Duties

The functions of a receiver in reorganization are a hybrid between those of an American trustee and an American examiner.\textsuperscript{260} The receiver is charged with care for the company's property.\textsuperscript{261} The receiver also has a duty to investigate whether

\begin{footnotesize}
\begin{itemize}
\item 253. Reorg. Art. 80 at LZ 37; Bankr. Art. 74 at LU 18.
\item 255. Reorg. Art. 90(1) at LZ 39.
\item 256. Reorg. Art. 90(2) at LZ 39 (incorporating Reorg. Art. 87(2) by reference); Bankr. Art. 83 at LU 20 (incorporating by reference Bankr. Art. 72(2)).
\item 261. Reorg. Arts. 174–85 at LZ 82–86.
\end{itemize}
\end{footnotesize}
the directors of the company have committed any acts for which they are liable to
the company. 262 This differs from the debtor-in-possession concept in the United
States. On application to the court, however, the company’s management may
remain in place under the supervision and direction of the receiver and investiga-
tion commissioners. 263

Like a trustee in the United States, the Japanese administrator is charged with
gathering the assets of the estate, investigating and handling claims, and other-
wise handling the administration of the estate. 264

B. General Description of Bankruptcy Liquidation Procedure

The administrator in bankruptcy proceeds on small matters on his own ini-
tiative with the consent of the inspection commissioner. The sale of assets, large
settlements, and assignments (over 100,000 yen) are subject to court approval. 265
If a bankrupt objects, he can ask for a court order directing that a meeting of
creditors be convened to consider a resolution to overturn the act of the
administrator. 266

A meeting of creditors on a “special day for investigation of claims,” begins
the process of closing a bankruptcy. Absent objection, the amount, priority, and
class of claims becomes final. 267 A list of dividends is then prepared. 268 Divi-
dends may be distributed with the consent of the inspection commissioners. 269
The last distribution, however, must be approved by the Court. 270 A meeting of
creditors is convened for a final report of account. 271 “Upon termination of the
meeting of creditors, the court shall rule for termination of the bankruptcy
procedure and give public notice of the principal text of the ruling as well as of
the tenor of reasons thereof.” No appeal may be filed against the ruling. 272

Overall, the procedure, except for the two meetings mentioned, is much like
that of a U.S. Chapter 7. The major differences in Japan are: 1) a proof of claim
need not necessarily be filed, and 2) there are usually three meetings of creditors,
as opposed to one in the United States.

262. Reorg. Art. 98-2(1) at LZ 42; Reorg. Art. 179, 181 at LZ 84–85.
263. Reorg. Art. 96(2) at LZ 41.
VI. Conversion or Dismissal

A. Conversion

Conversion of a case from one type of proceeding to another always points in one direction: from reorganization to liquidation and straight bankruptcy. This is similar to what happens in the United States. The Japanese court will generally "convert" a reorganization case if it appears the case is or is about to be unsuccessful or is "hopeless." Upon conversion from the Reorganization Law to Bankruptcy Law claims for common benefits become claims appertaining to the bankrupt estate. The unpaid claims appertaining to the bankrupt estate receive pro rata distributions prior to any distribution to general unsecured creditors. The rule is unlike that in the United States where expenses incurred in Chapter 11 are subordinate to the administrative expenses in Chapter 7.

B. Dismissal

Generally, the standards for dismissal of a case or application are similar to those in the United States. Those standards center on bad faith and lack of cooperation by the debtor. A debtor, by a "voluntary application," can convert from an involuntary bankruptcy/liquidation proceeding into a reorganization setting, if the debtor is a kabushiki-kaisha; or to composition, compulsory composition, or special composition, if the debtor is otherwise eligible.

Bankruptcy cases in Japan are rarely dismissed. The administrator disposes of all of the assets unless there has been some unusual abuse or fraud on the part of the debtor causing dismissal of the case.

VII. Reorganization Plan Confirmation Process

A. Introduction

The required terms of a Japanese plan are more numerous and more specific than in the United States. The plan in Japan is generally drafted by the receiver

274. See generally Reorg. Arts. 273–284 at LZ 139–42.
275. Reorg. Arts. 23(1) at LZ 10, 26 at LZ 11–12.
278. 11 U.S.C. 1112 (1982); see n. 274.
279. Reorg. Arts. 29 at LZ 13, 37 at LZ 17; Comp. Arts. 1, 12, 15–17 at LU 1, 3, 4; Spec. Comp. Art. 3 at LV 1. See also Reorg. Arts. 23, 26 at 27 at LZ 10–12.
in cooperation with the creditors.\textsuperscript{282} The shareholders have little or no voice.\textsuperscript{283} Because of this cooperation, it is rare that the reorganization plan is not approved at the final meeting of interested persons. Further, the Court has the ability to continue that final meeting from time to time until such confirmation is feasible.\textsuperscript{284}

**B. Who Proposes a Plan of Reorganization and Plan Requirements**

1. **Who may propose—no "exclusive period"

The receiver is charged with filing a plan of reorganization within a time specified by the court.\textsuperscript{285} If it cannot be prepared, the receiver must file a report to that effect with the court.\textsuperscript{286} Generally, the receiver has one year to prepare a plan.\textsuperscript{287}

In Japan, there is no exclusive period for filing a plan of reorganization. The reorganization secured and unsecured creditors who have filed reports of claims, the company, and the shareholders may all file a reorganization plan within the period the court specifies for a plan to be filed.\textsuperscript{288} This lack of exclusive right to file a reorganization plan is at least partially remedied because only upon application and approval by the court can a party file a liquidation plan.\textsuperscript{289} This right of a creditor to file a plan has yet to be exercised.\textsuperscript{290}

2. **What the plan must state**

The requisites for a reorganization plan are initially stated in the negative: it may not contravene provisions of law, it may not be unfair or inequitable, and it may not be impossible of execution.\textsuperscript{291} This is similar to the requirements of a U.S. plan: 1) there must be appropriate approvals by regulatory authorities, 2) the plan must be, in a sense, a new series of contractual relationships, and thus the plan must comply with the requirements of the Bankruptcy Code and any applicable State law, 3) the plan must respect the priority of classes, 4) the plan must permit creditors to receive as much as they would receive through Chapter 7 liquidation (unless otherwise agreed), and 5) the plan must be "feasible".\textsuperscript{292}

\textsuperscript{282} Reorg. Arts. 189 at LZ 86, 164(2) at LZ 78, 196 at LZ 88–89, 198 at LZ 89; Matsuo § 8.05[5] at 8–36.
\textsuperscript{283} Reorg. Arts. 164(2) at LZ 78, 129(3) at LZ 61.
\textsuperscript{284} Matsuo § 8.05[5] at 8–36 to 8–37; Reorg. Arts. 206–207 at LZ 92–93.
\textsuperscript{285} Reorg. Art. 189(1) at LZ 86 (which period can be extended an application \textit{sua sponte}. See Reorg. Art. 187(2) at LZ 86.)
\textsuperscript{286} Reorg. Art. 189(3) at LZ 86.
\textsuperscript{287} Matsuo § 8.05[1] at 8–30.
\textsuperscript{288} Reorg. Art. 190(1) at LZ 86–87.
\textsuperscript{289} Reorg. Art. 191 at LZ 87.
\textsuperscript{290} Matsuo § 8.05[1] n. 2 at 8–30.
\textsuperscript{291} Reorg. Art. 233 at LZ 107–08.
The Japanese plan must state the terms for modifying the rights of any creditors. It may state the method of raising funds for payment of obligations and the purposes for which income in excess of the amount estimated in the plan is to be expended. The plan must disclose the continuance of the company through amalgamation (merger), formation of a new company or transfer of business, and disclose if new securities are to be issued. If any of the latter are contemplated, there are specific rules as to exactly what must be stated in the plan. A plan must also make clear what the status of “insiders” (in the U.S. sense) will be after confirmation of the plan.

3. How claims must be treated

There is a principle of equality within classes of creditors: “The terms and conditions of the reorganization plan shall be equal as among the persons who possess the right of the same nature. . . .” There can be, however, discriminatory provisions with respect to claims. This is similar to the administrative convenience exception used for the treatment of small trade creditors under many U.S. plans. The claims are paid in the following order of priority: secured claims; claims having priority; unsecured claims; subordinated claims; and shareholder claims.

C. Notice

The Japanese plan must contain many more specific provisions relative to the treatment of classes of creditors than a U.S. plan. In a sense, the court previews the plan. The U.S. law has no such preview requirement.

Once these criteria listed above for a plan are met, the notice requirements of Japan are similar to the adequate notice requirements and disclosure statement requirements in the United States. The plan must be served on the receiver, the company, reorganization creditors, reorganization secured creditors, persons who assume obligations or furnish securities for the reorganization, any government agencies which supervise the business of the company, the minister of justice, the minister of finance, and, if so entitled, the shareholders.

295. Reorg. Arts. 211(3) at LZ 96, 220 at LZ 99, 230 at LZ 105–06.
298. Reorg. Art. 228 at LZ 105.
299. See supra note 281.
301. Reorg. Arts. 200(2) at LZ 290, 164–65 at LZ 78.
D. The Meeting of Interested Persons

The creditors who have filed reports of claims that are not disputed are entitled to vote on the plan at the meeting of interested persons.\(^{302}\) Each class of claims votes as a separate class. The required numbers of consents must be obtained in the groups of reorganization creditors in proportion to those who possess the right to vote. This means achieving set fractions of the totals of creditors who can exercise the vote.\(^{303}\) This is similar to the old Act requirement in the United States.\(^{304}\) It is different from the new U.S. Bankruptcy Code which merely requires that set percentages of creditors exercising votes approve a reorganization plan.\(^{305}\)

The relevant Japanese statutory language is:

In order to adopt the resolution approving the draft plan of reorganization at the meeting of the interested persons, the consent shall be obtained, in the group of reorganization creditors, from those who possess the right to vote corresponding to two-thirds or more of the total amount of the votes of [unsecured] reorganization creditors who can exercise the vote; and in the group of reorganization secured creditors, with regard to the draft plan which provides for the postponement of the time limit of reorganization security rights, from those who possess the right to vote corresponding to three-fourths or more of the total amount of the votes of reorganization secured creditors who can exercise the vote, with regard to the draft plan which provides for the reduction or exemption of reorganization security rights or otherwise contains the provisions affecting the security rights in manners other than postponement of the time limit of reorganization security rights, and those who possess the right to vote corresponding to four-fifths or more of the total amount of the votes of reorganization secured creditors who can exercise the vote, and with regard to the draft plan as provided for in Article 191 [liquidation], from all the reorganization secured creditors who can exercise the vote; and in the group of shareholders, from those who possess the right to vote corresponding to the majority of the total amount of the right to vote of shareholders who can exercise the vote.\(^{306}\)

Each class of creditors has significantly higher required percentages of affirmative votes for consent to a plan than in the United States. Recall votes are allocated by amounts of claims. Unlike the United States, there is no requirement that one-half in number of claims in each class approve a plan.\(^{307}\) An exception in Japan to the required consent rule set forth above exists for liquidating plans. For those plans, all secured creditors must consent.\(^{308}\) The meeting on the resolution to approve the plan can be continued if the percentages of consents cannot be

\(^{302}\) Reorg. Arts. 200(2) at LZ 90, 205 at LZ 91–92.
\(^{303}\) Reorg. Art. 205 at LZ 91.
\(^{305}\) II U.S.C. § 1126(c), (d)(1982).
\(^{306}\) Reorg. Art. 205 at LZ 91–92.
\(^{308}\) Reorg. Art. 205 at LZ 91–92.
obtained. Unlike the United States, consents in lower percentages must be obtained from each class for such a continuance (one-half from unsecured, two-thirds from secured, one-third from shareholders).  

E. Court Approval of the Plan and Appeals

“If the resolution approving the plan has been adopted at the meeting of interested persons, the court shall rule as to whether or not it approves the plan, either on the day of the meeting or on another day which it [the court] has set immediately [thereafter].”  

The court will approve the plan if it finds

(1) that the reorganization proceedings or the plan are in accord with the provisions of laws;
(2) that the plan is fair, equitable and feasible;
(3) that the resolution [at the meeting of interested persons] has been adopted in honest and just manner;
(4) with regard to the plan, the contents of which is amalgamation, a resolution has been adopted for approval of the agreement of amalgamation by the general meeting of shareholders of the other amalgamating company;
(5) with regard to the provisions in the plan which stipulate matters requiring permission, approval, license, and other actions of an administrative government agency, that it [the plan] does not contravene in important respects, the opinion of an administrative government agency. . . .  

If there is a dissenting “class” of creditors, the court may “cram-down” the plan, forcing the class to accept the plan, while making any necessary modifications to protect the class. “Cram-down” is possible if the court finds that, were the property liquidated, there would be no excess property for a lower class, taking into account the rules of priority, ranks of classes and distribution to them, or if the court finds fair and equitable protection is being given, including equivalent value to a secured creditor. These cram-down standards are similar to those in the United States.

The plan is effective immediately upon Court approval. The court retains jurisdiction to enforce the terms of the plan. A complaint (appeal) against the plan may be taken, but these appear to be rare. There are specific rules much like those in the United States, including a bond requirement, for a stay pending appeal.

312. Reorg. Art. 234 at LZ 108–09 (The value of property subject to a lien at a fair price, as determined by the court is sufficient for cramdown).
314. Reorg. Art. 236 at LZ 110.
316. Reorg. Art. 237(3) at LZ 110.
F. Effect of a Plan

The effect of the plan on behalf of the company and against the reorganization creditors, reorganization secured creditors and shareholders is like the discharge of liability set forth in Section 1141 of the U.S. Bankruptcy Code: no liability for claims except as set out in the plan.\(^317\) There is no express Japanese equivalent to U.S. section 1141, which states that the confirmation of a plan discharges the debtor from all liability for claims except as set forth in the plan. Japanese law accomplishes the same result by reducing the claim in amount and releasing the remainder. Neither a Japanese plan nor a U.S. plan affect guarantees of third parties with respect to indebtedness incurred by the debtor or dealt with in the plan.\(^318\)

Reorganization Articles 240–270 contain lengthy “safe harbor” and discharge provisions like Sections 1141 (governing discharge) and 1145 (governing the “safe harbor” from securities law liability) in the United States. The Japanese “safe harbors” run the gamut from anti-trust, tax, securities, and debentures to a “catch-all.”\(^319\) Modifications can be made subsequent to court approval of the plan because of “unavoidable causes.”\(^320\) However, if they “adversely affect” a creditor class, the modification is subject to the vote of the affected class. Other unaffected classes are deemed to accept the modification once approved.\(^321\)

VIII. INDIVIDUALS IN JAPANESE INSOLVENCY LAW

A. Applicable Insolvency Law

Individuals in Japan primarily proceed under the Bankruptcy Law.\(^322\) Individuals may proceed under the petty bankruptcy provisions for any estate that does not amount to more than 1,000,000 yen, which is approximately $3,300.\(^323\) Because there is no Japanese equivalent to the U.S. family farmer chapter 12, the Japanese petty bankruptcy chapter would be the only simple alternative for family farmers in Japan.\(^324\) In petty bankruptcy, there are no inspection commissioners. The court effectively functions as the overseer of the estate.\(^325\)

\(^{317}\) 11 U.S.C. § 1141 (1982); Reorg. Arts. 240(1) at LZ 111, 241 at LZ 112 (One exception to discharge relates to liability for retirement allowance of director subsequent to the commencement until after the ruling. See Reorg. Art. 241 at LZ 112).

\(^{318}\) Reorg. Art. 240(2) at LZ 111.


\(^{320}\) Reorg. Art. 271(1) at LZ 137.

\(^{321}\) Reorg. Art. 271(2) at LZ 137.

\(^{322}\) Technically, they are eligible for the composition Law, but no literature exists describing use of that alternative.

\(^{323}\) Bankr. Art. 358–59 at LV 75.


\(^{325}\) Bankr. Art. 363–64 at LU 76.
B. Japanese Discharge Process

In contrast to the United States, the bankrupt in Japan must apply for a discharge before the closing of the bankruptcy procedure. In the United States, discharge is granted automatically without significant procedural effort unless an objection to discharge or a complaint objecting to the dischargeability of a particular debt is filed. If that occurs, a hearing is held.

The road to a Japanese discharge can take two routes. For those guilty of bankruptcy crimes or liable for taxes, intentional torts, violations of fiduciary duty, and other like items, a discharge either cannot be obtained or does not cover the debt. Such persons must apply for rehabilitation. All other persons can receive an effective discharge.

The court automatically holds a hearing on an application for discharge. The debtor must appear, or be barred from discharge. The hearing can be consolidated with the creditor meeting or the meeting for investigation of claims.

A ruling of refusal of discharge may be granted only if a) a violation of the penal offenses has occurred, b) fraud has occurred, c) false statements were made to the court, d) a false register of creditors was given, e) a discharge has been obtained in the prior ten years or f) some breach of the duties of a debtor has occurred. Certain debts are not exempted by the discharge, including taxes, malicious torts, salaries of employees, cash bonds taken from employees and not repaid, unregistered or unscheduled claims, and criminal matters. A discharge can be annulled because it was fraudulently obtained. Discharge does not affect a bankrupt's guarantors.

If no discharge can be obtained, or debt is excepted from discharge, an application for rehabilitation may be filed. No application for rehabilitation can be granted until 10 years from the granting of a previous application for rehabilitation and until all of the Japanese equivalent of non-dischargeable debt has been paid.

Pending the passage of 10 years before the application for rehabilitation can be granted, and the repayment of the underlying debt, the debtor is a “bankrupt.” Other provisions of Japanese law leave an onus on bankrupts. Professional li-
licenses, such as that of an attorney, are revoked and cannot be used. Rehabilitation of such license may be impossible if there has been a violation of penal provisions. Similarly, a bankrupt cannot be a director of a publicly-held company.\textsuperscript{338} For this reason, and because of the non-dischargeable obligations of a manager for wages,\textsuperscript{339} there is effectively personal responsibility of officers of a corporation for certain debts of the corporation. The resultant pressure can compel an officer or director to personally underwrite some or all of a corporation's indebtedness.

The discharge provisions, therefore, are very onerous in Japan, beginning with a minimum of 10 years between discharges, as opposed to 6 years in the United States. Also, for fiduciaries and attorneys, and sometimes corporate directors, rehabilitation and restitution of debts owed may be the only means to return to that occupation, quite unlike the United States.

\textbf{IX. CONCLUSION}

In all cultures with concepts of property and credit, businesses and individuals suffer irreparable financial reversals. Bankruptcy in some form then occurs. Debtor's prison has fortunately faded as a remedy in the Western common law system and the reduction of Japanese debtors to a poverty status has also faded. Japanese insolvency law, like all law, has evolved to conform with the needs of Japanese society.

No reader should forget that the Japanese insolvency laws are superimposed on an ancient tradition and a complex body of statutory material. The early European Code traditions adopted into pre-World War II Japanese insolvency law were modified by many American concepts. The coincidence of certain processes of the old U.S. Bankruptcy Act and the Japanese Reorganization Law, passed in 1952 while Japan was occupied, are evident.\textsuperscript{340} The American practitioner should use this as a tool to discern patterns. United States law is an evolution of British common law and the Uniform Commercial Code laid over very recent civilizations. The Bankruptcy Act therefore is neither a model nor an ancestor of Japanese law—a modern law laid over an ancient tradition.

Hopefully, this article leaves the reader with great respect for the distinguished traditions of Japan. The Japanese bar has ingeniously reconciled a system of reorganization, liquidation and fresh start in the industrial era with Japan's unique history and customs.

\textsuperscript{338} Matsuo § 7.08[4] at 7-46.
\textsuperscript{339} Bankr. Art. 366-12(l), (3), (4) at LU 79.