INSOLVENCY-RELATED REORGANIZATION PROCEDURES IN JAPAN: THE FOUR CORNERSTONES

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I. INTRODUCTION

When a company experiences severe financial difficulties and cannot repay its creditors it has, broadly speaking, two options. It can either liquidate or reorganize. If a company chooses to liquidate, the proceeds obtained from liquidating the company's assets are distributed pro rata among the company's creditors. On the other hand, if the company chooses reorganization, it continues as a going concern and the company's creditors are repaid in full over time as per the reorganization plan. Theoretically, reorganization is the best solution to the company's financial problems when the value of a company as a going concern is greater than its liquidation value.[1] In such instances, all parties benefit more from the reorganization of the company than from its liquidation.

Once the decision to either liquidate or reorganize has been made, the company must decide how it wishes to accomplish the liquidation or reorganization. Liquidation is usually carried out pursuant to a bankruptcy statute and there is little room for negotiation between the company and its creditors.[2] Reorganization, on the other hand, can be accomplished either through private negotiation with the company's creditors or within a statutory framework under the protection of which a plan of reor-

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1. Professor Douglas G. Baird argues that in some instances the liquidation of a business as a going concern is more efficient than a reorganization, *see* Douglas G. Baird, *The Uneasy Case for Corporate Reorganizations*, 15 J. LEGAL STUD. 127 (1986).

2. This is not the case in Japan, however. Insolvent Japanese limited companies can liquidate without using the bankruptcy procedure. *See* Patrick Shea & Kaori Miyake, Insolvency-Related Liquidation Procedures in Japan (1995) (unpublished manuscript, on file with the author).

ganization can be developed. Although private negotiation is probably more cost-effective, reorganization is often only possible within a statutory framework because private negotiation can be stymied by creditor hold-outs.

The purpose of a reorganization is different than that of a liquidation. A liquidation seeks to ensure the fair and equitable distribution of a company's unsecured assets among its unsecured creditors. In contrast, a reorganization attempts to restructure a company's debt and equity in a manner acceptable to all of the parties concerned so that the company can continue to operate as a going concern and repay its debts. In essence, a statutory reorganization regime provides a framework within which a company can negotiate with its creditors so as to enable it to continue operating.

In recent years, as a result of the worldwide recession, the collapse of the "bubble economy," and the appreciation of the yen, many companies in Japan face the prospect of liquidating or reorganizing. While the economy has improved, yen appreciation continues to plague companies in Japan, and as a result, a large number of firms are likely to face the prospect of insolvency in the immediate future. This paper will examine the statutory reorganization regimes available to companies in Japan[3] in the context of the four cornerstones of any reorganization scheme.[4]

II. JAPANESE REORGANIZATIONS

Japanese companies facing financial difficulties that choose to reorganize can select from a variety of statutory regimes under which to accomplish the reorganization. In fact, Japan has four separate reorganization procedures: Corporate Reorganization, Company Arrangement, Composition, and Compulsory Composition. While company arrangements are governed by the Commercial Code[5] and compulsory compositions are covered in the Bankruptcy Law,[6] the other two regimes are laid out in separate, distinct codes. Corporate reorganizations are governed by the Corporate Reorganization Law[7] and compositions are regulated by the Composition Law.[8]

3. Note that Japanese reorganization regimes can be used by any company located in Japan, no matter where it is incorporated.

4. George G. Triantis, *Mitigating the Collective Action Problem of Debt Enforcement Through Bankruptcy Law: Bill C-22 and Its Shadow*, 20 CAN. BUS. L.J. 242 (1992).

5. COMMERCIAL CODE, Law No. 48 of 1899.

6. Bankruptcy Law, Law No. 71 of 1922.

7. Corporate Reorganization Law, Law No. 172 of 1952.

8. Composition Law, Law No. 72 of 1922.

Japan adopted most of its major laws from other countries and the four reorganization regimes are no different. The two laws governing compulsory composition and composition were adopted from Germany in 1921. The provisions covering company arrangement were borrowed from the English in 1938. The corporate reorganization regime was the most recent import, coming from America in 1952. Because old reorganization regimes were not eliminated when new ones were adopted and no attempt to integrate the four regimes was ever made, there are four separate reorganization regimes in Japan. For the foreseeable future it is likely that there will continue to be four separate reorganization procedures in Japan.[9]

While it is difficult to say which procedure will be used in a given situation, certain generalizations can be made based on the nature of the individual regimes and their inherent limitations. For example, although both corporate reorganization and company arrangement can be used only for *kabushiki kaisha* (the equivalent of joint-stock limited liability companies), corporate reorganization is usually restricted to complex reorganizations involving large *kabushiki kaisha*. It is the best procedure when uncooperative secured creditors are anticipated. In contrast, even though company arrangement can be used in complex and simple reorganizations, it cannot be relied on when there are uncooperative secured creditors because of the discretionary nature of the stay of proceedings against secured creditors. The third procedure, composition, is available to both individual and company debtors. However, it is usually used only in simple reorganizations where there are no secured creditors because it does not contain any provisions to stay secured creditors. Finally, compulsory composition is restricted to reorganizations that take place within a bankruptcy. It is rarely used because it requires a high level of cooperation among all of the parties involved.[10]

III. THE FOUR CORNERSTONES OF A REORGANIZATION REGIME

Statutory reorganization regimes are, on a theoretical level, intended to overcome the hold-out problem, which often occurs during negotiated reorganizations. Negotiated reorganizations are predicated upon the unanimous approval of the debtor company's plan of reorganization by its creditors. Because in any re-

9. A review of the Japanese insolvency procedures will begin soon. However, no major changes are expected for some time.

10. A chart comparing some of the aspects of the four regimes is included in the Appendix to this article. It provides information of concern to a company that is considering reorganizing.

organization there are numerous possible reorganization plans, a creditor who benefits under one plan more than any other will be inclined to reject all plans except the one under which it gains its maximum benefit.[11] When a creditor refuses to approve a plan because it is waiting for a plan under which it benefits more, the classic "hold-out" problem is created.

Hold-outs threaten the viability of the reorganization process. While a creditor is holding out, three things that are damaging to the reorganization process may occur. First, the value of the company as a going concern may fall. Second, secured creditors who are unwilling to wait for an acceptable plan to materialize may enforce their security by realizing on their collateral. Finally, the unsecured creditors may request the court to enforce their debts against the company's unsecured property.[12] If the going concern value of the company falls or enforcement actions are taken, it is often no longer possible or in everyone's best interest to reorganize. A successful reorganization is predicated on the ability of a company to continue doing business. Thus, if the assets necessary for the company's reorganization are realized on then reorganization is no longer possible. Furthermore, if the value of the company as a going concern is reduced to a point lower than its liquidation value, reorganization is no longer in the best interests of all concerned. Creditors would then gain more from liquidation.[13]

An effective statutory reorganization regime avoids the hold-out problem by placing the reorganization process under the supervision of the court. This limits the power of any individual creditor to disrupt the reorganization. Professor George G. Triantis suggested that there are four cornerstones of any reorganization regime:

(1) a stay of proceedings;
(2) measures to maintain the value of the debtor company's business during the reorganization process;[14]
(3) a negotiation and confirmation process for proposed plans of reorganization; and
(4) measures to limit the debtor company's resort to the reorganization regime.[15]

11. Unless, of course, there is some other compensating benefit.

12. *See* Triantis, *supra* note 4, at 246. Note that the threat of holding out can also be used by one creditor to gain advantage over the other creditors.

13. Realization by creditors and dissipation of the going concern surplus are connected insofar as the loss of assets also affects the going concern surplus.

14. This means the excess value that the business has as a going concern compared to its liquidation value.

15. *See* Triantis, *supra* note 4, at 248-49.

A stay of proceedings, the first cornerstone, is probably the most essential aspect of any reorganization regime because it limits the possibility of hold-outs. When creditors realize on a debtor company's assets it is difficult, and in most cases impossible, for that company to continue operating as a going concern and successfully reorganize. A stay of proceedings prevents creditors from realizing on the assets of the insolvent company and, as a result, limits hold-outs.[16] Because a stay strips creditors of their right to realize on collateral, creditors lose a lot of leverage in their dealings with a debtor company. Thus, creditors faced with the prospect of a stay are more willing to negotiate to reach an agreement respecting the reorganization of the debtor company.

In addition, the availability of the stay dictates, to a certain extent, the scope of the reorganization regime. If creditors are not stayed under the provisions of a reorganization regime, they are free to take steps to recover their debts unless an agreement is reached outside of the regime. If no agreement is reached and the creditors who are not stayed proceed to realize on the property of the debtor company, they can disrupt the reorganization process. Basically, a statutory reorganization regime that does not stay all creditors is vulnerable to hold-out problems.

The second cornerstone, preservation mechanisms, ensures that reorganization remains the best solution. A reorganization is preferable when the going concern value of the debtor company exceeds the liquidation value of its assets. This difference can be referred to as having a "going concern surplus." Essentially, creditors and shareholders stand to gain more from the continued operation of the company than from its liquidation because they may be repaid in full over time. If the reorganization is to succeed, the going concern surplus of the company must be preserved.[17] Preservation mechanisms serve this purpose. These mechanisms range from ensuring that the existing management controls the company properly to replacing the existing management with court appointed administrators. Preservation mechanisms also have a secondary purpose. They ensure that the assets of the company will remain available for creditors in the event that the reorganization fails. In sum, the preservation mechanisms protect the aggregate liquidation value of the company and

16. It also limits the threat of hold-outs. Such threats are attempts by the creditors to secure special benefits.

17. Professor Triantis points to numerous reasons why the management of a company may not always act to preserve the going concern surplus. These reasons range from the management being preoccupied with the reorganization to the management attempting to transfer wealth from fixed claimants, i.e., creditors, to equity holders. *See* Triantis, *supra* note 4, at 254.

often allow the court to ensure that the property of the company is not dissipated.

Notwithstanding the importance of the first and second cornerstones, the third cornerstone, a negotiation and confirmation process, is the essence of a statutory reorganization regime. This is the process by which the reorganization is accomplished and becomes binding. In the negotiation and confirmation process, the court must balance conflicting goals: fairness to all creditors and the freedom of each creditor to negotiate with the debtor company. Unlike privately negotiated reorganizations, statutory regimes rarely require unanimous creditor agreement. If a certain percentage of the creditors agree, a plan of reorganization developed under a statutory regime is usually binding on all of the creditors governed by the regime.[18] Consequently, fairness is essential. Statutory reorganization regimes usually require that the plan be fair to all creditors. In fact, they may even require that the reorganization plan include certain provisions. At the same time, a regime must also provide creditors with a certain degree of freedom to allow them to negotiate acceptable terms. Not all of the terms in a reorganization plan can be dictated and in certain instances, it may be necessary to treat creditors differently. Otherwise, it may be difficult to obtain the requisite level of creditor consent, especially when the reorganization involves only a few large creditors.

Under most statutory reorganization regimes, a court supervises the reorganization. The confirmation process usually adds the sanction of the court to the reorganization plan notwithstanding the fact that it may have already been accepted by the company's creditors. As part of the confirmation process, the court, in many instances, must ensure that the plan in fact conforms to all requirements and is fair. Once the plan has been approved, it generally becomes binding on all of the creditors who are within the scope of the regime and included in the plan. In most instances the court will retain supervisory jurisdiction to ensure that the plan is carried out according to its terms.

According to Triantis, the fourth cornerstone, screening mechanisms, ensures that statutory reorganization regimes are not used by debtor companies which do not have a going concern surplus.[19] In essence, screening mechanisms sort out hopeless reorganizations that are attempted for the sole purpose of tempo-

18. Creditors not governed by the regime, usually secured creditors, are generally free to enforce their security. If these creditors are necessary to the reorganization, i.e., they hold important property as collateral, then private negotiations must take place and the associated problems regarding holdouts arise. See *supra* pp. 403-04, for a discussion of the scope of a legislated reorganization regime.

19. *See* Triantis, *supra* note 4, at 249.

rarily staving off inevitable liquidations. They accomplish this by removing such reorganizations from the process or discouraging debtors from commencing frivolous reorganizations.

As one might expect, the four Japanese reorganization regimes provide for each of the four cornerstones. However, each regime differs in how they provide for the cornerstones and the extent to which they are able to effectively fulfill their functions. The next section of the paper will look at each of the reorganization regimes and how each provides for the cornerstones.

IV. THE FOUR CORNERSTONES IN JAPAN'S REORGANIZATION REGIMES

A. Corporate Reorganizations

Of the four reorganization regimes, the Corporate Reorganization Law is, at two hundred ninety-five articles, the longest and most comprehensive. The stated purpose of corporate reorganization is to bring about "the sustenance and regeneration of the business of a limited company . . . of which, despite its financial difficulty, there is a prospect of rehabilitation . . . ."[20] Significantly, it is the only procedure of the four in which the stay provisions automatically prevent secured creditors from realizing on their security. It is, therefore, the only procedure that can be consistently relied upon when uncooperative secured creditors are encountered.

Corporate reorganization can be used only by *kabushiki kaisha*, the equivalent of a joint-stock limited liability company. It may be commenced when "a company is unable to pay its obligations that are due without exceedingly impeding continuation of its business"[21] or "where the facts comprising causes of Bankruptcy are likely to take place with respect to the company."[22] In the former case, only the company is entitled to apply for corporate reorganization.[23] In the latter, creditors and shareholders are also entitled to apply.[24]

20. Corporate Reorganization Law, *supra* note 7, art. 1. While the intent is to reorganize, plans of reorganization that provide for the liquidation of the company are possible with the permission of the court. *Id.* art. 191. Even where there has been a petition for bankruptcy or a special liquidation has been initiated, a company may still apply for a corporate reorganization. *Id.* art. 29.

21. *Id.* art. 30, para. 1.

22. *Id.* art. 30, para. 1.

23. If the company is in liquidation, special liquidation or bankruptcy, a resolution must be approved by two-thirds of the shareholders who hold one-half of the shares. *See id.* art. 31. *See also*, Commercial Code, *supra* note 5, art. 343.

24. *See* Corporate Reorganization Law, *supra* note 7, art. 30, para. 2. Creditors must have debt claims equivalent to at least one-tenth of the capital of the company and shareholders must have at least one-tenth of the shares to apply. *See id.*

1. *Stays of Proceedings*

In corporate reorganization both interim and permanent stays of proceedings are available. By preventing both secured and unsecured creditors from disrupting the business of the company, these stays enable the company to concentrate on developing a viable reorganization plan.

The interim stay provides protection to the debtor company between the filing of an application for corporate reorganization and the commencement of the reorganization process. When an application for corporate reorganization is made, the court is entitled, but not required, to order the suspension of liquidation and other enforcement procedures initiated by secured or unsecured creditors. If ordered, this stay is effective until a ruling on the commencement of the procedure is made or a period of two months passes.[25] Courts typically grant this stay, even though it is discretionary in nature.

After corporate reorganization is ordered, an automatic stay protects the debtor company.[26] This permanent stay remains effective throughout the period of reorganization.[27] It precludes liquidation and other enforcement procedures by secured and unsecured creditors and, if commenced, suspends them.[28] It also stays lawsuits that are related to the assets of the company.[29] Proceedings by the government to collect delinquent taxes are suspended, but only for a period of one year.[30] To ensure that the stay only affects activities that adversely affect reorganization, the court may allow enforcement actions when reorganization is not compromised.[31]

2. *Preservation Mechanisms*

In a corporate reorganization, preservation mechanisms may be instated when the application to commence the procedure is filed. Although the company's management retains control of the company's operations until the formal commencement of the reorganization process, the court may order the appointment of an overseer to supervise the company as an interim measure.[32] If an overseer is appointed, the company must obtain the overseer's

25. *See id.* art. 37.
26. *See id.* art. 67.
27. After the reorganization plan has been accepted and approved, the plan will dictate.
28. *See* Corporate Reorganization Law, *supra* note 7, art. 67.
29. *See id.* art. 68.
30. *See id.* art. 67, para. 2. The one-year period can be extended. *See id.* art. 67, para. 3.
31. *See id.* art. 67, para. 6.
32. *See id.* art. 39.

permission when undertaking certain actions designated by the court.[33] This keeps the court apprised of the management's actions and reduces the possibility that management will dissipate the going concern surplus.

In addition, the court is entitled, where necessary, to take steps to preserve the property or business of the company prior to the commencement of the procedure.[34] When such measures are taken, the court appoints an interim trustee who has the exclusive right to manage the business and property of the company, subject to the court's supervision.[35] The power to appoint an interim trustee allows the court to displace the company's management before official commencement of the reorganization procedure when the going concern surplus is being dissipated due to improper management. By appointing an interim trustee, the court ensures that reorganization remains a viable solution.

Once corporate reorganization has been commenced, management loses control of the company. A trustee, usually an experienced insolvency lawyer, is appointed by the court to take over the management and assets of the debtor company.[36] These provisions may appear overly harsh by North American standards, where the idea of the debtor-in-possession is dominant. However, no one can deny that they ensure that the company is properly managed during the reorganization procedure.

The trustee is almost always a seasoned professional with extensive experience in managing companies that undergo reorganizations. As a consequence, the trustee is more effective in management situations that arise during the course of a reorganization than the company's former leadership.[37] The trustee acts under the supervision of the court[38] and is under a duty to act as a good manager when directing the company's business.[39] While the trustee generally makes day to day decisions without having to consult the court, the court may require the trustee to obtain court permission before performing certain acts, such as obtaining loans or disposing of company assets.[40] Furthermore, because the goal of corporate reorganization is to reorganize the

33. *See id.* art. 42.

34. *See id.* art. 39.

35. *See id.* art. 40.

36. *See id.* arts. 46, 53, 174.

37. Arguably, the existing management led the company into financial difficulty in the first place.

38. *See* Corporate Reorganization Law, *supra* note 7, art. 98-3.

39. *See id.* art. 98-4. Self-dealing by the trustee is restricted. *See id.* arts. 54-2, 55.

40. *See id.* art. 54.

company as a going concern, the court's permission is needed to suspend the company's business.[41]

3. *Negotiation and Approval of the Plan of Reorganization*

The trustee must prepare a draft plan of reorganization and submit it to the court.[42] At the most basic level, the plan must treat all persons who possess similar rights equally[43] and take into account the rank and priority of certain rights of creditors and shareholders.[44] Essentially, the plan must be fair to all creditors. The Corporate Reorganization Law also requires that the plan contain specific elements. Chapter VII of the law specifies terms that must be included in all plans, terms that may be included in a plan, and terms that must be included under certain circumstances, such as when the plan calls for guarantors or the formation of a new company.[45] Some of these provisions are extremely detailed. For example, if the plan calls for the creation of a new company, it must include information such as the name and the objective of the company, the locations of its head and branch offices, the names of the directors, representative directors and auditor, and the number of shares the company will issue.[46]

When reorganization is initiated, the court specifies the period within which a draft plan of reorganization must be submitted.[47] Once the draft plan is submitted, the court calls a meeting of interested persons to review it.[48] The law allows for the fact that negotiations respecting the plan may take place after the draft has been submitted and, in some instances, during the meeting of interested parties.[49] Thus, even after the draft plan is submitted, it may be amended without restriction until the meeting, provided the court approves. Changes may also be made at the meeting, provided they do not adversely affect the interests of the creditors and the shareholders.[50]

41. *See id.* art. 184. Court permission may also be required for other actions. *See id.* arts. 54, 54-2.

42. *See id.* art. 189.

43. *See id.* art. 229. There is an exception to this provision for creditors with small claims. *See id.*

44. *See id.* art. 228.

45. *See id.* arts. 211-31.

46. *See id.* art. 226.

47. *See id.* art. 189. The creditors and shareholders are also entitled to prepare draft plans and submit them within the time specified. *See id.* art. 190. Note that a draft plan may call for the liquidation of the company. *See id.* art. 191.

48. *See id.* art. 192.

49. *See id.* art. 196.

50. *See id.* art. 202.

It is important that the plan of reorganization that is ultimately adopted is acceptable to the court and all interested parties. At the meeting to review the draft plan, interested parties may present their opinions to the court.[51] While only creditors and shareholders are entitled to vote at the meeting,[52] a wide range of individuals, including the trustee, representative of the employees[53] and, in some circumstances, government agencies or ministries, may voice their opinions.[54] Based on this input, the court, on its own accord or on application of one of the interested parties, may order amendments to the draft plan. If amendments are ordered, the court will adjourn the meeting to consider the amended draft at a later date.[55] This process of consideration and amendment continues until the court determines that no further amendments are required. At this point, if the court believes that the plan is legal, equitable, and viable, the court will refer the plan to the creditors and shareholders to be considered for acceptance.[56]

Creditors, both secured and unsecured, and shareholders vote on the plan. When voting, the unsecured creditors, secured creditors, and shareholders are divided into classes. Article 159 of the Corporate Reorganization Law specifies six such classes:

(1) secured creditors;

(2) creditors possessing general preferential rights or other general priority rights;

(3) other creditors;

(4) creditors with deferred claims;

(5) preferred shareholders whose preference relates to the distribution of assets; and

(6) other shareholders.

Notwithstanding this scheme, the court retains jurisdiction to consolidate or divide the classes, taking into account the rights of the various parties and the relationships between their various interests. When considering whether to consolidate or divide classes, the court often receives input from the trustee, the debtor company, the creditors, and the shareholders, who are all entitled to state their opinions.[57] The only limit on the court's power to alter the voting classes is that secured creditors, unsecured creditors and shareholders may not be put in the same

51. *See id.* art. 193.
52. *See id.* art. 204.
53. *See id.* art. 195.
54. *See id.* art. 194.
55. *See id.* art. 198.
56. *See id.* arts. 199, 200.
57. *See id.* art. 159, para. 3.

class.[58] This restriction is based on the fundamental differences that exist in the interests of these groups.

The size of the majority required to approve a plan of reorganization varies depending on the class. While a simple majority of the shareholders is sufficient, a two-thirds majority of unsecured creditors is required. For secured creditors, the requisite majority varies depending on how the plan affects security rights. If the plan postpones security rights, a three-fourths majority of the secured creditors is required. However, if the plan otherwise affects security rights, a four-fifths majority is required.[59]

Once the creditors and shareholders accept the plan of reorganization, the court must approve it.[60] The court holds a hearing at which the debtor company, its receiver, creditors, shareholders, and any guarantors[61] may be heard. In addition, the court may seek the independent advice of investigation commissioners who may be appointed to counsel on such matters as the propriety of the reorganization plan.[62]

The court is generally entitled to approve a plan of reorganization when:

(1) the plan is in accordance with the law;
(2) the plan is fair, equitable and feasible;
(3) the resolution accepting the plan was adopted in an honest and just manner;
(4) if the plan calls for an amalgamation i.e., joining with another company, the general meeting of the shareholders of the other company has adopted the agreement of amalgamation; and
(5) if the plan calls for approvals, licenses, etc., it is in accordance with government officials' opinions that are obtained during the process of drafting the plan.[63]

Notwithstanding the above requirements, the court is entitled to approve the plan if, under the circumstances, it considers it inappropriate to disapprove.[64] This gives the court the authority to approve a plan that has been accepted by the creditors and

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58. *See id.* art. 159, para. 2. The court can alter the classification at any time until the plan is approved. *See id.* art. 159, para. 4.

59. *See id.* art. 205. Note that if the plan calls for liquidation, all secured creditors must approve. *See id.*

60. *See id.* art. 232, para. 1.

61. "Guarantors" are individuals who incur obligations or furnish security to facilitate the reorganization. They could be referred to as the "white knights" of corporate reorganizations.

62. *See* Corporate Reorganization Law, *supra* note 7, art. 101.

63. *See id.* art. 233, para. 1, and art. 194. In Japan, government officials have a great deal of influence over business.

64. *See id.* art. 233, para. 2.

shareholders even though it violates one of the above requirements.

The corporate reorganization procedure also accounts for situations in which a class of creditors dissents or is likely to dissent. In such instances, the court may modify the plan to protect the rights of the dissenters and approve the plan as modified. In addition, the drafter of the reorganization plan may anticipate the dissent and, with court approval, add such provisions.[65] However, this is not a "cram down." The creditors are not forced to take what is provided for in the plan. As a result of the protections that must be provided, the creditors in the dissenting class ultimately are repaid in full.

4. *Screening Mechanisms*

In a corporate reorganization a number of screening mechanisms are available to sort out doomed reorganizations at various points during the procedure. The Corporate Reorganization Law first provides for an initial screening prior to commencement of the reorganization process. A court order is required to commence a corporate reorganization. The court cannot order the commencement of the corporate reorganization procedure when (1) another procedure is more appropriate; (2) there is no prospect for rehabilitation; or (3) the procedure is utilized to avoid bankruptcy or tax.[66] These limitations prevent companies from commencing reorganizations that are likely to fail. Likewise, they prevent companies from using the procedure for illegitimate purposes.

Once the court commences the procedure by issuing a commencement order, other screening mechanisms eliminate reorganizations doomed to fail. A resolution respecting the plan of reorganization must be adopted within two months of the first creditors' meeting.[67] The court must discontinue the reorganization if a resolution is not adopted within that time.[68] The court also must discontinue corporate reorganizations when a draft plan is not submitted within the time specified by the court,[69] when an acceptable plan cannot be drafted,[70] or when there is no prospect of executing a plan that has been accepted.[71] In each of

65. *See id.* art. 234.
66. *See id.* art. 38.
67. *See id.* art. 207, para.2. While this time period may be extended by the court, it cannot be extended by more than one month. *See id.*
68. *See id.* art. 273.
69. *See id.* art. 273.
70. *See id.* art. 273-2.
71. *See id.* art. 277.

these instances the proposal is likely to fail, and further delay pursuing a doomed reorganization is not warranted.

Should an attempt to effect a corporate reorganization fail, the court may declare the company bankrupt if it finds causes comprising bankruptcy.[72] This provides an incentive to companies to attempt a corporate reorganization only when there is some prospect of success. It also provides some protection for creditors. When a bankruptcy is initiated, the management never resumes the control of the company. Control is transferred directly from the Trustee to the Administrator in bankruptcy. The management cannot, therefore, dissipate the company's assets.

C. Company Arrangements

As with corporate reorganizations, company arrangements can be made by *kabushiki kaisha* to prevent insolvencies. The Commercial Code allows for a *kabushiki kaisha* to effect a company arrangement when "it is deemed that there is a danger of its becoming insolvent or of its liabilities exceeding its assets."[73] The company arrangement procedure is not, however, as detailed as the corporate reorganization process. It comprises only one section of the Commercial Code. Applications to commence the procedure may be brought by a director, an auditor, a shareholder, or a creditor.[74] The procedure may also be initiated by the court on its own motion.[75]

1. *Stays of Proceedings*

Like corporate reorganization, there are both interim and permanent stay provisions. Once an application to commence the procedure is made or a notice of such an application is given, the court has the power, but is not required, to order the termination of enforcement procedures.[76] Once the court orders the initiation of reorganization, the process is protected by a stay that prevents executions from commencing and discontinues any procedures already commenced.[77] This latter stay is automatic and does not require a court order.

72. *See id.* art. 23.

73. Commercial Code, *supra* note 5, art 381, para. 1.

74. *See id* art. 381, para. 1. Note that an auditor, in this context, means the person referred to in Commercial Code, *supra* note 5, arts. 273-280. There are restrictions on the shareholders and creditors who can make applications. *See id.* art. 381, para. 1.

75. *See id.* art. 381, para. 2. The court may be given notice of the fact that circumstances exist with respect to the company which justify an arrangement by authorities supervising the company. *See id.* art. 381, para. 2.

76. *See id.* art. 383.

77. *See id.* art. 383, para. 2.

Perhaps the most significant difference between a corporate reorganization and a company arrangement is the stay as it applies to secured creditors. Unlike in a corporate reorganization, the stay provisions in a company arrangement do not automatically extend to secured creditors. The court may, however, order the stay of secured creditors if necessary for a successful arrangement.[78] However, the stay of secured creditors is purely discretionary. For the stay to be granted, the secured creditors must not be unreasonably injured by the imposition of the stay. If they are not stayed, they are free to enforce their security. This makes corporate reorganization, with its automatic stay, better when secured creditors are expected to be uncooperative. Only in a corporate reorganization is it assured that secured creditors will be stayed from enforcing their right to security.

2. Preservation Mechanisms

The company arrangement procedure has very flexible preservation mechanisms. Unlike in a corporate reorganization, the management of the company in a company arrangement is not automatically displaced. In fact, in most cases control of the company remains in the hands of its management. As a result, effective preservation mechanisms are essential because the management may reduce or eliminate the going concern surplus through willful or negligent mismanagement. In this vein, the Commercial Code provisions on company arrangements allow the court to make a variety of orders[79] to ensure that the company is properly managed while the reorganization is taking place. The variety of orders available gives the court flexibility to deal with specific situations as they arise. The management does not have to be displaced unless it is essential to do so. Different levels of supervision are possible, ranging from the appointment of an inspector who reports to the court on the company to the appointment of an administrator to manage the company's business. The court appointee's role and power vis a vis the business of the company depend on the court order.[80]

An inspector is appointed by the court when it orders an inspection of the company and its property.[81] The inspector is required to report on such things as whether it is necessary to supervise or manage the affairs of the company and whether

78. *See id.* art. 384.

79. *See id.* art. 386.

80. The circumstances under which the court will order an administrator, a supervisor, or an inspector during a company arrangement vary. However, this is a topic for a separate paper.

81. COMMERCIAL CODE, *supra* note 5, art. 386, para. 3, allows the court to make a number of orders. Inspection is one of them.

measures are necessary to preserve the property of the company.[82] An inspector may be appointed even before the court orders commencement of the company arrangement procedure.[83] Although not mandatory, the court usually orders inspections and appoints inspectors in arrangements.

If the court determines that the management of the company must be watched more carefully, it can appoint a supervisor. The supervisor does not actually manage the company, but the directors of the company are required to obtain the supervisor's permission before undertaking certain acts designated by the court. The supervisor also has the same investigatory powers as an inspector.[84] As with the appointment of an inspector, the court can appoint a supervisor before the company arrangement procedure commences.[85]

Although, as mentioned before, the management of the company usually retains control of the business, the court can also appoint an administrator to manage the affairs of the company.[86] The power to appoint an administrator allows the court to take measures to ensure that poor management by the company's existing management does not dissipate the going concern surplus. Administrators, when appointed, have the exclusive right to represent the company, administer its affairs, and manage and dispose of its property. An administrator also has the same powers as an inspector to demand reports and inspect books.

The Commercial Code also allows the court to order that preservation measures be taken both before and after the commencement of the company arrangement procedure. These measures are not limited to the preservation of the property of the company; they also allow the court to preserve the property of promoters, directors, auditors, and all others against whom the company may have a claim.[87]

3. *Negotiation and Acceptance of the Arrangement*

Should the court order the preparation of a plan of arrangement,[88] and it usually does, it is entitled to appoint a Reorganiza-

82. *See id.* art. 389. The inspector may also be called upon to investigate other matters necessary for the arrangement. *See id.* art. 388.

83. *See id.* art. 386, para. 2.

84. *See id.* art. 397.

85. *See id.* art. 386, para. 2.

86. *See id.* art. 398.

87. *See id.* art. 386, paras. 1, 2, 9.

88. The court may order the preparation or execution of a plan of arrangement or compromise. *See id.* art. 389.

tion Committee to draft the plan.[89] When preparing a plan, the Committee has the right to demand reports from the company and inspect books.[90] Because there are no provisions detailing the contents of a plan of arrangement, the Committee is essentially free to draft a plan acceptable to all concerned.

The lack of mandated provisions to ensure the fairness of a plan can be understood in light of the acceptance requirements. While there are no legislated provisions respecting the acceptance of plans of arrangement, as a general rule, an arrangement must be approved by all of company's creditors included in the plan. This makes achieving successful company arrangements very difficult, but ensures that the plan at least appears fair to all creditors. There are also no provisions in the Commercial Code regarding court approval of plans of arrangement. Generally, court approval is not required. This is not surprising given that all of the creditors must agree. If all of the creditors agree then there is no need for court approval. However, this causes problems when it comes to executing the plan because the court does not usually supervise the performance of the arrangement.

It is important to recognize that there is a serious problem associated with the unanimity requirement: the possibility of a hold-out. A single creditor can prevent a successful company arrangement by holding out for a plan under which it benefits more than other creditors. The stay provisions prevent other creditors from realizing on the property of the company. This provides more time for the company to negotiate with the creditor that is holding out than would be available in a negotiated reorganization process. However, a secured creditor that wishes to disrupt the reorganization can do so. If a hold-out occurs and the delay makes reorganization impossible, the court will initiate liquidation.[91] The secured creditors are then free to realize on their security.

4. *Screening Mechanisms*

The initiation of a company arrangement is, like corporate reorganization, not automatic. The court must order the procedure. The inspector, if appointed, reports to the court on the prospect of effecting an arrangement.[92] This allows the court to screen out cases when a successful arrangement is not possible. However, unlike some of the other procedures, there are no specific articles in the Commercial Code authorizing the screening of

89. *See id.* art. 391.
90. *See id.* art. 391. The inspector also has this power. *See id.* art. 390.
91. *See infra* part IV(C)(4).
92. *See* COMMERCIAL CODE, *supra* note 5, art. 389.

cases at the commencement stage. Of course, in cases involving secured creditors who are not cooperative and who are essential to the reorganization, the court can effectively screen out cases by refusing to grant an injunction against them.[93]

Once the arrangement has been commenced, the court has the explicit authority to screen out cases. Article 402 provides that in cases where an order instituting a company arrangement has been made, but where there is no reasonable prospect for reorganizing the company, the court is required to order an adjudication of insolvency pursuant to the Bankruptcy Law.[94] The adjudication of insolvency will usually result in the liquidation of the company using the bankruptcy procedure. This is most likely when unanimity cannot be reached among the company's creditors.

D. Compositions

"Composition" is intended to prevent bankruptcies by both companies[95] and individuals.[96] The procedure is available when a debtor is unable to pay its debts, has suspended payment of its debts, or has insufficient assets to fully perform its obligations.[97] If a company wishes to make a composition, all of the directors must agree.

The Composition Law is only 70 articles long and contains very little in the way of detailed procedures. Because of this, and because it cannot be used to effect a reorganization involving secured creditors, composition is typically used only in simple reorganizations.

1. *Stay of Proceedings*

Secured creditors possess the same right of separation that they possess in bankruptcy and are therefore outside the composition procedure.[98] The stay provisions do not cover secured creditors and, unlike in a company arrangement, it is not possible to stay secured creditors. It is, therefore, not possible to use composition in cases involving secured creditors, unless the secured creditors are cooperative. Even then, the possibility of a hold-out or a threat to realize on security to gain concessions in

93. Not screening out uncooperative creditors at the early stages only results in wasted expenses since they can prevent the reorganization.

94. *See* COMMERCIAL CODE, *supra* note 5, art. 402.

95. All types of companies, not just *kabushiki kaisha*, can use the procedure.

96. *See* Composition Law, *supra* note 8, art 1.

97. *See id.* art. 12, para. 1.

98. *See id.* art. 43. See *infra* part IV(E)(1) for a discussion of the right of separation.

the composition plan remain issues because secured creditors are not stayed and cannot be stayed.

In general, the stay provisions of the Composition Law are extremely limited. They serve only to prevent the composition creditors, i.e., unsecured creditors, from acting outside the composition to enforce their claims. Article 40 precludes composition creditors from enforcing their claims outside of the composition during the composition process. Any enforcement action commenced prior to the composition is suspended during the progress of the composition.

2. Preservation Mechanisms

The preservation mechanisms in a composition are rather weak and reflect the fact that the procedure is intended for simple reorganizations. They essentially consist of prohibitions against acting out of the ordinary course of business. As with a company arrangement, the management and property of the company remain in control of the company. However, there are no provisions in company arrangement law that allow the court to completely displace the company's management if the need were to arise. A receiver is appointed by the court, but does not take over the management of the company, and has very limited powers.

While there are both pre- and post-commencement preservation mechanisms, they are not as strong as those in other procedures. After the company applies to commence a composition, but before the court makes an order, the management is prohibited from acting out of the normal course of business.[99] The company is usually not supervised during this period. The only incentive for the company to obey is that if it acts out of the ordinary course of business the court may discontinue the composition.[100]

There is no supervision prior to an order commencing a composition procedure. Once the court orders commencement of a composition, it appoints a receiver with limited powers.[101] The receiver essentially has a supervisory role and usually is restricted to monitoring the activities of the debtor. The company's management retains the right to manage and dispose of the company's assets, subject only to the receiver's right to demand that it manage the receipt and disbursement of money.[102] However, the management is prohibited from acting out of the

99. *See* Composition Law, *supra* note 8, art. 31.
100. *See id.* art. 60.
101. *See id.* art. 27.
102. *See id.* art. 34.

ordinary course of business, unless the receiver consents.[103] While these provisions are weak compared to the preservation mechanisms in a corporate reorganization or company arrangement, the receiver does have the power to stop conduct that will dissipate the going concern surplus. For example, the receiver is entitled to object to conduct that it believes is unwise, even if within the ordinary course of business. In upholding its duties, the receiver may demand a report on the debtor's assets or investigate the state of the debtor's assets itself.[104]

Composition Law also provides for the court to take preservation measures against property before and after the commencement of a composition.[105] These measures allow the court to ensure that the company's property is not dissipated either before or after the composition procedure is commenced.

3. *Negotiation and Approval of the Composition*

When applying for a composition, the applicant is required to provide the court with the terms of its composition.[106] The Composition Law includes only limited provisions respecting the contents of a composition. The statute requires only that the terms of a composition treat creditors equally, unless the disadvantaged creditors agree to the differential effects.[107] Negotiations may take place and changes may be made to the terms of the composition up until the time that the composition is to be approved. Even when the meeting to consider a plan has been convened, the plan may be altered by the end of the meeting to allow further negotiation to reach an acceptable composition. However, the law prohibits changes to a plan once the meeting of creditors has commenced, unless the changes benefit the creditors.[108]

The composition must be approved by the creditors at a court supervised meeting.[109] Although the meeting is attended by the creditors, company representatives, and any guarantors,[110]

103. The receiver must consult with adjustment commissioners appointed by the court for matters out of the ordinary course of business that are considered important. *See id.* art. 32.

104. *See id.* art. 36, para. 1.

105. *See id.* art. 20.

106. *See id.* art. 13. A written report detailing the state of the applicant's property and a list of its creditors and debtors must also be submitted. If it is impossible to submit the report at the time the application is made, it must be submitted soon thereafter. *See id.* The applicant must also pay court costs in advance. *See id.* art. 14.

107. *See id.* art. 49.

108. *See id.* art. 49.

109. *See id.* art. 49.

110. *See id.* art. 46.

only the unsecured creditors are entitled to vote on a composition.[111] A majority of the creditors representing three-quarters of the claims is required to approve the composition.[112] Creditors vote as one class.

Once a proposal has been accepted by the creditors, it must be approved by the court.[113] At the hearing to determine the composition's fate, the creditors, the composition applicant, any guarantors, the receiver, and the adjustment commissioners are all entitled to state their opinions on the composition.[114] The adjustment commissioners are court-appointed officials who investigate the debtor and the terms of the composition and advise the court.[115]

Notwithstanding the review process, approval of the plan is favored. Under the Composition Law the court is entitled to reject a composition only in certain specified instances:

1) a resolution respecting a composition or the procedure at a meeting was illegal and the illegality is irremediable;
2) the location of the composition applicant is unknown;[116]
3) an act corresponding to fraudulent bankruptcy exists;
4) the resolution respecting the composition has been adopted in an unfair manner; or
5) a resolution respecting the composition is contrary to the general interests of the creditors.[117]

4. *Screening Mechanisms*

As with the other Japanese reorganization procedures, a composition is not automatic. A company must apply for a court order to commence the composition procedure. The Composition Law states that an application to commence a composition shall be dismissed if, among other things, the composition is intended to evade bankruptcy or the terms of the composition are against the general interests of creditors.[118] The court is also permitted to dismiss an application when a previous attempt at com-

111. Secured creditors are entitled to participate as unsecured creditors to the extent their security is not sufficient to satisfy their debt. *See id.* arts. 43, 49.

112. *See id.* art. 49. At the creditors' meeting, prior to the vote taking place, the receiver and the adjustment commissioners detail the circumstances which led to the composition and the present state of the debtor and the debtor's assets, and then state their opinion as to whether the terms of the composition are proper and suitable. *See id.* art. 48, para. 1.

113. *See id.* art. 50.

114. *See id.* art. 50, para. 2.

115. *See id.* arts. 21, 22.

116. This does not apply to corporate applicants.

117. *See* Composition Law, *supra* note 8, art. 51. For acts constituting fraudulent bankruptcy, see Bankruptcy Law, *supra* note 6, art. 374.

118. *See* Composition Law, *supra* note 8, art. 18.

position failed.[119] To assist the court in determining whether a composition should be commenced, the court appoints adjustment commissioners. Adjustment commissioners, as mentioned previously, investigate a debtor's assets and books and the terms of a composition.[120] They then submit their opinion to the court.[121]

Once a composition has commenced, one mechanism can derail reorganization: A strict time limit that screens out compositions doomed to fail. If a resolution accepting a composition is not adopted within two months of the first creditors's meeting, the court is required to discontinue composition.[122]

Finally, the Composition Law discourages frivolous compositions. If a composition is discontinued, disapproved, or annulled, the court is required to declare the debtor bankrupt.[123] If the court issues such an order, an administrator in bankruptcy takes over the assets of the company pursuant to the Bankruptcy Law. Management is divested of control.

E. Compulsory Composition

In addition to providing for liquidations, the Japanese Bankruptcy Law also makes provisions for a "compulsory composition."[124] This procedure is carried out within a framework established by the Bankruptcy Law. Theoretically, a bankrupt is entitled to propose compulsory composition at any time during bankruptcy[125] provided the company's directors agree.[126]

Because this final reorganization regime is seldom used, it is the least important of the four. There are probably no more than two per year in all of Japan. Although the liquidation of the bankrupt estate is suspended once compulsory composition is initiated and until the fate of the composition is known, in most cases, the liquidation of the company's assets is finished or at least well under way before the company can propose a composition. This makes reorganization difficult. In those cases in which

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119. *See id.* art. 19.

120. The composition applicant and its directors and managers are required to assist in the investigation. The penal provisions of the law contain sanctions for directors or managers who do not cooperate. *See id.* arts. 22, 23, 70. *See also* Bankruptcy Law, *supra* note 6, art. 153.

121. *See* Composition Law, *supra* note 8, art. 21.

122. *See id.* art. 59.

123. *See id.* art. 9.

124. *See* Bankruptcy Law, *supra* note 6, ch. IX.

125. *See id.* art. 290.

126. Note that the issue of whether to liquidate or reorganize and which procedure to use are discussed before any action is taken. It would be extremely rare for a compulsory composition to be decided upon after a bankruptcy has been commenced.

compulsory composition is used, the bankrupt and the administrator must be in agreement and work together or else it will fail.

1. *Stay of Proceedings*

In bankruptcy, certain secured creditors have a "right of separation." This allows property that is security for debt to be separated from the bankrupt estate and liquidated outside of the bankruptcy procedure.[127] The right of separation effectively removes secured creditors from a composition. Of course, in most cases in which secured creditors exist, it is necessary to include them for the reorganization to be successful because they often hold important property as collateral. In the rare cases in which compulsory composition is used, the cooperation of secured creditors is usually sought. The hold-out problem inevitably arises in such situations.

Because compulsory composition is a part of bankruptcy law, the stay provisions applicable in bankruptcy apply. Basically, the claims of unsecured creditors may be enforced only within the procedures provided for in the Bankruptcy Law.[128] Article 70 of the Bankruptcy Law provides that compulsory execution, provisional attachment, provisional disposition, or the enforcement procedures for enterprise hypothetically levied or ordered for bankruptcy claims cease to be effective once bankruptcy has occurred.[129] In addition, bankruptcy suspends administrative actions respecting property appertaining to the estate. Only measures against estate property commenced to collect taxes may continue.[130] It is generally understood that the stay provisions applicable in bankruptcy, aside from their inability to affect secured creditors, are the strongest of all the insolvency-related procedures in Japan. This is often the reason compulsory composition is used.

2. *Preservation Mechanisms*

In bankruptcy, the court appoints one trustee, usually an experienced insolvency lawyer, to administer the bankrupt estate.[131] The trustee takes possession of the bankrupt company's property[132] and has the exclusive right to manage the business of the bankrupt company[133] under the supervision of the court.[134]

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127. *See* Bankruptcy Law, *supra* note 6, art. 95.
128. *See id.* art. 16.
129. *See id.* art. 70. Procedures for compulsory execution may be continued by the administrator on behalf of the estate. *See id.*
130. *See id.* art. 71.
131. *See id.* arts. 157, 158.
132. *See id.* art. 185.
133. *See id.* art. 7.

However, in most bankruptcy cases the trustee does not manage the business of the company. The trustee's role is to liquidate the company's unsecured assets and distribute the proceeds among the unsecured creditors as bankruptcy dividends. Compulsory composition is not like most reorganizations because in a bankruptcy the business of the bankrupt company is not normally carried out by the trustee. Although the trustee may be directed to manage the company, that order is not commonly made. The fact that the business is not carried out can, by itself, result in the dissipation of the company's going concern surplus. Consequently, orders to continue the business of the company are probably essential for reorganization using compulsory composition. When such orders are made, the administration of the estate is probably sufficient because the estate is in the possession of a court-appointed officer and subject to court supervision.

The Bankruptcy Law also provides for the appointment of three or more inspection commissioners at the creditors' meeting. The inspection commissioners essentially supervise the trustee on behalf of the creditors.

3. *Negotiation and Approval of the Compulsory Composition*

The terms of the composition plan must be presented to the court when a compulsory composition is proposed.[135] This is one of the reasons that timing is critical. In most instances, the estate is dissipated by the time a plan is drafted, unless a composition is planned well in advance. However, the compulsory composition provisions are relatively short and do not try to detail the contents of a plan. In fact, other than requiring that the terms of a composition treat all creditors equally, unless any disadvantaged creditors agree,[136] the Bankruptcy Law dictates no requirements. The bankrupt company and its creditors are therefore free to negotiate a composition that is acceptable to all concerned. On a practical level, such negotiations usually, out of necessity, take place before a plan is filed.

Although the terms of a composition must be presented to the court when a compulsory composition is proposed, they may be changed until the meeting to consider it is held. Negotiations are also possible after the meeting has been commenced, provided that changes only benefit the creditors.[137] Creditors are

134. *See id.* art. 161.
135. *See id.* art. 294.
136. *See id.* art. 304.
137. *See id.* art. 302.

entitled to adjourn the meeting to accommodate such negotiation at a later date.[138]

Once a composition has been negotiated, it must be accepted by the creditors. The court calls a meeting so that creditors can vote on the plan.[139] Only the unsecured creditors vote. Due to the right of separation, secured creditors are not permitted to participate in the bankruptcy, even to vote on a compulsory composition, unless they cannot satisfy their debt by exercising or relinquishing their right of separation.[140] Secured creditors rarely relinquish their right of separation.

Creditors are not divided into classes to vote. A compulsory composition must be approved by a majority of what would represent three-quarters of the claims.[141] Once a resolution accepting a compulsory composition has been made, the court must approve its terms.[142] While persons with an interest in the outcome are entitled to appear at this hearing and state their opinions,[143] the Bankruptcy Law favors approval. Article 310 provides that the court may disapprove of a composition only where:

1) the composition or the resolution accepting it contravene the law and cannot be remedied;
2) the location of the person proposing the composition is unknown, there has been a conviction for fraudulent bankruptcy, or proceedings for fraudulent bankruptcy have been commenced;
3) the resolution accepting a composition was adopted in an unjust manner; or
4) the resolution is against the general interests of the creditors.

In the case of companies, there is an additional requirement for court approval. Although the law appears to favor court approval of a composition, the court must be assured that the corporate existence of the company will be continued before approving compulsory composition for a bankrupt company. When a company is declared bankrupt, it usually does not retain its corporate existence. In cases where the corporate existence is not being continued, the court is required to reject the composition.[144]

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138. *See id.* art. 307.

139. *See id.* art. 299.

140. *See id.* art. 96. This also applies to creditors whose collateral does not form part of the bankrupt estate but who nevertheless are creditors of the bankrupt. *See id.* art. 97.

141. *See id.* art. 306.

142. *See id.* art. 308, para. 1.

143. *See id.* art. 308, para. 2.

144. *See id.* art. 312.

4. *Screening Mechanisms*

The compulsory composition provisions contain few screening mechanisms. In fact, the only screening mechanisms included in the procedure are those that allow the court to dismiss a proposal for compulsory composition. However, this ability is limited.[145] Basically, the court may dismiss a proposal only when a previous proposal has failed. Of course, due to the situations in which it is used, screening mechanisms are for the most part unnecessary. The procedure is rarely used. When it is used, all of the parties usually agree that composition is a viable and appropriate solution. This in itself provides an effective screening mechanism. The different interests of the parties will tend to limit the use of compulsory compositions when a successful reorganization is not possible.

V. CONCLUSION

When a company cannot repay its debts, it can choose to either liquidate or reorganize. Reorganization is the best option when the company has a going concern surplus, i.e., when its value as a going concern is greater than the liquidation value of its assets. Once the decision to reorganize is made, the company must deal with a second question: how should the reorganization be carried out. A reorganization can be accomplished through either a private negotiation with creditors or under a statutory reorganization regime. Reorganizations are usually accomplished through statutory regimes to minimize the potential for creditor hold-outs. In Japan, companies facing financial difficulties that decide to pursue a reorganization pursuant to a statutory regime must make an additional decision: which statutory regime should be used to accomplish the reorganization. Companies in Japan can reorganize using one of four statutory reorganization regimes. The company and its legal advisors must analyze the characteristics of each regime to determine which regime offers the best chance for success given the company's particular circumstances.

Each of the four Japanese legislated reorganization regimes provides for the four basic cornerstones described by Professor Triantis. Each protects the reorganization with a stay of proceedings to prevent creditors from attaching the assets of the company and thereby disrupting the reorganization. Each preserves the business of the company during the reorganization. Each regime provides for the creation of a plan of reorganization and an approval process. Finally, each regime attempts to ensure that

145. *See id.* art. 296.

the procedures are not used except when there is a reasonable chance that the reorganization will succeed. Although each regime provides for the four cornerstones, they differ in certain fundamental respects. These differences limit the circumstances in which each procedure may be used and are critical when determining which regime to use. It is possible to effectively carry out a successful reorganization under each regime. However, each has different characteristics that tend to make it more appropriate in particular circumstances. It is impossible to adequately assess whether the variety of reorganization procedures in Japan benefits companies or creditors, but it certainly complicates matters for lawyers who must advise companies as to which procedures to use.[146] The availability of four procedures means that reorganizing companies and their legal advisors must evaluate their circumstances and goals before selecting a regime.

146. Lawyers play a much larger role in Japanese insolvencies than they do in U.S. or Canadian insolvencies. They are usually appointed as administrators and trustees, as well as advisors of the company on the proper procedures to use.