

Bankruptcy Resolution in Japan : Corporate Reorganization v.s. Civil Rehabilitation

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Table 1 Time series of bankruptcy filings in Japan (Sample period: Jan/1987-Aug/2002)

Year	Corporate Reorganization	Civil Rehabilitation	Liquidation	Total
'87-'96	10	-	0	10
'97	6	-	0	6
'98	4	-	3	7
'99	3	-	0	3
'00	4	7	0	11
'01	3	12	1	15
'02*	8	12	4	24

Rules and procedures of bankruptcy in Japan

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Corporate Reorganization Law

- The firm is expected to continue as a going concern
- A court-appointed receiver in reorganization take the control, while directors depart the firm
- Automatic stay to protect the firm from creditor harassment
- Reorganization plan approved by secured creditors, unsecured creditors and shareholders

Composition Law

- The firm is expected to continue as a going concern
- No court-appointed receiver
- No automatic stay to protect the firm from creditor harassment

Liquidation Law

- Roughly equivalent to Chapter 7 of the U.S. bankruptcy code
- The firm is liquidated
- A court-appointed receiver in bankruptcy

Rules and procedures of bankruptcy in Japan (continued)

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- Composition Law is abandoned
- Instead, Civil Rehabilitation Law takes effect
- Similar to Corporate Reorganization Law, the purpose of Civil Rehabilitation Law is to properly adjust relation of civil rights between the debtor and its creditors, and to rehabilitate the business of the debtor
- Consequently, Corporate reorganization Law, Civil Rehabilitation Law and Liquidation Law are available for Japanese firms after April 2000

Main differences between Corporate Reorganization Law and Civil Rehabilitation Law

Corporate Reorganization

Continue as a going concern

A court-appointed receiver in reorganization take the control, while the debtor management departs the firm

Automatic stay to protect the firm from creditor harassment

Civil Rehabilitation

Continue as a going concern

The debtor management continues to take the control (debtor in possession), unless the debtor management is incompetent, for instance, management frauds. And the court may appoint receivers in case of the incompetence of the debtor management based on an application of an interest party

The court may order a discontinuance of exercise of a security right existing on properties. And in a case where collateral are indispensable for continuation of business, the rehabilitation debtor may make an application to the court for an approval of extinguishing all the security rights on the properties, by paying money equivalent to the market value

Main differences between Corporate Reorganization Law and Civil Rehabilitation Law (continued)

Corporate Reorganization

A reorganization plan is approved by secured creditors, unsecured creditors and shareholders

Civil Rehabilitation

Roughly speaking, a rehabilitation plan is approved by unsecured creditors. Generally, secured creditors may exercise their rights without following the rehabilitation proceedings.

Table 2 Panel B Intended positions/occupations reported of replaced presidents, who did not remain Chairmen and representative directors. Management changes tracked starting four years before the year of *civil rehabilitation* filing

Number of managers holding specified positions/occupations	
Director and Chairman	3
Advisor with directorship	2
Director but no other titles	5
Consultant	3
Managing director of other group firm	2
No information	15

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Presidents' careers who remain after rehabilitation

	Career less than 2 years	Career more than 2 years
Outsiders	1	4
Insiders	5	4

Table 3 Involvement of bank lenders

Number of firms intervened by bank lenders

Required principal payments on loans are reduced

5

Required interest payments on loans are reduced

5

Bank lenders dispatch managers

10

Average time from bankruptcy petition to resolution

JAPAN(current paper)			
Corporate Reorganization		2 years	13 firms
Civil Rehabilitation		0.6 years	16 firms
		1.3 years	29 firms
U.S.A.(Franks and Torouts (1989))			
Before 1979		4.5 years	16 firms
Afterward		2.7 years	14 firms
U.S.A.(Weiss (1990))			
After 1979		2.5 years	37 firms

Table 4 Summary of claims resolution for 12 public traded firms filing bankruptcy under *Corporate Reorganization Law* between January 1997 and August 2002

Firm name	Percentage or description of claim paid		
	Secured creditors	Unsecured creditors	Shareholders
Priority violated for secured creditors only			
YAOHAN JAPAN	90%	3%	0
DAI-ICHI HOTEL	90%	4%	0

Table 4 Continued

Firm name	Percentage or description of claim paid		
	Secured creditors	Unsecured creditors	Shareholders
		Priority held	
Kyotaru	100%	20%	0
Tokai Kogyo	100%	8%-2%	0
TADA	100%	13%	0
Daito Kogyo	100%	8%	0
TOSHOKU	100%	8%	0
Asakawagumi	100%	5%-10%	0
Longchamp	100%	9%	0
JDC	100%	9%-10%	0
NAGASAKIYA	100%	0.50%	0
LIFE	100%	47.72%-	0

Table 5 Summary of claims resolution for 13 public traded firms filing bankruptcy under *Civil Rehabilitation Law* between April 2000 and August 2002

	Percentage or description of claim paid	
Firm name	Unsecured creditors	Shareholders
	Priority violated for unsecured creditors only	
KAWADEN	22.43%	21%
NICHIBOSHIN	4.14%	1%

Table 5 Continued

Percentage or description of claim paid		
Firm name	Unsecured creditors	Shareholders
	Priority held	
SOGO	5%	0
MARUTOMI	15%	0
FUJI CAR MFG.	8% to 10%	0
IKEGAI	Average 1.59%	0
FUJII	50%	0
FOOTWORK INTE	?	0
BETTER LIFE	10%	0
ELECTRIC	1.50%	0
AOKI	2% to 100%	0
SHOKUSAN JUTAKU	?	0
KITANOKAZOKU	6%	0

Table 6A Descriptive Statistics for 28 publicly traded firms at the fiscal end prior to *Corporate Reorganization* in January 1997 - August 2002

Variable	Mean	SDEV	Median	Obs.
Duration	1.7174	1.1379	1.652	28
Log(asset)	11.3906	1.4728	11.533	28
Dummy for outstanding bonds	0.3929	0.4973	0	28
Secured loans/Total debt	0.436	0.2842	0.42334	28
Loss carried forward/Ass	0.0886	0.1735	0.0077328	28
Short-term debt/total debt	0.7609	0.1742	0.78944	28
Total debt/Asset	0.9112	0.1324	0.92963	28

Table 6B Descriptive Statistics for 31 publicly traded firms at the fiscal end prior to *Civil Rehabilitation* in April 2000 - August 2002

Variable	Mean	SDEV	Median	Obs.
Duration	0.6478	0.479	0.529	31
Log(asset)	10.3486	1.1696	10.217	31
Dummy for outstanding bonds	0.4516	0.5059	0	31
Secured loans/Total debt	0.3702	0.2427	0.35498	31
Loss carried forward/Ass	0.7799	1.871	0.096857	31
Short-term debt/total debt	0.7443	0.1875	0.74051	31
Total debt/Asset	1.268	1.2419	0.93232	31

Logistic model for survival data

Density function : $f(w) = \exp(w)/(1+\exp(w))^2$

Survival function : $S(t, \cdot) = \text{Prob}[T \geq t]$

$$S(w) = 1/(1+\exp(w))$$

where

$$w = P(\log t - \beta'x)$$

Likelihood function $L = \prod_i [Pf(w_i)]^{\delta(i)} [S(w_i)]^{\delta(i)}$

where $\delta(i)$ is right censoring indicator.

Table 7A Log-logistic duration model estimation for *Corporate Reorganization* duration of 28 publicly traded firms in January 1997 - August 2002

Variable	Coefficient	s.e.	Prob
Constant	8.589537	2.3268	0.00022
Log(asset)	-0.5390837	0.14282	0.00016
Secured loans/Total debt	-1.418359	0.42186	0.00077
Dummy for outstanding bonds	8.92E-02	0.14488	0.53788
Loss carryforwards/Ass	-2.41041	0.77204	0.0018
Short-term debt/total debt	-1.299506	0.97522	0.18269
Total Debt/Asset	0.3714953	0.74015	0.61572
P	6.9810	3.7001	0.0592

Table 7B Log-logistic duration model estimation for *Civil Rehabilitation* duration of 31 publicly traded firms in April 2000 - August 2002)

Variable	Coefficient	s.e.	Prob
Constant	-2.645991	0.61274	0.00002
Log(asset)	0.1655191	9.23E-02	0.07296
Secured loans/Total debt	0.6911025	0.57544	0.22975
Dummy for outstanding bonds	0.3579829	0.21352	0.09363
Loss carryforwrads/Ass	0.8432705	0.37551	0.02472
Short-term debt/total debt	1.153884	0.83157	0.16526
Total debt/Asset	-0.9591752	0.42426	0.02377
P	5.7638	1.3972	0.00004

Table 7C Log-logistic duration model estimation for reorganization, rehabilitation duration of 59 publicly traded firms in January 1997 - August 2002

Variable	Coefficient	s.e.	Prob
Constant	7.762658	1.9793	0.00009
Rehabilitation Dummy	-9.354593	2.1393	0.00001
Log(asset)*Reorganization dummy	-0.5210272	0.1473	0.0004
Log(asset)*Rehabilitation dummy	0.1683284	9.47E-02	0.07554
(Secured loans/Total debt)*Reorganization dummy	-1.443861	0.55263	0.00898
Dummy for outstanding bonds*Rehabilitation dummy	0.194865	0.17	0.25169
(Loss carryforwards/asset)*Reorganization dummy	-2.239691	0.78718	0.00444
(Loss carryforwards/asset)*Rehabilitation dummy	0.7214432	0.26747	0.00699
(Total debt/asset)*Rehabilitation dummy	-0.8498692	0.36304	0.01923
P	4.99139	0.98846	0

Conclusion

- Once uncommon bankruptcy filings for large Japanese firms are sharply increasing in Japan
- Quite a few large firms straight file for bankruptcy, without following a a period of close involvement by the main bank
- Most bankrupt firms experience abnormal senior management turnover around bankruptcy filings, regardless types of filings
- Priority of claims in bankruptcy resolution is less violated in Japan than in the United States
- The passage of Civil Rehabilitation Law enables bankrupt Japanese firms to spend less time in bankruptcy than before
- In summary, Japan is successfully reforming its legal system for bankruptcy