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CORPORATE/DEBT RESTRUCTURING: JAPAN, THE HONG KONG SAR & THE PEOPLE'S REPUBLIC OF CHINA

A ROUNDTABLE DISCUSSION ¹

Introduction

MR. KELAKOS:

Good morning, good evening, good afternoon.

The crash of the Thai baht ² in the summer of 1997 triggered an economic crisis that quickly spread throughout Asia with repercussions worldwide. ³ While the impact of the Asian crisis varied greatly from country to country, the resultant rise of NPLs ⁴ in Asia invariably led to a meteoric growth of corporate and debt restructurings in the region. ⁵

As we approach the fifth year anniversary of the crisis, we see that while many countries in Asia are still grappling with their economic woes, ⁶ their troubles are exacerbated by fallout from the U.S., ⁷ European ⁸ and Japanese economic downturns and by the events of September 11.

On the positive side, the economic downturn and resultant increase in NPLs and business failures resulted in the adoption and use of Western-style insolvency and restructuring laws, structures and techniques in many of the countries in Asia. ⁹

In other countries, existing laws and structures combined with social, political, and cultural roadblocks have impeded the resolution of NPLs and have slowed down the rate of corporate and debt restructuring.

Overview

This roundtable discussion spotlights Japan, the Hong Kong SAR ¹⁰ and the People's Republic of China. During the course of this roundtable, we hope to provide a summary of each country's or region's insolvency regime and will highlight some of the unique reorganization and debt restructuring problems and issues that are particular to that country or region.

We will also highlight which structures, strategies and tools have worked well in these countries and the region over the past five years and which have not. Finally, the panelists will offer their views on trends, prospects for the future and perhaps suggest approaches that may accelerate the reduction of NPLs and corporate and debt restructurings in these countries and region.

Let us begin by turning our attention to Japan. Satoru Murase, would you please begin by summarizing the existing corporate and debt restructuring regime in Japan.

I. Japan

MR. MURASE: Thank you very much. My perspective is basically from an attorney dealing with cases in Japan involving U.S. investment in insolvent companies and in DIP financing deals¹¹ in that country. And for my five minutes, I'll rush through some topics and then address them as we go offhand.

I believe the biggest topic in Japan has been, and is, the continuing corporate economic deterioration in the country. It has continued on for a good twelve years.

Japan is facing a major banking crisis and bank nationalizations which many think will be triggered after banking regulation changes where deposit insurance on deposits are removed for amounts in excess of about \$80,000.¹²

This is creating incredible pressure on the banks which essentially are holding, by various estimates, between half a trillion dollars to a trillion dollars of nonperforming debt directly or through affiliates.¹³

So, let's look at what essentially has happened in the interim on the insolvency regime. I was just going to point out a number of matters. I would go back to a major change in the Japanese bankruptcy law from the change of the Composition Law (Wagi Ho) in Japan and the enactment of the Civil Rehabilitation Law (Minji Saisei Ho) in April 2000.¹⁴

This actually was, in retrospect, a revolutionary law. Essentially a debtor-in-possession law focused on small to medium sized companies when it was enacted, but essentially allowed expedited proceedings in an insolvency situation. We have seen cases essentially from filing to finish in some cases lasting only six months, in an insolvency regime that had usually experienced two or three year proceedings.¹⁵

And also — let me backtrack — under that old Composition Law, actually filings were usually about 20 to 30 a year. Under the Civil Rehabilitation law since April of 2000, it has averaged nearly a thousand cases a year.¹⁶ Another actual factor has been that while the law states that it is for smaller companies, we have seen recent cases like *Mycal*, both large retailers, filing for civil rehabilitation. I will note that the *Mycal* case had been converted to a Corporate Reorganization Law (Kaisha Kosei Ho) case.¹⁷ However, there are numerous large company Civil Rehabilitation Law cases showing a major shift in Japan.

Another factor which relates again to Arnold's good friend and my mentor, former Tokyo High Court Judge Shinjiro Takagi, is an attempt to create an environment encouraging expedited pre-bankruptcy negotiations by creditors and debtors in order to restructure companies while they can.¹⁸

One of these trends has been the implementation of some of the INSOL Global Principles for Multi-Creditor Workouts based on the London Approach.¹⁹ The INSOL principles have been basically redrafted and reformulated and called the Guidelines for Multicreditor Out of Court Workouts. These guidelines are not law. They were basically developed as voluntary guidelines and were announced by a special commission headed by Judge Shinjiro Takagi.²⁰ The attempt is in summary twofold.

One is to deal with a chronic problem in Japan, where the main banks of debtor corporations feel forced to or take large debt write-off/debt waivers in exchange for no real assurance of restructuring. The bank would rather keep the debtor alive than take the full loss on its books.

The idea for these guidelines is to attempt to have the main bank and especially other creditors, involved in negotiations with the debtor to see if there is a realistic possibility of restructuring and then having a condition placed on debt waivers. Also, banks were concerned about debt waivers as there was a very large corporate and public outcry about indiscriminate debt waivers given many times preferentially to certain companies.

The second point of these guidelines was an attempt reportedly by the banks, government and the judiciary, as well, to have a platform to lead into early action and even prepackaged insolvencies where debtor companies, banks and trade creditors, would have some sort of structure for discussion before they brought cases into court. So this is essentially an attempt for private initiative and a non-judicial forum to expedite corporate restructuring.

Turning to another trend, since the fall of 2001, a major public topic and actually a very widely discussed issue, has been corporate restructuring. This has resulted in the debate and creation of a private equity fund structure to encourage corporate restructuring and also attempt to encourage early action. The hope is to create a regime where companies could avoid bankruptcy and go through major restructuring, which has been traditionally difficult in Japan.

The Japanese government has actually undertaken the private equity fund concept which was initially proposed by my partner, Richard Gitlin. The government has funded the Development Bank of Japan with initial funds of about a billion dollars to support private funds, headed by private investors or banks for example, to encourage restructuring and investment through the use of debt for equity swaps, and other methods common in the U.S. On the post-petition end, DIP financings are also being encouraged.²¹ There is one other factor.

The other matter that's on the radar screen right now in Japan is the amendments proposed to the Corporate Reorganization Law and even the overall insolvency law regime itself. This is another place where Judge Takagi's name pops up frequently. This is an attempt by the Courts, Ministry of Justice, and practitioners to initiate changes to the Corporate Reorganization Law (Kaisha Kosei Ho) which is essentially a law that I would say is based on the old Chapter X of the U.S. Bankruptcy Code and which is traditionally used in large corporation insolvencies where trustees are appointed. This may occur as soon as next year.

With the success of the civil rehabilitation law in Japan, they are attempting to try to speed up the process in the Corporate Reorganization Law. The major highlights that are being discussed, as I was reading through Japanese academic papers on it, is essentially to deal with perceived defects in the current law. An example commonly given is that plan approval by the creditors can easily take up to two years. There is going to be an attempt to shorten that to at least one year. There actually is some discussion of bringing it down to six months. In addition there are discussions of giving U.S. style superpriority rights to financiers to encourage DIP financing. Actually, that DIP financing discussion is also being considered under the Civil Rehabilitation Law.

Ultimately, in talking to those persons involved in this revolution, it appears that what the Japanese will consider a unified Bankruptcy Code combining the Corporate Reorganization Law with the Civil Rehabilitation Law and other laws, similar to our chapter 11 regime.

My last comment is that while all this is going on, there are some unfortunate factors in the very rapid deterioration of the Japanese economy and the marked deterioration of Japanese bank balance sheets. This has caused the government and politicians in early 2002 to start taking a "go slow" approach while providing support for the stock market.²²

There is very serious concern that while they can avoid any public crisis from occurring in the coming months or year, that an attempt to speed up corporate restructuring may further impact an already weak and deflationary economy.

MR. KELAKOS:

Arnold Quittner, do you have anything to add?

MR. QUITTNER:

I guess two of the questions would be: (1) Are we looking at the debtor-in-possession being in management control with the supervisor; and (2) is there a role for a creditors' committee, which traditionally there hasn't been?

MR. MURASE:

I agree, and Arnold is on point. The problem has been that in the thousands of Civil Rehabilitation cases, there have only been a few, I recall, where there has actually been a creditors' committee. The reason for it is the main bank system, where the main bank takes control of negotiations and discourages creditors' committees from being formed.

As to the DIP financing question on the Corporate Reorganization law as well there is a debate about DIP financing. The Corporate Reorganization law is not a debtor-in-possession law so a trustee is appointed. But there has been a

recent debate to allow existing management in some cases to remain and to speed restructuring even under this law, together with DIP financing.

MR. QUITTNER:

As I understood it, under the rehabilitation law, where management may remain in control, there will be a supervisor who in effect has veto power, although perhaps not the initiative such as a chapter 11 trustee would have, but he is able to say no. If the DIP doesn't agree, the DIP will have to go to the Tokyo district court to try to get approval.

MR. MURASE:

My only comment to that is looking at the representative cases, the supervisor has not had a major role.

MR. KELAKOS:

Does the rest of the panel have anything they want to add or should we move on?

MR. STERLING:

One comment and one question. The comment is that when the London Rules (or London Approach) ²³ was first conceived, it was to provide a framework for the continued provision of working capital to distressed corporates in order to allow distressed corporates to trade while the workout plan was promoted. ²⁴

What we have seen in many jurisdictions in Asia is a version of the London Approach being adopted but applied in a context where the corporate has already run out of cash. ²⁵ So the rules are being used for a different purpose, which is to provide a framework for negotiation in circumstances where the business of the corporate has already ceased. That's the comment.

The question is: what is the experience in Japan? Are the Japanese rules for corporates in difficulty being applied to allow continued provision for both working capital to corporates in difficulty, or are they being used as a framework for negotiation in the context where business is already ceased?

MR. MURASE:

There are reportedly very few cases where the guidelines have been attempted to be applied. The first case company is Kotobukiya, ²⁶ another retailer related case. That case, however, ended in insolvency. Some say that the Japanese guidelines are too strict; not allowing for management flexibility and imposing unrealistic restructuring guidelines. ²⁷

The government has tried to encourage them to be applied in some fashion, but the problem goes back to the main bank system and the main bank trying to essentially control the negotiations, which may be understandable since the main bank has the most to lose and usually has intertwined relations with the debtor. ²⁸ However, this can result in the lack of meaningful participation by other creditors, trade creditors, and the like. Such participation is very important in the retailer cases where such cooperation is vital.

MR. QUITTNER:

If you go back ten years to Maruko, ²⁹ the thing that really startled me was that Japanese banks, and of course the main bank, would send their officers off to the debtor's board of directors, take the chop away and have total and complete control. I'm wondering if there's anything in the new civil rehabilitation law that puts a penalty on the bank for seizing domination and control over the borrower?

MR. MURASE:

From my knowledge, no. A famous case was the *Sogo Department Store* one. ³⁰ In that case, there was a shareholders' lawsuit on-going and criminal charges against the former management of the company, who were largely sent from the bank to manage the company. ³¹

Arnold, you have more experience than I do in this area, but I think the main banks tend to be so intertwined with debtor's management –

And in that context, it's clearly becoming a situation where banks are on notice that they could be liable, especially through their involvement in everyday management. However, while it's a problem in Japan, the tradition is too ingrained in the system and whether one can create a bright line rule may be questionable.

MR. QUITTNER:

In the *EIE International* case, ³² where LTCB was the main bank, it had an unsecured loan. It then took control over the debtor that was the parent of a U.S. company in Guam. After it took control, it required every subsidiary of this Japanese corporation to guarantee the loan and collateralize the guaranty. ³³

When we got involved in that matter, we said, "You know, under U.S. law, an upstream guaranty is a fraudulent conveyance". And they sort of said, "Are you kidding? We do this every day." The problem was, of course, you can't do it in Guam.

MR. KELAKOS:

Let me jump in here. In your introduction, Satoru, and with your comments, Arnold and Mark, I think already we have touched upon some of the points where I wanted to take us, such as identifying or highlighting some of the key players and what some of the principal obstacles are to streamlining debt restructuring and corporate reorganization in Japan.

And you have also identified perhaps what went wrong in some of the earlier failures. I want to bring you back to some of these points. One question I want to throw out there to Satoru Murase and to the rest of the panel: it's been my observation in Asia, and I am generalizing, that when we talk about creditors' committees we are really talking about steering committees.

The U.S. concept of an unsecured creditors' committee or equity security holders' committee seems to be a rarity. ³⁴ Is it fair to say that the key players in a typical Japanese restructuring case would be their financial creditors? Where the trade creditors come in, are they represented at all, do they have a voice?

MR. MURASE:

Offhand, I think it is a steering committee situation. Essentially the main actors would be the main banks, and they would probably have a number of syndicated banks that are aligned with the main bank. They would be the main players.

However, there is obviously a position for the trade creditors. But this is probably more cultural than anything else. Trade creditors do not usually have legal representation. Actually, they have a voice, but they usually don't have formal representation. There are too few lawyers in Japan in any case. ³⁵

Secondly, they are not willing in many cases to disagree with a major bank. However, I would qualify that with one example. In a very large retailer case, the *Mycal* case, involving another famous insolvency attorney, Mr. Hideyuki Sakai, who Arnold knows well, you reportedly had a situation where the company forcefully filed for civil rehabilitation against the will of its main bank and rehabilitation was failing because the trade creditors refused to go along with the management plan of rehabilitation. This was a chaotic case but one that shows change in the old ways of Japan.

I would say my central theme about Japan is that there is a revolution in the insolvency regime going on. But while the revolution is ongoing, it's been excruciatingly slow from a U.S. perspective. Secondly, this is going on under economic conditions that are worse and worse every day and so there's dynamism, but in a very troublesome environment.

MR. KELAKOS:

Arnold, do you have any comment on that?

MR. QUITTNER:

I think the difficulty is that it takes so long to get the Diet to finally approve and adopt something. And the political aspects of it are so strong and the cultural aspects are so strong, that nobody is surprised in Japan if the lending bank simply takes domination and control over the borrower.

In the *Maruko* case, what startled me is that when the interim trustees applied for fees, there wasn't any notice to creditors. Nobody even knew there was a hearing.

MR. KELAKOS:

Have there been improvements under the existing structure providing notice to, or participation by, overseas creditors in a debt restructuring or plan or rehabilitation process in court proceedings in Japan?

MR. MURASE:

Essentially in the Civil Rehabilitation law, ³⁶ there are provisions to provide for more transparency, and more availability of basic information about the company involved, etcetera. But it's still woefully lacking if you look at it from a U.S. standard. However, there is a realization of this. The reason is that, going back several years, I think the main bank could have actually quietly taken over and restructured the companies easily and basically taken the blow. But the Japanese banks' financial situation is very poor. Also you have the participation by the big U.S. players, G.E. Capital, Ripplewood, Wilbur Ross, and other private equity funds like Carlyle Group, as well as Goldman Sachs and other investment bankers in the market.

Their participation and the availability of those funds has really changed the rules in Japan such that they are requiring basic disclosure. Still it's very, very difficult.

I think one classic example of a major change is that for the investment banks, one major income-producing role that they have is as financial advisor to the Japanese bankruptcy court or the trustee in introducing investors, economic analysis, and evaluation of deals. The court and trustees in those situations are actually paying major fees to the financial advisors. That is actually quite a revolutionary development in Japan.

MR. KELAKOS:

Mark Sterling, Charles Booth, do you have any comments?

MR. STERLING:

No further thoughts.

MR. KELAKOS:

Now that we have highlighted some problem areas, it seems there's a movement afoot as you put it, sort of a two-tiered revolution in Japan with restructuring laws, providing more notice, providing more transparency, and new players that are now coming into the mix.

Any suggestions? If you had your druthers and you were drafting amendments to the law, what would you like to see other than the points you covered? Are there any additional structures that you've tried in other countries or strategies that you haven't seen yet that might be applied?

I leave that open. I'll start with Satoru Murase. Do you have any thoughts on those points?

MR. MURASE:

Actually, I have too many points. I wish there was one or two major suggestions I could make that would really further improve the system, but I do think of what was mentioned earlier. I think the transparency of the system needs to be continually improved. And this effort that the Japanese are making to increase transparency to allow for foreign players to be on an even level playing field is very, very important for the future in Japan and for investors in those types of companies, which really is very important.

Also transparency within the companies and through changes in corporate governance is crucial as I would believe that more and more Japanese companies are going to be acquired by other domestic companies, as well as by overseas companies. There is clearly a problem with transparency now in Japan.

As Arnold had mentioned, in many cases main banks would be sending in management to their customer companies and there would be various payments and expenses incurred, which in U.S. companies, other than Enron, would be properly reported to the shareholders.

My personal view is the more disclosure and more open air you expose to the system the better.

MR. KELAKOS:

Let's turn to Arnold Quittner.

MR. QUITTNER:

They did pass a recognition of foreign insolvency cases with the new law and purport to have sort of an ancillary type proceeding.

The Japanese have adopted something similar to the United States ancillary proceedings in the sense that they have adopted a new law to recognize foreign insolvency proceedings and foreign administrators whereas before it was strict territoriality.

MR. KELAKOS:

Any other points that you can think of, Arnold?

MR. QUITTNER:

That's enough for me.

MR. STERLING:

Just to reiterate a point that's been made a couple of times already, although my experience of Japanese restructurings is fairly limited, what does stand out is the absence of proper disclosure, whether it's absence of disclosure standards or just absence of disclosure.

The quality of disclosure for rehabilitation or reorganization plans is even by Asian standards not good in my experience.

MR. MURASE:

I think that is clearly the case. Unfortunately, it stems from the fact that there is such poor disclosure in the viable companies to begin with that it has been very difficult to implement strict standards in the insolvency regime.

MR. STERLING:

I guess. But it's a cultural thing as much as a legal thing.

MR. MURASE:

I think it's cultural and also I think it stems from what many say, that the Japanese still tend to look as the company not being run for the shareholders, but really being run for the employees and it's all one family.

Information about the family, you keep within the family. There's no need to really have those things hanging out there for other people to see.

MR. QUITTNER:

Just one comment, which comes out of the *Maruko* insolvency. I happen to have been over there quite a bit of the time, and if you met with someone from MOF, ³⁷ one thing they would say is if we need to disclose that they are insolvent, all the depositors would cause a run on the bank.

MOF didn't want that. So for MOF, it's much better to conceal the fact that the bank is bankrupt.

MR. BOOTH:

There was an article in the *Asian Wall Street Journal* a few weeks ago which said that Enronitis is a problem in the States because Americans had thought there was transparency and that it really isn't a problem in Asia because people assume that there is little or no transparency. ³⁸

And one really can't overemphasize this point, because Americans often focus on the openness of the disclosure process. That's really part and parcel of the openness of the overall corporate governance process.

It is interesting to take a look at what happens when there are various collapses around the world; whether it be in Russia, Argentina, etc. In the United States, within a month or so of the collapse, banks and investment banks each come to the market and disclose what they expect their overall exposure to be and the market takes that information into account.

When we take a look at what happens in Asia, that type of disclosure just doesn't occur. And then, of course, by the time that information does come out, it's generally too late to do much about it.

MR. MURASE:

The issues of shame and bankruptcy are so strong. Even bankruptcy I guess is shameful in the United States in many contexts, but the shame is still great in Japan and the loss of faith is such that there is just a natural disincentive to disclose or to be open.

The more you're open, the more I think you get hit hard from your shareholders, creditors, in the public and the newspaper, certainly in Japan.

MR. STERLING:

That's certainly right in other areas of Asia. Bankruptcy still has a stigma; certainly in Hong Kong and in other parts of Asia outside of the PRC.³⁹ In the PRC, I guess it's too early to tell because there's no real experience of bankruptcy happening. But all the indications are, and Charlie can probably comment better than I can, that it has the same face issues in the PRC.

II. The Hong Kong SAR

MR. KELAKOS:

At this point, unless anyone has any concluding remarks on Japan — actually, your comment, Mark, is a nice segue to Hong Kong. I think we should focus on that next.

MR. KELAKOS:

Charles Booth, could you provide a summary for us of the current regime in Hong Kong both for in-court and out-of-court debt restructuring, insolvency, and corporate restructuring matters?

MR. BOOTH:

In brief, of course the Hong Kong situation is quite different. The historical situation is different from the Japanese in that Hong Kong inherited its insolvency regime as part of its colonial status.⁴⁰ Historically, Hong Kong legislation is based on English legislation and Hong Kong company law is no exception.⁴¹

The Hong Kong Companies Ordinance is primarily a liquidation regime. I think one of the main differences between Hong Kong and the States, and I think this is true of almost every jurisdiction in Asia when you compare it to the States, is that in the States the primary focus is on chapter 11 and on reorganization.

But certainly up until the time of the Asian financial crisis, the primary orientation of ordinances and legislation in Asia in general, and in Hong Kong in particular, was on liquidations.⁴² And although there is a procedure in the Companies Ordinance under section 166 for entering into a scheme of arrangement, that provision is quite rarely used. Hong Kong lacks an effective formal corporate rescue procedure. That is the first general factor.

The second factor has to do with the out-of-court situation. The out-of-court situation in Hong Kong historically has been bank led. One possible mechanism has been through receivership whereby a bank that has fixed and/or floating charges on substantially all the assets of the company appoints a receiver to take control of that company and through that receivership might be able to restructure the company. Granted, however, receivership is infrequent in Hong Kong, and when it does occur, a rescue does not necessarily follow.

But, until recently, Hong Kong did not have any guidelines for promoting successful restructuring. I think one of the important changes, and this is where Mark would have more experience than me, has to do with the adaptation in Hong Kong of the London Approach for out of court restructuring, whereby that Approach began to be used to come up with solutions for trying to save companies.

This informal approach is called the Hong Kong Approach to Corporate Difficulties, and it was established by the Hong Kong Association of Banks and the Hong Kong Monetary Authority.⁴³ This Approach changes the process somewhat, because a secured bank's first option is no longer going to be whether or not they will appoint a receiver. Rather, pursuant to this Approach, this is not supposed to occur unless the banks cannot reach an agreement.

One of the interesting occurrences in Hong Kong is that although the situation in Hong Kong after the financial crisis was desperate, and although the number of liquidations and workouts increased dramatically, I don't think the number of liquidations really hit a level that many of us expected that it would.

The banks have exhibited much more of a wait and see attitude. Even right now things just seem to be in a period of abeyance. Possibly this gets to Mark's point that the Approach is being used somewhat differently here. But you

haven't seen a deep cleaning out of companies as would more likely occur in the West.

MR. KELAKOS:

I hate to jump in here, but perhaps in your summary here you might point out that in certain countries, for instance, and Mark knows full well, Thailand was always viewed as a debtor's paradise.

Let's take the case of a typical corporate debtor in Hong Kong: would you say on the spectrum of debtor's hell or debtor's paradise, where does Hong Kong fall?

MR. STERLING:

Charlie, maybe you'll answer that and I'll jump in. That's a very interesting question.

MR. BOOTH:

I just want to say one thing before I answer that. One of the interesting factors about Asia pre-crisis is that in almost every jurisdiction, perhaps except for Singapore, the insolvency law was underdeveloped. ⁴⁴

There was a sense pre-1997 that we didn't have to worry about that because everything was going quite well in Asia. Then when the baht collapse occurred in Thailand, one by one all the countries in the region began focusing on reform. One of the interesting things about Hong Kong is they started that reform process much earlier than the other jurisdictions, many years before the baht collapsed. ⁴⁵ And although Hong Kong was one of the first to start, it will be one of the last to finish. Hong Kong still has not enacted an effective formal corporate reorganization law. It's one of the few jurisdictions in the region that has not moved in that direction. That issue is probably worth discussing.

But on the sort of the continuum that you're mentioning—it's a little difficult to answer the question because there's sort of a curious aspect to it in that in Hong Kong, although the banks are in a very, very strong position legally, in practice there are many impediments that make it difficult for them to enforce their rights.

On the one hand Hong Kong law offers very strong secured creditor protection, ⁴⁶ and the banks can be in a very good, a very strong position, in the restructuring. On the other hand, you also have a tradition of many companies being family controlled. ⁴⁷ And even many of the large publicly traded companies are family controlled. As in other Asian jurisdictions, the result is that companies are often able to put the banks at bay sometimes by failing to provide relevant information. But ultimately when the banks decide to take steps, they are able to get at the assets, which is much more difficult in Thailand and elsewhere in Asia.

Overall, Hong Kong would be more on the creditors' side of that continuum. Where banks are able to appoint a receiver they are in a very strong position, and there have been a number of successes under the Hong Kong Approach. The banks have been relying on existing procedures and now that it's time to reform the corporate rescue law, they are basically asking, How would this new procedure be better for us than receivership, or the Hong Kong Approach?

And here, what I think is quite interesting, is that, although the United Kingdom is now in the process of moving away from receivership because of the argument that administrative receivership ⁴⁸ favors the small group of secured creditors rather than creditors generally, in Hong Kong this debate really has not occurred.

It's been commonly accepted that banks generally should be in a strong position. And it's therefore been a matter of coming up with a formal corporate rescue regime that will allow the banks to basically opt out if they so choose.

An additional point is that in the region generally one of the benefits of the enactment of formal corporate insolvency regimes, and this comes out in a study by the Asian Development Bank in which I took part, is that the enactment of a formal corporate rescue regime does not necessarily lead to a dramatic increase in the number of cases under that regime, but rather happens to facilitate more out of court workouts. ⁴⁹

The difficulty you have in a jurisdiction without an effective formal corporate rescue system, is that unanimity is required for a rescue to be achieved. You have a problem of holdout creditors whereby certain creditors can basically just slow down the process by asking for a larger payout and refusing to agree to less.⁵⁰ And once you pass an effective formal reorganization law that sets forth a mechanism whereby a majority in number and two-thirds of the value, or three-quarters of the value, it really doesn't really make a difference what the exact percentage is, you prevent that from happening.

MR. KELAKOS:

By having the threat of a formal system that can bind dissenters, you are saying that, in and of itself, will help expedite the flow of sort of the out-of-court negotiations?

MR. BOOTH:

Correct. That's one of the conclusions.

A further point has to do with the position of the secured creditor in insolvency generally. In a place like Hong Kong, it is still very, very strong. So when you approach the changes to the law, it's from a quite different orientation than in the States where it's so ingrained in the system that the automatic stay should apply to the secured creditors and that historically you're able to stop action by secured creditors by filing a petition. That is not the situation in Hong Kong.

One of the things you'll see is that when the corporate law reform process started in Hong Kong, there was agreement that an aim of the law should be to provide major secured banks with a veto power over that process, some sort of veto in terms of whether formal corporate rescue should go forth.⁵¹

MR. KELAKOS:

Thank you, Charles. Mark, do you have any comments?

MR. STERLING:

Yes. To answer your question debtor's hell or debtor's paradise, if you look at the rules, Hong Kong should be debtor's hell. If you look at what happens in practice, Hong Kong is much more like debtor's paradise. Let me try to explain that paradox a little.

As Charlie says, secured creditors have a strong position in Hong Kong. We recognize the floating charge under which banks can take a security interest over the whole business enterprise of a borrower.

Now, that enables a bank when a business gets into difficulty to appoint an out of court receiver to run the business in the interests of the bank and realize the security for the benefit of the bank. And the bank is insulated from liability because the management liability vests in the receiver.

However, in practice, very few banks in Hong Kong actually take floating charges from their borrowers. So they have an enormously strong weapon but they don't often use it. As Charlie says, Hong Kong does not have an effective corporate rescue regime.

We have a composition proceeding called a scheme of arrangement that is becoming much more widely used in Hong Kong than in other Anglo Saxon jurisdictions in the world that have such regimes. But it's a composition proceeding that doesn't have the benefit of a stay.

So it's kind of difficult to be confident to use the process because at any stage during the rescue negotiations they can be upset by creditors putting the company into formal bankruptcy proceedings. That then leaves Hong Kong with two alternatives, which are formal bankruptcy proceedings or out of court rescues.

Now, out of court rescues are pretty common in Hong Kong. They are difficult to achieve, certainly in larger cases, because Hong Kong borrowers are traditionally extremely multi-banked. So we have had deals in Hong Kong with up to a 150 different bank creditors, and that's excluding bondholder creditors and vendor finance suppliers. These are mostly bilateral trade lines.

One of the features of Hong Kong corporates is that the holding company will be listed. That holding company may have a number of other associated listed companies. Each of those listed companies will have a large number of operating subsidiaries, and each of the categories of company that I mentioned will have their own working capital lines. So lending is a pretty straightforward process.

MR. KELAKOS:

Is there a culture such as in Thailand of upstream guarantees or where you can obtain floating and fixed charges so you can get essentially an all-asset lien in Hong Kong? Is that something that's not typically used or is that part of the mix?

MR. STERLING:

Again, upstream guarantees are possible in Hong Kong, that is, they can be lawfully given under certain circumstances. But, in practice, it's unusual to see a full guaranty net, full cross guaranty net as a security structure.

MR. BOOTH:

When one gets back to a comparison between Hong Kong and a place like Thailand, one of the main differences is that in a place like Thailand, it's almost impossible for the creditors to force the company into bankruptcy over its objections.⁵²

That is why a *TPI*⁵³ is so important in Thailand. It was the first time in that jurisdiction where a company was forced into bankruptcy over its objection.⁵⁴ In Hong Kong, of course, it would be a liquidation. But at least the banks in Hong Kong have a trigger for liquidation that they can use.

And Mark has pointed out that what looks like what perhaps should be a creditor's paradise can, at times, be hell. To a certain extent, I think the banks bear some responsibility for this. The powers they can have under the law are quite varied, for example, to take fixed and floating charges, to be able to require the disclosure of information, and to petition for liquidation.

And yet the banks often don't exercise these powers. There was an interesting article in the *Asian Wall Street Journal* focusing on the fact that a growing number of companies in Hong Kong are late in complying with their obligations under the Companies Ordinance to file their annual audited accounts.⁵⁵ When I prepared my study on Hong Kong for the ADB, I learned that the same was true of many companies in regard to their obligations under the loan agreements with their banks—they were often late in complying with their reporting deadlines and the banks were often not properly policing their agreements.

That was certainly true pre-1997. One would hope it's better now. And maybe one aspect of this is that up until 1997 when Hong Kong was booming, there was much less of a focus on the downside risk.

MR. STERLING:

Charlie, just to pick up on your train of thought, you're right. The key leverage of banks is the ability to place a corporate in bankruptcy. Bankruptcy (or liquidation as we call it) is an effective process in Hong Kong.

However, it's like the bank taking a big stick which it can hit the corporate over the head with, but the bank is also hitting itself over the head because the liquidator has no power to carry on the business except for the limited purpose of winding up the company.

So the assets of the corporate are sold in a fire sale and the bank will traditionally get a return of a very few cents on the dollar. In some jurisdictions, I believe the U.S. and to a certain extent the U.K., bankruptcy is an effective process in that a liquidator in practice is able to investigate antecedent transactions and misconduct or breaches of fiduciary duty by the management.

But again, in Hong Kong, by the time a company has gone into liquidation, all or virtually all its assets would have disappeared. And except in extreme cases, lenders do not have the appetite to fund a liquidator to conduct a thorough investigation into the causes of failure.

So that liquidation, when it occurs, is an admission by the banks that they will get no or virtually no return on their lending.

MR. BOOTH:

I think you're absolutely right. Again, I think this gets back to the problem of the process starting too late in the day. In most cases, the formal process starts much too late to be of much benefit to the bank because most of the corporate assets are gone.

I also think it again ties into the fact that even in Hong Kong the level of disclosure is not as high as it should be. I think that in many situations leading up to corporate financial crises that the banks did not have the information they should have had to be really tracking the status of their loans. And when the problems were discovered, it was really too late to address them.

One gets back to the point Mark made about the large number of banks involved which causes great difficulties. The second aspect is that this problem is further exacerbated if the banks are from different countries, with different workout cultures.

MR. KELAKOS:

What I'd like to do is sort of head towards a wrap-up and perhaps talk a little bit about Hong Kong and talk about some suggestions for improvements, observations of what may be coming down the pike and also open it up to Arnold Quittner as I heard you in the background.

And perhaps, Satoru, you have some questions or observations. Let me start with you, Arnold.

MR. QUITTNER:

Are you referring to Hong Kong or just generally?

MR. KELAKOS:

Hong Kong in terms of what you heard. Perhaps you have some questions that you would like to follow up on.

MR. QUITTNER:

I guess one question is if you have 15, 20, 30, 40, 50 banks and it's not a syndicated loan, how do they share priority in the collateral?

MR. STERLING:

There's no fixed rules, Arnold. In some cases, banks will take entity priority in accordance where they lent. In other cases, entity priority is just too difficult and you have some sort of pooling scheme. But as I say, there are no hard and fast rules.

MR. KELAKOS:

Mark, perhaps to follow up on an earlier comment, does the London Approach ⁵⁶ help you in this regard by getting people to talk and perhaps as an adjunct to that is there a movement afoot to perhaps formalize or adopt or encourage the use of ADR to facilitate these disputes when you have multi-bank situations like this where you don't have a syndicated loan?

MR. STERLING:

The Hong Kong guidelines as we call them have been very helpful in setting out a framework for the negotiation of multi bank workouts in Hong Kong. ⁵⁷ I haven't seen any ADR in operation in these situations. Personally I doubt whether it would be particularly effective.

What is needed and what does tend to happen in these situations is a strong lead bank with an experienced steering committee. And if you have those two things together with a bank group which understands the Hong Kong guidelines, then you have the best framework possible for an out of court workout.

MR. KELAKOS:

Satoru Murase, do you have any comments?

MR. MURASE:

Actually, I had a question. Obviously a lot of Japanese banks are major creditors in these Asian workouts. ⁵⁸ Many times I advise these banks. But from your viewpoint, are the Japanese banks very difficult to deal with in light of the fact that in their home country there isn't as yet a fully developed regime for out of court workouts?

MR. STERLING:

It is certainly true that when you're drawing up your list of problematic issues on day one of a workout, if there are Japanese banks, there will be an item on your list which says "buy in Japanese banks."

Having said that, there have been a number of major workouts. I'm thinking in particular of the restructuring of Guandong Enterprises, ⁵⁹ where there was significant Japanese involvement in both number and value, but all the deadlines were met by the Japanese banks, and the Japanese banks were comfortable to accept the new equity instruments as well as the other securities which were offered on the restructuring.

MR. MURASE:

Would you attribute that to the banks or to good lawyers?

MR. STERLING:

I would attribute it entirely to the banks!

MR. KELAKOS:

Does anybody have any further closing comments on Hong Kong or with the mention of Guandong Enterprises can we turn to the PRC?

MR. BOOTH:

I just want to make a few more points. I think that one of the important factors in Hong Kong that has helped immeasurably since 1997 is that the banks themselves are in quite good financial shape. And if you take a look at the

banks in Hong Kong compared to banks in other jurisdictions, that's one of the huge differences in terms of the relative stability of the whole corporate sector.

In many of the other jurisdictions, certainly in China, the banks themselves are confronting systemic insolvency problems. ⁶⁰ That creates a whole other series of pressures on the system that Hong Kong has been able to avoid.

The second point, one I mentioned earlier and one with which I'd like to finish off, has to do with Hong Kong's enacting of a formal rescue regime. As I said, Hong Kong was one of the first jurisdictions to start the law reform process and will be one of the last to finish.

And one of the factors there that has been probably the cause of most of the delay has been what exactly to do with workers in corporate restructuring. In Hong Kong, the government proposed that before a company can utilize the proposed corporate rescue process, which is called provisional supervision, the company must first pay all the workers' entitlements in full. ⁶¹ Just recently another proposal has been made to cap this pre-petition payment to each worker at 258,500 Hong Kong dollars, which is still over 30,000 U.S. dollars. By proposing this level of protection to workers the government is ensuring that very few companies will actually be able to use provisional supervision, if enacted, because most companies won't be able to get over that hurdle and commence the process.

III. The People's Republic of China

MR. KELAKOS:

With those comments, let's now move on to the PRC. Charles?

MR. BOOTH:

Turning to China, China passed its first national bankruptcy law in 1986 ⁶² which was a bankruptcy law focusing on state owned enterprises: ⁶³ And although there is other legislation that pertains to the bankruptcy of certain other corporate enterprises, it's probably most helpful to the debate to focus on the SOEs. That is where the problem has been.

China itself was not as hard hit in the first wave after 1997 as many of the other jurisdictions that have been mentioned here. However, one factor that China shares with many of those jurisdictions is that the banking sector is also in financial difficulty.

So where exactly is China heading is the question. There are two avenues for reform right now in that there is a drafting committee that has been working on drafting a new bankruptcy law since 1994. ⁶⁴ And this law will be much broader in scope than the '86 law that only applies to SOEs.

This new law will also have more of a focus on reorganization. ⁶⁵ At the same time, there is a process being led by other groups in China, such as the State Economy and Trade Commission ("SETC"). ⁶⁶ The SETC is one of those groups that is focusing on the out of court restructuring of state owned enterprises. ⁶⁷

And there is some intersection between those two processes, because under existing bankruptcy law, for a bankruptcy to occur involving an SOE, you need permission of the government agency in charge of the SOE ⁶⁸

This, of course, has led to a bit of a debate right now. If one moves ahead with the new law in the direction of reorganization, questions arise: What do you do with the state owned enterprises? And should they be exempt from bankruptcy law? If the SOEs are exempted, the government agencies now in charge will likely be able to retain control; if not then the opposite will occur.

And as of this date, it looks as if there will be an exemption for many of the older SOEs, which also happen to be some of the larger, more inefficient SOEs. So even when the new bankruptcy regime comes in, it's unclear at this point whether it will apply to many of those entities.

I think that's one reason why groups like the SETC are trying to focus on out of court rescue. I'll make a few more general points and then turn the phone over to Mark.

In a jurisdiction like China, there's all the difference in the world between what your procedures say on the books and what is actually happening in practice. And part of the reason for that is when one is taking a snapshot of the insolvency law process, you have to fit that snapshot into the overall existing situations.

And in a place like China, when turning to the issue of who will actually participate in this process, it is clear that you don't have sufficient professionals— be it lawyers, accountants, individuals who can do valuation, or individuals who can actually make the process work if one is moving towards reform of corporate reorganization procedures.

Secondly, you have great problems with the enforcement of security. This gets back to some of the examples mentioned earlier. Thirdly, the SOEs have huge amounts of debt and their lending banks themselves are in great financial difficulty.

Fourthly, many of the SOEs are poorly managed and retain far too many employees than they need. And there are frequent allegations of incompetence and/or corruption in regards to many of these entities.

Although at one level we can talk about the need for reform, we must acknowledge that it will be a slow process. I'll finish up with my introduction with a few final thoughts.

There are two factors that are especially significant in explaining why China has not bankrupted more SOEs. The first is that if China actually just liquidated all the nonperforming SOEs there would be massive unemployment, which in turn would lead to social unrest.

Secondly, if all the SOEs were liquidated, many of the banks would follow.⁶⁹ So when taking a look at some of the efforts that are developing, we need to realize the importance of avoiding these two consequences. It is therefore understandable why China is trying to come up with a solution that focuses on preserving employee jobs wherever possible and on ensuring that the banks will not get devastated by the process.

There have also been some efforts at out-of-court restructuring recently. One of the approaches being tried is called the Changchun Approach. To generalize, this Approach has been used in some situations where there was primarily one state bank that had lent money to an SOE. Under this Approach there would be a hive down in which the best assets in the old SOE would be shifted to a new entity and the state bank that had been the primary lender of the old SOE would make a loan to the new entity, which in turn would pass that money back to the old entity, which in turn would pass that money back to the bank.

The money would go around in a circle. And although at first glance it looks like not much has happened, at closer inspection it is clear that the bank ends in a much stronger position because the money paid back to the bank is paid back on behalf of the old preexisting debt at a time when the other preexisting creditors do not get paid anything.

In addition, the loan advanced to the new entity would now be a new loan that would arguably have a greater likelihood of getting paid, because the repayment obligation would be from the new enterprise rather than from the old enterprise.

So in essence, to summarize, the Changchun regime focuses on the bank and not on the creditors generally. The system is premised on trying to keep the bankers relatively happy so they will participate in the process.

What the SETC⁷⁰ is in the process of doing is considering how to improve this process and come up with a regime that will address their main concerns as well as perhaps be internationally accepted.⁷¹

MR. KELAKOS:

Charlie, you're currently working on a project on that issue, aren't you?

MR. BOOTH:

Yes, I am co-manager of a World Bank project advising the SETC on the out-of-court restructuring of the SOEs. ⁷² We have commented on the Changchun Approach and have suggested ways in which it could be improved.

MR. KELAKOS:

Mark Sterling?

MR. STERLING:

Just a few thoughts. The first is that we do have a reasonable amount of experience of out of court restructuring of PRC enterprises. But I think it's fair to say that there's still virtually no experience of PRC bankruptcies.

I'm actually aware of only one major case in which foreign enterprises have been involved. The experience of out of court restructurings is pretty favorable in that PRC borrowers have found themselves to be receptive to restructuring in accordance with international principles, and they have been serious in carrying out their plans.

There are actually a number of very successful restructurings and workouts of PRC or PRC owned corporates. ⁷³ On the bankruptcy side, as Charlie says, the law is a bit thin, although the basic Code which is the current trial bankruptcy act of 1986 is not a bad Code. ⁷⁴

The problem one has is there is almost no experience of bankruptcy proceedings in the PRC courts. So the parties in interest don't have the predictability and the precedent that one would need to be confident to rely on the process. ⁷⁵

Going forward, the PRC will be a very interesting place for bankruptcy and workouts. The reason I say that is that the PRC are receptive to international principles and western ideas. ⁷⁶ But they will want to adapt those ideas to the PRC context.

On the demand side, a couple of years ago four major commercial banks in the PRC set up asset management companies to which they transferred a lot of their nonperforming loans. The face value of those loans is in excess of 150 billion U.S. ⁷⁷

The asset management companies are charged with disposing of those loans, and one of their main strategies for disposal is sale to international investors. This is a deliberate strategy by the PRC government to examine the application of international workout and collection techniques to NPLs, how effective that is as a process for collection, and to see what effects the collection process has on wider social objectives like employment and stability in local communities.

MR. BOOTH:

If I can follow up with two further observations — it's absolutely correct that the bankruptcy law itself is very rarely used, especially for any entity of any major size. In the West, if a rescue fails, eventually you will usually have a bankruptcy under the formal law.

That just does not happen in China. If the out-of-court negotiations are unsuccessful the SOE is rarely made bankrupt. Moreover, even under the Changchun Approach where a rescue has been attempted, the old SOE is not made bankrupt.

The second point has to do with asset management companies. I think this ties into another point that can be made more generally about what has been happening in Asia. In many of the countries in the region, and China is no exception, where there are systemic insolvency problems and there is a tradition of administrative rather than legal responses to problems, entities such as asset management companies often will play a major role.

If one takes a look at what happened in Malaysia or Indonesia and now in China, at the same time that a formal court-based reorganization system is established, an out-of-court process is also set up that involves the use of these asset management companies. They often are used to address problems in the financial sector by taking control of the NPLs owed to the banks by corporate debtors.

MR. KELAKOS:

I have a question for both you, Charlie, and for Mark. I'm glad you brought up the AMCs. I had a meeting when I was in Beijing last year with some representatives from one of the AMCs that was set up for the four state owned-banks you were referring to.

In our meeting we discussed SOEs, among other things. I understand that we are dealing with state owned banks, but is there any talk of the establishment of a National Centralized Asset Management Corporation, as, for example, the establishment of the Thai Asset Management Corporation in Thailand? ⁷⁸ —

Is there any discussion, or a trend in that area, to have one centralized AMC that might have more super powers or more ability to consolidate some of these things or are their tasks going to be piecemealed out?

MR. STERLING:

Not so far as I'm aware, George. The four AMCs were initially established to get the bad loans off the PRC commercial banks. For the first 18 months of the AMC's existence, nothing much happened.

Over the last year, we have seen each of the four AMCs actually taking proactive steps to start managing their NPLs and indeed disposing of their NPLs to foreign investors. Now, if that process goes well, then I wouldn't have thought that there was any particular need for one huge central authority.

Again, if you look at the size of the total NPLs, an authority administering NPLs with a face value of 150 billion U.S. is likely to be fairly slow moving and bureaucratic versus the situation you have at the moment where you have four smaller AMCs charged with the disposal and administration of four very, very large portfolios.

And as long as the process works, as indeed in my view it is working at the moment, and these asset management companies are taking active steps to manage and dispose of their portfolios, I would question the need for one huge super authority.

MR. KELAKOS:

Let me ask the rest of the panel. Arthur Quittner, Satoru Murase, do you have any comments or questions?

MR. QUITTNER:

When you have an AMC, what kind of cost structure is involved and how do they get their fees?

MR. STERLING:

Well, with the deals we have seen so far, the AMCs will sell their portfolios at a fraction of face. But obviously in order for the purchase of portfolios to be able to administer and collect the loans, they need the contacts of the loan officers of the AMC.

So there's generally some sort of incentive structure in which the AMC will retain some upside interest in the collections.

MR. KELAKOS:

Satoru, do you have any comments or questions?

MR. MURASE:

The impetus for the changes is the recognition on the part of the government for the need to do this or maybe this is just market related? What is the incentive from the government's perspective to continue to do —

MR. BOOTH:

You have to look at the historical context here changing from a socialist economy to more of a market economy. That goes back to the trial law in 1986. That was the first step. In a relatively short period of time, China has come far.

MR. MURASE:

This pace is continuing to accelerate?

MR. BOOTH:

Yes, with the drafting of a new law and the SETC's out-of-court rescue efforts, much is happening. China has come amazingly far since 1986. I think that many of the people involved in the drafting process are quite good, and they are also very knowledgeable about what is happening elsewhere.

It's a matter of trying to find procedures that can be adapted for use in China, and there is a growing view that value is going to be created through some kind of restructuring rather than through liquidating at very low prices.

When one looks at the time frame for law reform, one similarity between Hong Kong and mainland China is that the period keeps getting extended. It's my sense that the enactment of the new law in China is still a couple of years away.

MR. MURASE:

That's interesting. The Japanese context in the national debt overhang, a large portion of that overhang is government related institutions, government credit institutions that have non-performing loan problems. It is a private sector problem with massive government sector nexus, which it is always difficult to deal with from the government perspective.

Conclusion

MR. KELAKOS:

Gentlemen, I thank you for your participation in this program. We could spend many hours on the phone just talking about further developments and sharing experiences on Japan, Hong Kong and the People's Republic of China.

One interesting thing that has come out of these discussions is that in each country and region there are unique attributes to the restructuring processes. There are different players, different driving forces.

To those who make assumptions that all the rules are the same and that all the dynamics are similar as that what you would find, let's say, in the United States or in the U.K., I believe we have highlighted significant differences in these countries and the region. And I would point out we've highlighted significant traps for the unwary.

Thank you again for your participation.

FOOTNOTES:

¹ Telephonic roundtable discussion moderated by George M. Kelakos on Friday, March 1, 2002 via conference call. George M. Kelakos is a partner at Cohn, Kelakos, Khoury, Madoff & Whitesell, LLP in Boston, and the Managing Director of Tonson Planners, Ltd., Bangkok, Thailand. Since 1998, Mr. Kelakos has organized and has served as a chair or panelist on numerous educational exchange programs with the Thai Ministry of Justice, Office of the Judiciary and private sector groups on ADR and business bankruptcy and reorganization law and practice. Mr. Kelakos has served as Co-Chair of the ABI's International Committee since 1999. The Participants are: Satoru Murase; Arnold M. Quittner; Mark Sterling and Charles D. Booth. Satoru Murase is a partner with Bingham Dana LLP, an international law firm with over 500 lawyers worldwide. Bingham's 85-lawyer Financial Restructuring Group advises investors, corporations, international agencies, and governments on restructuring, multi-national workouts/insolvencies, and sovereign debt issues. Mr. Murase graduated from Harvard College and Georgetown University Law Center. Arnold M. Quittner is of counsel at Pachulski, Stang, Ziehl, Young & Jones, P.C., in Los Angeles, and is a graduate of Loyola University of Los Angeles (J.D. 1951 magna cum laude). Mr. Quittner was admitted to the California Bar in 1952, the United States Supreme Court in 1960, and currently chairs the Inter-Pacific Bar Association Insolvency Committee. Mark Sterling is a partner at Allen & Overy in Hong Kong. Mr. Sterling's practice areas include business reconstruction and insolvency. Charles D. Booth is an Associate Professor and Director of the Asian Institute of International Financial Law (AIIFL), in the Faculty of Law at the University of Hong Kong, Hong Kong. Mr. Booth has served as co-manager of a World Bank Project for the Chinese State Economy and Trade Commission on the out-of-court restructuring of State-Owned Enterprises and as a consultant on an Asian Development Bank Project focusing on insolvency law reform in Asia. [Back To Text](#)

² See Ron Insana, Fortunetelling: How to Read Unruly Markets' Tea Leaves, Wall St. J., Oct. 5, 2000, at C1 (explaining Thai currency is measured in baht). [Back To Text](#)

³ Id. (stating fall in Thai Baht is "an early warning sign of problems in the world financial system that would pummel markets"). [Back To Text](#)

⁴ See Craig Karmin, Asian Stocks Decline Sharply Across the Board, Deepening Bearish Near-Term Outlook on Sector, Wall St. J., Sep. 12, 2000, at C18 (stating NPL is acronym for non-performing loans). [Back To Text](#)

⁵ See Laurent L. Jacque, The Asian Financial Crisis: Lessons From Thailand, 23 Fletcher F. World Aff. 87, 91-95 (discussing counter-measures resulting from Thai baht crash, including corporate and debt restructuring). [Back To Text](#)

⁶ See generally Ming-Yu Cheng & Sayed Hossain, Malaysia and the Asian Turmoil, 2 Asian-Pacific L. & Pol'y J. 125 (evaluating recent economic difficulties in Malaysia since 1997 Thai baht crash). [Back To Text](#)

⁷ See The Name of Recession, N.Y. Times, Nov. 27, 2001, at A18 (stating U.S. recession officially declared on previous day). [Back To Text](#)

⁸ See Robert Cole, Avis Europe, Times (London), Dec. 18, 2001, at Business Sec. (noting deep blow to economy in Europe from September 11 attacks). [Back To Text](#)

⁹ See Ronald J. Silverman & Timothy B. DeSieno, The "Asian Contagion:" Understanding Cultural and Legal Differences, 1998 ABI JNL. LEXIS 157, *2-*5, May 1998 (describing Asian insolvency and restructuring cultures); Wisit Wisitsora-At, New Thai Statute Blends Chapter 11 with Singapore Practices, 1999 Am. Bankr. Inst. J. LEXIS 17, (March 1999) (describing genesis of new Thai business reorganization law. See Bankruptcy Act B.E. 2483 (1940) as amended by Bankruptcy Act (no. 6) B.E. 2543 (2000) [hereinafter Thai Bankruptcy Act]). [Back To Text](#)

¹⁰ See Marcus W. Brauchli, Homecoming: In Many Ways, Return Of Hong Kong to China Has Already Happened, Wall St. J., June 9, 1997, at A1 (transforming Hong Kong from British colony to special administrative region (SAR) of China after signing Sino-British Joint Declaration). [Back To Text](#)

¹¹ See Makato Sato, Banks Throw DIP Lifeline To Sick Firms, The Nikkei Weekly, Jan. 4, 2002 (explaining debtor-in-possession financing (DIP), which permits loans for insolvent companies, is uncommon in Japan vis-à-vis

US). [Back To Text](#)

¹² See Guaranteeing Deposits, Mainichi Daily News, Mar. 29, 2001, (Opinion/Analysis) at 2 (noting "blanket" guarantee available to depositors at financial institutions set to expire in April 2002 for certain deposits in excess of 10 million yen). [Back To Text](#)

¹³ See *id.* (noting, in response to removal of guarantees "banks are currently rushing to write off bad debts...and to create conditions that will eliminate the need for [the guarantees]," and opining "efforts to write down bad loans will inflict pain on the economy and society as a whole, triggering a temporary surge in corporate bankruptcies and a rise in the unemployment rate."). [Back To Text](#)

¹⁴ See generally Minji saisei ho [Civil Rehabilitation Law], Law No. 225 of 1999 (passed by Diet (Japanese Parliament) on Dec. 14, 1999 and in effect on Apr. 1, 2000); Collier International Business Insolvency Guide, Ch. 28 (MB) (setting forth insolvency law in Japan). [Back To Text](#)

¹⁵ See Resort Looks for Revival Under New Law, The Nikkei Weekly, July 24, 2000, (indicating Japan's prior corporate rehabilitation law would take up to two years in some instances). [Back To Text](#)

¹⁶ See Bankruptcies Trigger Legal Rethink, The Nikkei Weekly, Feb. 12, 2002 (stating approximately 950 companies filed in 2001 under Civil Rehabilitation Law); Bankruptcy Process Overdue For Update, The Nikkei Weekly, Mar. 4, 2002 (noting in two years since Civil Rehabilitation Law was enacted approximately 2,000 filings have occurred). [Back To Text](#)

¹⁷ See Bankruptcies Trigger Legal Rethink, The Nikkei Weekly, Feb. 12, 2002, (noting Mycal Corp. switched to Corporate Rehabilitation Law from Civil Rehabilitation Law in Sept. 2001). [Back To Text](#)

¹⁸ See Arthur J. Alexander, Business Failures Rising In Japan As New Bankruptcy Law Takes Effect, 22 Japan Econ. Inst. Rep., (June 9, 2000) (noting bankruptcy experts believe successful rehabilitation is likely achieved when financial problems are addressed quickly. To facilitate this end law should provide "a predictable, transparent and fair way to restructure the balance sheet of a failing business so that both the debtor and its creditors see advantages in going that route rather than dissolving the company," characteristics absent in old Japanese bankruptcy laws). [Back To Text](#)

¹⁹ See Terry Bond, Global Development: A Global Approach for Multi-Creditor Out-of-Court Restructurings – A New Initiative and the Wider Issues, 17 Conn. J. Int'l L. 41, 41 (2001) (describing start of INSOL's involvement in developing "Global Principles"). [Back To Text](#)

²⁰ See Asahi Shimbun, Rules for Waiving Loans Tightened, Sept. 2, 2001 (stating purpose of guidelines: "Companies should basically be rebuilt through legal liquidation. . . [d]ebt forgiveness should be limited to cases that are economically viable."), available at <http://www.asahi.com>. [Back To Text](#)

²¹ See generally Six Firms, Gov't Lender to Set Up Y100bn Corporate Rehab Fund, The Nikkei Weekly (Tokyo), Feb. 3, 2002. [Back To Text](#)

²² See Japan's Premier Doesn't Grasp the Banking Crisis: Koizumi's Blind Spot, The Oriental Economist, Mar. 2002, at 1, 4. [Back To Text](#)

²³ See Courtney C. Carter, Note, Saving Face in Southeast Asia: The Implementation of Prepackaged Plans of Reorganization in Thailand, Malaysia, and Indonesia, 17 Bankr. Dev. J. 295, 313 (discussing London Approach). [Back To Text](#)

²⁴ See *id.* (stating effective application is critical to success of informal procedures since it provides necessary incentives for meaningful negotiations). [Back To Text](#)

- ²⁵ See generally Satoshi Koreeda & Yomiuri Shimbun, Bad-loan study panel needs focus, *The Daily Yomiuri* (Tokyo), May 11, 2001, at 16 (discussing guidelines concerning corporate rebuilding and debt relief of banks that are incorporated in emergency economic package). [Back To Text](#)
- ²⁶ See Japan Supermarket Chain Kotobukiya in Crisis, 12/19/01 Jiji Press Eng. News Serv., available at [2001 WL 29489823](#) (summarizing Kotobukiya's troubles with bankruptcy and reorganization). [Back To Text](#)
- ²⁷ Hugh Patrick, How the Japanese Financial System and its Main Bank System Have Dealt with Generic Issues of Financial Development 10 (Sept. 1997) (noting that banks act as management consultants since they have access to very detailed information about plans, prospects and monitor performance), available at <http://www.gsb.columbia.edu/japan/pdf/op33.pdf>. [Back To Text](#)
- ²⁸ Mark M. Spiegel & Nobuyushi Yamoori, Financial Turbulence and the Japanese Main Bank 4 (Jan. 11, 2001) (stating main bank bears more than a proportional share of losses when there are financial difficulties) available at <http://www.frbsf.org/econsrch/workingp/pbc/2000/wppb00-04.pdf>. [Back To Text](#)
- ²⁹ See generally One-Room Condo Developers Face Crisis After Tax Change; Filling of Loophole Has Livex Near Collapse, *The Nikkei Weekly*, May 23, 1992, at 18 (commenting on Maruko Inc.'s folding, leaving behind Y285.8 billion). [Back To Text](#)
- ³⁰ See Banks Should Not Let Down Their Guard, *The Daily Yomiuri*, (Tokyo) Apr. 19, 2000, at 6 (stating "[t]he Sogo department store chain asked banks to waive 630 billion yen worth of credit claims..."). [Back To Text](#)
- ³¹ See Japan-Business Stockholders Sue Former Chairman and Auditors of Japan's Sogo, *Financial Times Information*, Apr. 20, 2001 (discussing shareholder suit filed against Sogo department store). [Back To Text](#)
- ³² EIE Guam Corp. v. The Long Term Credit Bank of Japan, Ltd., No. 99-849, 120 S. Ct. 980 (Guam Terr. 2000). [Back To Text](#)
- ³³ *Id.* at 4 (citing 11 GCA § 106730 (1994)) (stating foreign banking corporations are not prohibited from making loans in this Territory secured by mortgages). [Back To Text](#)
- ³⁴ For instance, while the Thai law provides for the appointment of a creditors' committee in a business reorganization case, the committee is only appointed towards the end of the case after creditors have voted on a plan of reorganization. See Thai Bankruptcy Act § 90/50, supra note 8. [Back To Text](#)
- ³⁵ Shozo Ota & Kahei Rokumoto, Issues of the Lawyer Population: Japan, 25 Case W. Res. J. Int'l L. 315, 320-21 (stating Japan has been able to function with so few lawyers, while it maintains highly industrialized market economy). [Back To Text](#)
- ³⁶ 4 Doing Business in Japan: Changeover and Bankruptcy of Small and Medium-Sized Businesses § 9.06 (MB 2001) (4-XI-9 DBJAPN § 9.06). [Back To Text](#)
- ³⁷ The Ministry of Finance. [Back To Text](#)
- ³⁸ See Sarah McBride & Phillip Day, Asia Looks Immune to "Enronitis" – Region's Investors Long Ago Learned Not to Expect Transparency, *Asian Wall St. J.*, Feb. 8, 2002. [Back To Text](#)
- ³⁹ People's Republic of China. [Back To Text](#)
- ⁴⁰ See Charles D. Booth, The Transnational Aspects of Hong Kong Insolvency Law, 2 Sw. J.L. & Trade Am. 1, 13-14 (1995); see also James V. Feinerman, Internationalizing U.S. capital markets in global context: problems and prospects; Symposium: Capital Markets and Financial Services in the Pacific Rim: Prospects for Harmonization, 28

Law and Policy In International Business 605, 649, Mar. 22, 1997 (stating basic policies of People's Republic of China regarding Hong Kong sets forth Basic Law but common law shall be maintained). [Back To Text](#)

⁴¹ See [Booth, supra note 39, at 14](#); see also David Evans, Honest Bankrupts Get Reprieve, Hong Kong Standard, Mar. 25, 1998 (stating most Hong Kong company ordinances are modeled on 1948 UK Act); Masuda & Ejiri, A Lawyer's Guide To Japan, Ch. 2(B) (1995), available at <http://www.hg.org/huide-japan.html#invest>. [Back To Text](#)

⁴² See National Trade Data Bank Market Reports (Sept. 1, 1999) (stating Asian financial crisis has had negative effect on Hong Kong's economy), available at http://govpubs.lib.umn.edu/stat/tool_ntdb.phtml. [Back To Text](#)

⁴³ HKMA, Quarterly Bulletin, Nov. 1999, available at

<http://www.info.gov.hkma/eng/public/qb9911/toc.htm>. [Back To Text](#)

⁴⁴ See Charles D. Booth, Hong Kong Corporate Rescue Proposals: Making Secured Creditors More Secure, 28 Hong Kong L.J. 44 (1998) (emphasizing glaring weakness in Hong Kong insolvency law has been lack of acceptable corporate rescue procedure). [Back To Text](#)

⁴⁵ See [id. at 45](#). [Back To Text](#)

⁴⁶ See [id. at 47](#) (pointing out veto power secured creditors have due to lack of stay to bind creditors, allowing them to withdraw capital, even if it prevents restructuring scheme). [Back To Text](#)

⁴⁷ See generally [Fang Liufang, China's Corporatization Experiment, 5 Duke J. Comp. & Int'l L. 149, 264–65 \(1995\)](#) (discussing abundance of family controlled businesses in Taiwan and Hong Kong). [Back To Text](#)

⁴⁸ The recent White Paper, Insolvency: A Second Chance, (Cm. 5234, July 2001) proposed to abolish administrative receivership, subject to certain limited exceptions. These recommendations have now been incorporated into the Enterprise Bill, introduced to the House of Commons on Mar. 26, 2002. [Back To Text](#)

⁴⁹ See Ronald W. Harmer, Insolvency Law Reforms in the Asian and Pacific Region: Report of the Office of the General Counsel on TA 5795–Reg: Insolvency Law Reforms, Law & Policy at the Asian Development Bank 10, 71–73 (2000). [Back To Text](#)

⁵⁰ See generally [Steven L. Schwarcz, Sovereign Debt Restructuring: A Bankruptcy Reorganization Approach, 85 Cornell L. Rev. 956 \(2000\)](#) (noting fundamental problems concerning holdout creditors). [Back To Text](#)

⁵¹ Cf. [Booth, supra note 39, at 48](#) (noting previous power of secured creditors to effectively veto restructuring process due to lack of mechanism to compel negotiations). [Back To Text](#)

⁵² Under Thai law, the entry of a business reorganization order is predicated on a finding of insolvency by the Central Bankruptcy Court. See the [Thai Bankruptcy Act § 90/3, supra note 8](#). As the test for insolvency in Thailand bankruptcy cases has traditionally been limited to a "balance sheet" test, petitioning creditors in business reorganization cases face an uphill battle in proving insolvency at the outset of a business reorganization case. [Back To Text](#)

⁵³ Referring to the Thai Petrochemical Indus. PCL case. See 35 BCD, May 9, 2000, at A3. [Back To Text](#)

⁵⁴ See Workouts in Thailand: Beyond the TPI Ruling, Asian Lawyer, Apr. 2000. [Back To Text](#)

⁵⁵ Gren Manuel, Story Behind the Story: Why Hong Kong Firms are Late Filing Results, Asian Wall St.J. Aug. 3–5, 2001, at 1. [Back To Text](#)

⁵⁶ See Courtney C. Carter, Notes & Comment: Saving Face in Southeast Asia: The Implementation of Prepackaged Plans of Reorganization in Thailand, Malaysia, and Indonesia, 17 Bankr. Dev. J. 295, 313 (2000). [Back To Text](#)

⁵⁷ See generally Charles D. Booth, Asian Development Bank Regional Technical Assistance Project No. 5795-REG, Insolvency Law Reforms Report on Hong Kong, China, Section R, Inter-Relationship Between Lenders and Borrowers in Context of Financial Difficulty/Insolvency of the Borrower (last visited Mar. 13, 2002) (discussing Hong Kong Guidelines on Corporate Difficulties), available at

http://www.insolvencyasia.com/insolvency_law_regimes/hongkong/pdf/section_r.pdf. [Back To Text](#)

⁵⁸ See generally A need to do the neighborly thing in Asia, The Daily Yomiuri (Tokyo), Feb. 18, 1998, at 7 (noting Japan's reputation as world's top creditor nation and its genuinely useful contributions to other Asian economies). [Back To Text](#)

⁵⁹ See Beijing Pins Hopes on Guandong, Financial Times (London), Dec. 29, 2000, at 13 (calling Guandong restructuring "the largest deal in China's corporate history."). [Back To Text](#)

⁶⁰ See The Death of Gradualism, The Economist, Mar. 8, 1997, at S16 (stating by any conventional calculation the Chinese banking system is insolvent). [Back To Text](#)

⁶¹ See Hong Cong Companies (Amendment) Bill 2000 and Hong Kong Companies (Corporate Rescue) Bill 2001. Information is on the web at <http://www.legco.gov.hk/english/index.htm>; see also Philip Smart & Charles D. Booth, Corporate Rescue: Hong Kong Developments, 10 Am. Bankr. Inst. L. Rev. 41 (2002) (setting forth discussion of the Hong Kong government's proposed corporate rescue procedure); Philip Smart & Charles D. Booth, Provisional Supervision and Workers' Wages: An Alternative Proposal, 31 Hong Kong L.J. 188 (2001) (for further discussion of the treatment of workers). [Back To Text](#)

⁶² See Law of the People's Republic of China on Enterprise Bankruptcy (Trial Implementation), Standing Committee of the National People's Congress, Dec. 2, 1986, available at http://www.novexc.cn/banruptcy_law_html; see also Roman Tomasic, Insolvency Law Principles and the Draft Bankruptcy Law of the People's Republic of China, 9 Austl. J. Corp. L. 211 (1998) (noting China's first insolvency law, Bankruptcy Act of 1935, was repealed in 1948, and China did not enact further insolvency law until the PRC Enterprise Bankruptcy Law (Trial Implementation), which was enacted in 1986, and came into effect in 1988). [Back To Text](#)

⁶³ See Law of People's Republic of China on Enterprise Bankruptcy (Trial Implementation), art. 2 (1986) (stating that it "applies to enterprises owned by the whole people."). [Back To Text](#)

⁶⁴ See Tomasic, supra note 61 (noting China is currently broadening its insolvency law). [Back To Text](#)

⁶⁵ See, e.g., Draft Law, ch. 5, art. 97, (stating secured creditors "shall not exercise the right of disposal of the security collateral" unless it is in danger of being damaged or devalued). [Back To Text](#)

⁶⁶ See State Economic and Trade Commission at http://www.setc.gov.cn/english/index_e.htm (describing SETC and its main responsibilities and functions). [Back To Text](#)

⁶⁷ See China's Baoshan Iron and Steel Co seeks public listing, BBC WORLDWIDE MONITORING, Nov. 10, 2000 (noting SETC's plans to guide restructuring of state owned enterprises). [Back To Text](#)

⁶⁸ See Law of the People's Republic of China on Enterprise Bankruptcy (Trial Implementation), art. 8. [Back To Text](#)

⁶⁹ See Xianchu Zhang & Charles D. Booth, Chinese Bankruptcy Law in an Emerging Market Economy:

The Shenzhen Experience, 15 Columbia J. Asian L. 1, 3 (2001). [Back To Text](#)

⁷⁰ See State Economic and Trade Commission at http://www.setc.gov.cn/english/index_e.htm (describing SETC and its main responsibilities and functions). [Back To Text](#)

⁷¹ See The State Economic and Trade Commission, China, available at http://www.chinacp.com/eng/cporg/cporg_setc.html (last visited March 14, 2002) (outlining functions of SETC). [Back To Text](#)

⁷² See Wang Weiguo & Charles D. Booth, Study on Alternative Approaches for Debt Restructuring of Enterprises in China (2002); see also Mark E. Monfort, Reform of the State-Owned enterprise and the [Bankruptcy Law in the People's Republic of China](#), 22 Okla. City U.L. Rev. 1067 (1997) (explaining special problems regarding State-Owned Enterprises and need for reorganization system). [Back To Text](#)

⁷³ See Leslie Burton, An Overview of Insolvency Proceedings in Asia, 6 Ann. Surv. Int'l & Comp. L. 113, 119 (2000) (stating, "[I]t is far more common for the state-owned enterprises to be acquired by another entity than to be liquidated."). [Back To Text](#)

⁷⁴ See Law of the People's Republic of China on Enterprise Bankruptcy (1986), available at http://www.novexc.cn/bankruptcy_law.html. [Back To Text](#)

⁷⁵ See Burton, *supra* note 72 at 119 (stating "[b]etween 1986 and 1996, over 2,000 bankruptcies were reported, a figure which is probably low, but only 20 of them were for state-owned businesses."). [Back To Text](#)

⁷⁶ See *id.* at 120 (discussing how, despite past refusal to provide assistance to foreign bankruptcy representatives, both the Chinese and Taiwanese governments are studying cross-border insolvency issues). [Back To Text](#)

⁷⁷ See Aspiring to Fresh Heights, South China Morning Post, Oct. 1, 2001, at supp. 6 (describing how China set up asset management companies to take over non-performing loans). [Back To Text](#)

⁷⁸ The Thai Asset Management Corporation (TAMC), which was established by emergency decree [Emergency Decree on the Thai Asset Management Corporation B.E. 2544 (2001)], came into force on June 9, 2001. [Back To Text](#)