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Discussion Paper No. 99-E-26
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International Dimensions of Japanese Insolvency Law:  
A Contextual Approach

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Abstract

This paper offers an introduction and overview of the international aspects of Japanese insolvency law. The paper is designed for non-specialists, and for those specialists seeking a review of the subject. Thus, the paper takes a contextual approach. Rather than delving into those aspects immediately, the paper identifies two contexts in which that law should be analyzed: the Japanese economic crisis, and comparative and international law on insolvency. The Japanese economic crisis, the most severe in the country’s extraordinary post-Second World War history, underscores the importance of insolvency law. Of late, there have been a number of developments in the insolvency regimes of other countries, and in international law, and these provide a point of reference for understanding Japan’s regime.

There are three international dimensions to Japan’s insolvency law: jurisdiction of Japanese courts; the status of foreign claimants; and recognition and enforcement of foreign proceedings. Animating in these dimensions is a distinctly territorial approach. This inward-looking way of handling insolvency cases is incongruous with developments in the comparative and international law context. It also is at odds with broader globalization trends, some of which are evident in Japan’s economic crisis. Analogies to international trade law are useful: the post-

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The author would like to express his appreciation to Dr. Kunio Okina, Director, Institute for Monetary and Economic Studies, The Bank of Japan for the opportunity to serve as a Visiting Scholar. It is hard to imagine a more friendly, hospitable environment in which an overseas guest can work. Special thanks are owed to Mr. Michio Ayuse, Chief Manager, and Mr. Wataru Takahashi, Chief Manager, Research Division II, for their help in designing this project and providing invaluable information and contacts. Special thanks also are due to Mr. Masao Okawa and Ms. Keiko Harimoto for the many courtesies they extended to the author, which the author sincerely hopes to repay whenever they find themselves in Washington, D.C. The author benefitted from comments and suggestions made by the Institute Staff through discussions and a seminar at the Bank of Japan on 26 July 1999 at which this paper was presented.

The author is blessed by the extraordinary research assistance provided by Ms. Kris Hansen and Ms. Preeti Kapoor, The George Washington University Law School Class of 2000, without which this project could not have been completed. The specifics of their excellent work are cited below.

Finally, the author would like to thank Dean Michael Young of The George Washington University Law School. His friendly guidance in navigating the ways of Tokyo smoothed the transition and enriched the experience.

The views expressed in this paper are solely those of the author and should not be attributed to The Bank of Japan or its staff. The author is responsible for all errors.
Uruguay Round dispute resolution mechanism has insights for the problem of jurisdiction; the famous national treatment principle is a basis for critiquing the status foreign claimants have in Japanese insolvency proceedings; and trade negotiations might be a model for expanding recognition and enforcement of foreign proceedings.

As a corollary, the relationship between the extant insolvency regime and Japanese banks – many of which are internationally active – is explored. Problem banks are at the heart of the economic crisis. Yet, the insolvency law regime has not been applied to failed or failing banks, partly on grounds of the systemic risk that would be triggered by a stay of creditor proceedings. Whether the reluctance to use the regime in bank cases is open to question on a number of grounds. Similarly, the failure to develop a harmonized set of international bank bankruptcy rules to avoid BCCI-type liquidation problems is addressed, and a proposal for proceeding in this direction is offered.

For the convenience of readers unfamiliar with the Japanese legal system, an Appendix is provided. This system, a civil one with limited judicial discretion, is the setting in which the insolvency framework necessarily sits. The Appendix provides basic background information about what could fairly be considered a third context for the international dimensions of insolvency law, Japan’s legal system.

Key words: Japanese insolvency law, international insolvency law, bank insolvencies

JEL classification: K33
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It is universally accepted that well-functioning economies need well-designed bankruptcy procedures.


**INTRODUCTION: TWO KEY CONTEXTS**

Insolvency is a sober affair. Creditors are unhappy because they know they are unlikely to recover what they lent to the debtor – the proverbial “ten cents on the dollar,” if they are lucky. The debtor is miserable, not simply because of its adverse legal position, but also because of the death of its dreams. Shareholders are in almost all events wiped out financially. The affair is all the more sober in Japan nowadays. Corporate bankruptcies are at record levels, and these failures – because they translate into ever-greater numbers of unemployed workers – are causing record numbers of personal bankruptcies.\(^1\)

But, bankruptcy is also a fascinating affair – at least intellectually for those not immediately involved in it. And, it is an increasingly international one. Country after country seems to be revising (or, in some cases, starting anew) its legal regime for handling the financial affairs of its debtors. And for good reason. Globalization means, in part, that companies know no boundaries. Their assets and liabilities are spread across geo-political borders that, for conventional bankruptcy proceedings, matter. The obvious concern that arises amidst all of the legal revision in which countries are engaged is how the many bankruptcy regimes, shifting as they may be, relate to one another, or, indeed, whether they relate to one another at all. Was this not the very problem over which central banks fretted when the Bank of Credit and Commerce International (BCCI) collapsed on 5 July 1991? How could the trustee responsible for marshaling BCCI’s assets possibly make good on the $10 billion owed creditors when those assets were located in 72 countries? After all, officials in at least some of those countries might – and did – refuse to transfer control over BCCI’s local assets, preferring domestic creditors first.

To be sure, when BCCI’s Tokyo branch suspended operations on 5 July 1991, a special liquidation proceeding was commenced in Tokyo District Court.\(^2\) The Court appointed a liquidator, who decided to participate in the world-wide pooling arrangements, based in Luxembourg, with the approval of BCCI’s creditors. As of July 1998, in accordance with the pooling arrangement, a second dividend payment was made to the creditors. The point is that not every liquidator in every country will behave in as globally-minded a way as the liquidator for BCCI-Tokyo. Even in Japan, the decision was easy given the peculiar circumstances. Creditor claims against BCCI-Tokyo far-exceeded the branch’s assets (if it is proper to speak of a branch having assets and liabilities separate from those of the parent). Japanese authorities realized creditors would fare better in the global liquidation proceeding than in a “ring-fenced” Japanese one. Thus, Japan’s traditional territoriality approach to insolvency issues (discussed in Parts Two and Three below) never was severely tested by the BCCI scandal. That test would have come if BCCI-Tokyo had assets far in excess of creditor claims.

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\(^2\) Liquidation, along with the other types of Japanese insolvency procedures, is discussed in Part Three below.
(as was the case with BCCI’s New York and California operations, which were ring-fenced by state regulatory authorities).

There is, then, a context to consider – in fact, there are two contexts to consider: the economic context, and the comparative and international legal context. The need to appreciate insolvency law and its reform in these contexts is the central thesis of this paper. Any discussion of a country’s insolvency law, including Japan’s, could launch into the details. But, lacking the context, seeing how and why those details matter is difficult. Context shapes our understanding of law, and this is no less true with respect to insolvency law than any other specialty. To rush into the inner workings of Japan’s insolvency law regime would be to neglect consideration of why that regime is important and forego consideration of possible analytical tools for assessing that regime.

What is the economic context in which Japanese insolvency law – as presently constituted, and as proposed – is set? That is the question addressed by Part One, below. In brief, the economic context is rather desperate. There is not much risk of an overstatement: insolvency law is more important to Japan than at any time in the last half-century. Its importance is not confined to the Japanese. An economically sick Japan is not in America’s long run, broader national economic (or, for that matter, security) interests. Whether or not the two nations are the partners in the most important bilateral relationship in the world, they are the two largest economies and two of the hegemonic trading powers. Japanese businesses are a source of supply for American consumers; Japanese consumers are a source of demand for American businesses. It is hardly a pretty sight to watch one’s clients and customers deteriorate, particularly where the rules designed to address deterioration – insolvency law – are problematic, if not antiquated.

Appreciating Japan’s present economic predicament is not the only challenge. How Japanese insolvency law relates to regimes in other countries, and to emerging principles in international insolvency law, cannot be ignored. This comparative and international legal context is the subject of Part Two. This perspective is especially timely. Presently, two major study groups are considering the revision of Japan’s insolvency regime. Each group is approaching the problem from a different angle. One group, sponsored by the Ministry of Finance, is considering what the optimal bank deposit insurance scheme for Japan would be. It is attempting to design a new safety net for financial institutions to replace the present comprehensive safety net (discussed in Part Four below) that is set to expire in March 2001. A second study group, sponsored by the Ministry of Justice, is examining what the optimal insolvency regime for Japan would be, i.e., it is engaged in a comprehensive reform project on insolvency laws. A new scheme for handling cross-border assets is possible, but no special consideration has been given to bank failures. Thus, in Japan an intense discussion of the insolvency regime, including the insolvency of banks, has yet to emerge. Part Two is designed with this discussion in mind.

In Part Three, Japanese insolvency law itself, and its international dimensions, are assessed. The focus is not limited just to understanding the conventional types of insolvency proceedings, nor should it be. Inevitably, there are creditors located overseas of Japanese companies. Inevitably, there are Japanese debtors with assets and liabilities located overseas. What does Japanese insolvency law say – or not say – about these situations? How does the Japanese regime contrast with the American one? What insights might be provided by other international law fields – most notably, international trade law – to improve the
Japanese regime? These points are considered in Part Three.

In Part Four, the special – or ostensibly special – case of banks is considered. How have Japanese bank collapses been handled? What role, if any, has Japanese insolvency law played in resolving these cases? What role ought it to play? What about the international dimensions of Japanese bank operations? How might a harmonized set of rules for international bank bankruptcies emerge? These matters are discussed in the last Part.

Finally, for the convenience of readers unfamiliar with the Japanese legal system, an Appendix is provided. The material in the Appendix could well be considered a whole context for insolvency law: what is the legal structure of Japan into which its insolvency law is supposed to fit? That is the question addressed in the Appendix. Any country’s insolvency law must fit well within that country’s overall legal system, because insolvency law is so closely related to (indeed, made up of) so many other areas of law. To be sure, the outlines of the Japanese legal system are easy to trace. However (as discussed in Part Three), there are five different insolvency laws – a monstrously complicated scheme whose evolution began in 1911. Strangely, the exact fit of banks within this scheme is not altogether clear. While in theory they are subject to all five of the laws, Japan has had no practical experience in applying these laws to banks after the Second World War. In the present economic context, one question (addressed in Part Four) is whether banks ought to remain subject to the extant regime, or whether a new insolvency architecture should be drawn for them.

A word of caution is in order. Bankruptcy law is not only sobering and fascinating, it is difficult even when the contexts in which it is set are understood. This paper is not an advanced discussion of all of the particularities of international aspects of Japanese insolvency law. Nor can it be, for the author is himself a beginning student of the specialty. It is very much an introduction and overview. No previous knowledge of the Japanese economic crisis or legal system is assumed – hence the need for Part One and the Appendix, respectively. No training or experience in comparative or international insolvency law is expected – hence the importance of Part Two. No familiarity with Japanese insolvency law or the arguably special positions of banks is required – hence the relevance of Parts Three and Four, respectively. Readers who are already familiar with subjects discussed in some of these parts, particularly Part One, should proceed to other parts. The aims of the paper are modest: to provide the key contexts for discussion, and highlight the principal points of debate. At the same time, the intended audience is ambitious: non-specialists, who need an accessible introduction to the topic, and specialists, who need a rigorous review.
PART ONE: THE ECONOMIC CONTEXT

Japan has grown itself in the world’s second largest economy in the world. It is the world’s largest creditor nation, and maintains a persistent current account surplus. It is politically stable, and is blessedly free from foreign debt. As is well chronicled in many histories, including Walter LaFeber’s 1998 work, The Clash, Japan’s post-war rebuilding, following a dirigiste model of government-regulated, or non-market, capitalism, was breathtaking in speed and result. It was just a decade ago that Japan basked in the glory of “bubble” years. Its economic prowess, indeed superiority, was the model for the rest of the world. But, as economists predict and bankruptcy lawyers experience, the good times do not last forever.

To be sure, the annals of bankruptcy law – in Japan and around the world – are replete with stories of debtors that failed in good times because of incompetent or evil management. The annals are also full – perhaps more so – of cases in which well-run debtors simply could not cope with bad economic times. Japan now struggles with its biggest economic crisis since 1945. Those in Japan struggling include Japanese debtors – both financial and non-financial corporations – and their creditors along with them.

It is now the conventional wisdom that Japan’s economic problems are structural, not merely cyclical. The specific diagnoses are many, too numerous for this paper, but the gist of most of them is that there are too many large, inefficient companies in virtually every sector of the economy. To recover, the fresh winds of a supple, market-driven system must blow. But, these winds will blow over weaker companies, exacerbating an
unemployment rate that already has reached an all time high of 4.8 percent. Firms plagued by high debt and high excess capacity are slashing investments and reducing exports to the rest of Asia. For some firms, even drastic moves along these lines will not work. They will go bankrupt.

Japan’s insolvency law regime thus takes on added – indeed, critical – importance. It must, on the one hand, safeguard the interests of creditors. If it does not, then they will not lend. On the other hand, it must not be so onerous in its treatment of debtors that it discourages risk-taking. After all, Schumpeter-style entrepreneurial capitalism can be a cornerstone of a new Japanese economic miracle, and an insolvency regime can facilitate the development of this brand of capitalism. Most importantly for the purposes of this paper, and as stressed in Part Three, Japan’s insolvency regime needs to meet these twin challenges in a global economy in which debtors are sure to have assets and liabilities spread across the globe. Thus, it needs to “fit” in a changing international legal environment, and maybe even encourage some of that change.

The above points should not, of course, be overstated. Even in the most robust of macroeconomic scenarios, insolvency law remains important, and its reform should go forward. Conversely, whether the Japanese economy remains sluggish is not dependent solely, or even largely, on the speed and nature of the insolvency law reform project. The point, then, is simply that the present difficulties are part of the context to understand the heightened importance of insolvency law, and lawyers and economists need to appreciate each other’s language in this respect.

I. WHENCE THE JAPANESE ECONOMIC CRISIS?

The famous model of “Japan, Inc.” is based on close links among firms, banks, and government officials. After the Second World War, an important economic policy goal was the availability of cheap financing for industrial reconstruction. Regulations that in retrospect seem anti-competitive were implemented to support this goal. Banks were tied to their corporate clients through cross shareholdings and corporate “families,” the keiretsu system. There was little in the way of American-style shareholder activism. In particular, shareholders of Japanese banks never made demands for disclosures about business performance. If only they had, because banks did little in the way of applying prudent credit controls, Managers were sheltered not only from shareholders, but also foreign competition. To be sure, they were able to focus on long-term investments, rather than short-term profits.

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9 See Tett, Japan’s Bombshell Explodes, supra note 6.
10 See id.
11 See id.
12 See id.
13 See Japan’s Economic Plight, supra note 8.
But, mollycoddling government officials encouraged banks to keep weak firms in business. The system was one of non-market, rather than market, capitalism.

The American Treasury Secretary, Lawrence Summers, ascribed the origins of Japan’s economic crisis to (1) a weak domestic financial system, (2) an unsustainable mix of monetary and exchange rate policies, and (3) the absence of strong and credible domestic institutions coupled with large volumes of mismatched borrowing. Summers is on the mark (though he politely left out corruption). Japanese banks loaned extraordinary sums in South East Asia to help finance current account deficits in the region. The loans were made at low interest rates after applying lax credit standards. The fact that Asian borrowers were acquiring huge debts denominated in hard currencies, particularly the United States dollar seemed not to matter. After all, were not the local currencies of the borrowers – the Thai baht, the Malaysian ringgit, the Indonesian rupiah, the Singapore dollar, and the Hong Kong dollar – all pegged to the United States dollar directly or through a basket? Currency mismatches on the balance sheets of the borrowers (i.e., their notes payable were in hard currencies, while their accounts receivable were in softer local currencies) were coupled with mismatches on the balance sheets of Japanese banks. They built up incongruities between foreign liabilities and domestic assets, and between liquid liabilities and illiquid assets.

When the yen tumbled in value relative to the dollar, Asian borrowers could no longer pay back their debts. Yen depreciation, coupled with speculative attacks from overseas portfolio investors (most infamously, George Soros) led to pressure on Asian currencies that was too much to bear. Pegs in country after country fell off, and currencies tumbled. Customers of Japanese banks throughout Asia now held staggering dollar-denominated debt, but earned meager revenues in local currencies. They could no longer afford Japanese exports. Indeed, the collapsed Asian market robbed Japan of nearly 45 percent of its exports. Japanese banks were left holding the proverbial banks. They did not want to, or could not, lend new money until they were repaid, a dim prospect without fresh funds or an economic turn-about. To make matters worse, in 1997, Japan’s value-added tax increased from 3 to 5 percent. The resulting decline in consumer spending was entirely foreseeable. So was the decline in gross domestic product (GDP). It fell at an 11 percent rate in the second quarter of 1998, and Japan’s economic growth has averaged less than 1 percent a year since 1992.

To view Japan’s woes as cyclical or temporary is naive. They are structural, deeply embedded in a system that includes its legal regime for insolvency, but much more as

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14 See Martin Wolf, Before They All Fall Down, FIN. TIMES, Nov. 25, 1997, at 17.
15 See Martin Feldstein, Japan’s Folly Drags Asia Down, WALL ST. J., Nov. 25, 1997, at A22.
16 See Wolf, supra note 14.
17 See Feldstein, supra note 15.
19 See Reviving Japan, supra note 7.
20 See Editorial, WALL ST. J., supra note 18.
21 See id.
well. One example of a structural defect is excessive borrowing by firms to over-invest in projects with low returns.\textsuperscript{22} Japanese firms flock to any promising new market. Once in that market, they tend to stay put whatever the fortunes. During the 1980’s and early 1990s, Japanese companies took advantage of the cheap and easy financing from their banks to splurge on new factories and tools.\textsuperscript{23} Industrial capacity increased, and exports soared.\textsuperscript{24} Given the excessive borrowing to pay for these unwise investments, it should be no surprise that the average debt-equity ratio of Japanese firms is 4:1 – very high by international standards.\textsuperscript{25} Another example of a structural problem is its high savings ratio that exceeds its investment needs.\textsuperscript{26} Nor should the large deflationary influence of these debts on Japan’s economy raise eyebrows.\textsuperscript{27}

Crises evoke response, or at least they are supposed to. Paralysis seems to be a better description of the present atmosphere. Why? Kathy Matsui of Goldman Sachs argues that the single biggest reason for Japan’s lack of change is that neither its financial and tax system nor its social environment create any incentive for Japanese managers to maximize profits.\textsuperscript{28} There is much talk about the end of life-time employment for the “salary man.” For most managers, however, the reality still is that even if their firms fail to produce decent profits, they risk neither job loss nor corporate takeover, at least as long as their companies are not going bankrupt. (To be sure, unemployment has risen due to the bankruptcies of smaller firms. Culturally, however, firing is still not a common option. The culture is reinforced by labor laws, which make firing difficult unless bankruptcy is imminent.\textsuperscript{29}) Only when managers are rewarded for taking difficult decisions and risks will Japanese companies

\textsuperscript{22} See Japan’s Economic Plight, supra note 8.

\textsuperscript{23} To be sure, commercial banks were (and are) not the only source of funding. Japanese firms increasingly have tried accessing capital markets directly – in part because of changes by commercial banks. As a result of bank failures, some of the remaining solvent banks are becoming more discriminating about how they price capital. See Philip Gawith, Landmark Deals Indicate the Scale of Change, FIN. TIMES, July, 14, 1998, at 3. This move suggests a more efficient allocation of resources, and is forcing a growing number of companies to tap the capital markets for funds. See id. Nevertheless, about 60 percent of Japanese corporate funding takes the form of bank loans, compared to less than 10 percent in the United States. See id.

\textsuperscript{24} See Reviving Japan, supra note 7, at 21.

\textsuperscript{25} See Japan’s Economic Plight, supra note 8, at 21.

\textsuperscript{26} See WALL ST. J., April 10, 1998

\textsuperscript{27} See id.

\textsuperscript{28} See Corporate Japan Goes to Waste, THE ECONOMIST, Aug. 29, 1998, at 55, 56. To be fair, some companies are moving away from their traditional preoccupation with sales growth and market share, and beginning to place a greater emphasis on shareholder value and the return on capital. See Gawith, supra note 23. Kao, the cosmetics and household products group, is one example. See id. The drive for greater efficiency is beginning to break the social contract between labor and the corporate sector. Barriers between banks, insurers, and securities companies are being broken down. In the process, foreign access to Japanese markets has improved, as deregulation efforts are beginning in various sectors. As Masashi Kaneko, Nikko’s president, said at the time of the Citicorp – Travelers merger: “[t]he problem we face is globalization. Companies can no longer satisfy customers by themselves, without a global partnership.” See id.

\textsuperscript{29} See Corporate Japan Goes to Waste, supra note 28, at 55.
become competitive and seek to maximize profits, receiving high returns for their investors. That reward structure is the hallmark of entrepreneurial capitalism.

Some scholars believe that the biggest supply-side obstacle to future growth will not be excessive regulation or inflexible labor markets, but a corporate culture that finds it easy to tolerate low returns and difficult to stomach outright failure. To be sure, there is now an increasing emphasis on return on equity and on assets (ROE and ROA, respectively). However, traditionally managers have faced little pressure to improve ROE and ROA, given that most of their capital came from banks and other financial institutions that also held equity in the firm. Troubled firms could simply stay in business by borrowing more. Now, however, as bad loans erode their capital base, banks are beginning to say “no” to prospective corporate borrowers, or at least to charge higher risk premiums. This change has caused some firms to turn to the bond market and compete with foreign firms to attract capital. In so doing, the firms are forecasting a decline in the importance of protection through their relationship with their bank and through cross-shareholdings held by friendly companies. The firms are coming to terms with the fact that even friendly companies are demanding a better return or selling some of their own shareholdings to financial institutions to gain some cash.

Weak management and stifling government regulation, which have led to

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30 See id. at 56. To be sure, some managers now are threatened with firing for “under-performance” through mergers and acquisitions (“M&A”), as a market for M&As is starting to emerge. See id. In the first six months of 1998, there were 383 M & A deals, worth a total of ¥ 1.3 trillion, and nearly two-thirds of these involved foreign firms. See id. This activity has occurred because so many companies were severely under-performing (which, perhaps, motivated the Travelers Insurance – Nikko deal). Three of Japan’s five car makers — Mazda, Mitsubishi Motors, and Nissan — were hardly making a return above their capital cost, if at all. See Fin. Times, May 6, 1998. Japan Airlines is expected to make group net losses of ¥ 70 billion in 1998. The stock of one-half of second-tier companies trades near or below their break-up value. M&A activity surely will lead to cost-cutting, including plant closures, lay-offs, and rising unemployment, in the drive to use assets more efficiently and raise returns on capital.

Still, while some companies are inefficient, they remain protected from outside competition by non-tariff barriers. (The United States Trade Representative provides an annual chronicle of such barriers in Japan and other countries.) They invest without realizing the need to make a return on capital, thus destroying the value of the company. The average return on equity for Japanese companies in 1998 was 4 percent, compared to 20 percent in the United States. See id. Plainly, mis-management and mis-allocation of capital have yet to be dealt with in full.

One glimmer of hope is that some Japanese companies are beginning to adopt “Anglo-Saxon” methods to boost profitability, cash flow, and share prices. See Corporate Japan Goes to Waste, supra note 28. Because they cannot obtain financing from banks, at least not on the traditional cheap and easy terms, some companies are resorting to equity and bond offerings. But, such offerings mean companies have to pay attention to investor interests. By August 1998, about 168 companies announced share option schemes for senior employees. These executives now have an incentive to pursue shareholder’s interests fervently and maximize profits, because they too will make money off of increases to their company’s share price. See id. Also by August 1998, over one thousand companies had announced plans to buy back own shares. This move would increase share returns, because the number of shares outstanding (the supply of equity) will fall. But, the move does not necessarily improve profits, so for many indebted companies, this may not be a wise solution. See id.

31 Japan’s Economic Plight, supra note 8.

32 See id.
widespread inefficiency and dwindling returns on capital, are not the only culprits for Japan’s anemic average growth of 1.3 percent a year.\(^{33}\) Oft-criticized fiscal and monetary policies may be causes of the country’s stagnation. For example, in the early 1990s, Japan was said to be too reluctant to cut taxes or interest rates. Then, it quickly tightened fiscal policy a year after its financial bubble burst.\(^{34}\)

In addition, in any economy, growth in potential output depends on the growth in the labor force and rising productivity. As of June 1998, Japan’s potential output was growing by about 2 percent a year.\(^{35}\) But, because its actual growth has been less than this over the past six years, the economy now has a sizeable “output gap.” In other words, Japan possibly could grow faster for several years without encountering bottlenecks.\(^{36}\) Consequently, some economists cite this as proof that part of the problem is inadequate demand. Monetary policy possibly could stimulate the economy through exchange rates. The 20 percent drop in the yen against the dollar over 1997-1998 should help to boost exports, raise import prices and prevent deflation,\(^{37}\) albeit with the sort of delay predicted by the J-curve. Japanese products will, after the adjustment, be cheaper by international standards and thus more attractive to foreign buyers.

Japan’s problems may well worsen before they improve.\(^{38}\) The banking system remains in a near-depressed state. The amount of bad (\textit{i.e.}, non-performing) loans held by banks, according to one estimate, is as high as ¥ 87 trillion (roughly U.S. $600 billion),\(^{39}\) or 12 percent of GDP. This is staggering, even by American savings-and-loan industry scandal standards. It has caused new lending to stop immediately, which in turn, depresses demand even further.\(^{40}\) Moreover, bad debts raise anxieties about the security of the banking system, further undermining consumer confidence. Japan needs to close its output gap, and take steps

\(^{33}\) See id.
\(^{34}\) See id.
\(^{35}\) See id.
\(^{36}\) See id.
\(^{37}\) See id. As of June 1998, the weakness of the yen is partly due to the markets’ immense uncertainty about the policy response to Japan’s economic crisis. See John Plender, \textit{Can Japan Reflate?}, FIN. TIMES, June 11, 1998 at 13. As suggested in the text, the immediate problem is one of deficient demand in an economy burdened with flagging asset prices, excessive debt and rising unemployment. See id. Japan is in a position strikingly similar to that of the United States at the start of the Great Depression of the 1930s. However, unlike the United States position then, in Japan there was a gap of several years between the pricking of the Japanese bubble and the descent of the economy into its present liquidity trap. The delay is due in large part to fiscal policy. Fiscal boosts that culminated in the big package of September 1995 were estimated by the OECD to have contributed 1.5 percent to GDP growth. Yet, Japan’s stop-go approach to public works reduces the confidence-building impact of these fiscal measures, and the inefficiency of much public investment means that its impact on the whole economy is less than its potential. See id.

\(^{39}\) See Harney, supra note 1.
\(^{40}\) See Japan’s Economic Plight, supra note 8.
II. AND THE POSSIBLE SOLUTIONS?

There is no shortage of ideas for remedying the Japanese economic crisis. Old-fashioned, Keynesian pump-priming, supply-side structural reform, and de-regulation are the most commonly advanced, and the first option is the one most famously used by the Japanese government thus far. In addition, unconventional monetary policy has been suggested, based on a very plausible diagnosis that Japan is stuck in a liquidity trap.

These ideas are surveyed below. Which one of these proposals, if any, might be the successful prescription is, as yet, uncertain. Diverse as they are, they have a common denominator. All are largely, if not entirely, economic policy prescriptions. They say little about Japan’s legal system (though de-regulation comes the closest), and nothing about its insolvency law regime.

This silence is unfortunate, but not surprising given that lawyers and economists do not talk much to one another (even when they serve the same paymaster), and few are trained in the other’s discipline. The truth is that lawyers have as much to contribute to the debate as economists, because Japan’s “economic” crisis is a misnomer: it is more than just an economic one. Part of the puzzle is entrepreneurship, or – to borrow from the title of John Commons famous book – the legal foundations of capitalism.

Insolvency law is one such foundation. Indeed, this body of law has a lot to do with the entrepreneurial culture of a country. In turn, entrepreneurship, that is, risk-taking – as Joseph Schumpeter taught – is the engine of free-market capitalism. Entrepreneurship can be encouraged (or, at least not discouraged) through insolvency rules that balance debtor and creditor interests, and acknowledge the global nature of those interests, and that ensure efficient, transparent, and fair re-organizations and liquidations.

Thus, insolvency law and its reform, discussed in Parts Three and Four below, need to be seen as part of a long-run cure for Japan’s current ailment. To be sure, remedies developed in the economic context are important. They must be understood by lawyers, who are, after all, working in this context – hence the need for the present Part. But, just as legal proposals made without an understanding of the economic context may be of little practical value, economics alone cannot complete the puzzle.

A. Keynesian Tactics And Their Limits

One strategy for revitalization is a fiscal stimulus package coupled with further yen depreciation. Former Prime Minister Ryutaro Hashimoto proposed multiple stimulus

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41 See id.

42 Is fiscal policy really important? Some economists dispute the notion that it is, at least in the present Japanese context. The stimulus packages introduced have included measures that had no direct impact on growth. The actual amount injected into the economy over the past five years, through increased public works or tax cuts, was only one-third of all the measures announced by the government. See Japan’s
packages full of classic Keynesian government expenditures and tax cuts. Overall, the proposals called for a ¥ 16 trillion (U.S. $ 120 billion) fiscal stimulus package to restore confidence in Japanese markets and add 2-3 percent to GDP. The proposal also called for ¥ 4 trillion (U.S. $ 30.5 billion) in income-tax cuts. The new Prime Minister, Keizo Obuchi, followed suit, persuading the Diet to enact a budget containing additional public spending – a whopping ¥ 24 trillion (roughly U.S. $200 billion), the equivalent of the entire GDP of Turkey or Austria – coupled with tax cuts.

Ironically, the government may have exhausted all of the conventional Keynesian pump-priming remedies, with little effect during the past two years. As of early 1999, private consumption, which accounts for nearly 60 percent of GDP, continues in a slump. A collapse in consumer demand, production cuts, and a shortage of capital have caused a sharp contraction in investment. Unemployment (as mentioned earlier) is at a record high of 4.8 percent and climbing. Japan’s Economic Planning Agency (EPA) estimated that for the financial year ending 31 March 1999, the economy shrank for the fifth quarter in a row, with a contraction of around 2.5 percent.

The Bank of Japan has cast about for alternatives, including the possibility of stimulating the economy through appropriate monetary policy. For example, in early 1999, the Bank was put in the position of examining whether to purchase more Japanese government bonds to support bond prices and boost liquidity. Fortunately, the EPA predicts growth of about 0.5 percent in the coming fiscal year (1999-2000). It may be right. As of June 1999, the economy is experiencing its first signs of growth since the summer of 1997. If these signs point to a broader recovery, then the Bank of Japan may not be quite so hard-pressed to find alternatives remedies.

B. Supply-Side Structural Reform

There have been other suggested remedies beyond traditional Keynesian and monetary policy tactics. Some economists, including the President of Nakamae International

Economic Plight, supra 8. Much of the deterioration in Japan’s budget, from a general government surplus of 1.5 percent of GDP in 1992 to a deficit of 3 percent in 1997, reflects the axiomatic fall in tax revenues due to the downturn. Id.

45 See Paul Abrahams & Will Dawkins, Hey, Big Spender, FIN. TIMES, June 22, 1999, at 18.
46 See Gillian Tett, Japan’s Big Issue, FIN. TIMES, February 12, 1999, at 19.
47 See id.
50 See id.
Economic Research, believe that Japan’s only hope for a sustainable recovery is massive supply-side structural reform to get the new economy growing. The argument is that Japan must abandon attempts to stimulate demand in favor of structural reform to promote a service-based economy. Cuts in capital investment are said to be the primary cause of Japan’s prolonged economic slump in the 1990s, and over-supply in the old economy has gone hand-in-hand with over-employment. These cuts in investment now translate into unemployment and job insecurity, which have eroded consumer confidence.

Yet, the Japanese government seems to continue to view Keynesian tactics as the primary path toward economic salvation. The use of demand-side palliatives may well undermine the structural reform process. A realistic target for sustainable economic growth in the 21st century is 3 percent a year, requiring Japan to improve productivity by 3 percent a year, and industries to cut employment by 3 percent a year, thus creating 2 million newly unemployed every year. The best hope is that the newly unemployed are absorbed into a rapidly expanding service-based economy. Japan’s future hinges on whether this new economy grows fast enough over the next decade to provide new jobs for 20 million Japanese, roughly one-third of the present working population.

The engine for growth in the new economy could well be small service-providing companies. Two hundred thousand small companies would need to be created. How can this entrepreneurial spirit be stimulated?

Tax reform is one possibility. It must aim specifically to provide incentives for business creation and growth on the supply-side. It also ought to aim at encouraging consumption expenditures. One interesting proposal, offered by Professor Gary Saxonhouse, is to raise Japan’s 5 percent consumption tax. An anticipated future increase might cause consumers to spend more before the increase takes effect. Moreover, it might persuade pensioners that their social security benefits will not be cut in the future in order to cover Japan’s massive fiscal deficits, and service the resulting debt that has accumulated. To the extent consumers, especially pensioners, spend on services, they will be helping small service-providing companies.

Of course, tax reform is not the only possibility. Currency policy must play a supportive role. The problem with an over-valued yen is that it only aggravates the potentially catastrophic deflationary spiral that supply-side structural reform has set in motion. However, perhaps the key catalyst for entrepreneurship is a revolution in the way Japanese companies are run, and the way they deploy capital.

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52 See Tadashi Nakamae, Out with the Old, FIN. TIMES, December 31, 1998, at 10.
53 See id.
54 See id.
55 See id.
56 See id.
57 See Gary Saxonhouse, Japan’s Growth Conundrum, FIN. TIMES, June 14, 1999, at 16.
58 See Nakamae, supra note 52.
59 See generally Japan’s Growth Companies, THE ECONOMIST, June 26, 1999, at 69-70 (discussing roughly a dozen Japanese corporate success stories, specifically, companies that have
C. **Deregulation**

Still another non-Keynesian strategy for managing the economic crisis is deregulation. Like supply-side structural reform, this remedy is a long-term one. Nevertheless, Japan’s leaders appear to have embraced it, as a compliment to fiscal stimulus packages. They have promised a strong effort at deregulation. However, as late as April 1998, American officials questioned the commitment to make real change, and complained that de-regulatory efforts had resulted in only limited progress and were incomplete.60 They encouraged Japan to focus on specific sectors and problems, especially telecommunications, medical devices and pharmaceuticals, housing, competition policy,61 and the distribution system.62

How will deregulation in these sectors help? Deregulation in telecommunications would allow for greater competition and thus lower costs. Indeed, the liberalization efforts already taken have contributed to a fall in the cost of telephone calls. Health care reform would include shorter approval processes for medical devices and drugs, which would lead to more open markets and lower prices. Reform in the housing sector would lower housing costs, assuming Japan adopts construction standards that are widely accepted in other countries. Reform in Japan’s competition policy would allow for greater enforcement power for the national antitrust authority, the Japan Fair Trade Commission (JFTC), which would result in transparency to government procurement and better conditions for consumers.63 Market barriers in the distribution system include strict regulations on inspection and testing of equipment, limitations on the activities of energy service providers, and the use of narrow technological standards. The result will be greater import penetration and thus eased access to imported goods.64 Likewise, relaxing the laws controlling large stores already

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60 See ASIA/PACIFIC RIM, April 29, 1998.

61 A recent development from the international trade law realm is relevant here, namely, the United States – Japan Enhanced Initiative on Deregulation and Competition Policy. The objective of the Initiative is “to conduct a serious exchange of views and to undertake measures, as called for in the Framework [i.e., the United States – Japan Framework for a New Economic Partnership], to ‘address reform of relevant government laws, regulations, and guidance which have the effect of substantially impeding market access for competitive goods and services,’ in order to enhance consumers’ interests and to increase efficiency and promote economic activity.” See First Joint Status Report on the U.S.-Japan Enhanced Initiative on Deregulation and Competition Policy, released at G-8 Summit, 15 May 1998, reprinted in 15 ASIA/PACIFIC RIM no. 20 at 891, May 20, 1998. Since June 1997, both countries have been trying to fulfill this objective and promote deregulation and active implementation of competition policy. They believe these measures will improve market access for competitive goods and services, enhance consumers’ interests, increase efficiency and promote economic activity. The Initiative aims at providing non-discriminatory treatment for foreign goods and services. As a result, Japanese government has undertaken a series of deregulation measures, and on 31 March 1998, the cabinet adopted three-year program for the promotion of deregulation. See id.


63 See id.

64 See Japan’s Economic Plight, supra note 8.
has increased competition by encouraging rapid growth in the number of big supermarkets and foreign retailers. Overall, it is estimated that these sorts of deregulation efforts could save consumers almost U.S. $40 billion a year.65

In sum, the objectives of the deregulation efforts are two-fold: (1) to open Japanese markets to imported goods, and (2) to lower prices for domestic consumers. If these objectives are achieved, it follows that domestic demand will increase, and demand-led growth will occur. This result is important not only for Japan, but also the rest of Asia. The converse also is true, namely, that recovery in the rest of Asia is a key to stimulating demand in Japan.

D. The Krugman Thesis

Noted economist Paul Krugman diagnoses Japan’s illness as far more serious than is commonly acknowledged, and he prescribes an unorthodox cure.66 Professor Krugman diagnoses Japan’s current situation as a classic “liquidity trap.” He defines a “liquidity trap” as a situation in which conventional monetary policies have become impotent, because nominal interest rates are at or near zero: injecting monetary base [i.e., increasing the quantity of money] into the economy has no effect, because base and bonds are viewed by the private sector as perfect substitutes. By this definition, a liquidity trap could occur in a flexible price, full-employment economy; and although any reasonable model of the United States in the 1930s or Japan in the 1990s must invoke some form of price stickiness, one can think of the unemployment and output slump that occurs under such circumstances as what happens when an economy is trying to have deflation – a deflationary tendency that monetary expansion is powerless to prevent.67

What Professor Krugman is saying is this: investors are indifferent between holding bonds and money. After all, if nominal interest rates are at or near zero, what is gained by holding bonds instead of money? When the central bank increases the money supply through, for example, purchases of government bonds, the prices of those bonds rise, hence nominal interest rates falls. As long as the inflation rate is unchanged, the decline in nominal interest rates means real interest rates also fall. Businesses are assumed to make investment decisions based on real interest rates, and consumers are assumed to make spending (versus savings) decisions.

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The sectors mentioned above are not the only relevant ones. There has been some deregulation of Japan’s U.S. $150 billion energy sector and electric market. See id. About four years ago, Japan began allowing independent producers to sell power to Japan’s nine regional electric power monopolies. As of last year, allowing independent producers to sell directly to consumers was “under discussion.” See id. Similarly, deregulation in the oil industry has led to a sharp reduction in petrol prices. See Japan’s Economic Plight, supra note 8. Japanese Ministry of International Trade and Industry (MITI) official Nobuo Tanaka commented in May 1998 that the progress of deregulation was moving at an appropriate pace and was satisfactory. See ASIA/PACIFIC RIM, May 6, 1998.


67 Paul R. Krugman, It’s Baaack: Japan’s Slump and the Return of the Liquidity Trap, 2 BROOKINGS PAPERS ON ECONOMIC ACTIVITY 137, 141 (William C. Brainard & George L. Perry eds. 1998).
decisions based on real interest rates. A decline in real interest rates should stimulate business investment, and encourage consumers to save less and spend more. But, in a liquidity trap, nominal interest rates already are by definition at or near zero, and real interest rates may well be negative. Increasing the supply of money through open market purchases of government bonds might well push real interest rates into (or further into) negative territory. Yet, this change in rates will have no impact on investment or consumption decisions. The interest-rate incentive for businesses to invest and consumers to spend already is as good as it can be, and they simply will not invest or save any more. Thus, in a liquidity trap, a central bank finds itself “pushing on a string;” despite increasing the money supply, people simply will not spend more, and businesses simply will not invest more. Monetary policy affects neither output nor prices.

The liquidity trap explanation, while perhaps unconventional, ought to be given considerable deference. Two facts of Japan’s present macroeconomic condition stand out: (1) short-term interest rates are at or near zero, and (2) monetary policy is ineffective at stimulating aggregate demand. Both facts are defining criteria for a liquidity trap. These facts ought to focus our attention away from “easy” diagnoses and cures. Professor Krugman’s point is compelling:

[M]any of the common explanations of why Japanese monetary policy is ineffectual are wrong, or at least inadequate. One often hears, for example, that the real problem is that Japan’s banks are troubled, and hence that the Bank of Japan cannot increase monetary aggregates; but outside money is supposed to raise prices regardless of the details of the transmission mechanism. Aside from the bad loans, one also often hears that corporations have too much debt, that the service sector is over-regulated and inefficient, and so on. All of this may be true and may depress the economy for any given monetary base, but it does not explain why increases in the monetary base should fail to raise prices, or output, or both. Recall that the neutrality of money [i.e., the widely accepted macroeconomic proposition that an increase in the money supply will cause a roughly proportional increase in the general price level] is not a conditional proposition; it does not depend on banks being in good financial shape, or the service sector being competitive, or corporations not taking on too much debt. Money (which is to say, outside money) is supposed to be just plain neutral.68

The obvious challenge is how to stimulate aggregate Japan given the ineffectiveness of monetary policy.

On this matter, Professor Krugman argues against using the traditional way out of a liquidity trap, namely fiscal policy. One reason is that the Japanese public believe that government expenditures and tax cuts eventually will be reversed – after all, the government deficit is yawning to ever-greater amounts. The public will, therefore, save rather than spend.69 A second reason concerns the difference between actual and potential output. Professor Krugman contends that aggregate demand in Japan is insufficient to employ the country’s productive capacity. Why? Even if Japan were at full employment, the supply of

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68 Krugman, BROOKINGS PAPER, supra note 67, at 141-42 (emphasis original).
69 See Kathryn M. Dominguez, Comments and Discussion, in Krugman, BROOKINGS PAPER, supra note 67, at 189.
Japanese savings exceeds the sum of demand for investment plus the current account surplus.\(^70\) To put it bluntly, even at full employment, the Japanese still would not spend enough to stimulate the economy. Thus, Professor Krugman argues it is necessary for Japan to reduce its savings-investment gap, a goal that fiscal stimulus packages cannot achieve. In the long run, only structural change will cause the Japanese to save less and invest more.

In making this argument, Professor Krugman disputes the “clogged pipe” theory. This theory urges that the weakness of Japan’s banks depresses investment because it prevents liquidity from getting through to credit-constrained firms. Professor Krugman asserts that simply increasing the capital of Japanese banks, in the hopes that the banks will become more willing to lend, actually could worsen the savings-investment gap. The banks will not lend, hence savings will accumulate while investment does not increase. In other words, injecting capital into banks is unlikely to restore favorable credit conditions, and the belief that weak banks lie at the heart of Japan’s distress is misleading.

What is Professor Krugman’s advice for the short-term to reduce the savings-investment gap? A policy of “managed inflation.” He argues the Bank of Japan ought to engage in unconventional monetary policy to convince the private sector that inflation, not deflation, will prevail in the future. The managed inflation strategy, Professor Krugman suggests, can be implemented by announcements from the Bank of Japan concerning inflation targets (say, 2 percent), coupled with the use of open market operations to drive up prices of assets that can be increased (e.g., long-term bonds and foreign currencies).

What is the intuition behind Professor Krugman’s advice? It is based on the conceptual difference between nominal and real interest rates, and how that difference effects the behavior of investors (businesses) and savers (individuals). Presumably, if Japanese businesses develop inflation expectations, they will invest more. Why? Because, as suggested above, it is assumed that businesses base their investment decisions on the real rate of interest (the difference between (1) the nominal rate of interest a business pays for borrowing funds and (2) the rate of inflation). If businesses believe the real interest rate is falling, because of rising inflation, then they will invest more.

Likewise, a managed inflation policy may persuade Japanese consumers to save less and spend more, again assuming they internalize inflation expectations. The intuition, as suggested earlier, is that the public makes savings decisions based on the real rate of return (again, (1) the nominal rate of interest of an interest-bearing asset minus (2) the rate of inflation). If consumers believe real interest rates are headed downward, then they will curtail savings (in the form of interest-bearing assets), and spend more. Their decision to increase consumption expenditures will be reinforced by their inflation expectations. Saving now and buying later will be costly, because inflation means consumer prices are headed up, so why wait?

\(^70\) It will be recalled that there is a basic macroeconomic identity concerning the equivalence of the savings-investment gap and the export-import gap. The underlying concept is that the two gaps must be equal. If savings exceeds the sum of investment and the current account surplus, then it suggests a country is not producing all the output it could, \textit{i.e.}, it is lagging behind its productive capacity. However, in the sources cited above, this point is not made as clear as it might be by Professor Krugman.
PART TWO: THE COMPARATIVE AND INTERNATIONAL LEGAL CONTEXT

I. COMMONALITIES IN INSOLVENCY LAWS ACROSS COUNTRIES

It is a strange fact that in the increasingly inter-disciplinary atmosphere in which scholars now work, or at least laud, all of the macroeconomic diagnoses and remedies are just that – macroeconomic. If legal reform is mentioned, it is only under the general rubric of structural form. Insolvency law in particular is not appreciated as part of the essential landscape of a well-functioning, developed capitalist economy. That must change.

Stripped to its essentials, insolvency law creates a collective procedure for the recovery of debts by creditors. The common feature of all insolvency situations is that there are insufficient funds to pay off all creditors in full. Insolvency law is all about deciding who to pay, in what order to pay, and how much to pay. The collective procedure created is designed to resolve the “who?,” “in what order?,” and “how much?” questions in an efficient and equitable manner. Of course, efficiency and equity sometimes may be competing policy goals. In the way it pursues those goals, insolvency law says a lot about the attitudes of a country’s legal system, and about the relationship between the parts of that system (as suggested by the Appendix). This specialty has even been dubbed the most important of all commercial legal disciplines.

As country after country revises, or in some cases writes anew, its bankruptcy law, some common themes are beginning to emerge. Japanese insolvency law can be gauged partly in a comparative legal context, specifically, in relation to these themes. In general, three legal doctrines resonate in all or virtually all modern bankruptcy regimes. First, all actions taken by individual creditors against the debtor are frozen and replaced with rights to claim a portion of the pool. Second, all assets of the bankrupt belong to the asset pool, the debtor’s estate, which is made available to pay off creditor claims once the size of the pool has been maximized. Third, creditors are paid on a pari passu, or pro rata, basis, out of the pool, each according to their claims.

What policies compel these three doctrines, referred to respectively as the automatic stay, the maximization of the asset pool, and the proportionate payment of claims? Again, efficiency and equity. By automatically staying creditor claims, a “grab race” for assets among creditors is prevented. It may well be that if the debtor’s asset pool is preserved and strengthened over time, each creditor will wind up with a greater recovery than it otherwise would have gotten through immediate, unilateral and selfish behavior. That is, fairness means

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71 The author gratefully acknowledges the background memorandum, “International Insolvency Laws” (June 1999), by Ms. Preeti Kapoor, GW Law School Class of 2000, which assisted in the preparation of this Part.


73 See id.

74 See id. at 2.

that, relative to all other creditors, no creditor ought to recover out of turn or in an amount greater than the proportionate share of its claims. But, how much, in absolute terms, this recovery amounts to depends very much on the efficiency of the bankruptcy procedure. Observe, then, that efficiency and fairness work in tandem.

II. THE PRO-DEBTOR – PRO-CREDITOR CONTINUUM

A. Defining “Pro-Debtor” And “Pro-Creditor”

The commonality across borders of the three doctrines and their underlying policy rationales does not necessarily translate into commonality of implementation. Different countries implement the doctrines differently, a not very surprising result. After all, emphases on efficiency and fairness are bound to differ, and there are unique economic circumstances and legal traditions to boot (such as those in Japan discussed in Part One and the Appendix, respectively). The styles in which the doctrines appear allow for a conceptual classification along a continuum that focuses on a single question: how pro-debtor or pro-creditor is the country’s bankruptcy regime?76

The answer says a lot about the kind of capitalist system in a country. Certainly, there is a lot more to differentiating brands of capitalism than insolvency law. Still, it may be said that a pro-debtor regime encourages entrepreneurial risk-taking, while a pro-creditor regime encourages the provision of liquidity to business. Yet, operating at either extreme on the continuum is problematic. Credit may be hard to come by for many firms in a pro-debtor regime, simply because lending institutions fear the all-too-favorable rules for debtors. Conversely, rules that are skewed too far in favor of creditors hardly create an environment friendly for entrepreneurs.

What is a “pro-debtor” regime? In the most rigorous sense, it is one that dwells on increasing the size of the debtor’s estate by destroying creditor and ownership rights.77 In a pro-debtor jurisdiction, every effort is made to maximize the value of the debtor’s assets for ultimate distribution to creditors.78 The justification for this effort is that debtors and their employees ought to be saved, and if need be, all creditors ought to contribute to this rescue.79 The argument is that increasing a debtor’s estate improves the lot of unsecured creditors in particular.80 Accordingly, in a pro-debtor jurisdiction, the class of third-party owners is limited, because every effort is made to aggrandize the debtor’s estate for the benefit of the debtor and its unsecured creditors.81

76 See Wood, supra note 72, at 3.
77 See id.
78 See id.
79 See id.
80 See id.
81 See id. at 35.
At the other end of continuum from “pro-debtor” regimes are “pro-creditor” ones. To affix the label “pro-creditor” on a regime is to connote that creditors ought to be able to avoid losses that result from the default of a debtor.82 Thus, a pro-creditor jurisdiction allows creditors to avail themselves of protection through security interests and set-offs.83 Otherwise, it is said that the insolvency will create risks for everyone, and perhaps even generate risks for the system itself.84 Concomitantly, a jurisdiction is pro-creditor if it allows a wide class of third party owners to claim their property held by the bankrupt ahead of other creditors.85

B. The “Empirical” Results

How do various countries stack up on this pro-debtor – pro-creditor continuum? On a scale of one to ten, with one being extreme pro-creditor and ten being extreme pro-debtor, the results are depicted in Chart 1 below. It is worth highlighting that Japan is considered to be roughly in the middle of the continuum. It is also worth emphasizing that, as in any comparative legal analysis, the empirical results are rather general characterizations, subject to criticism on finer details.

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82 See id. at 3.
83 See id.
84 See id.
85 See id. at 35.
**Chart 1: The Pro-Debtor – Pro-Creditor Continuum**

**Most Pro-Creditor**

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Λ (1) Hong Kong and Singapore.
∥ (2) Australia, England, and Ireland.
∥ (3) Germany, the Netherlands, Sweden, Switzerland.
∥ (4) Japan, Korea, New Zealand, Norway, and Scotland.
∥ (5) Canada and the United States.
∥ (6) Austria, Denmark, and South Africa.
∥ (7) Italy.
∥ (8) Greece, Portugal, Spain, and most Latin America countries.
∥ (9) Belgium and Luxembourg.
∥ (10) France.86

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**Most Pro-Debtor**

How are countries placed on this continuum? Seven criteria distinguish the bankruptcy laws of the countries. These are: (1) the scope and efficiency of security interests and title financing; (2) the right of set-off in insolvency situations; (3) contract and lease rescission; (4) the way in which preferential transfers are treated; (5) the strength of the veil of incorporation (e.g., as between corporate parents and subsidiaries); (6) the circumstances of ownership of assets in the possession of the debtor; (7) the existence and nature of corporate rehabilitation statutes (i.e., rescue proceedings).87

The first, second, and sixth criteria are straightforward. The broader the scope and efficiency of security interests and title financing, the more pro-creditor the jurisdiction. The stronger the right of set off, the more pro-creditor the jurisdiction. The more rigorous the circumstances of ownership of assets in the debtor’s possession, the more pro-creditor the jurisdiction. However, special mention should be made of the third, fourth, fifth, and seventh criteria.

Consider the third criteria. The most common approach to contract and lease rescission found across countries is that the debtor’s estate has the power to disclaim, abandon, or reject a contract or a lease, or to call upon the counter-party to perform the contract.88 A good example is found in Japan’s Bankruptcy Law, which contains the power to perform or

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86 See id. at 4.
87 See id. at 6.
88 Id. at 60.
reject contracts. Similarly, under the American Bankruptcy Code, a trustee has the power to assume or reject any executory contract or unexpired lease, as long as certain conditions exist. However, there are also important exceptions to rules on contract and lease recission, found (for example) in the United States and the United Kingdom. Suppose that a seller of land in the United States or England becomes insolvent after entering into a contract of sale, but before completion of performance of this contract. Then, the purchaser can insist on transfer and possession of the land upon payment of the price. Thus, the trustee for the seller’s estate lacks the power to disclaim the real estate sale contract.

As regards the fourth criterion, all contemporary bankruptcy laws provide a system of preferences for the re-capture of assets. In determining whether the corporate insolvency law of a particular jurisdiction is pro-creditor or pro-debtor based on this criterion, it is necessary to examine the extent of creditor protections for general preferences, the protection of the ordinary course of business payments, the validity of security for pre-existing debt and the length of the suspect period. This examination, obviously, is rather involved.

A fundamental decision that must be made in many corporate insolvency cases, which concerns the fifth criterion, is whether to honor the veil of incorporation. The problem arose in a curious way in the infamous BCCI insolvency. There, BCCI had subsidiaries in some countries, branch offices in other countries, and agencies in still other countries. Standard Anglo-American corporate legal doctrine would have it that a subsidiary is a separate entity from its parent, with its own assets, liabilities, and capital. An agency or branch is, by contrast, part and parcel of the parent. It has no separate balance sheet, and it is not separately capitalized. Accordingly, there ought not to have been any question about the treatment of assets or liabilities in BCCI’s subsidiaries versus its agencies or branches. The former were distinct from those of the parent, whereas the latter were not. However, ring-fencing laws of various jurisdictions – New York and California being examples – got in the way of a straight application of corporate law. Local bank regulators applied their banking laws to keep assets and liabilities of agencies and branches – a corporate law incongruity – in their jurisdictions.

As for the continuum, the test to determine whether the corporate veil is honored is whether the law holds persons other than the company personally liable for the company’s debts once the company has become insolvent. If there is absolutely no way to impose such liability, then the veil is respected in the purest sense. In reality, the most pure form exists with respect to the liability of shareholders for the debts of a corporation. There is a broad international consensus that shareholders are not personally liable for the debts of a company beyond the unpaid amount of their shares. As for the liability of directors, respect for the veil is far less pure. A comparative analysis of countries reveals six circumstances in which a director may be held personally liable for the debts of a company: (1) fraudulent trading; (2) wrongful trading; (3) obligations to act when the company is insolvent or has lost most of its capital; (4) negligent management; (5) breach of company law or securities

89 See id. at 61.
91 See Wood, supra note 72, at 61.
92 See id. at 72.
93 See id. at 160.
regulation; and (6) miscellaneous liabilities, including tort and breach of general statute. In the United States, much emphasis is placed on the third circumstance, which is also known as the “business judgment rule.” The rule demands that a director act honestly and with the best interest of the company in view. Similarly, Japan imposes a due diligence duty on directors. In both countries, the “bottom line” for directors is that they are immune from liability in the event their company “goes bust” so long as they have fulfilled their obligation to act appropriately on behalf of their company.

The seventh criterion used to construct the pro-creditor – pro-debtor continuum is the adoption of corporate rescue proceedings. They are designed to assist debtor companies in distress. Modern forms of corporate rehabilitation laws impose a freeze on creditor proceedings, which, of course, impinges on creditor rights. The justification for the freeze and consequent impingement is that during the delay, the corporate debtor can be rehabilitated (at least partly). Countries differ substantially on eligibility for rehabilitation. Under Japan’s Corporate Rehabilitation Law of 1952, access is rather difficult, whereas under Chapter 11 of the United States Bankruptcy Code, rehabilitation proceedings can be commenced rather liberally. Specifically, in Japan, the possibility of corporate reorganization exists only for publicly-held limited companies, but it is effective (if at all) only with respect to the properties of a company that exist in Japan. Reciprocity does not exist; that is to say, corporate reorganization proceedings commenced in a foreign country are not effective with respect to properties situated in Japan. To qualify for corporate reorganization under Japanese law, a corporate debtor must show (1) it cannot pay its debts as they fall due without materially impeding the continuance of its business or (2) absent rehabilitation, the causes of bankruptcy are likely to occur. In contrast, in the United States, the scope of Chapter 11 embraces most business enterprises, whether they are incorporated or unincorporated. It is not necessary for the debtor to show insolvency or feasibility in order to qualify for Chapter 11, i.e., a solvent corporation can file.

III. THE LACK OF COMITY

The fact that a pro-creditor – pro-debtor continuum exists and different

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94 See id. at 142.
95 See id. at 149.
96 See id.
97 See id. at 182.
98 See id.
99 See id. at 186.
100 See id.
101 See id. at 188.
102 See id. at 187.
103 See id.
countries appear at different points on it bespeaks a lack of comity in relation to international bankruptcy law. Why has this come about? An obvious explanation is the sharp division between pro-debtor and pro-creditor bankruptcy policies, as mentioned above. A second explanation is what might be called a “ring-fencing mentality,” namely, a desire to ensure local assets are not used to pay foreign taxes or foreign preferred creditors, at least not unless and until local creditors are satisfied. Related to this mentality is another contributing factor: the “xenophobic protection of local creditors.” Foreign debtors that have caused loss to local creditors are resented. This resentment translates into distrust of foreign legal systems.

These reasons do not, however, justify the lack of comity that exists in insolvency laws of most countries. It is incongruous with the modern global economy. Multinational corporate debtors hold assets in several different countries. Creditors are scattered around from Toronto to Tokyo. Thus, trustees seeking to marshal the assets of a debtor, in order to distribute them among the creditors in their own country, as well as those domiciled in other countries, necessarily must pay increasing attention to the principle of comity.

IV. ORGANIZING PRINCIPLES FOR THE INTERNATIONAL ASPECTS OF A COUNTRY’S INSOLVENCY REGIME

The problem of comity, or the lack thereof, raises an obvious question: are there any principles emerging in the insolvency laws of various countries that might provide for greater respect, indeed, recognition, of foreign insolvency proceedings? Happily, the answer is yes. The world at the end of the twentieth century is not retreating entirely into fortresses, at least not with respect to insolvency law. Two broad principles are emerging in international insolvency law, i.e., in the provisions of local laws dealing with international aspects of bankruptcy. These principles are universality and territoriality.

The dichotomy between universality and territoriality is an ideal type. In practice, there are many combinations and variations of these, for example, modified universalism, secondary bankruptcy, corporate-charter contractualism, and cooperative territoriality. Once again, there is a continuum, depicted in Chart 2 below, which might be dubbed the “Organizing Principle Continuum.” Almost every country falls within one of these variations, with their domestic insolvency laws and recognition policies being a mixture of the two broad principles. It is worth emphasizing, then, that the principles are not confined to any one country or group of countries. They are as worthy of consideration in Japan, for example, as in other country examining its insolvency regime with a view to improvement.

104 See id. at 227.
105 See id.
A. The Pure Form Of The Universality Principle

What is the universality principle? Its key premise is that only the courts of the bankrupt company’s “home country” should have control and jurisdiction, thus applying the home country’s laws to the core issues of the proceeding.107 It is the ultimate expression of the importance of the location of the debtor, and attempts to rationalize the bankruptcy proceeding based on the answer to a single question: where is the debtor domiciled? In this context, “domicile” refers to the headquarters of the debtor, or its principal place of business. For the universality principle to work well, therefore, a solid test to determine the country in which headquarters or principal place of business exist is essential.

A country adhering to the universality principle agrees that all of the debtor’s assets are to be administered in one insolvency proceeding, regardless of where those assets are located.108 The single insolvency proceeding in the jurisdiction of the debtor would have full effect in all other countries where the debtor’s assets are located.109 Consequently, the only courts that ought to have jurisdiction to decide whether a debtor is indeed insolvent, and to have control over the assets of a bankrupt multinational firm, are the courts of the debtor’s domicile or principal place of business.110 These courts would apply their own country’s insolvency laws to decide whether the best strategy is corporate reorganization or liquidation, and to determine priorities among competing claims of creditors.111 These courts would control the administration of all assets of the debtor, both local and global, and make the requisite distributions to all creditors worldwide.112

The universality principle boasts a few important advantages. The most apparent one is the avoidance of the costs and inefficiencies of having two competing insolvency administrations.113 There is, moreover, clarity of expectations. All creditors

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107 See id. at 696.
109 See id.
110 See Wood, supra note 72, at 228. See also LoPucki, supra note 106, at 704.
111 See LoPucki, supra note 106, at 705.
112 See id.
113 See Wood, supra note 72, at 228.
dealing with a domiciliary know that, should the domiciliary “go bust,” the laws of the
domiciliary will govern the subsequent insolvency proceeding. Indeed, all creditors know
they will be treated equally under those laws. Finally, an international “grab race” among creditors is avoided. All of the debtor’s property, wherever located, is pooled, and there is a
universal restraint on creditor proceedings.114

But, the universality principle is not without drawbacks. Its advantages generally are from the perspective of an uninvolved observer – an antiseptic academic view – or from the perspective of the debtor and creditors located in the debtor’s jurisdiction. When the perspective of creditors that are not local, i.e., that are from outside the debtor’s jurisdiction – foreign creditors, as it were – the universality principle becomes controversial. First, a country accepting the universality principle must permit foreign laws and courts (i.e., the laws and courts in the debtor’s home country) to govern domestic relationships and local assets (i.e., relations between the debtor and creditors outside of the debtor’s home country). The results could be unpredictable.115 After all, how issues will be resolved under one’s own law are more or less understood (assuming the issues are not entirely novel). How they may be resolved under another legal regime may be quite unclear, or at least demand a great deal of study of, and experience with, the other regime before a certain comfort level is reached. It might be unreasonable to demand detailed study of the other regime, and it might be intolerable to suffer the trials and tribulations sure to come with experience.

Worse yet, allowing foreign law to govern the affairs of a debtor and creditors, regardless of where the debtor’s assets and its creditors are, may be seen as an infringement on sovereignty. A country that accepts the universality principle, without any restrictions, runs the risk that a foreign liquidator will assume control over assets in the country, and remove them to the debtor’s home country.116 Imagine a debtor that has engendered plenty of resentment among creditors outside (as well as within) its home country. Some of this resentment may be expressed in terms of the language of sovereignty. “How can we allow a foreign liquidator onto our soil to remove assets of the wretched debtor out of our country to pay off others?” will be the bottom-line demand.

Aside from certainty and sovereignty, there are some hard-headed concerns about the interests of creditors outside of the jurisdiction whose laws are applied to settle the case. If the universality principle is followed, then how will creditors not located in the debtor’s jurisdiction be treated vis-a-vis local creditors? What is hoped for is – to borrow a critical concept from international trade law – national treatment. Local creditors, that is, creditors in the debtor’s jurisdiction, ought not to be treated more favorably than foreign creditors.117 Put conversely, foreign creditors ought to be treated no less favorably than local creditors. If the analogy to international trade law is continued, the idea is not identical treatment. Rather, it is de jure and de facto equality of treatment.

Still other hard-headed problems will arise if the universality principle is

114 See id.
115 See LoPucki, supra note 106, at 709.
116 See Berends, supra note 108, at 314.
117 See id. See also Wood, supra note 72 at 228.
followed without qualification.118 How will claims be filed? Will there by any choice of law issues, and if so, how will they be resolved? What differences exist between the priority scheme under the law where the debtor is located and the law of the country accepting the principle? To the extent these questions are not addressed clearly, or are answered in unfamiliar ways, there may be increased resentment against the universality principle.

It is, at least in theory, possible to conceive of a more extreme principle around which a country can organize the international aspects of its insolvency laws than universality. This more extreme version is known as “unity.” It may so happen, even if a purely universalistic approach is taken, that some aspects of an insolvency proceeding will be governed by law other than the one in which the proceeding is being held (the home country law). The unity principle demands that all aspects of the proceeding be governed by one single law, that of the country of the opened proceeding, regardless of any ancillary proceedings used.119 Needless to say, implementation of the unity principle requires an extraordinary degree of cooperation among players in all relevant countries.

B. **The Pure Form Of The Territoriality Principle**

At the opposite end of the continuum from the universality principle is the territoriality principle. It creates a system in which each country has jurisdiction over the portion of the multinational corporate debtor within its borders.120 Here, then, is the ultimate deferral to the interests of every country involved. If the territoriality principle is applied, then each country in which the debtor has assets “gets a piece of the action.”

Specifically, every country where the debtor has assets will administer those assets, but only those assets within its territory and no more. There is no obligation whatsoever for the administration going on in one country to recognize concurrent insolvency proceedings being conducted in other countries. Indeed, quite the contrary, no such recognition is expected. Thus, the effects of an insolvency proceeding do not reach further than the sovereignty of the state where the insolvency proceeding has commenced.121

The obvious advantage of applying the territoriality principle is its respect for sovereignty. Related to this advantage is the mitigation of any uncertainty about results under foreign law, because foreign law is immaterial. In addition, there is no concern about creditors from one country (such as the debtor’s home country) being preferred over creditors from another country. If there is any discrimination based on national origin, it arises under the law in which the proceeding is taking place, and the locals—through their political representatives—presumably are satisfied with the discrimination (probably because it favors them).

There also are some obvious disadvantages. First, the principle is atavistic. If debtors and creditors know no boundaries when they give birth to and nourish a business, then why should the law—or laws—suddenly declare those boundaries to mean something when

118 See id.
119 See Berends, supra note 108, at 315.
120 See LoPucki, supra note 106, at 696.
121 See Berends, supra note 108, at 314.
the business is ailing? Second, the principle is inefficient. When the assets of insolvent debtors are located in numerous countries, an insolvency proceeding would have to be undertaken in each country. 122 A disinterested observer would find a single, rationalized procedure to be more logical if the desired goal is to maximize the size of the debtor’s estate and pay out claims according to the pari passu principle.

C. Modified Universalism

In practice, neither the universality nor the territoriality principle is likely to be observed in pure form. More likely is a hybrid of some sort. Modified universalism is one example, and this principle is evident in the American Bankruptcy Code. Conflicts tend to arise between a debtor’s principal place of business, on the one hand, and a foreign country in which the debtor’s assets are located, on the other hand. Therefore, it becomes necessary to view the insolvency proceeding first from the perspective of the domicile of the debtor – the so-called “domiciliary,” or “principal,” or “home” forum – and then to consider the likely reactions of foreign jurisdictions – the ancillary forum – to the operation of the laws of the home forum. 123 This two-step approach is modified universalism. The first step is the universality principle, and the second step is its modification to account for the reality of conflicts.

What will be the state of affairs in the ancillary forum during this two-step process? Either no bankruptcy proceedings will have started, or parallel proceedings will have commenced. 124 Once bankruptcy proceedings have begun in the home forum, the insolvency administrator wishing to gather the debtor’s overseas assets must be able to freeze local attachments of those foreign assets, freeze dealings with the assets by the debtor, and compel a turnover of the foreign assets or their proceeds to the home forum for distribution to creditors. 125 This is a tall order, but not an impossible one.

The insolvency administrator has three main options: (1) it can attempt to collect the debtor’s foreign assets locally without local proceedings, possibly through an assignment or power of attorney; (2) it can seek the aid of the local court by getting recognized as a (or the) representative of the debtor; or (3) it can commence bankruptcy proceedings locally, either via an ancillary proceeding or a full proceeding. 126 Under United States law (specifically, Section 304 of the Bankruptcy Code, discussed below), when a multinational debtor or its creditors file a petition of bankruptcy, the court of the forum country appoints a representative for the debtor. 127 The appointed representative takes possession of the debtor’s assets and either sells them in a liquidation or uses them for a corporate re-organization. Most bankruptcy regimes, including those in the United States, Canada, and the United Kingdom,
claim jurisdiction over the assets of a filing debtor wherever located, including assets located in other nations. Accordingly, under these regimes, the debtor’s representative can take possession of assets in other nations, just as a purchaser from the debtor could in the absence of bankruptcy.

In the American Bankruptcy Code, Section 304 – a proceeding of interest in the BCCI affair, among many other cases – is the key provision permitting this result. Section 304 authorizes the qualified representatives of foreign bankruptcy estates to seek assistance by filing an ancillary proceeding in the United States. Section 304(a) states:

(a) A case ancillary to a foreign proceeding is commenced by the filing with the bankruptcy court of a petition under this section by a foreign representative.

The debtor or creditors filing the case can determine which country will serve as the main forum. To be sure, the American standard for recognition constrains the choice of a country; however, it still leaves a particular debtor free to choose among several countries. The assistance provided to the foreign representative is evident from Section 304(b):

(b) Subject to the provisions of subsection (c) of this section [discussed below], if a party in interest does not timely controvert the petition, or after trial, the court may –

(1) enjoin the commencement or continuation of –

(A) any action against –

(i) a debtor with respect to property involved in such foreign proceeding; or

(ii) such property; or

(B) the enforcement of any judgment against the debtor with respect to such property, or any act or the commencement or continuation of any judicial proceeding to create or enforce a lien against the property of such estate;

(2) order turnover of the property of such estate, or the proceeds of such property, to such foreign representative; or

(3) order other appropriate relief.

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128 See LoPucki, supra note 106, at 726.
129 See id.
132 See LoPucki, supra note 106, at 726.
133 See id.
134 11 U.S.C. § 304(b) (emphasis added).
As is apparent from the italicized language, the assistance provided by Section 304(b) allows the qualified representative to do its job of marshaling assets, including those located in the United States, and paying out claims to creditors around the world.

A touchstone of modified as distinct from pure universalism is the ability to refuse cooperation that may prejudice creditors in one country. This refusal is found in the American Bankruptcy Code in Section 304(c), where one of the important concerns is prejudice against American creditors.135

(c) In determining whether to grant relief under subsection (b) of this section, the court shall be guided by what will best assure an economical and expeditious administration of such estate, consistent with –

1. just treatment of all holders of claims against or interests in such estate;
2. protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
3. prevention of preferential or fraudulent dispositions of property of such estate;
4. distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;
5. comity; and
6. if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.136

Thus, Section 304(c) – reflecting the modified universalist impulse – relieves the courts of the non-forum country (here, American courts) from the unpleasant obligation they would have under pure universalism to sacrifice their own (American) creditors’ interests for the benefit of foreigners.137

Modified universalism is, then, a pragmatic accommodation. It is not, however, a problem-free one. Among its disadvantages are uncertainties regarding choice of law, because the forum proceeding plus the ancillary proceedings create dozens of extra complex proceedings.138 In addition, because Section 304 allows the debtor or creditor filing the petition to choose among countries to determine the forum proceeding, the process becomes particularly subject to strategic manipulation.139

135 See LoPucki, supra note 106, at 728.
136 11 U.S.C. § 304(c) (emphasis added).
137 See LoPucki, supra note 106, at 728.
138 See id. at 729.
139 See id. at 730.
D. Secondary Bankruptcy

Secondary bankruptcy is yet another principle around which a country can organize the international aspects of its insolvency regime. Under this principle, bankruptcy proceedings go forward simultaneously in each country in which the debtor has a substantial presence. As is true under modified universalism, under secondary bankruptcy, the proceeding in the debtor’s home country is the “main” proceeding. The courts of all other relevant nations are expected to surrender assets of the debtor for distribution. (The converse situation is not true, i.e., should there be any overage of assets in the main proceeding, there does not seem to be any expectation that they would be distributed pro rata in the secondary proceedings, discussed below. At the same time, such a distribution is not expressly ruled out.)

However, secondary bankruptcy proceedings are implemented. In contrast to an ancillary proceeding, which only assists the main proceeding, a secondary bankruptcy proceeding is the same proceeding that would be filed even if no foreign proceedings were pending. In a secondary bankruptcy proceeding, the court reorganizes or liquidates the debtor’s local assets and makes the necessary distributions to protect creditors entitled to priority under local law. Thereafter, the court transfers any remaining proceeds of the debtor’s local assets to the estate in the main case, whereupon they are available for distribution according to the priority rules of the home country.

Plainly, secondary bankruptcy is a hybrid of universalism and territoriality, because part of the debtor’s assets (those in countries outside the home forum) are distributed according to local priorities. This smacks of the territoriality principle. The fact that any remainder is distributed according to home country priorities bespeaks the influence of the universality principle. Equally plain is that secondary bankruptcy is somewhat closer to the territoriality principle than modified universalism. Modified universalism does not call for the protection of local creditors before turning over assets to a foreign trustee, whereas that is the hallmark of secondary bankruptcy.

E. Corporate-Charter Contractualism

Professor Rasmussen has offered yet another hybrid principle on the continuum between universality and territoriality. He emphasizes the ability of firms to specify in their corporate charters the country that would administer their bankruptcies. The courts of all jurisdictions would be bound to enforce those charters, save for instances in which the results would be “unreasonable and unjust.” Indeed, the debtor not only would be able to select a
country, but also could determine the system for cooperation among countries. The debtor’s choice would be limited in only one major respect: the debtor could not direct one country to apply the bankruptcy law of another country.

The emphasis on what the debtor says in its corporate charter accounts for the name of this hybrid, and there are some obvious advantages. First and foremost, there is respect for what in conflicts of law is called “party autonomy.” Organizers of a corporation get to select the law in which they incorporate, and that law governs all of their corporate affairs. Why should they be any less free to select the law that will govern their firm’s liquidation or re-organization? Moreover, there is no harm to creditors. Any prospective creditor can see from the charter what law will govern an insolvency proceeding. If a prospective creditor does not like the law, then it can forsake the debtor. Finally, there is the advantage of a unified proceeding under a single law. In this respect, corporate-charter contractualism veers toward universality on the universality – territoriality continuum, albeit as a result of private rather than public decision-making.

While free marketeers thus may be inclined to corporate-charter contractualism, there are some concerns. First, sovereignty may rear its head. Will every country really agree that a private company’s choice of law should override what might be regarded as a sovereign decision, namely, the decision of what law to apply in insolvency? Second, might there be room for strategic behavior by debtors? They can scour the globe looking for the most pro-debtor law on the available pro-debtor – pro-creditor continuum. Third, is there a possibility of a “race to the bottom”? That is, could powerful multinational corporations bully less potent sovereign governments into enacting all-too-pro-debtor insolvency laws as a condition for foreign direct investment in those countries? All of these concerns are reason for some pause with respect to the laissez-faire orientation of corporate contractualism.

F. Cooperative Territoriality

Cooperative territoriality, another hybrid principle for the international aspects of a country’s insolvency law, recognizes other countries’ rights of territoriality. In this respect, it lies closer to the territoriality end of the universality – territoriality continuum. Under the cooperative territoriality principle, bankruptcy courts in one country will administer the assets of a multinational debtor within the borders of that country as a separate estate. If a debtor has significant assets in several countries, then several independent bankruptcy cases might occur. None of these cases will be considered “main,” “ancillary,” or “secondary.” In effect, they all will be of equal stature.

What rationale underlies cooperative territoriality? To answer this question, it is useful to recall that the main aim of pure universalism, facilitating a worldwide reorganization or worldwide sale of the debtor’s assets, can be implemented only if the home

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147 See id.
148 See id.
149 See id. at 744.
150 See id.
country exercises jurisdiction over the entire group of assets and claims. This “group” jurisdiction is intensely problematic in reality, because it broadens bankruptcy jurisdiction beyond acceptable limits. Cooperative territoriality attempts to solve this problem by “severing” the firm (that is, its links to assets and liabilities overseas) at the national border. The principle thus creates an incentive for multinational corporations to compartmentalize their operations by country, thereby further reducing the damage. However, exactly how cooperative territoriality solves this problem in particular cases is not entirely clear.

V. THE PROBLEM OF RECOGNITION

The universality – territoriality continuum does more than provide a range of principles around which a country can organize the international aspects of its bankruptcy laws. It highlights the fundamental problem of recognition, that is, whether one country will give legal effect to insolvency proceedings conducted in another country. It is not unduly optimistic to see an increasing tendency internationally to recognize the right of a foreign administrator from the home forum of the debtor to collect local assets, as well as an increasing tendency to recognize the automatic stay of creditor executions (though this freeze sometimes takes effect only after local recognition proceedings have begun).

Having said this, the fact remains that most countries now allow concurrent proceedings to be opened, whether they be ancillary or full. Thus, in practice the unilateral efforts of a foreign trustee typically are overtaken rather quickly by local proceedings that “guillotine” any further attachments. The effect of these local proceedings is to allow the local jurisdiction to give effect to its own bankruptcy laws. Under those laws, the issues become (1) choosing what law applies, (2) deciding whether local creditors are paid first, and (3) determining whether the local forum will turn over local assets to the foreign forum that may, in turn, go to pay creditors in a different order from that contemplated under local law, or that may go to finance a foreign rehabilitation proceeding as opposed to a final bankruptcy.

The central issue in all this is whether the local jurisdiction recognizes foreign insolvency proceedings and, if so, the extent of such recognition. Recognition may be mandatory, discretionary, or selective (i.e., with respect to certain issues). Other forms of recognition include retroactive recognition, non-retroactive recognition, and recognition limited to asset collection.

As intimated above, recognition is a question of degree. That is to say, once again, there is a continuum, a “Recognition Continuum,” depicted in Chart 3 below. At one

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151 See id.
152 See id.
153 See Wood, supra note 72, at 242.
154 See id.
155 See id. at 243.
156 See id.
157 See id.
extreme is complete recognition. It amounts to the faithful execution of the universality – or, better yet, the unity – principle. There appear to be few (if any) countries at this extreme.

At the other end of the continuum is total non-recognition. Here, the territoriality principle is followed. This extreme means that, in the absence of a treaty, a country does not recognize a bankruptcy proceeding in the principal foreign forum, and hence does not give it any local effect over local assets.\footnote{158} The result is that the administrator in the home forum has no status to collect assets in the country. At the risk of a pejorative connotation, the country is the ultimate “obstructionist.” Examples include Argentina, Austria, Denmark, and Norway. None of these countries recognizes foreign bankruptcies, so a foreign trustee is powerless to collect local assets.\footnote{159}

**Chart 3: The Recognition Continuum**

<table>
<thead>
<tr>
<th>Total Non-Recognition</th>
<th>Complete Recognition</th>
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<tbody>
<tr>
<td>(Territoriality Principle)</td>
<td>(Universality or Unity Principle)</td>
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Japanese insolvency regime is without doubt at or near the total non-recognition end of the continuum. A bankruptcy procedure commenced outside Japan is not effective with respect to the properties of the debtor located in Japan.\footnote{160} That is, no recognition exists at present, a deficiency discussed in more detail in Part Three below. Indeed, Japan’s Bankruptcy Law does not contain any mechanism for recognizing a foreign bankruptcy procedure.\footnote{161} But, there is some relaxation of this territorial policy, as evidenced below.

In between these extremes are full or partial recognition. In this vast middle, the insolvency proceeding in the domiciliary forum achieves a measure of recognition in other countries with respect to freezes on execution and collection, with or without local recognition proceedings.\footnote{162} The United States stands in between these extremes. In a case where a debtor is subject to a foreign bankruptcy proceeding outside the United States, and foreign creditors want to place assets located in the United States under the control of a foreign insolvency representative, there are three possible options: (1) no proceeding in the United States; (2) a concurrent bankruptcy proceeding in the United States; or (3) an ancillary proceeding in the United States.\footnote{163} Under the first option, there is immediate recognition without the necessity

\footnote{158} See id.  
\footnote{159} See id.  
\footnote{160} See id. at 268-269.  
\footnote{161} See id.  
\footnote{162} See id. at 244.  
\footnote{163} See id. at 259-260.
of any court proceedings. In other words, the foreign forum recognizes the bankruptcy proceeding in the forum without any formal recognition proceeding in the foreign forum. This option is mostly taken by the American Bankruptcy Code.\textsuperscript{164} The recognition entitles the foreign insolvency representative to collect local assets, and it freezes creditor attachments of local assets and the powers of the debtor to dispose of local property.\textsuperscript{165}

At bottom, the most practical problem with respect to the international effect of insolvency proceedings is whether, and to what extent, each relevant country is willing to cooperate with a principal foreign proceeding or to allow for the intra-territorial effect of multiple foreign proceedings.\textsuperscript{166} There is a reform movement emerging in international insolvency law toward greater cooperation in international insolvencies.\textsuperscript{167} The end point may be universality, though the world is nowhere near that point yet. Ancillary proceeding conducted under the auspices of Section 304 of the American Bankruptcy Code are a hopeful sign in this reform movement. Other examples come from Europe, through possible conventions and new domestic laws, and the International Bar Association, which has prepared a model act. Yet another positive example is found in Japan, which is making efforts to relax its territoriality policy and creating preliminary drafts of a reform law and a bilateral treaty.\textsuperscript{168}

The reforms on the table or drawing board for cooperation in international insolvency cases vary country to country. The two main methods for implementation have been through domestic law reform and/or focusing on international conventions/treaties. Whatever method is used, what is required is deliberate cooperation with foreign laws within a country’s own legal and economic policy. A simple waiver of jurisdiction or submission to foreign laws is not enough.\textsuperscript{169} As discussed more fully in Part Three below, in Japan, the key barrier to increased international cooperation is its current legislative policy of territoriality.\textsuperscript{170}

VI. THE UNCITRAL MODEL FOR INTERNATIONAL INSOLVENCY LAW

Perhaps the most hopeful sign of all as regards greater international cooperation on the problem of recognition comes from the United Nations Commission on International Trade Law (UNCITRAL). On 30 May 1997, UNCITRAL adopted the text of a Model Law on Cross-Border Insolvency.\textsuperscript{171} To be sure, a model law had to be used instead of a convention,

\textsuperscript{164} See id.
\textsuperscript{165} See id.
\textsuperscript{167} See Tagashira, supra note 166, at 3.
\textsuperscript{168} See id.
\textsuperscript{169} See id.
\textsuperscript{170} See id.
\textsuperscript{171} See Berends, supra note 108, at 312. Work on the Model Law commenced in 1995, and it
because a convention would hold no effect if it were not ratified, and it seemed unlikely that a large number of countries would ratify such a convention. Why? Harmonization of insolvency law across borders is difficult, because this area of law is akin to a symphony. Just as a symphony is made up of many different kinds of musical instruments that must work perfectly together, insolvency law consists of many parts – contracts, corporate law, civil procedure, etc. – that must fit together. Any attempt to unify insolvency law thus entails a gargantuan effort: the unification of many other bodies of law. This task is perhaps too ambitious for the present.

Nevertheless, the Model Law is an impressive achievement. In the long run, it may be a stepping stone toward harmonization, toward a single “world law” on insolvency. Just as creditors of American railway companies in the late nineteenth and early twentieth century were scattered across state lines, as were the assets that they looked to for satisfaction, creditors of modern corporations in the global economy, and the assets of those firms, are scattered across national boundaries. And, just as railway creditors as a whole could be better off by a federal bankruptcy statute that inhibited destructive grab races, multinational corporate creditors can be better off by a unified insolvency law that preserves the highest value of the debtor’s estate for re-organization or liquidation.

In the nearer term, the Model Law has persuasive power. Countries can look to it as a paragon embodying internationally agreed-upon principles when they contemplate revising or drafting anew their own insolvency regimes. To the extent countries do indeed use the Model Law, confidence among investors, traders, and banks may be enhanced. After all, if bankruptcies cannot be resolved under the same set of rules around the world, then the second-best solution is that they be resolved in as consistent and transparent a manner as possible regardless of the forum in which cases happen to be brought.

The basic purpose of the UNCITRAL Model Law is to provide an effective mechanism for dealing with cases of cross-border insolvency. This Law is based on nine principles, which are as follows:

First: The court of the enacting State shall recognize only one foreign proceeding as a foreign main proceeding.

Second: The recognition of a foreign proceeding shall not restrict the right to commence a local proceeding.

Third: A local proceeding shall prevail over the effects of a foreign proceeding


See Berends, supra note 108, at 319.

See id. at 323.
and over relief granted to a foreign representative, regardless of whether
the local proceeding was opened prior to or after the recognition of a
foreign proceeding.

Fourth: When there are two or more proceedings, there shall be cooperation and
coordination.

Fifth: A foreign proceeding shall be recognized as a foreign main proceeding
if the foreign proceeding is opened in the State where the debtor
maintains the center of his main interests. A foreign proceeding shall be
recognized as a foreign non-main proceeding if the foreign proceeding
is opened in a State where the debtor has an establishment.

Sixth: Upon recognition of a foreign proceeding as a foreign main proceeding,
some types of relief will come into effect automatically. They will be in
effect until modified or terminated by the court. Upon recognition of a
foreign proceeding as a foreign main proceeding, some other types of
relief may be granted by the court, but they will not come into effect
automatically. Upon recognition of a foreign proceeding as a foreign
non-main proceeding, relief can only come into effect if it is granted by
the court.

Seventh: Coordination may include granting relief to the foreign representative.
In granting relief to a foreign representative of a foreign non-main
proceeding, the court must be satisfied that the relief relates to assets
falling under the authority of the foreign representative.

Eighth: Creditors shall be allowed to file claims in any proceeding. Payments
to creditors from multiple proceedings shall be equalized.174

Ninth: If there are surplus proceeds of a local non-main proceeding, they shall
be transferred to the main proceeding.175

It should be apparent from these core principles that the Model Law is based on a minimalist
philosophy: nothing in the Law should prevent legislators from giving more rights to foreign
creditors than to local creditors.176 (This minimalist approach does no damage to the national
treatment analogy from international trade law mentioned earlier. National treatment under
Article III of the General Agreement on Tariffs and Trade (GATT) does not bar better
treatment for imported goods than for like domestic products.) It also should be apparent that,
while the Model Law clearly rejects territorialism, it is not perfect in its adherence to the

174 This is the so-called “Hotchpot” rule, which derives from English insolvency law. It is set
forth in Article 32 of the Model Law. The idea is that if a creditor recovers X percent in one foreign
proceeding (e.g., in the United States), and then tries to recover more in a second foreign proceeding (e.g.,
in Japan), the court in the second foreign proceeding (Japan) will bar any further recovery for this creditor
until other creditors in the second proceeding have gotten X percent. The rule is a move away from
territoriality. Under a pure territorial approach, the court (e.g., in Japan) could not take account of any
collection by the creditor in a foreign insolvency proceeding (e.g., in the United States). After all, other
insolvency proceedings are neither recognized nor enforced. See UNCITRAL Guide, supra note 166, at 64.

175 See Berends, supra note 108, at 321-322.

176 See id. at 344.
universality principle. The First and Fourth-Sixth points steer in that direction, but the Second and Third do not.

In other words, the Model Law is somewhat of a “mixed bag,” perhaps reflecting the pragmatic accommodation required to get a consensus among UNCITRAL delegates. Under the Model Law, recognition of a foreign proceeding and any relief granted are given effect either automatically or through a court order. Concurrent proceedings may take a variety of forms. The court of the enacting State is required to decide whether it will recognize a foreign proceeding as a foreign main proceeding or as a foreign non-main proceeding. Any concurrent proceeding is governed by three rules. First, the effects of a foreign proceeding must always be adjusted to the effects of a local proceeding. Second, the effects of a foreign non-main proceeding must always be adjusted to the effects of a foreign main proceeding. Third, the effects of more than one non-main proceeding must be adjusted to each other. These adjustments are possibly the best illustration of the pragmatic bargain the Model Law seems to strike.

To what extent are countries – in particular, Japan and the United States – likely to adopt the Model Law? Japan is not likely to adopt the Model Law as a whole, provision-by-provision. The wording of, and concepts embedded in, the Model Law are appropriate for an Anglo-American common law system. They do not fit so easily into the Japanese legal system (discussed in the Appendix). Thus, not surprisingly, two bills were introduced during the 105th session of the United States Congress that would have incorporated the Model Law almost verbatim into the American Bankruptcy Code. The bills would have created a new Chapter 15 to the Code for the provisions of the Model Law. Unfortunately, both bills were defeated, though not because of any controversy over the Model Law. Rather, issues surrounding consumer bankruptcy and Chapter 13 sent the bills down. However, very similar legislation has been introduced in the 106th Congress, and it seems inevitable that the United States will – sooner or later – incorporate the Model Law into its Bankruptcy Code.

As for Japan, there appears to be a strong momentum to integrate the essential parts of the Model Law into the insolvency regime. Fitting these parts into the regime is the

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177 Id. at 349-350.
178 Id. at 385.
179 Id. at 387.
180 The author is grateful to Professor Junichi Matsushita, Faculty of Law, Gakushuin University. He patiently explained the problems of Model Law implementation at a meeting on 12 July 1999, and kindly provided a copy of his excellent paper on the Model Law. See Junichi Matsushita, UNCITRAL Model Law and the Comprehensive Reform of Japanese Insolvency Laws (March 1999) (unpublished manuscript, submitted for publication).
182 The “First Questionnaire” (“Kentou-Jikou”) publicized in December 1997 by the Advisory Committee for the Reform of Insolvency Laws, Civil Bureau of the Ministry of Justice, raises various issues relating to international insolvency, including the scheme of recognition of foreign main proceedings.
challenge. More than just a change of wording is necessary. For instance, the Model Law contains provisions that impart discretionary power to judges. Yet, concerning the authority to create a remedy, judicial discretion is more constrained in Japan than in the United States, and even than in France or Germany. As an example, Article 21 of the Model Law says that “the court may, at the request of the foreign representative, grant any appropriate relief, including:” and then lists seven possibilities, (a) through (g), where (a) through (f) are measures that are expressly spelled out, and (g) states “granting any additional relief that may be available to [insert the title of a person or body administering a reorganization or liquidation under the law of the enacting State] under the laws of this State.” This provision would not fit within the Japanese legal context because of the discretion it imparts to judges. The larger point, then, is that Japanese officials and legal scholars will have to import the Model Law only after carefully examining each and every provision at the border and making adjustments – additions, deletions, and the like – to fit in the Japanese legal context.
I. CAUSES OF BANKRUPTCY

What causes bankruptcy? The question usually is thought of as an economic one, and Part One, above, followed this conventional approach by examining the Japanese economic crisis as a pretext for bankruptcy. This pretext, however, leads to the legal dimension of the question, for what “causes” bankruptcy in the mind of the businessperson has to be translated into legal justifications for the filing of an insolvency petition. The translation is not always intuitive. Indeed, in Japan’s case, the translation is monstrously complex. There are many possibilities, and many sources of law, thus creating the accurate impression – at least to outsiders – that Japan’s insolvency regime is neither streamlined nor easily workable.

Presently, the Bankruptcy Law recognizes three causes of bankruptcy: (1) insolvency; (2) suspension of payment; and (3) an excess of liabilities over assets (i.e., a balance sheet test). These causes operate regardless of any international dimensions to a case. That is, it does not matter whether the debtor has assets overseas – the same causal tests are applied. This conclusion is nowhere stated expressly, but the absence of a provision to the contrary suggests it is a reasonable inference to draw.

Use of the word “insolvency” as a cause is a bit confusing. It means an obligor cannot cover its indebtedness. Accordingly, the primary purpose of an insolvency proceeding is to provide the greatest distribution to creditors. The term “insolvency” thus must be understood in context. It is often used interchangeably with the word “bankruptcy,” and indeed has been employed in this manner throughout this paper. However, when thinking of the causes of bankruptcy under Japanese law, it is “bankruptcy” that is the generic term, and “insolvency” is simply one of three sub-categories. Of these three causes, insolvency is by far the most important, and the focus below shall be on this cause with respect to corporate debtors.
II. TYPES OF INSOLVENCY PROCEEDINGS

It is often said that there are five different types of insolvency proceedings under Japanese law. It is, thereafter, commonly indicated that two of the five are liquidation proceedings, while the remaining three (corporate reorganization, company arrangement, and composition) involve rehabilitation of the debtor, i.e., corporate reorganization. The idea of “five” types can be confusing for an outsider. The point is that since 1922, Japan has enacted four statutes that bear on bankruptcy. They are the (1) Bankruptcy Law of 1922, (2) Composition Law of 1922, (3) Commercial Code of 1938, and (4) Corporate Reorganization Law of 1952 (enacted during the Occupation, and bearing the influence of the American Bankruptcy Code as it then existed). (As noted later, the Commercial Code includes two chapters, one providing for special liquidation and one for reorganization (specifically, company arrangements)). The dates of these sources of law ought to be underscored. There have been no major changes to the legal regime in nearly half a century (with the exception of special legislation in 1996, discussed below, designed for failed banks). This fact in itself is stunning given the changing fortunes of the Japanese economy and developments in the global economy in post-Second World War era.

The point is that to say there are five different types of insolvency proceedings in Japan masks the fact that there are really four different sources of law – three statutes (the Bankruptcy Law, Composition Law, and Corporate Reorganization Law) plus the Commercial Code – that govern insolvency proceedings. As for the conceptually distinct question of how many types of proceedings exist, the answer – five – is depicted in Table 1 below. These types are likely to be equally applicable regardless of any international dimensions to the case at hand, i.e., while there may be serious intra- or extra-territorial issues at stake (as discussed later), the availability of these procedures does not usually turn on the international dimensions to the case. This conclusion is nowhere stated expressly. Rather, the inference is drawn from the silence of Japan’s legal regime on the point.

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188 See id.


193 See Ito, supra note 186, at 178.
Table 1: Conventional Categorization of Japanese Insolvency Proceedings

<table>
<thead>
<tr>
<th>Broad Classification: Liquidation or Rehabilitation?</th>
<th>Specific Procedure?</th>
<th>Source of Law Governing the Procedure?</th>
<th>Who is Eligible to Use the Procedure?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liquidation</td>
<td>Bankruptcy</td>
<td>Bankruptcy Law</td>
<td>Any kind of debtor (natural or legal person)</td>
</tr>
<tr>
<td>Liquidation</td>
<td>Special liquidation</td>
<td>Commercial Code</td>
<td>Only a stock corporation</td>
</tr>
<tr>
<td>Rehabilitation</td>
<td>Corporate reorganization</td>
<td>Corporate Reorganization Law</td>
<td>Only a stock corporation</td>
</tr>
<tr>
<td>Rehabilitation</td>
<td>Composition</td>
<td>Composition Law</td>
<td>Any kind of debtor (natural or legal person)</td>
</tr>
<tr>
<td>Rehabilitation</td>
<td>Reorganization (of a company), also known as company arrangement</td>
<td>Commercial Code</td>
<td>Only a stock corporation</td>
</tr>
</tbody>
</table>

Clearly, the five procedural devices are divided into two broad categories, liquidation and rehabilitation. There are two types of liquidation procedures, one set forth under the Bankruptcy Law, known simply as bankruptcy, and a so-called special liquidation procedure created by the Commercial Code. There are, in addition, three types of reorganization procedures: corporate reorganization under the Corporate Reorganization Law; composition (including compulsory composition) under the Composition Law; and reorganization of a company under the Commercial Code, which is also known as a company arrangement.

Significantly, not every debtor is eligible for every kind of procedure. Only the bankruptcy and composition procedures can be applied to all debtors, whether natural or legal persons. Corporate reorganization, special liquidation, and the reorganization of a company under the Commercial Code are avenues reserved for stock companies. These avenues are, of course, available to any company located in Japan, regardless of its place of incorporation. To put the point differently, corporate debtors can avail themselves of all five procedures. Debtors other than stock companies are confined to either liquidation through bankruptcy or rehabilitation through composition.

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194 See id.
III. THE MECHANICS OF INSOLVENCY PROCEEDINGS

As explained earlier, when a Japanese corporate debtor goes bankrupt by reason of insolvency, as defined above, any of the five legal proceedings may be occur. How exactly do these procedures work? This question is addressed below. The four most significant possibilities – corporate reorganization, company arrangements, compositions, and liquidation through bankruptcy are discussed in turn below. In Table 2 below, the principal features of each of these possibilities are summarized.

A. Corporate Reorganization

Japan’s Corporate Reorganization Law is the longest and most comprehensive of all the reorganization regimes. The goal of a corporate reorganization is to bring about “sustenance and regeneration of the business of a limited company . . . of which, despite its financial difficulty, there is a prospect of rehabilitation.” The contrast with liquidation should, then, be obvious. If a stock company chooses to liquidate, then its assets are distributed on a pro rata basis among the company’s creditors. Upon reorganization, however, a company continues as a going concern. 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.

In other words, the justification for reorganization is the proverbial “the whole is greater than the sum of the parts.” Reorganization is, at bottom, the restructuring of a company’s debt and equity in a way that is acceptable to all relevant parties.

As indicated earlier, stock limited liability companies may take advantage of either the corporate reorganization or company arrangement proceedings. Generally, however, corporate reorganization is restricted to complex reorganizations involving large limited liability companies that anticipate dealing with uncooperative secured creditors.

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196 Liquidation through special proceeding under the Commercial Code is omitted. The procedure was used in the BCCI – Tokyo branch affair, and is discussed above. See supra note 2 and accompanying text.

197 See Shea & Miyake, supra note 195, at 249.

198 Corporate Reorganization Law, supra note 192, at Art. 1.


200 Id.

201 See id. at 244.

202 See id. at 245.

203 See id.
<table>
<thead>
<tr>
<th>Type of Proceeding</th>
<th>Causes of Bankruptcy that Trigger the Proceeding</th>
<th>Scope of the Stay on Creditor Action</th>
<th>Status of Management of the Debtor</th>
<th>Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate reorganization</td>
<td>(1) Company cannot pay its debts, or (2) Bankruptcy is likely.</td>
<td>Stay blocks actions by secured creditors.</td>
<td>Trustee must displace management of the debtor.</td>
<td>Reorganization plan must be fair and equitable. Creditors, shareholders, and the court must approve the plan. “Cram down” is possible.</td>
</tr>
<tr>
<td>Company arrangement</td>
<td>Can be commenced at a very early stage, namely, it is probable that (1) the company is unable to pay its debts, or (2) that the company’s liabilities exceed its assets.</td>
<td>Stay blocks actions by secured creditors at the discretion of the court.</td>
<td>Trustee does not displace company management except in extreme circumstances.</td>
<td>No legal criteria for elements of the plan. But, plan must be approved by all creditors. Approval of court is not necessary.</td>
</tr>
<tr>
<td>Composition</td>
<td>Any of the three causes of bankruptcy, i.e., (1) debtor is unable to pay its debts, (2) debtor has suspended payment of its debts, or (3) debtor’s liabilities exceed its assets.</td>
<td>Stay does not block actions by secured creditors.</td>
<td>Company’s management is not displaced.</td>
<td>Plan must be fair and equitable. Plan must be approved by unsecured creditors and court.</td>
</tr>
<tr>
<td>Liquidation under Bankruptcy Law</td>
<td>Same as composition, above.</td>
<td>Stay does not block action by secured creditors.</td>
<td>Trustee must displace management of debtor.</td>
<td>Not applicable.</td>
</tr>
</tbody>
</table>

A company may initiate a corporate reorganization when it “is unable to pay its obligations that are due without exceedingly impeding continuation of its business,” or “where
the facts comprising causes of bankruptcy are likely to take place with respect to the
company." To begin the proceedings the company must file an application for
commencement of reorganization proceedings. Upon filing, the applicant must pay court
costs in advance. A court’s mandate is fairly clear. It “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.”

In corporate reorganizations, both interim and permanent stays of proceedings
by creditors against the debtor are available. “A stay of proceedings prevents creditors form
realizing on the assets of the insolvent company.” Stays are essential, because they limit the
possibility of hold outs, i.e., of one or more creditors not agreeing to a reorganization plan in
the hopes of obtaining a better deal. Because each creditor in a negotiated reorganization are
motivated by self-interest, each tends to “hold out” for the terms most favorable to its
circumstances. Holding out creates several problems, including: (1) the value of the
company as a going concern may fall while waiting for creditor approval; (2) impatient
secured creditors may enforce their security by realizing on their collateral; and (3) unsecured
creditors may “request the court to enforce their debts against the company’s unsecured
property.” Statutory reorganization regimes combats these evils by giving the court
supervisory power, and utilizing the device of the stay.

In a corporate reorganization, the court has discretion to ordering interim stays
that protect the debtor between the time of filing and the actual commencement of the
reorganization proceeding. Once the reorganization order is issued, the automatic stay
protects the debtor company throughout the reorganization period. It must be stressed that
the stay is unique to the corporate reorganization context. Under Japanese law, corporate
reorganization “is the only procedure of the four [reorganizations, company arrangements,
compositions (including compulsory compositions), and liquidations] 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

204 Corporate Reorganization Law, supra note 192, at Art. 30, ¶ 1.
205 See id. at Art. 30.
206 See id. at Art. 34.
207 Shea & Miyake, supra note 195, at 255; Corporate Reorganization Law, supra note 192, at
Art. 38.
208 See Shea & Miyake, supra note 195, at 250.
209 Id. at 247.
210 See id. at 247.
211 See id. at 245.
212 Id. at 246.
213 See id. at 250.
214 See Corporate Reorganization Law, supra note 192, at Art. 67.
creditors are encountered.”

In this respect, it is the only analog in Japan’s insolvency regime to Section 362 of the American Bankruptcy Code.217

Of course, assets of a corporate debtor may begin to dissipate well before the court has had a chance to issue a reorganization order. Consequently, courts are empowered to take measures prior to the commencement of a corporate reorganization in order to preserve the property and assets of the debtor.218 Usually, they do so by appointing an interim trustee, who has the exclusive right to manage the business and property of the company, albeit under the court’s supervision.219 This appointment harbingers the end of management control over the company. “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.”220 When the corporate reorganization proceeding begins, management loses control of the company, and control over corporate assets formally and finally passes to the court-appointed trustee.221

One of the trustee’s most important responsibilities is to draft a reorganization plan and submit it to the court.222 The plan obviously must be fair and equitable. It is subject to amendment by interested parties unless and until the court finds no further changes are necessary. The process of negotiating over amendments can be tortuous and lengthy.

When the court ultimately determines no more amendments are needed, it “will refer the plan to the creditors and shareholders to be considered for acceptance.”223 Creditors – secured and unsecured – plus shareholders vote on the plan,224 though a “cram down” is possible (as it is under the American Bankruptcy Code). Voting is divided into the classes of interested parties depending on priority interest, e.g., secured creditors, unsecured creditors, preferred shareholders, regular shareholders, etc. The requisite majority for approval of the plan varies with each class.225 After creditors and shareholders accept the plan, the court must approve it.226

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216 Shea & Miyake, supra note 195, at 249 (emphasis added). As indicated below, in a company arrangement, at the discretion of the court, the automatic stay can be used to block actions of secured creditors.


218 See Shea & Miyake, supra note 195, at 251.

219 See id.

220 Id. at 250.

221 See id. at 251.

222 See Corporate Reorganization Law, supra note 192, at Art. 189.

223 Shea & Miyake, supra note 195, at 253; Corporate Reorganization Law, supra note 192, at Arts. 199-200.


225 See id. at 254.

The court holds a hearing at which the debtor company, its receivers, creditors, shareholders, and any guarantors 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. Thus, approval of the plan after affirmative creditor and shareholder votes is hardly automatic.

Corporate reorganizations can and do fail. After all, whether to choose the reorganization option is a predictive judgment about the value of the company as a whole versus its value broken up. Predictions are, by definition, subject to error. What happens under Japanese law if the prediction proves erroneous? The supervising court may declare the company bankrupt, if the court finds that any one of the three causes of bankruptcy exist. The very possibility that a court might make this declaration probably has a sort of in terrorem effect. That is, it helps ensure that only companies with a real prospect of success attempt to reorganize.

B. Company Arrangements

An old set of legal provisions governing the reorganization of a company, also known as a company arrangement, is adopted from English law provisions. This option, which does not appear to be particularly widely used, is available to limited stock companies when “it is deemed that there is a danger of its becoming insolvent or if its liabilities exceeding its assets.” In other words, a company arrangement can be commenced at a very early stage – before actual insolvency, and before liabilities actually exceed assets. This procedure is not as detailed as the reorganization process, and must not be confused with the mandates of the Corporate Reorganization Law. Rather, the source of law on company arrangement is meager: one section of Japan’s Commercial Code.

A director, auditor, creditor, or shareholder of a limited stock company may initiate a company arrangement proceeding, or a court may begin proceedings sua sponte (on its own). As in a corporate reorganization, in a company arrangement, both interim and permanent stays are available. “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.” However, in sharp contrast to a corporate reorganization, the stay provisions in a company arrangement do not automatically extend to secured creditors. Whether it does so depends on the discretion of the court. Thus, a corporate reorganization is a better option in cases where it is anticipated that secured creditors

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228 See Corporate Reorganization Law, supra note 192, at Art. 23.
229 See Shea & Miyake, supra note 195, at 245.
231 See Shea & Miyake, supra note 195, at 256.
232 Id.
Company arrangements also differ from corporate reorganizations in that the management of the debtor company is not automatically displaced. Therefore, preservation measures may be needed to protect the going concern value from negligent or willful mismanagement.\textsuperscript{234} Article 386 of the Commercial Code grants a court the power to issue assorted orders aimed at ensuring the debtor company is properly managed. For instance, the court can appoint an inspector to report on whether it is necessary to supervise or manage the affairs of the company, and the court can appoint a supervisor to watch over the company affairs.\textsuperscript{235} Should the court appoint a supervisor, then directors of the company must get the supervisor’s permission before taking certain kinds of actions. In extreme circumstances, the court may appoint an administrator to manage the company.\textsuperscript{236} An administrator has “the exclusive right to represent the company, administer its affairs, and manage and dispose of its property.”\textsuperscript{237} The Commercial Code also allows the court to order measures that preserve the property of the promoters, directors, auditors, and all others against whom the company may have a claim.\textsuperscript{238}

A company arrangement is commenced by a court order. Article 402 of the Commercial Code indicates a court is required to order an adjudication of insolvency pursuant to the Bankruptcy Law, when there is no reasonable prospect for reorganizing the company. If the court orders the commencement of a company arrangement, it then is entitled to appoint a Reorganization Committee to draft an arrangement plan.\textsuperscript{239} No statutory provisions exist as to what the plan should include. However, it is clear that the plan must be approved by all of the company’s creditors.\textsuperscript{240} Because the Commercial Code is silent as to whether a court must approve the plan, generally such approval is not necessary. Moreover, the court does not supervise the execution of the arrangement plan.\textsuperscript{241}

\textsuperscript{234} See Shea & Miyake, \textit{supra} note 195, at 257.
\textsuperscript{236} See id.
\textsuperscript{237} Shea & Miyake, \textit{supra} note 195, at 258.
\textsuperscript{239} See id. at Art. 391.
\textsuperscript{240} See Shea & Miyake, \textit{supra} note 195, at 259.
\textsuperscript{241} See id.
C. Compositions

The option of using the composition procedure is one that is available to both corporate and individual. Consequently, it is the most frequently used type of rehabilitation proceeding.\textsuperscript{243} When the debtor is a company, all company directors must agree on this course of action. A composition is intended to prevent the bankruptcy of the debtor.\textsuperscript{244} The key criterion for eligibility is that the “debtor is unable to pay its debts, has suspended payment of its debts, or has insufficient assets to fully perform its obligations.”\textsuperscript{245} It should be apparent that these are the three causes of bankruptcy.\textsuperscript{246}

To initiate a composition, a debtor files a composition plan at the time it files its petition for composition proceedings.\textsuperscript{247} When the plan is lodged, the court appoints an examiner to investigate the debtor’s financial condition.\textsuperscript{248} Also at the time the petition is filed, the court may order preservative measures. “Typical preservative measures include prohibitions against payment of debts, disposition of debtors’ properties, and borrowing money.” But, significantly, “[c]ourts may not stay secured creditor foreclosure

\textsuperscript{242} In addition to the composition proceeding discussed in the text, there is a procedure known as “compulsory composition.” A compulsory composition is an option only with regard to reorganizations that take place in the context of a bankruptcy. \textit{See} Shea & Miyake, \textit{supra} note 195, at 245. In addition to providing for a liquidation, Japan’s Bankruptcy Law contains provisions for a compulsory composition. \textit{See} Bankruptcy Law, \textit{supra} note 189, at Ch. IX. This procedure is carried out within a framework established by the Bankruptcy Law.

In theory, a bankrupt debtor is entitled to propose a compulsory composition at any time during bankruptcy, provided the company’s directors agree. \textit{See} Shea & Miyake, \textit{supra} note 195, at 264; Bankruptcy Law, \textit{supra} note 189, at Art. 290. In practice, companies very rarely use this option. “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.” \textit{See} Shea & Miyake, \textit{supra} note 195, at 264. In brief, a compulsory composition is an “escape hatch” for debtors from liquidation – a last chance for rehabilitation – but the hatch is usually stuck shut.

The Bankruptcy Law explains that the stay provision available in bankruptcy applies to compulsory compositions. “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.” \textit{See id.}

When a compulsory composition is proposed, parties must present the terms of the composition plan to the court. \textit{See} Bankruptcy Law, \textit{supra} note 189, at Art. 294. There are no statutory provisions on what should be included in the plan, so the bankrupt company and its creditors are free to negotiate an acceptable composition. As with other proceedings, the creditors must approve the plan.

\textsuperscript{243} \textit{See} Theodore Eisenberg & Shoichi Tagashira, \textit{Should We Abolish Chapter 11? The Evidence from Japan},” 23 J. LEGAL STUD. 111, 116 (1994).

\textsuperscript{244} \textit{See} Composition Law, \textit{supra} note 190, at Art. 1.

\textsuperscript{245} Shea & Miyake, \textit{supra} note 195, at 260.

\textsuperscript{246} \textit{See} Composition Law, \textit{supra} note 190, at Art. 12, ¶ 1. It should be noted, however, that suspension of payment itself is not a cause of bankruptcy. \textit{See supra} note 184.

\textsuperscript{247} \textit{See} Eisenberg & Tagashira, \textit{supra} note 243, at 116.

\textsuperscript{248} \textit{See id.} at 117.
proceedings.”249 “Secured creditors possess the same right of separation that they possess in bankruptcy and are therefore outside the composition procedure.”250 This right of separation allows secured creditors to enforce their rights against the bankrupt estate or company outside of the composition proceeding.251 Accordingly, stays of proceedings serve only to prevent unsecured creditors from enforcing their claims.252

When a composition proceeding is commenced, the court appoints a trustee. Unlike a trustee in a corporate reorganization, a trustee in a composition is not authorized to operate the debtor’s business.253 Rather, the trustee acts as a supervisor and performs administrative duties.254 Article 32 of the Composition Law states “the commencement of composition shall not affect the debtor’s right to manage and dispose of his assets; provided however, that any act not falling within the scope of ordinary acts shall not be done unless the consent of the [trustee] is obtained.” Thus, compositions preserve debtor autonomy to a greater degree than corporate reorganizations.

Naturally, the autonomy cannot be without bounds. While Japan’s Composition Law contains no detailed criteria for the acceptability of a composition plan, it mandates that the terms of the composition be fair and equitable.255 Moreover, the plan must meet approval from the unsecured creditors. “A plan is considered to be accepted if approved by unsecured creditors holding at least three-fourths in amount of the allowed claims and more than one-half in number of unsecured creditors who attend the meeting.”256 Finally, the court must also confirm the plan once it has met the approval of the creditors.257 As discussed at the end of Part Three below, it is possible that the Composition Law will undergo revision in the future.

D. Bankruptcy (Liquidations)

The causes of bankruptcy are the same as those of a composition: the debtor is unable to pay its debts; the debtor has suspended payment of its debts; or the debtor’s liabilities exceed its assets.258 In any of these circumstances, there is the option of liquidation pursuant to the Bankruptcy Law. The proceeding is a general liquidation one available to nearly all natural and legal persons. (The “nearly all” qualification concerns the status of foreign claims, discussed below.) Though there are some procedural differences, in substance this proceeding is very similar to Chapter VII proceedings under the American Bankruptcy Code.259

249 Id.
250 Shea & Miyake, supra note 195, at 260.
251 See Matsuo, supra note 184, at 7-22.
253 See id. at 118.
254 See id.
255 See Composition Law, supra note 190, at Art. 49.
256 Eisenberg & Tagashira, supra note 243, at 118.
257 See id.
Both obligees and obligors may file a petition for bankruptcy. When a petition for bankruptcy is filed, the court can render an adjudication on the petition simply by examining the documents submitted. Additionally, a court can order preservative measures at the time the petition is filed. When the court declares the debtor bankrupt, the court appoints a trustee. The trustee takes over the management of the debtor affairs. The trustee’s job is to convert all of the debtor’s assets into cash, and then distribute the proceeds to the obligees.

Upon conclusion of the final distribution, the trustee asks the court to set a date for the final obligees’ meeting. At that meeting, the trustee submits his final accounting to the obligees. After the final obligees’ meeting, the court orders the conclusion of the bankruptcy proceedings and gives public notice of the test of such order and the reasons supporting the orders. Since no appeal may be taken against the court order, the date of such public notice is deemed to be the date of the conclusion of the bankruptcy proceedings.

Thus, at least in comparison with rehabilitation proceedings, liquidation under the Bankruptcy Law typically is a straightforward affair.

IV. INTERNATIONAL DIMENSIONS – AND SOME PERSPECTIVES FROM INTERNATIONAL TRADE LAW

One of the grave concerns about Japan’s insolvency law regime is its lack of international dimensions. Thus the incongruity: Japan is the world’s second largest economy, Japanese corporations boast an empire of business interests around the world, and yet the regime says precious little about how to handle international aspects of an insolvency case. It is as if the insolvency regime were written in and for the most inward-looking days of the Tokugawa Period and never updated to account for changing reality of globalization. This is not to say the regime is utterly silent. There are a few sounds, three in particular: jurisdiction; the status of claims; and the recognition of foreign insolvency proceedings.

Before listening to the sounds, it is worth trying to organize what there is to hear. International dimensions of any country’s insolvency law regime may be divided into two categories: intra-territorial effects, and extra-territorial effects. The first category concerns

260 See Matsuo, supra note 184, at 7-11, 7-12.
261 See id. at 7-13.
262 See id. at 7-45.
263 Id.
264 The author is grateful to Professor Junichi Matsushita, Faculty of Law, Gakushuin University. Professor Matsushita patiently explained many aspects of the international dimensions of Japanese insolvency law, and the reform of Japan’s insolvency regime, at a meeting on 12 July 1999. He also kindly shared a copy of his excellent paper that deals with these issues. See Junichi Matsushita, Current Japanese Insolvency Law and the Comprehensive Reform Project (April 1999) (unpublished manuscript, submitted for publication).
the effect of a foreign insolvency proceeding within a country, for example, the effect in Japan of a bankruptcy case adjudicated in the United States. Recognition and enforcement is the obvious element in this category. Will decisions made by the bankruptcy court in the United States be recognized as legally valid in Japan, and enforced by a Japanese court as such?

The category of extra-territorial effects is the mirror image of the first category. At issue is the effect overseas of an insolvency proceeding in a particular country. For example, what effect would an insolvency proceeding in Japan have on the United States? In particular, will a Japanese trustee be able to collect assets of the debtor in overseas jurisdictions like the United States? In this category, then, falls the matter of jurisdiction. Also, the status of foreign claims may be considered an intra-territorial matter, because at issue is whether foreign creditors will be able to make claims in the proceedings of another country. Obviously, whether an effect is “intra-” or “extra-” territorial depends on the perspective used. In the second example, the effect on the United States of a Japanese insolvency proceeding are extra-territorial from Japan’s perspective, but intra-territorial from the American perspective.

A. Jurisdiction – And GATT-WTO Dispute Resolution

Does a court have the power to hear the case? That is the necessary starting point for any insolvency proceeding, whether or not the debtor’s affairs have cross-border dimensions. Aside from the few mentioned below, there are no direct provisions on international insolvency jurisdiction in Japan. To be sure, there are guidelines contained in Sections 105 and 107 of the Bankruptcy Law, and Section 6 of the Corporate Reorganization Law,265 that reflect relevant venue rules. Under these rules, a district court in Japan is the proper venue for a foreign debtor.266 However, these venue rules still do not get at the fundamental extraterritorial question of jurisdiction.

In the absence of specific jurisdictional rules on international insolvency matters, general jurisdictional principles are used. The gist of them is that a Japanese district court must have either ordinary or complementary jurisdiction in order to preside over an insolvency proceeding.267 Ordinary jurisdiction exists if a debtor has a center of business within the district in which the court sits, or in the case of an individual debtor, if that district is the debtor’s domicile.268 For example, if a foreign corporate debtor has one or more offices in Japan, then the district court in which the debtor’s main Japanese office is located would have exclusive jurisdiction over the case.269 If the court lacks ordinary jurisdiction, then it will analyze whether the location of the debtor’s assets give rise to complementary jurisdiction.270 In other words, complimentary jurisdiction is a fall-back: the court does not have the power to hear the case based on the debtor’s “headquarters,” but perhaps it might have the power based

265 See Tagashira, supra note 166, at 9.
266 See id.
267 See Ito, supra note 186, at 179.
268 See id.
269 See Tagashira, supra note 166, at 9.
270 See id.
Japanese courts apply these jurisdictional criteria to both foreign and domestic debtors.\textsuperscript{272} The territoriality principle, discussed in Part Two, governs the exercise of jurisdiction over a debtor’s assets located abroad.\textsuperscript{273} This principle – to which Japan subscribes – bars a Japanese court in which commencement of an insolvency proceeding is sought from exercising jurisdiction over a debtor’s assets located outside Japan. The textual bases for the lack of any extra-territorial jurisdiction are Articles 3 of the Bankruptcy Law and Article 4 of the Corporate Reorganization Law. The result is, of course, that overseas assets may be the target of execution by an individual creditor, or they may remain under the control of the debtor,\textsuperscript{274} and thus out of the reach of creditors participating in the Japanese proceeding.

Obviously, Japanese creditors are sure to be dismayed if the debtor’s overseas assets are considerable but could not be used to satisfy their claims. (If the depositor or creditor is a claimant against the Japanese branch of a foreign bank, such as BCCI-Tokyo, then that depositor or creditor may be even more disappointed. Under Japanese law, accounts of a branch that, in turn, are held at the branch’s parent (for example, in New York) are not considered to be located in Japan.)\textsuperscript{275} Why, then, does Japan’s insolvency regime take this approach?

The rationale for the territoriality principle includes some of the following propositions:

First, bankruptcy is a collective and comprehensive execution on the debtor’s assets; thus, its effect must be limited within the geographical boundary of the state’s sovereign power. Second, it would be impractical to apply the universal principle because there is no system of cooperation relating to insolvency between Japan and other countries. Third, the territorial principle would lighten the burden of trustees and facilitate proceedings.\textsuperscript{276}

However, none of these propositions is compelling. Internationally-minded academics like to believe – statutory authority notwithstanding – that insolvency administrators do have extra-territorial authority over a debtor’s assets. Thus, not surprisingly, the territoriality principle is widely, and not unfairly, criticized.

The first and third arguments are the easiest to dispose of. The first argument – that bankruptcy is a collective matter and, therefore, its effect must be limited geographically –

\textsuperscript{271} See id.
\textsuperscript{272} See id.
\textsuperscript{273} See Ito, supra note 186, at 180.
\textsuperscript{274} See id.
\textsuperscript{275} What property of the debtor is considered to be located in Japan and, therefore, subject to the insolvency proceeding in Japan? Any claim that can be enforced under the Code of Civil Procedure (Law No. 109 of 1996) is said to be located in Japan. See Bankruptcy Law, supra note 189, at Art. 3(3); Corporate Reorganization Law, supra note 192, at Art. 4(3).
\textsuperscript{276} Matsushita, supra note 187, at 73.
is a non sequitur. It is precisely because bankruptcy is a collective matter, coupled with the
debtor’s far-flung assets, that demand a single, rationalized resolution that is deliberately
ingnant of national boundaries.

As for the third argument, bankruptcy is not about the convenience of trustees. It is about satisfying creditors in an efficient and fair manner, and perhaps also allowing the possibility of a “fresh start” for the debtor so as not to create crushing disincentives for risk-taking in a capitalist market economy. Even if application of the territorial principle makes the trustee’s life easier, it does not improve the quality of that life. The trustee works with a geographically-limited asset pool, but faces a mountain of creditor claims. Would not the trustee be better off in international insolvency cases if it could satisfy a larger percentage of each claim, and a larger percentage of claims overall, through cooperative participation in a universal regime?

The second argument – that there is presently no universal bankruptcy resolution scheme – is not really an argument at all. It is merely a translation of reality into an excuse for the status quo. This is not to imply that present reality is thoroughly regrettable. Some Japanese courts appear to be departing from the “traditional territoriality doctrine with respect to the extraterritorial effect of Japanese insolvency proceedings.”277 Yet, for the most part, territoriality is still the rule in Japan. The point is that it may well be time to consider the creation of a global insolvency resolution system, whereas the second argument is defeatist.

A good model for a universalistic international insolvency regime comes from an allied field of international law, namely, international trade law. On 1 January 1995, the World Trade Organization (WTO) was born, and with it the Uruguay Round Understanding on the Rules and Procedures Governing the Settlement of Disputes (DSU) entered into force.278 The DSU marked a shift from the old-style system of resolving disputes under the General Agreement on Tariffs and Trade (GATT). That system was characterized by ad hoc mechanisms created through power-based political negotiations. The system lacked legal rigor; there were few fixed time deadlines for the procedural steps of a case, and the procedural steps themselves were not well defined. The system was plagued by the same problem that haunts international insolvency cases: a key player could decide not to participate. In the pre-Uruguay Round dispute resolution system, that meant that either party – the complainant or respondent – could block formation of a dispute resolution panel, block adoption of a panel report (assuming it agreed to the formation of the panel), and decline to implement the recommendations of the panel. Trustees around the world are in the same position as the pre-Uruguay round complainant or respondent: they can decline to participate in a sensible, world-wide proceeding.

Fortunately, during the Uruguay Round, the world trading community understood that a shift to a consistent, rules-based dispute resolution process was in order. The DSU contains tight deadlines for every step of the dispute resolution process, and these

277 Ito, supra note 186, at 181.
steps are spelled out with care. No party can block formation of a panel or adoption of a panel report (or, in the even the report is appealed, of the WTO Appellate Body’s report). If the losing party in a case does not comply with the recommendations of the panel (or Appellate Body), then it must pay compensation to the winning party, or suffer retaliation. Thus, dispute resolution in international trade now has the certainty, predictability, and enforceability – in a word, the “teeth” – that international insolvency law lacks. It is not a starry-eyed overstatement to say that the DSU represents the most sophisticated mechanism for resolving international disputes that humankind has yet devised. To be sure, it has its warts, but warts and all it stands as an achievement of which those involved in international insolvency reform would do well to take note.

Until they do, the world shall remain beset with the possibility of simultaneous bankruptcy proceedings in multiple jurisdictions, “with the debtor’s estate in each one consisting only of the assets available within that country.”279 This possibility is not only inconvenient, it is also costly for the parties involved.280 Additionally, multiple proceedings in different countries may give rise to potentially conflicting decisions and evasive action by savvy creditors.281

B. The Status of Foreign Claims – And National Treatment

The status of foreign claims is the second sound of international insolvency that resonates, albeit softly, in the Japanese regime. It is an overstatement, though not an uncommon one, to say that Japanese courts do not discriminate between foreign and local claims in insolvency proceedings, hence the status of the foreign claim is the same as that of the local claims.282 In international trade law terms, the court affords foreign creditors “reciprocity.” Article 2 of Japan’s Bankruptcy Law outlines the principle for the treatment of foreign individuals and companies, providing that “an alien or foreign corporation [i.e., the creditor, be it an individual or corporation from overseas] shall have the same status as a Japanese national or Japanese corporation in regard to bankruptcy, provided however, that this shall apply only when Japanese nationals or Japanese corporations have the same status under the native laws of the alien or the foreign corporation.”283 In addition, Article 485 of Japan’s Commercial Code, and Article 51 of its Banking Law, allow for the commencement of proceedings against the assets located in Japan of a foreign corporation or bank, respectively. It appears that foreign creditors can file their claims in such proceedings (though whether the debtor, if it is a foreign bank, will be treated as a single or separate entity may be open to question), assuming they can meet the applicable proof-of-claim requirements. In other words, as regards status, foreign claims have an intra-territorial effect insofar as they can be pressed in Japan.

280 See id.
281 See id. at 4.
282 See Ito, supra note 186, at 181.
283 Bankruptcy Law, supra note 189, at Art. 2. See also Tagashira, supra note 166, at 6 (discussing varying interpretations of this reciprocity principle).
Perhaps Article 2 of the Bankruptcy Law can be justified on pragmatic grounds. It can be argued that because insolvency proceedings are a part of Japan’s economic system, Article 2 should be available to all foreigners engaged in economic activity in Japan, and thereby include foreign entities. Yet, foreign assets are beyond the powers of a Japanese trustee. There is no choice but to leave them exposed to collection efforts by individual creditors. The result may be unequal treatment among creditors, and in reorganization cases, an obstacle to the debtor’s reorganization, but so be it.

This sort of justification – which is, in effect, the territoriality principle at work – would be at odds with Japan’s overseas interests. When adhered to by another country, that other country denies effect to insolvency proceedings in Japan that seek to block the collection actions of individual creditors abroad (a “general staying effect”). That is, it prevents a Japanese proceeding from stopping creditor actions against properties in that country. The result is that the efforts of the Japanese trustee to maximize the size of the debtor’s estate (in a global sense), and obtain the best possible pay-out for the broadest array of creditors, are frustrated. Only if the other country does not adhere to pure territoriality will Japan’s proceedings stand a chance of being recognized. Section 304 of the American Bankruptcy Code is an example. This Section admits eligibility of Japanese trustees; they can file ancillary proceedings.

It also must be stressed that reciprocity is not nearly as progressive a principle as – to borrow another international trade law concept – national treatment. At first blush, it seems quite appropriate that Japanese courts treat foreign and domestic creditors equally, and it is. The problem is that the treatment is conditional on the courts in the home countries of the foreign creditors offering Japanese creditors the same treatment (i.e., not discriminating against Japanese creditors in favor of their own local ones). This demand is not the hallmark of an advanced approach – at least as judged from the perspective of GATT principles. To be sure, in international trade negotiations, concessions are made on the basis of reciprocity. Nowhere, however, in the GATT national treatment provision (Article III) is there a demand for reciprocity. All WTO Members are expected not to discriminate against imports vis-a-vis like domestic problems. (Likewise, there is no such demand in the famous Article I, concerning most-favored nation (MFN) treatment. Every WTO Member is obliged to treat the imports of every other Member equally.) Were Japan to stake out an aggressive universalistic approach to international insolvency law, it would drop the reciprocity condition and treat foreign creditors as well as Japanese creditors, regardless of the treatment of Japanese creditors.

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284 Tagashira, supra note 166, at 5.
285 See id.
286 See id.
287 See id.
288 It is assumed here that the stricter interpretation of reciprocity under Article 2 of the Bankruptcy Law – that Japanese creditors must be treated under a foreign insolvency law in the same way that they would be treated under Japanese law – is not applicable. This interpretation would render some foreigners entirely ineligible for Japanese bankruptcy proceedings, on the grounds that their law does not treat Japanese creditors as they would be treated by Japan’s law. The interpretation above is less strict, namely, that Japanese creditors not be discriminated against under foreign law, regardless of the nature of that foreign law. See generally Tagashira, supra note 166, at 6 (discussing these interpretations).
creditors in foreign insolvency proceedings. Apparently, this principle already has been discarded in the Corporate Reorganization Law.

Would such a change to the Bankruptcy Law be criticized as naive, as “giving up something for nothing”? Perhaps, particularly by Japanese creditors that have obligations outstanding to debtors in countries that do not treat foreign creditors akin to domestic creditors. But, those creditors ought to enter into such obligations with their “eyes open.” If they fear the possibility of a local insolvency proceeding and attendant discrimination, then they can put a price tag on their fear: they can increase the cost of credit they are extending to the debtor. Moreover, it is important not to view the matter from the narrow perspective of Japanese creditors. There is a larger context to consider, namely, the reaction of the international business and legal community. Foreign creditors would applaud the move. They might interpret it as signaling a more favorable business climate, and react by extending more credit, or credit on easier terms, to Japanese debtors. No doubt Japanese debtors would welcome the increased liquidity. As for the international legal community, might it not see Japan as staking out leadership on international insolvency reform?

C. Recognition of Foreign Insolvency Proceedings – And International Trade Negotiations

Given the grip of the territoriality principle on Japan’s insolvency law regime, it ought not to come as a surprise to learn that Japanese courts neither recognize nor give effect to foreign insolvency proceedings or judgments with respect to property situated in Japan. In other words, these proceedings and judgments have no intra-territorial effect. Article 3(2) of the Bankruptcy Law puts it plainly: “a bankruptcy adjudged in a foreign country shall not be effective with respect to properties existing in Japan.” Other Japanese insolvency statutes have similar territoriality provisions.

Fortunately, Japanese courts have not turned a deaf ear to the rising chorus of criticism of the territoriality principle and its deployment in Japan. For example, in 1981, the Tokyo High Court held that the territorial provisions of the Bankruptcy Law were simply intended to limit the general staying effect of foreign proceedings, and did not deny a foreign trustee’s rights to manage the debtor’s assets in Japan. Some scholars have interpreted this holding to mean that foreign insolvency proceedings can be effective in Japan, provided that they meet several requirements for recognition. Perhaps, then, Japanese courts are “tending

289 Bankruptcy Law, supra note 189, at Art. 3.

290 See, e.g., Composition Law, supra note 190, at Art. 11 (1922); Corporate Reorganization Law, supra note 148, at Art. 4.

291 See Tagashira, supra note 166, at 9. In the case, a Swiss trustee was allowed to litigate the rights of a foreign debtor, a Swiss corporation, in Japan. A Japanese creditor had arrested a registered trademark of the Swiss corporation. In the ensuing Swiss bankruptcy proceeding, the trustee sought to cancel the action of the Japanese creditor (the arrest). The Tokyo High Court agreed the trustee had “a right to manage the debtor’s assets in Japan.” Id. at 9; see also Judgment of 30 January 1981, Tokyo Kosai [Tokyo High Court], 32 Kaminshu 10, 12.

292 See, e.g., Tagashira, supra note 166, at 9.
to relax the strict attitude toward foreign proceedings.”

Article 3 paragraph 2 of the Bankruptcy Law provides only that foreign bankruptcy adjudication does not automatically have an effect, in particular effect of collective execution, to the debtor’s property. It does not necessarily mean that the court must ignore the foreign bankruptcy itself or must deny the right of the foreign administrator to manage and dispose of the debtor’s property which is granted by the law of the foreign country.

Accordingly, under certain circumstances, Japanese courts may allow a foreign trustee to administer the debtor’s assets located in Japan. What are those circumstances? Simply put, there must be no Japanese creditors seeking to attach the same assets. Obviously, there is always a strong chance of a long line of Japanese creditors knocking at the debtor’s door. Moreover, “it is still difficult or at least unknown if the trustee may vacate such attachment, which is either caused by a local creditor or foreign creditor, by way of the recognition of the foreign insolvency proceeding.”

It is, therefore, perhaps harsh but by no means unfair to characterize Japan’s approach toward foreign insolvency as non-cooperative, and certainly distinct from that of the United States. Section 304 of the American Bankruptcy Code is an effort at international cooperation. The absence of an analogous provision in Japanese law reflects a territoriality policy that has deep historical roots. The initial intent of that policy was to protect Japanese creditors from being forced to attend foreign proceedings. As long as they did not have to participate in these proceedings, they would be spared the costs associated with presenting evidence and defenses to meet or rebut issues of proof. Thus, the thinking was that foreign proceedings ought not to have an effect on a debtor’s assets in Japan. Accordingly, almost a century ago, Japan’s former highest court, the Grand Court of Judicature, denied effect to an order of discharge issued by a Hawaiian court. The Grand Court reasoned that the essence of a bankruptcy proceeding is its power of compulsory execution, thus its effects should be limited to the territory within which it is enforceable, in this case, only within the United States.

In sum, the best that can be said is that in general, “as long as there is no concern about the protection of local creditors, it does not contravene the provision [Article 3(2)] to be flexible with respect to the extent of the power of a foreign administrator.” This general statement hardly can be regarded as acceptable. First, ad hoc behavior by judges is far less satisfying than decisive action by the Diet. As a theoretical matter, this sort of judicial activism might be viewed as unacceptable – judicial over-reaching, as it were. As a practical

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293 Ito, supra note 186, at 182.
294 Matsushita, supra note 187, at 76-77.
295 See Ito, supra note 186, at 183.
296 Id.
297 See Tagashira, supra note 166, at 8.
298 See id.
299 See id.
300 Matsushita, supra note 187, at 79.
matter, it is hardly predictable. How a particular judge will behave is uncertain. Even if a judge does accord recognition to a foreign insolvency proceeding, that decision does not technically rise to the level of a formal source of law, in a *stare decisis* sense, given that Japan is a civil law country.

Worse yet, Article 3(2) reflects a “me first” attitude, a perspective of both thinking and acting locally rather than globally. Even reciprocity – whereby Japanese courts offered recognition and enforcement to foreign insolvency proceedings in those countries that did the same for Japanese proceedings – would be a more internationally-minded approach. How might such a reciprocity regime come about?

Here again, recourse may be had to an international trade law analogy. As intimated earlier, concessions in negotiations over tariff and non-tariff barriers typically can be made when a country that is the principal supplier of the product at issue commence discussions with one or more countries to which it exports that product. In other words, discussions are conducted on a bilateral basis, or in a small group. In return for opening its market to products that matter to its negotiating partner (or partners), the principal supplier wins a reduction in barriers against its product. Eventually, the countries involved may expand the product list they discuss, and agree to an across-the-board reduction in barriers.

There would appear to be little holding Japan back from commencing negotiations with its largest trading partners with a view to developing an agreement on the recognition and enforcement of foreign insolvency proceedings. Indeed, Japan seems already to have the substantive legal framework that might be a starting point. Article 118 of the Code of Civil Procedure provides that a foreign judgment will be recognized as valid in Japan if (1) the jurisdiction of the foreign court is recognized under Japanese law or applicable treaty, (2) the defendant received personal service of process or appeared voluntarily, (3) the foreign judgment does not contravene public order or good morals in Japan, and (4) reciprocity is guaranteed as regards the recognition of Japanese judgments. Similarly, under Article 24 of the 1979 Law of Civil Execution, Japanese courts will enforce a foreign judgment if these four conditions are met, and that judgment is final. Possibly, these conditions could be the “talking points” in the early stages of negotiations toward recognition and enforcement criteria for an international framework.

Logistically, how might the negotiations proceed? One possibility would be for Japan to begin talks with the countries in which Japanese companies have the most assets, and from which creditors have the most obligations due in Japan. The presumptive candidates would be the United States, the members of the European Union, Canada, and various South-East Asian countries. The negotiations could be conducted bilaterally, with the aim of an agreement stating that Japan will recognize and give effect to an insolvency proceeding in the other country, and the other country will do likewise for Japanese proceedings. After a critical mass of bilateral agreements is obtained, Japan could move to “multilateralize” the process by calling for a treaty among countries. The signatories would offer recognition and enforcement to each other, much like each WTO Member accepts the schedules of concessions of every other Member. Japan, of course, would stand out as a leader in international insolvency reform.

Is this scenario chimerical? Perhaps not. Consider an example involving the

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See Law No. 4 of 1979.
United States and Japan. How might these two nations form a mutually desirable structure for dealing with ancillary proceedings? Radical change in its current legal framework, particularly the abandonment of the territoriality principle, is a possibility discussed below. But, suppose that does not occur, or at any rate, not in the near future. Japan, then, is compelled to explore possible cooperation modalities with foreign insolvency proceeding within the current legislative framework. After all, in the United States, Section 304 helps fit the American Bankruptcy Code in the context of the overall system of international insolvency cooperation, but Japan has no such provision. Nor does it have a bilateral treaty with the United States calling for recognition and enforcement. Thus, as between the world’s two largest economies, the specter of concurrent insolvency proceedings looms large. Indeed, depending on the nature of a debtor’s affairs, concurrent full proceedings may be commenced in more than just Japan and the United States. Japan’s adherence to the territoriality principle, and its lack of a special ancillary procedure, virtually assures this result.

A possible solution in the Japanese-American context is cooperation through ad hoc agreements between bankruptcy officials from each country. When concurrent proceedings do erupt, the officials in both proceedings, as well as the debtor, could conclude an agreement that “constitutes a bilateral treaty” for that specific international reorganization case. To be sure, as discussed earlier, Japanese insolvency law places a trustee under court supervision and requires the trustee to obtain court approval before taking important actions, including entering into a settlement. Therefore, an ad hoc agreement of the kind suggested would raise three issues.

First, is the trustee even allowed to strike such a bargain? Second, must the trustee enter into such an agreement whenever it is possible to do so? Third, what criteria should the supervising court apply to decide whether to approve the so-called bilateral treaty? The first two questions are the easiest to answer. Presently, Japanese law neither prevents a trustee from attempting to harmonize with a foreign proceeding, nor does it oblige the trustee to do so. The third question remains one open for debate. Arguably, the “bottom-line” criterion is whether the deal will result in the maximization of the size and value of the debtor’s estate, and whether it represents the most fair and equitable settlement for the broadest array of creditors and shareholders.

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302 See Tagashira, supra note 166, at 23.
303 See id.
304 See id.
305 See id.
306 See id.
307 See id. at 35.
308 See id.
309 See id. at 36.
V. **Whispers of Reform: Ending Territoriality?**

The above discussion suggests that jurisdiction, status, and effects all remain critical problems demanding attention. The Japanese approach to these international insolvency issues, as embedded in current law, is distinctly territorial. It is, therefore, out of step with developments at UNCITRAL – namely, the Model Law. It is also incongruous with the potential role of Japanese corporations, both financial and non-financial, as major players in the global economy. What, then, is to be done?

One starting point is to focus on how to construct a proceeding that is ancillary to a main (or principal) proceeding conducted in another country. In the United States, courts often apply comity to foreign insolvency proceedings, hence international cooperation is a consistent policy in American bankruptcy law.\(^{310}\) To argue that foreign proceedings should receive automatic “full faith and credit” is to argue for a major change in Japan’s current regime.\(^{311}\) Yet, there are whispers that such change might be afoot.

Japan’s reform work on its insolvency laws began in 1996.\(^{312}\) As part of this reform effort, an advisory committee is scheduled to complete preparation of a draft of the new laws by 2001 or 2002.\(^{313}\) The committee faces three main issues: (1) consumer bankruptcy, in particular, the requirement and effect of discharge; (2) a simple and effective rehabilitation proceeding for corporations, especially small and mid-size businesses; and (3) international insolvency.\(^{314}\) As to the third challenge, there exists a Preliminary Draft of the International Bankruptcy Related Provisions in the Japanese Insolvency Proceedings (Preliminary Draft). This Draft was prepared by leading Japanese scholars. Thankfully, it proposes to abolish the territorial principle in favor of a universality. Indeed, no one doubts that the principle must be abandoned; the only question is the extent of the abandonment. One proposal, which is set forth in Section 4 of the Preliminary Draft, adopts a recognition approach, wherein the decision of a foreign court opening a foreign proceeding is recognized and the legal effects of the decision are supposed to be determined basically by the foreign law. This approach is probably patterned after the recognition of foreign judgments. In contrast, the U.S. Bankruptcy code adopts an “ancillary proceeding approach [\textit{11 U.S.C. § 304(a)}], wherein relief available to a foreign representative is provided in the U.S. law independent from foreign law.\(^{315}\)

Additionally, Section 6 of the Preliminary Draft abolishes the reciprocity principle and provides for unconditional equal treatment of foreigners.\(^{316}\)

Unfortunately, these sorts of proposals might not go far enough in calling for

\(^{310}\) See id.

\(^{311}\) See id.

\(^{312}\) See Matsushita, \textit{supra} note 187, at 72.

\(^{313}\) See id.

\(^{314}\) See id.

\(^{315}\) Id. at 80.

\(^{316}\) See id. at 87.
intra-territoriality, i.e., the recognition in Japan of foreign insolvency proceedings. For example, the Preliminary Draft abandons the territoriality principle only when certain circumstances are satisfied. The first such circumstance is the existence of ordinary jurisdiction. As explained earlier, ordinary jurisdiction exists where a debtor has its principal office in Japan; complementary jurisdiction exists if the debtor has its principal office in another country, but has property in Japan.\textsuperscript{317} Under the Preliminary Draft, a foreign proceeding under ordinary jurisdiction would be given effect in Japan upon recognition by a Japanese court, as long as it meets certain criteria.\textsuperscript{318} Upon recognition, a foreign proceeding would become effective retroactively as of its commencement.\textsuperscript{319}

Another requirement that would have to be fulfilled to avoid invocation of the territoriality principle would be fair treatment of the rights of all interested parties.\textsuperscript{320} How would this be determined? The Preliminary Draft sets forth a series of factors for a Japanese court to apply in order to decide whether all interested parties will receive fair treatment in a foreign insolvency proceeding:

- whether the proceeding is under the control of courts or other competent authority; whether both individual proceedings by creditors toward the debtor’s assets and transfers by the debtor are restricted after the commencement of the insolvency proceeding; whether there is a process for addressing fraudulent and preferential transfers; whether the estate is distributed on a pro rata basis without discrimination based on nationality or residency; and whether creditors are properly notified on important matters.\textsuperscript{321}

The rationale for giving intra-territorial effect to foreign insolvency proceedings is to protect local creditors by minimizing the expense of presenting proof, evidence, and defenses abroad. However, “simple delay or greater expense in litigating abroad is insufficient proof of prejudice...otherwise, almost all foreign insolvency proceedings would fail to have any effect in Japan.”\textsuperscript{322}

Still other requirements would have to be met to avoid invocation of the territoriality principle and the consequent denial of recognition to a foreign insolvency proceeding.\textsuperscript{323} They include an assurance that the interests of local creditors would be protected. They also include a determination that there is no substantial discrepancy in the system for determining priorities of rights as between Japanese and the foreign law. Finally, the Preliminary Draft would require accordance with Japanese public policy.

While each one of these criteria for the recognition of foreign insolvency proceedings may be defensible on its own, taken together they might be troublesome. They

\textsuperscript{317} See Tagashira, supra note 166, at 10.

\textsuperscript{318} See id. at 11.

\textsuperscript{319} See id.

\textsuperscript{320} See Matsushita, supra note 187, at 81.

\textsuperscript{321} Id. at 82.

\textsuperscript{322} Id.

\textsuperscript{323} See id. at 81-82.
would codify and institutionalize judicial discretion as to whether to grant recognition. Japanese legislators need to consider whether Japanese district courts can exercise these discretionary powers without significant delay or excessive burden on judges. In addition, the criteria do not distinguish between liquidation and reorganization proceedings. Providing for appropriate cooperation in liquidation proceedings cannot suffice; attention must be given to reorganization proceedings.

Despite these concerns, the sorts of changes called for in the Preliminary Draft are at least hopeful signs that Japan is moving away from territorialism. In fact, two other related proposals that give cause for hope are worthy of mention. First, the Preliminary Draft suggests an amendment to Japanese insolvency law concerning how to handle concurrent proceedings. Specifically, section 5 of the Preliminary Draft deals with concurrent proceedings. Adjustment of distribution in paragraph (1) [of Section 5] is an internationally accepted rule, and the right of a foreign administrator to file for a Japanese insolvency proceeding in paragraph (2) seems to be a corollary of the recent case law allowing a foreign administrator to act on behalf of the debtor in Japan. Additionally, Section 5, paragraph (2) states that a recognized foreign main proceeding shall override an antecedent domestic proceeding, and that a foreign administrator will manage the debtor’s assets. Clearly, this amendment would materially alter Japanese law. But, until it is effective, the traditional principles of territoriality and reciprocity will apply.

Second, it is anticipated that in the fall 1999, the Diet will enact a new law on so-called “debt adjustment proceedings,” informally known as the Debtor Rehabilitation Law. The new legislation is scheduled to take effect in the spring 2000 and replace the Composition Law of 1922. The new law will contain both extra- and intra-territoriality features. A Japanese trustee will have jurisdiction to collect assets of a debtor located overseas, and some recognition will be granted to foreign insolvency proceedings. If the new law is implemented, it will represent an important step away from territorialism.

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324 See Tagashira, supra note 166, at 37.
325 See Matsushita, supra note 187, at 86-87.
I. HOW HAVE BANKS BEEN DEALT WITH?

The discussion in Parts Two and Three is a general one in that it concerns debtors without making much of a distinction between banks and non-banks. But, what about the case when the debtor is a bank? Is this a special case? Should it be? As is evident from the discussion of Part One, the woes of the Japanese banking system are a significant aspect of the country’s overall economic crisis. Estimates of the amount of non-performing loans on the books of Japanese banks vary, including estimates in the tens of trillions of yen (i.e., tens of billions of U.S. dollars), possibly as high as ¥ 87 trillion (approximately U.S. $600 billion). Already, approximately 60 problem banks have failed (and perhaps more may follow). An obvious question that arises is what law applies to bank bankruptcy? Put more generally, how, in practice, have bank bankruptcies been handled, and how should they be handled? These are the sorts of issues discussed, in a preliminary way, in this Part. After all, any attempt at a thorough overview of the international dimensions of Japanese insolvency law cannot end without mentioning banks, particularly internationally active banks, as debtors.

A brief excursion into Japanese banking law and recent banking history provides the answers. Japan’s Deposit Insurance Law was enacted in 1971, with major reforms made to the Law in 1986, 1996, and 1998. (The 1996 and 1998 changes are of particular importance, because they were designed to deal with the current economic crisis.) After the 1986 change, under Japan’s “safety net,” two strategies were available to deal with failing or failed commercial banks. The first strategy, known as a “payoff,” resulted in the protection of depositors up to a threshold. By law, each depositor (whether Japanese or not) was (and still is) protected up to ¥ 10 million. After that, whether a depositor incurred a loss, and in what amount, were matters determined during the liquidation process, i.e., they depended on the remaining value of the liquidated bank. However, the payoff strategy has not yet been applied in any case, because of fear of systemic risk it might engender, particularly given the circumstances of the financial sector.

The second strategy was “financial assistance” by the Deposit Insurance Corporation. A loss incurred by a failed bank was covered by a money transfer from that Corporation. For example, if a bank had lost ¥ 100 million worth of assets over its capital, then the Corporation simply covered this loss with a transfer of ¥ 100 million for the bank’s liability. In this way, depositors and other creditors of the bank were protected.

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326 For a discussion of some of the issues dealt with herein, see Hiroshi Nakaso, Recent Banking Sector Reforms in Japan, FED. RES. BANK OF N.Y. POLICY REV. 1 (July 1999).

327 See Harney, supra note 1. One estimate was that as of October 1998, upwards of half of Japan’s nineteen largest banks were said to be insolvent, with non-performing loans of approximately ¥ 70 trillion (though they had admitted “just” ¥ 22 trillion). See Wolf, Serious, Yes. Hopeless, No., supra note 44. As for the solvent banks, they had become dangerously under-capitalized, hence the re-capitalization efforts discussed below are most welcome.

328 See Law. No. 34 of 1971.
However, there was a limit on the amount the Deposit Insurance Corporation could transfer in any one case, known as the “pay-off cost limit.” That limit was defined as the amount that would have been incurred by the Corporation had the failed bank opted for a pay-off, which in formulaic terms was as follows:

\[
\text{Pay-off Cost} = \frac{(\text{Insured Deposits}) - (\text{Remaining Value of Assets}) \times (\text{Insured Deposits plus Non-insured Deposits and other obligations})}{\text{(Insured Deposits)}}
\]

Consider an example. Suppose insured deposits are ¥ 120 million, the remaining value of assets is ¥ 100 million, and non-insured deposits and other obligations are ¥ 80 million. Then, the pay-off cost limit would be

\[
120 - 100 \times \frac{120}{120 + 80}
\]

i.e., ¥ 60 million. If the bank had lost ¥ 100 million over its capital, then there would be a “hole” of ¥ 40 million (the ¥ 100 million loss minus the ¥ 60 million pay-off cost limit) that the Corporation could not “plug” through or by financial assistance. For application of financial assistance to such a case, the “hole” would have to be plugged by third parties – e.g., solvent financial institutions from which “voluntary contributions” would be requested by financial authorities.

This approach was used frequently in the early and mid-1990s, including in the 1992 case of Toyo Shinkin Bank and the 1996 case of Cosmo Credit Corporation. In the Toyo Shinkin Bank case, the Deposit Insurance Corporation provided a grant of ¥ 20 billion to Sanwa Bank, which served as a relieving financial institution, i.e., it took over the business of Toyo Shinkin Bank. In the Cosmo Credit Corporation case, the Deposit Insurance Corporation provided a grant of ¥ 125 trillion to Tokyo Kyodo Bank, which served as a relieving financial institution.

It is important to understand the policy logic underlying this approach. Suppose banking officials believe application of the pay-off strategy would cause social unrest (not an unreasonable belief, because the Japanese public has not experienced losses from bank failures in the post-Second World War era). Their response is to collect the funds necessary to plug the hole from solvent banks. Thus, banking officials are in the position of going to financial institutions and informally requesting contributions from them. The financial institutions agree insofar as they see a collective interest in maintaining financial stability.

During the early and mid-1990s, this hybrid strategy of financial assistance plus “contribution” worked for the first few cases. But, as Japanese banks continued to fail, remaining solvent institutions began to grumble – and rightly so – about contributing funds, particularly for banks with which they had no close relations. Contribution, then, no longer was an option for bank regulators. Yet, official policy remained that all depositors should be

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covered fully. To be sure, the government deliberately ensured that shareholders lost their money, *i.e.*, shareholders were penalized – again, rightly so. But, depositors and other general creditors had to be kept whole in the interest of financial system stability and social harmony.

What spawned the 1996 reform of the Deposit Insurance Law was the death of contribution as a viable option for dealing with failed or failing banks. The 1996 legislation established a temporary period, until March 2001, during which all losses of depositors and other general creditors would be covered without asking remaining solvent banks to contribute to plug holes beyond the pay-off cost limit. In effect, the pay-off cost limit was removed. This legal reform was thought to be a big step forward, but the crisis continued. In particular, the “Autumn crisis,” referring to the fall of 1997, which included the failure of Hokkaido Takushoku, once an internationally active bank, and Yamaichi Securities. Some other banks went down thereafter or faced the possibility of a bank run. In retrospect it was during this period that Japanese politicians, and the public at large, really understood there was a crisis in their midst.

The Bank of Japan had consistently argued that the essence of the crisis was the under-capitalization of Japanese banks. Confidence in the banks was at a low ebb because they lacked capital. Indeed, ever since the Basle Accord of 1988 was implemented, particularly after the burst of the “bubble” in the early 1990s, Japanese banks had eroded their capital bases by writing down bad loans, and making provisions against them. To replenish their capital, Japanese banks had just two options: increase profitability, or access private capital markets. Neither option worked. The sluggish Japanese economy limited profit potential, and because capital markets had no confidence in Japanese banks, they would not offer funds (or would do so only on expensive terms – the so-called “Japan premium”).

There was, consequently, no other place for the banks to turn than public coffers. However, after the 1995-96 crisis involving housing loan corporations (*jusen*), in which approximately ¥ 680 billion of taxpayer funds were used, talk of using public funds to bail out the banking system was “taboo.” The Autumn 1997 crisis ended the taboo. In the spring of 1998, a framework for capital injection was established. The framework authorized the use of up to ¥ 13 trillion of public funds to replenish the capital of Japanese banks. A capital injection of ¥ 1.8 trillion into the 21 major Japanese banks was applied in March 1998.

The injection seemed to work. April and May of 1998 were relatively quiet months in Japanese financial markets. But, the illusion was shattered when, in the summer of 1998, problems at the Long Term Credit Bank (LTCB) of Japan surfaced. LTCB failed in the autumn. It was the largest and most serious failure in Japan’s distinguished banking history. LTCB had assets of ¥ 26 trillion – far in excess of Hokkaido Takushoku. It was internationally active. The outstanding notional principal of derivatives transactions in which LTCB was engaged was an incomparable sum: ¥ 50 trillion. A substantial portion of the financial institutions involved in such transactions with LTCB were foreign. Bank regulators in Japan and around the world naturally feared the systemic risk implications of LTCB going bust in a disorderly way.

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330 The Bank of Japan was not alone. The *Financial Times* correspondent, Martin Wolf, seemed to agree, arguing the only viable re-capitalization strategy was the injection of public funds, ideally by means of share purchases. See Wolf, *Serious, Yes. Hopeless, No.*, supra note 44.

In October 1998, as a result of the intensive Diet discussions, new legislation designed to deal with the disposal of failed or failing banks was enacted – the “Law concerning Emergency Measures for the Reconstruction of the Functions of the Financial System,” also known simply as the “Revitalization Law.” The Law provides a useful framework within which authorities can deal with a failed or failing bank, without necessarily finding beforehand a sound bank to assist in the resolution (e.g., through an assisted merger or takeover). The framework includes a Financial Reconstruction Commission (FRC). The FRC (rather than the judiciary through an insolvency proceeding) is empowered to order the administration of failed or failing banks by a financial reorganization administrator. Also, the framework permits the temporary nationalization (formally known as “special public management”) of failed or failing banks, and allows for the setting up of bridge banks. Within the framework, failed or failing banks can continue to provide their financial services while meeting their liabilities.

Experience (as of this writing) with the Revitalization Law is modest but growing. There have been two cases of temporary nationalization – LTCB and the Nippon Credit Bank. There have been eight cases of administrations by financial reorganization administrators, three involving banks and five involving credit cooperatives. One noteworthy feature of this experience is the absence of any dreadful implications for international aspects of insolvency law. For example, after the temporary nationalization of LTCB, the Bank of Japan expressly declared that all of LTCB’s liabilities – whether on- or off-balance sheet – would be made good, and backed the declaration with a pledge to provide the funds necessary to assure international financial markets that LTCB would make good on all of its obligations. The Ministry of Finance and Prime Minister offered similar statements. The assurances worked: none of LTCB’s counter-parties, domestic or foreign, declared a default, and a potential systemic crisis was averted.

A second noteworthy feature is how a strategy for dealing with a failed or failing bank is selected. If a bank is on the verge of suspending the repayment of deposits, then the FRC can appoint an administrator to ensure the bank’s condition does not become any more precarious. That administrator will take control of the bank’s assets and look to either merge the institution with a healthy bank, or have it taken over by a healthy bank. If no acceptable partner exists, then the Deposit Insurance Corporation can establish a temporary public bridge bank (a subsidiary that is 100-percent owned by the Corporation) to serve as a rescue vehicle, which must complete its work (e.g., arranging a merger or take-over, or dissolving the problem bank) within one (or, with extensions, three) year(s). As for temporary nationalization, the FRC may arrange this if the problem bank is on the verge of suspending repayment of deposits and there is a danger of serious damage to the financial system if the bank were to cease operating, or of an adverse effect on international financial markets. In a temporary nationalization, the Deposit Insurance Corporation takes control of the problem bank by purchasing its shares (at a price based on the bank’s net worth) and appointing a new management. The operation of the bank continues pursuant to a plan approved by the FRC. Work must finish by March 2001, the outcome being either a take-over by a healthy partner or transfer of shares to another institution. How, then, in practice, is the choice made between appointment of an administrator versus temporary nationalization? A custom and practice seems to be developing: a bank whose failure would have large systemic risk implications will

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332 Bank regulators are (as of this writing) still searching for a purchaser of LTCB.
be dealt with through temporary nationalization; a bank that could go under without such
disruption will be dealt with by the financial reorganization administrator.

Perhaps the most important part of the framework set up by the Revitalization
Law concerns the comprehensive safety net, which already had developed into a considerable one.\footnote{333 For a detailed discussion of the Japanese experience with deposit insurance and failing banks, see Curtis J. Milhaupt, \textit{Japan's Experience with Deposit Insurance and Failing Banks: Implications for Financial Regulatory Design}, Bank of Japan IMES Discussion Paper Series 99-E-8 (March 1999).} The revamped safety net protects all depositors and creditors of any bank to the full extent (that is, 100 percent of the value) of their claims. The revamped safety net is temporary. There is a sunset provision in the Law that calls for an end to the protection in March 2001.

Arguments have been made to extend this sunset date on the ground that
Japan’s financial system still will be fragile in March 2001. However, most of the authorities concerned, including the Bank of Japan, are adhering to the original date. They point out – quite rightly – that the comprehensive safety net has two ill effects. First, it is provided at potentially tremendous cost to public finances. Second, it creates a giant moral hazard problem. By sticking to the date, Japanese financial institutions know they had better be stronger and more competitive by March 2001.

How is this generous though temporary safety net possible? The October 1998
Law made available for capital injection purposes ¥ 25 trillion of public funds. An injection of ¥ 7.5 trillion was applied in March 1998. The thinking was that the sums authorized by the Spring 1998 framework – ¥ 13 trillion made available, ¥ 1.8 trillion disbursed – had been too small. Is ¥ 25 trillion enough?

On the one hand, a pessimistic answer is no, because ¥ 25 trillion may prove to be far below actual collections on the huge sum of non-performing loans. Suppose the actual amount of non-performing loans is ¥ 50 trillion, a conservative estimate. A collection rate of less than 50 percent – which, by historical experience, is quite high – would mean losses in excess of ¥ 25 trillion. In this hypothetical, the allocated funds of ¥ 25 trillion would not be enough to avoid a threat to the capital bases of banks. However, is this hypothetical realistic? There are different categories (or “types”) of non-performing loans, and a different recovery rate applies to each category. For some categories, the recovery rate is as high as 75 percent; for other categories, it is well below 50 percent. Thus, whether the hypothetical is realistic depends in part on the volume of loans in each category, and on whether individual loans have been categorized correctly in the first place. Moreover, recovery rates depend on the real-world circumstances of borrowers. If the Japanese economy performs above expectations, then the hypothetical is unduly pessimistic; if not, then it may be “in the ball park.”

On the other hand, the answer might be yes, ¥ 25 trillion may prove to be more than enough. The argument is that ¥ 25 trillion would cover the unrealized losses from the equity positions held by banks, and those positions count as Tier Two capital under the Basle Accord. In other words, the public funds made available would cover the most significant “hit” to the capital of banks, the write-down of their stock portfolios.

What about the capital injection of ¥ 7.5 trillion – is it enough? Arguments can be made both ways along the lines suggested above. The hopeful response is yes. Many major Japanese banks now have a risk-adjusted capital adequacy ratio of around 11 percent,
exceeding the 8 percent Basle risk-adjusted minimum.

What is certain is that the work hardly is over. Japanese banks still need to remove bad loans from their balance sheets, a move that would improve their cash flows. Consolidation in the banking system is necessary. The system remains plagued by over-capacity. Staffs need to be laid off, branch networks need to be trimmed, and mergers and acquisitions need to occur. Perhaps the failures may not be over either.

II. THE IRRELEVANCE OF THE INSOLVENCY LAW REGIME?

So, where does the excursion leave off in terms of the relevance of Japanese insolvency regime to failed or failing Japanese banks? In theory, any of the five Japanese bankruptcy laws could apply to a failed bank. In addition, in 1996 special legislation was enacted that created procedures for the reorganization and bankruptcy of financial institutions. This legislation, formally known as the “Law to Provide Special Procedures for Reorganizing Financial Institutions,” or simply the “Special Reorganization Law,” had three key features.

First, it enabled cooperative-type insured banks (e.g., shinkin banks, labor banks and credit co-ops) to resort to reorganization proceedings that are practically identical to the standard corporate reorganization procedure discussed below. Absent this change, the legal scheme for corporate reorganization could apply only to stock corporations. Second, the law empowered the Deposit Insurance Corporation of Japan to act as an agent for depositors of a failed financial institution in a bankruptcy or reorganization proceeding. The idea is to ensure that reorganizations do not get bogged down owing to a large number of depositors in the bank being reorganized. The Corporation can draw up a single list of depositors and submit it to the supervising court, and this list replaces the filing of proof of claims by each depositor. The Corporation also can act on behalf of depositors and vote on the reorganization plan. Third, the law granted supervisory authorities the ability to file a petition for bankruptcy or reorganization with respect to any failed financial institution under their supervision.

As is often the case, theory is one thing, the facts are another. While Japan’s present legal regime for insolvency is in theory applicable to banks, a reasonable guess is that the Bankruptcy Law and the Corporate Reorganization Law would be the most likely candidates to govern a bank insolvency case. Guessing is all that is possible. Japan has virtually no experience with bank insolvency after the Second World War. As the above excursion shows, bank failures invariably have been resolved through out-of-court means, namely, an assisted merger or takeover with the help of the Deposit Insurance Corporation. In every one of these resolutions, the failed bank was able to meet all of its liabilities. Thus, the insolvency regime never had to be tested by a bank. Rather, the laws applied included the Deposit Insurance Law, the Revitalization Law, and the others mentioned above, along with the general Banking Law. In sum, there simply is no leading case on the international aspects of the insolvency of a Japanese bank.

Why is there such a disconnect between the law that is theoretically applicable to bank bankruptcies, on the one hand, and the actual manner in which these messes have been cleaned up, on the other hand? In a word, politics, though not in a pejorative sense. Rather, somewhere, sometime, by someone, a political decision was taken – or perhaps more
accurately, a policy evolved – that a bank bankruptcy would be unacceptable for two reasons.

First, as is clear from the above discussion of Japanese insolvency law, a stay of creditor action against the debtor operates once proceedings of whatever type are commenced (though only in a corporate reorganization does the stay cover secured creditors). Banks typically have a tremendous number of outstanding obligations – deposit liabilities, inter-bank loans, foreign exchange and over-the-counter (OTC) derivatives contracts, wire transfer and other settlement transactions, letters of credit and other trade finance vehicles, to name just a few. The counter-parties in almost all such transactions are unsecured creditors. Thus, their unilateral efforts to obtain satisfaction against the assets of a bankrupt bank would be stayed upon commencement of a rehabilitation or liquidation proceeding under Japanese law. In other words, a stay pursuant to insolvency law would mean the cessation of all bank functions for a certain period of time. How would these counter-parties react to the inability of the debtor bank to make good on its obligations?

Inevitably, the counter-parties would declare the debtor in default. Suppose the creditor banks were relying on payments from the debtor bank as their source to finance their own obligations to other financial institutions. The creditor banks now would be in a perilous position. They might not be able to make good on their own obligations, which, in turn, would cause their financial institution creditors to call a default, and put the liquidity positions of these creditors in jeopardy. This chain reaction of defaults is, of course, systemic risk. The bottom-line fear, then, about resorting to insolvency law to resolve a troubled bank case is that the stay of creditor action will trigger a systemic risk nightmare. Better, then, for government and central bank authorities to step in and resolve the matter through extra-insolvency law means than to sit idly by while entity after entity in the financial system tumbles like dominoes. As the above excursion shows, Japanese authorities did just this. In all cases of bank failure, bank functions were continued.

The second reason for eschewing insolvency law where the debtor is a bank follows logically from the first. Systemic risk, if it materializes, has broader social implications. The Japanese public has no experience after the Second World War with losses from bank failures. Imagine the panic that could spread among the populace if they lost their precious savings, or even a portion thereof, in banks that had closed their doors. They would be powerless in the face of the judicially-condoned stay. In the end, after months or years of

334 Article 59 of the Bankruptcy Law and Article 103 of the Corporate Reorganization Law empower a trustee to assume or reject executory contracts. Some of the financial contracts in which a bank debtor is likely to have engaged may be subject to bilateral or multilateral netting arrangements. The subject of netting is beyond the scope of this paper. Suffice it to say that the famous November 1990 Bank for International Settlements report – commonly known as the “Lamfalussy” Report – requires that netting have a well-founded legal basis in the event of insolvency. Japan’s Law Concerning Close-out Netting (Law No. 108 of 1998) is designed to provide this basis for close-out netting arrangements on specified financial transactions, including OTC derivatives.

335 Interestingly, the banking functions of Hokkaido Takushoku were continued for one year after its failure. The continuation was made possible by special loans from the Bank of Japan, also known as “Article 38 loans,” the outstanding amount of which peaked at ¥ 2.6 trillion. (“Article 38” refers to the applicable section of the Bank of Japan Law.) The Bank of Japan later covered the Hokkaido Takushoku loans by proceeds from the sale of assets of the failed bank, and with funds provided by the Deposit Insurance Corporation.
insolvency proceedings, they might collect little or nothing. The panic among depositors in
the failed bank likely would spread to depositors in otherwise solvent banks. A flow of
withdrawals would follow from banks around Japan, putting severe liquidity pressures on
these banks. The irrational (initially, anyway) but unstoppable behavior of depositors would
exacerbate the systemic risk chain already set in motion by the string of defaults called by
financial institution creditors. Indeed, the combined operation of defaults and withdrawals
would reinforce each other and, in the end, be too much to bear.

Thus, as long as the minimization of systemic risk and social unrest remain the
dominant political concerns among Japanese authorities, the country’s five-part insolvency law
regime will be relevant to banks as debtors only in theory. Resolving bank failures speedily
will remain the ken of specialists. For banks, the practical import of the “regular” or “normal”
insolvency regime will be that it will be applied to them as creditors of failed non-financial
institutions.

III. SHOULD INSOLVENCY LAW BE IRRELEVANT?

Perhaps the conventional wisdom about the need for a separate regime for bank
failures should be re-examined. That is, should authorities allow the insolvency regime to do
its work with a failed bank? After all, concerns about systemic risk and social unrest are not
testable hypotheses. Rather, they are testable, but at potentially great costs. Thus, in the hands
of government and central bank officials, they are more nearly axioms than hypotheses.

Most authorities would be likely decry any attempt to apply the “regular”
insolvency rules to banks. In the one instance where the Corporate Reorganization Law was
used, Sanyo Securities, the results, they would say, were disastrous. To be sure, Sanyo was
not a commercial bank, but a securities firm, but no matter. The systemic risk fears
materialized. The automatic stay triggered by use of the Reorganization Law led a small
financial institution counter-party of Sanyo to call a default on an indebtedness of several
million yen owed by Sanyo to the counter-party. The inter-bank market participants reacted to
the default by slashing their credit lines to each other. (Sanyo, of course, could receive new
lending after the legal proceeding had commenced only with court permission, but most
creditors would be unlikely to offer up new funds in such circumstances). The result was a
shrinkage in inter-bank market transactions among other institutions. The subsequent
reorganization process has not proceeded smoothly, and Sanyo might be liquidated. The
authorities likely would add – not unreasonably – that what matters is not whether bank
bankruptcies are resolved in a court house under the same set of rules that apply to non-bank
debtors. Rather, what matters is whether bank bankruptcies are resolved in a consistent
manner using transparent rules.

Arguably, however, the Sanyo case ought not to inhibit discussion of whether
to continue on the road of treating bank debtors specially. Why, indeed, should there be a
separate set of rules designed uniquely for bank insolvency cases? There are arguments that
counsel against special provisions for banks as debtors in these cases. If special rules are to be
had, then they will be more legitimate if these arguments are successfully met.

First, it hardly would be elegant to add yet another set of insolvency rules to the
regime. The sources of law are in need of rationalization and simplification. Adding a new set of rules risks transforming an already complex and opaque body of law into a positively byzantine one. If an analogy to international trade may be permitted, GATT Article X stresses the importance of transparency in a trade regime. The theory is that transparency is a hallmark of the rule of law: all similarly-situated players, regardless of national origin, ought to have equal opportunity to learn of the existence of, and understand, the rules. Whether Japan’s insolvency regime could be called “transparent,” particularly if a new body of bank bankruptcy rules were implemented, is an open question.

Second, special insolvency rules for banks beg an important question: are banks special? In an early 1980s piece published by the Federal Reserve Bank of Minneapolis entitled *Are Banks Special?*, former Federal Reserve Bank of New York President E. Gerald Corrigan answered this question in the affirmative by saying that banks are the mechanism for transmitting monetary policy and are the essential ingredients in the payments system. Mr. Corrigan’s argument may or may not be right. Arguably, financial institutions other than commercial banks play important roles (securities firms are primary dealers in open market operations conducted by the Federal Reserve Bank of New York, and payments can be made through a variety of services offered by these firms). But, assuming his argument holds true, does it translate into a justification for unique insolvency rules for banks? Somehow, the case has to be made that Japan’s five insolvency law work well for non-financial institutions, but cannot be made to work for banks. Perhaps the argument might go along the lines of the systemic risk associated with the failure of a major financial institution. But, here it would be wise to specify the causal chain – the “parade of horribles” – carefully, not just in the skeletal form as above. Simply waving the words “systemic risk” in the air, as bank regulators have been wont to do, will not do. Equally important will be to show why the same severe repercussions would not occur were a major non-financial corporation to go under. After all, could not the failure of the likes of IBM, Microsoft, Disney, or General Motors – or their Japanese analogs – start off a market panic?

If the case for a separate bank insolvency law cannot be made – and whether it has been made persuasively as yet is arguable – then there is a third argument against enacting legislation on insolvency just for banks. In a word, favoritism. The Japanese polity may well view such legislation as favoring banks over non-banks. The segment of the polity that may be especially vocal on this point are non-banks. Despite *keiretsu* relationships, managers of non-financial firms, and their shareholders, could hardly be expected to agree that their firms should remain subject to one set of insolvency rules, while banks get the benefit of a new, more debtor-friendly, set of rules.

There is yet one more argument counseling against special bankruptcy rules for banks: moral hazard. If those special rules amount to bailing out banks, then what incentive exists for bankers to avoid the same foolhardy behavior in the future that got them in trouble in the past? It is perhaps too early to view the history of the Japanese response to the banking crisis as a bailout that has created a moral hazard problem, though in the end that may prove to be the correct judgment. Doubtless officials would respond to any such suggestion that they were supporting the financial system, not bailing out individual banks. As for the managers at the banks, they were tossed out, and shareholders were penalized to boot. But, again, the facts – after enough time has passed to allow for a less biased perspective – might suggest otherwise.

Despite all of the arguments that might be made against a separate bank
insolvency regime, the issue seems resolved for now. For banks as debtors, the insolvency law regime simply is not relevant in practice. For banks as creditors, given the economic straits in which Japan finds itself, the regime is as relevant as ever.

IV. A TREATY ON INTERNATIONAL BANK INSOLVENCY?

Why an international bank bankruptcy law has not been written is somewhat of a mystery. Perhaps there is simply a lack of vision and leadership among relevant international and domestic institutions, a deficit that ought not to be excused easily in the wake of the BCCI clean up. Part of the explanation may be that there is an overhang of territorialism from the discussions of international insolvency in the non-bank context. Part of the explanation for the mystery may be that there is no genuine consensus about the need for a separate set of bank bankruptcy rules. Whatever the reason, there ought to be no dispute that BCCI-type liquidation problems should be, in some reasonable way, avoided. The obvious way to do so would be for countries to band together on a multilateral treaty that would cover international bank bankruptcies.

To keep matters simple, the treaty could apply to “international banks,” defined as banks (1) whose assets (both on- and off-balance sheet) are worth at least a certain threshold amount (say, for example, U.S. $500 million) and (2) which have assets (again, both on- and off-balance sheet) in two or more countries. The treaty would be implemented into the local law of each signatory country, perhaps on a self-executing basis. Under the treaty, once the home-country regulator of a bank decided to close a bank, a single closure proceeding would take place under the auspices of a Multilateral Insolvency Facility (MIF). One candidate for the MIF would be the International Monetary Fund (IMF), given its extensive membership. Another candidate would be the World Bank which, after all, offers a facility for the international settlement of investor disputes (ICSID). A third candidate might be Bank for International Settlements (BIS), though it would suffer from a less diverse membership and thus could not encompass as many international bank debtor scenarios. (That problem could be dealt with through patch work efforts by treaty countries to make suitable arrangements with non-treaty countries, and the result could be a rather complex quilt.)

Under the multilateral treaty, all creditor claims brought in a local court of a treaty country would be stayed automatically by virtue of the country’s treaty obligations. The court would inform all potential claimants that they are to file proof of claim with the MIF. The MIF would resolve the bank bankruptcy under the rules set forth in the treaty. These rules would include a unified set of priorities, and criteria for the determination of fraudulent conveyances. Under the treaty, the MIF would marshal the world-wide assets of the failed international bank, and pay out claimants in accordance with treaty rules. The MIF could call upon the assistance of relevant local authorities, including central banks, which would be obliged to help.

Perhaps this sort of treaty would entail too much of a loss of sovereignty for individual countries. They might have an attachment to their local laws on bank bankruptcy, and might not be able to come to a unified agreement. Negotiations might, for example, break down on priority orderings among creditors of a failed international bank. Likewise, if the treaty covered bank reorganizations as well as liquidations, then countries simply might not
like the idea of the MIF having the power to replace managers of local banks. Accordingly, a second, somewhat less ambitious, treaty might be possible.

In this “fall-back” scenario, creditors of a failed bank would present their claims against the assets of a failed international bank (as defined above) under the local applicable law. This law would not be displaced by the treaty. Actual execution of claims would be stayed, however, again by operation of a treaty. Courts in the various countries where the claims are brought would be responsible for developing a list of creditors that have proven their claims, and the order of priority among these creditors, under local law. Each court would then transmit this list to an international authority – again, perhaps the IMF, World Bank, or BIS. That authority would then give effect to the lists. That is, it would marshal assets, and pay out creditors as the assets permit in the order of priority determined by the local courts. The authority would have the power to resolve conflicts among priorities. But, absent inconsistencies would not contain a unified set of priorities. Likewise, fraudulent conveyance issues would be left to local courts. The authority would be empowered to resolve inconsistent adjudications in local courts about whether a transfer from the debtor-bank antecedent to the insolvency was a fraudulent conveyance.

In effect, this second type of treaty would be an institutionalization of some (but not all) of the *ad hoc* procedures that emerged in the BCCI affair. The authority would implement decisions already made by local courts under local law, which the treaty would give effect to and provide rules for resolving conflicts. In contrast, under the first type of treaty the MIF would conduct the insolvency proceeding under treaty law.

The first treaty proposed would be a clear manifestation of the universality principle. The second treaty would reflect modified universalism. Both aim at the speedy and fair resolution of failures of large banks that are internationally active. Perhaps the political prospects for actually negotiating a multilateral treaty of either type seem dim. However, naysayers must remember that international law has progressed towards unified dispute resolution schemes, not just in the trade field, but also in the areas of commercial arbitration and criminal law. The successful efforts in these fields may be cause for some hope in the international bank insolvency area.
SUMMARY: REFORM IN CONTEXT

Few if any observers doubt that international cooperation in the international insolvency law field is desirable and necessary. Yet, so formidable are the obstacles to formulating an ideal unitary system that the notion seems a bit quixotic.336 Different national policies and mechanisms are the primary obstacles. Political will to overcome them – a will as strong as that observed in the international trade law arena during the 1986-93 Uruguay Round – does not yet seem to exist among insolvency officials around the world.

Section 304 of the American Bankruptcy Code is a case in point. Ancillary proceedings conducted thereunder are considered to be one of the boldest and most innovative attempts toward universality in the history of international insolvency law.337 Yet, under these proceedings foreign laws can be compared primarily for the purpose of protecting local creditors.338 To achieve complete universality, the United States, along with all other countries, would have to unify their priority schemes, as well as the rest of their substantive and procedural insolvency laws. If this point can be made about American insolvency law, then a fortiori it applies to the Japanese context. The extent of international cooperation under current Japanese law is depressingly limited. To deal with a central reality of the global economy of the new millennium – multinational debtors with assets and liabilities scattered across the globe without regard to geo-political boundaries – a complete overhaul of Japan’s insolvency law regime is needed. With its diverse sources and inward-looking nature, the regime now seems akin to a fragmented hard drive. A single, outward-looking regime is needed.

Fortunately, work toward this end has started. The exact details and drafting of new insolvency rules are best left to the experts now involved in the reform project. However, this paper offers some broad guidance. The central thesis is that comprehensive reform needs to be seen in two contexts: the economic crisis, and recent developments in comparative and international insolvency law.

First, reform ought to address Japan’s economic health, or lack thereof. The attention-grabbing headlines focus on Keynesian tactics, supply-side structural reform, deregulation, and liquidity trap counter-measures. But, perhaps the most important underlying implicit theme of this paper is that there is more to recovery than economic measures. Appropriate legal reform, including insolvency, is critical. Yet, legal reform ought not to be simply a reaction to the crisis. It should not only safeguard the interests of creditors, but also ensure that debtors are encouraged to take entrepreneurial risks – and that creditors will provide financing for them to do so. Creative capitalism is, after all, a cornerstone on which Japan’s economic recovery can proceed. A flexible insolvency regime can be an element in that brand of capitalism.

Second, insolvency law reform in Japan ought to account for trends in the international insolvency arena. Possibly, it also ought to put to rest the nagging matter of the status of banks as debtors. Thankfully, pure or nearly pure territoriosity, a principle animating in Japan’s insolvency regime, has seen its best days. Twenty-first century thinking, as

336 See Tagashira, supra note 166, at 37.
337 See id. at 37.
338 See id.
exemplified by the UNCITRAL Model Law, and, by way of analogy, the Uruguay Round trade agreements, points toward universalism.
APPENDIX:

THE DOMESTIC LEGAL CONTEXT

It might well be said that there is a third context in which to consider Japanese insolvency law and its reform: the domestic legal context to consider. That context is a civil law structure. For instance, outside pressures that demand far-reaching changes in judicial discretion would be mis-directed. At the same time, insolvency reform ought not to be accorded either a low status or low priority in the legal scheme. After all, even a forward-looking set of insolvency rules is not worth much if the rules are subject to override by higher-level statutes or codes. Furthermore, insolvency law is indeed redolent of a symphony. All of the components of that law, and the reforms made to them, like all of the instruments in a symphony, must work in harmony.

The Japanese legal system in which its bankruptcy law is embedded is a history of contributing influences. Very little of the content of current Japanese law is authentically Japanese. Indeed, the legal imports have impacted on the country’s social, political and economic systems. Importation of legal doctrine in large volumes began during the Meiji Era (1868-1912), when Japan looked to the west for legal models following nearly 200 years of closure during the Tokugawa period. To develop a constitutionally-based government, Japan looked to France and Germany. From that sprung six legal codes that Japan adopted, which became the primary sources of law in Japan’s civil law system.

The influence of the early French and German imports are still felt today through these codes. More obvious, however, is the impact of the United States following the Second World War. During the Occupation Period, which pursuant to the Potsdam Declaration lasted from 2 September 1945 until 28 April 1952, the Americans introduced several legal reforms. Japan adopted a new constitution and modernized several of areas of law. The result remains largely in place.

339 The author gratefully acknowledges the background memorandum, “Japanese Legal System” (June 15, 1999), by Ms. Kris Hansen, GW Law School Class of 2000, which assisted in the preparation of this Appendix.


342 See id. at 2401.

343 See id. at 2402.

344 See id. at 2403.

345 See id. at 2601.

346 See id.

347 See L.W. Beer, The Present Constitutional System in Japan, in CONSTITUTIONAL SYSTEMS IN LATE TWENTIETH CENTURY ASIA 176 (L.W. Beer, ed. 1992) (noting that although it was an Allied occupation, the American influence dominated).
I. CONVENTIONAL SOURCES OF LAW

A. The Six Codes

As a civil law country, Japan’s the primary source of law is its six codes – five codes plus the Constitution. Collectively, they are known as roppo, the “six laws,” and are supplemented by statutes, ordinances, regulations, and other provisions. The codes are the indispensable starting point for any analysis of Japanese law, and each cannot be viewed in isolation. It is often critical to make conceptual linkages to maneuver among the codes. This need should come as no surprise to the seasoned bankruptcy attorney. Bankruptcy cases often require research outside the narrow confines of the field into, for example, contracts, civil procedure, and even criminal law.

Constitution

Japan’s Constitution is the first among equals with respect to the six codes, i.e., it is the supreme law of Japan. Of the codes, it is in the Constitution, which entered into force in 1947, where American influence is most detectable. It bespeaks the political and legal theories that underlie the United States Constitution, Bill of Rights and Declaration of Independence. But, it is hardly a mindless reincarnation of these theories. Japan’s constitution was drafted by American lawyers under the supervision of General Douglas MacArthur, the Supreme Commander of the Allied Powers, with a view to reform. Democratization and demilitarization were prime reform goals.

Accordingly, the 1947 Constitution embodies the principles of pacifism, sovereignty of the people, and inviolability of human rights. In addition, it creates three branches of authority. Article 41 vests the legislative power in the Diet, a bicameral body of the House of Representatives (the Lower House) and the House of Councillors (the Upper House). Article 65 confers executive power on the Cabinet. Article 76 grants judicial power to the courts, and Article 81 makes plain that the Supreme Court is the “court of last resort with power to determine the constitutionality of any law, order, regulation or official act.”

Civil Code

Following the Constitution, the Civil Code is the most general pronouncement

349 See id.
350 See JAPAN CONST. Art. 98 (1947).
353 See id.
354 See Port, supra note 340, at 45.
355 See id.
356 See id. at 46.
of law.\textsuperscript{357} Yet, it is hardly a static pronouncement. Since its original enactment in 1898, the Civil Code has undergone several revisions.\textsuperscript{358} It is comprehensive in that it covers property, contracts, torts, family law, and the law of succession.\textsuperscript{359} Thus, it is divided into the following five books: (1) the General Part, which outlines basic principles and rules of civil law; (2) “real rights,” concerning property and real security; (3) Law of Obligations, e.g., torts and contracts; (4) Family Relations; and (5) Inheritance.\textsuperscript{360} These books are, in effect, supplemented by the other codes and statutory provisions that operate within the Civil Code framework and provide more particularized rules.

**Commercial Code**

Japan’s Commercial Code, which bears an obvious relevance to its bankruptcy law given the special liquidation proceeding that it provides, closely follows the French Commercial Code.\textsuperscript{361} The Commercial Code applies to merchants, and sets forth various rules for the formation and operation of different kinds of business associations. In this respect, the Commercial Code modifies and supplements the provisions of the Civil Code and sets forth special provisions. When there is no applicable provision of the Commercial Code, commercial custom is applied. Only when there is no such custom, is the Civil Code applied.\textsuperscript{362}

The original Commercial Code was divided into five books concerning different topical areas. These were (1) general concepts, (2) corporations, (3) commercial transactions, (4) bills of exchange and checks, and (5) maritime law.\textsuperscript{363} Since 1932, however, the number of books in the Commercial Code has been cut to four. In that year, the Geneva Convention on the Unification of the Law of Bills and the Law of Checks replaced Book 4.\textsuperscript{364} The four parts have since been renamed and re-organized. Substantial changes in company law, in particular, reflected American post-war influence.\textsuperscript{365} The Japanese, too, have instituted various other reforms of the company law, including (for example) the 1990 Law on Limited Liability Companies.\textsuperscript{366} Thus, the Commercial Code now consists of the “General Part,” “Company Law,” “Commercial Transactions,” and “Merchant Shipping.”\textsuperscript{367}

\begin{footnotes}
\item[357] See Yanagida, supra note 348, at 32.
\item[358] See Young & Jameson, supra note 341, at 2404.
\item[359] See Oda, supra note 352, at 133.
\item[360] See id.
\item[361] See Young & Jameson, supra note 341, at 2451.
\item[362] Oda, supra note 352, at 134.
\item[364] See id.
\item[365] See Oda, supra note 352, at 262.
\item[366] See id.
\item[367] See id. at 261. The Merchant Shipping part of the Commercial Code includes provisions on insurance.
\end{footnotes}


**Code of Civil Procedure**

Japan adopted its first Code of Civil Procedure in 1891. As with other areas of Japanese law, the Code of Civil Procedure was revised in the post-Second World War era. The revamped Code introduced a more adversarial system – arguably a mixed blessing from the United States. Likewise, it increased the responsibility of parties to litigation to produce evidence and examine witnesses. This Code is not, however, a re-hash of the Federal Rules of Civil Procedure. It bears a distinctly Japanese touch: encouragement for the use of alternative dispute resolution procedures. Thus, Dean Young and Professor Jameson comment that “[a]s a system that defined legal procedures in [Western] terms never before articulated in Japan, the procedural code was, to say the least, a major legal innovation. At the same time, it was designed to reflect some elements of the indigenous preference for conciliated settlement.”

**Code of Criminal Procedure**

The Code of Criminal Procedure, originally enacted in 1880, was superseded by the present code in 1923. Both were drawn from the German analog. Following the Second World War, Japan introduced major changes to criminal procedures that were instigated by constitutional reforms. “The Constitution incorporated a provision requiring the due process of law and guaranteed the right to a defense and other related rights in the Bill of Rights. This necessitated a fundamental reform of criminal procedure.” Not surprisingly, some of the changes were distinctly American in style. For instance, a right against self-incrimination was introduced. Some of the changes also mirrored those made to the Code of Civil Procedure. For example, trials became more adversarial, less inquisitorial, in nature, and the prosecution and defense were given the responsibility of producing evidence and examining witnesses.

**Criminal Code**

What is considered criminal activity in Japan is itemized in the Criminal Code. Japan revised this Criminal Code in 1907 to resemble the German version. Japan’s Code is bifurcated. The General Part covers basic concepts of criminal law such as intention, negligence, etc. The Special Part lists individual types of crimes. Post-War revisions in the Code helped bring it into compliance with the new Constitution. It is an unfortunate hallmark of a modern and fast-changing society that the Criminal Code frequently

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368 See Young & Jameson, supra note 341, at 2451.
369 See id.
370 Id.
371 See id. at 2452.
372 See Oda, supra note 352, at 398.
373 See id.
374 See id. at 402.
375 See id. at 388.
376 See Young & Jameson, supra note 341, at 2452.
377 See Oda, supra note 352, at 388.
is amended to keep pace with new types of crimes. However, the fundamental formula for criminal conduct remains unchanged, and the same as that in Anglo-American jurisprudence: for an act to be punishable, it must fit the definition of a specific crime (the *actus reus*) and be blameworthy (the *mens rea*).

B. Statutes And Treaties

There is more to the legal context for bankruptcy law than the six codes. Statutory provisions compliment these codes with particularized rules. How are statutes enacted? Under the Constitution, the Diet is the supreme and only law-making body. Usually, a bill is drafted and submitted to the Diet by the relevant ministry. If an issue is especially complicated, or when a proposal involves one of the major codes (e.g., the Commercial Code or the Criminal Code), the Diet may consult an advisory committee (e.g., the Legislative Advisory Committee).

Once one of the two houses passes proposed legislation, the bill is sent to the other House for discussion. Suppose the Lower House passes the bill with which the Upper House disagrees. The Lower House can overrule the Upper House by a two-thirds majority. Conversely, if the Upper House does not act on a bill within sixty days, then the Lower House may assume the bill as vetoed. Suppose the Diet passes a bill and the relevant minister, along with the Prime Minister, signs the bill. Then, the Emperor must, upon the advice and approval of the Cabinet, promulgate the law in Japan’s official gazette. The law enters into force twenty days after promulgation, or the day designated by the law or any related order.

Like statutes, treaties supplement the six codes. Curiously, however, the Constitution does not address the status in the Japanese legal system of a properly signed and ratified treaty. It is clear that the Cabinet may enter treaties with the approval of the Diet, pursuant to Article 73(3) of the Constitution. The mandate of Article 98(2), that treaties are to be “faithfully observed,” also is straightforward. Article 98(1) instructs that the Constitution takes precedence over acts of the government, including the conclusion of

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378 See id.
379 See id. at 392.
380 See Dean, supra note 363, at 149.
381 See JAPAN CONST. Art. 41 (1947).
382 See Oda, supra note 352, at 46.
383 See id. at 46-47. The system of committees and practice of seeking out the advice thereof was introduced by the United States after the Second World War. See id. at 48.
384 See Oda, supra note 352, at 49.
385 See id.
386 See id.
387 See Dean, supra note 363, at 151.
388 JAPANESE CONST. Art. 73(3) (1947).
389 Id. at Art. 98(2).
While there has been some scholarly debate in the matter, there is a consensus on how to handle an inconsistency between the Constitution and a treaty provision: treaties occupy a middle ground, in which they are subordinate to the Constitution, but superior to ordinary legislation passed by the Diet.

II. OTHER “SOURCES”

A. Case Law And Commentaries

The theory of sources of law in civil law countries is that only the Constitution, codes, statutes, and regulations qualify. Before the early twentieth century, most Japanese scholars agreed with the theory, agreeing with Montesquieu in his Enlightenment classic, The Spirit of the Laws, that judges – who are not directly accountable to the people – should solve only the dispute before them and not make new law. In other words, in theory, the doctrine of stare decisis did not exist in Japan. The “official” line remains that case law may be “considered a source of law, but it is in no way binding or authoritative as it is in a system where stare decisis operates.” Currently, however, the “importance of judicial decisions has been recognized for some time, particularly in the field of civil and commercial law.” As in most civil law countries – even the quintessential one, France – there is now a blend of civil and common law traditions that can be attributed not only to American influence during the Occupation, but also the Anglo-Americanization of legal systems generally. To be sure, no provision of Japanese law addresses the status of case law as a source of law, except that Article 4 of the Court Reorganization law of 1947 provides that “a conclusion in a decision of a superior court shall bind courts below in respect of the case concerned.” Nonetheless, at a minimum it is safe to say that the system is one more akin to case consistency, rather than binding authority.

390 See id. at Art. 98(1).

391 See Oda, supra note 352, at 52. Similarly, foreign laws that are contrary to public policy are subordinate to Japanese laws, or in some instances inapplicable. See Law on the Application of Laws, No. 10, 1898, Art. 33.


393 Dean, supra note 363, at 154. Similarly, case commentaries and scholarly opinions are not formal sources of law, but they have a great impact on judicial decisions and lawmaking in general. See id. at 155. Japanese lawyers rely on case commentaries rather than on the case reports. See id. at 153.

394 Dean, supra note 363, at 154.


396 See Dean, supra note 363, at 154.

397 Id.

398 See id.
This safe statement, in the judgment of some legal scholars, underestimates the value of judicial opinions. It is indeed defensible to argue that “in the practical meaning, court decisions, especially precedents of the Supreme Court, have not only high persuasive authority but also strong binding force.”\textsuperscript{399} This binding force is felt whenever reversal of a Supreme Court opinion is sought. “The Supreme Court has an important function to insure the uniformity of judicial decisions and to assure enforcement of the uniform application of the law. For this purpose the new Court Reorganization Law provides that if the case proves to require a change in established precedents of the Supreme Court, it shall be heard by the Grand Bench comprised of all members of the court.”\textsuperscript{400} Accordingly, reversals of “precedent” are very difficult.

Perhaps the most formidable barrier to the development of at least a \textit{de facto} doctrine of \textit{stare decisis} is not theory but transparency, namely, the way cases are reported. Only a fraction of all cases are reported. Worse yet, in the few cases that are published, a precise and complete explanation of the facts typically is absent, because the factual aspects of each case is rarely emphasized.\textsuperscript{401} It is, therefore, difficult to distinguish cases, or to frame consistent legal arguments based on factual analogies. Moreover, in all but the Supreme Court, opinions are unanimous, without dissenting or concurring opinions to help supplement the legal reasoning of a decision.\textsuperscript{402}

**B. Administrative Guidance**

Any discussion of sources of law in Japan would be incomplete without mentioning administrative guidance (\textit{gyosei shido}) by government agencies. Like case law, this guidance cannot be counted as a formal source of law.\textsuperscript{403} But, also like case law, its prominence in shaping the legal regime cannot be ignored. In fact, administrative guidance has received much criticism because of its wide influence notwithstanding its nebulous legal roots.

\textsuperscript{399} Ishida, \textit{supra} note 392, \textit{in} Dean, \textit{supra} note 363, at 185.

\textsuperscript{400} \textit{Id.}

\textsuperscript{401} \textit{See} Yanagida, \textit{supra} note 348, at 50.

\textsuperscript{402} \textit{See id.} One scholar rightly observes:

\begin{quote}
[I]n Japan the prior opinion is looked to primarily for its “gloss on the statutory language;” the manner in which it has interpreted the relevant statutory language is normally of greater importance than distinctions between the basic facts of cases. This does not mean the factual distinctions are irrelevant, of course. Rather, the statutory reasoning constitutes the centerpiece of the opinion, with factual distinctions being relatively less important than in the typical common law cases. Accordingly, in addition to examining the relevant language of the Codes and related statutes, Japanese legal practitioners typically consider both precedent and scholarly commentary, but frame their arguments primarily in statutory construction terms.
\end{quote}

\textit{Id.} at 50-51.

\textsuperscript{403} \textit{See} Oda, \textit{supra} note 352, at 61.
What exactly is “administrative guidance”? Dean Young defines it as “a common Japanese regulatory technique that, although generally non-binding, seeks to conform the behavior of regulated parties to broad administrative goals.” Japan’s Cabinet Legal Department offers the following definition:

[Administrative guidance] is not legal compulsion restricting the rights of individuals and imposing obligations on citizens. It is a request or guidance on the part of the government within the limit of the task and administrative responsibility of each agency as provided for in the establishment laws, for the purpose of achieving some administrative objective through cooperation on the part of parties who are the object of the administration.

Administrative guidance is manifest in a variety of form. Directives, requests, warnings, suggestions, or encouragements are all examples, and all may be issued with a greater or lesser degree of subtlety.

How much deviation from administrative guidance is permitted? In most instances, the degree of variance or non-compliance that the government allows is unclear. Consequently, administrative guidance is the ultimate form of bureaucratic control. It is likely to induce full compliance simply because whether there is an alternative, and what the penalties might be for pursuing an alternative if one exists, are uncertain. Administrative guidance is thus troublesome. It lacks a legal foundation, it lacks procedural fairness and transparency, and there is very narrow access for judicial review. Yet, in practice it operates on par with formal sources of law.

Fortunately, the administrative guidance apparatus seems to be changing. In 1993, the Diet enacted an Administrative Procedure Law. Its purpose is to make the Japanese administrative process more uniform, fair, and transparent.

C. Custom

Tradition in Japanese civil law says that only the state can make law. But, from time to time, there is a need for interstitial rule-making. The Japanese allow for custom to fill these gaps, and it is not an overstatement to say that in some instances custom can have the force of law. The Law Concerning the Application of Law indicates that customs not

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405 Dean, supra note 363, at 157.
406 See id. at 159.
407 See id., at 159.
408 See Young, supra note 404, at 935; Oda, supra note 352, at 63.
411 See Dean, supra note 363, at 152.
412 See Port, supra note 340, at 50
contrary to public order shall “have the same force as law insofar as they are recognized by the provisions of the law and ordinances, or are related to matters which are not provided for by law or ordinances.” Additionally, the Great Council of State Decree No. 103, 1875, Article 3 explains that written law is the primary source of law, but gives significant importance to custom and, failing any, reason: “[i]n civil trials, those matters for which there is not written law are governed by custom and those matters for which there is no custom shall be adjudicated by inference from reason (jori).” Similarly, Article 92 of the Civil Code provides “if in cases where there exists custom which differs from any provisions of laws or ordinances which are not concerned with public policy, it is to be considered that the parties to a juristic act have intended to conform to such custom, that custom shall prevail.”

III. THE JUDICIARY

The 1947 Constitution reformed the judicial system, establishing its supremacy and independence. In addition, the Court Reorganization Law, effective 3 May 1947, implemented Chapter VI, Articles 76-82 of the Constitution, forging a new structure and role for the judiciary. The Law liberated the judiciary from the control of the Ministry of Justice by making it autonomous and placing it under the Supreme Court’s leadership. The modern Japanese judiciary thus has five elements: (1) the Supreme Court; (2) High Courts; (3) district courts; (4) family courts; and (5) summary courts.

The Cabinet nominates one individual to be the Chief Justice, and the appointment is made formally by the Emperor. In turn, fourteen additional persons are appointed by the Cabinet and authorized by the Emperor to serve as justices on the Court. The fifteen-justice Supreme Court is located in Tokyo. Each justice faces periodic reconfirmation by the electorate, though no sitting justice has ever lost an election. The Supreme Court Secretariat nominates the over 2,000 non-Supreme Court judges, who are then appointed by the Cabinet. The Secretariat, acting as the administrative center of the courts, appoints these judges to new assignments every two to three years.

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413 Law Concerning the Application of Law, No. 10, 1898, revised Law No. 223, 1947, Art. 2.
414 Article 3, Decree No. 103, 1875, quoted in Dean, supra note 363, at 150 n. 16.
415 Japanese Civil Code, Art. 92.
416 See Port, supra note 340, at 61.
417 See Court Reorganization Law, No. 59, 1947.
418 See Port, supra note 340, at 61.
419 See id.
421 See id. at 65-66.
423 See id. at 17.
assignment, a judge may move up or down the judicial hierarchy.  

The eight High Courts hear appeals from the district and family courts, and have original jurisdiction in cases involving crimes of insurrection. District courts are the courts of general jurisdiction for most cases. Japan has fifty district courts, one in each of its forty-seven prefectural units, with Hokkaido having four. Depending on the nature of the case, a three judge panel or a single judge may preside. Family courts have jurisdiction over domestic matters and most juvenile delinquency cases, and summary courts handle minor criminal cases and civil cases with claims not exceeding ¥ 900,000.

Two important differences relevant to insolvency law between the Japanese and American judiciary stand out. First, Japan has no specialized courts to handle bankruptcy cases. In the United States, federal bankruptcy courts exist for this purpose. Second, the Japanese Court system is notorious for its lengthy delays. It is not uncommon for civil and criminal cases to be pending for more than a year. The main cause of the delays is a shortage of judges. Approximately 2,000 judges must handle all of the claims of the country. To be sure, American courts are stressed with backlogs, but various statutory and procedural measures, and aggressive case management by certain judges, aim at speeding up the litigation process.

424 See id.
425 See Port, supra note 340, at 64.
426 See id.
427 See id.
428 See Yanagida, supra note 348, at 47.
429 See id. at 41.
430 See Oda, supra note 352, at 79.
431 See id.
432 See id. at 80.
433 See id.