Asian insolvency trends

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There has been a vast increase and further expansion of global business enterprises in the region, along with the expansion of domestic markets in emerging economies in Asia. In some parts of Asia, global enterprises commonly find advantages such as cheap labour, but they are also increasingly pursuing opportunities for potential growth in developing markets within the region. However, many local subsidiaries and joint companies and global business enterprises are likely to become insolvent, and will need to file for bankruptcy or other insolvency proceedings because of:

- Political risk.
- Inadequate infrastructure.
- Risk of rapid and drastic changes to local laws.
- Risk of vastly increasing labour costs.

In Asia, insolvency laws and even entire legal systems (including their operation) are often vague and unsophisticated. Governmental institutions in Asian countries have initiated some reforms aimed at promoting efficient insolvency procedures. However, in several countries the reforms are still insufficient. Asian countries can be classified into three broad groupings in respect of the bankruptcy procedures they use.

ASIAN COUNTRIES WITH WELL-DEVELOPED INSOLVENCY PROCEDURES

Firstly, there are countries that have well-developed insolvency procedures, both in terms of how the system is set up and how it is operated. Japan and Korea are typical examples of these countries. In some respects, the Korean framework for bankruptcy proceedings is even more advanced and sophisticated than the Japanese framework, as it has efficiently used US and Japanese bankruptcy procedures and judicial precedents as a guide during its rapid development.

Korea. The Corporate Restructuring Promotion Laws (CRPL), which were enacted in 2005, are a good example of demonstrating the sophistication of Korean insolvency procedures. The CRPL have repeatedly been extended as temporary two year measures in 2007, 2009 and 2011. They were extended again by two years from 2013 to 31 December 2015, to enable a binding super majority vote for out-of-court workout proceedings. Under the CRPL, if creditors holding debts of more than 75% of the total amount of debts agree to a debt restructuring plan in an out-of-court work-out, debts can be impaired according to the plan and new money will be provided to the distressed companies. Under the CRPL, dissenting creditors can request that assenting creditors buy its debts, and the assenting creditors must be jointly and severally obliged to purchase the debt at a fair price (which may be lower than its face value). The case of Ssangyong Motor Co Ltd. is important. On 13 November 2014, the Korean Supreme Court overturned a previous ruling from the Seoul High Court that nullified the dismissal of Ssangyong employees due to economic conditions, ruling that the dismissal had been valid. The decision is significant, because it provided the grounds for determining whether or not dismissals for the purpose of restructuring under corporate reorganisation proceedings are justifiable.

Japan. In Japan, the Ministry of Economy, Trade and Industry of Japan (METI) is currently working to modify the Alternative Dispute Resolution Procedure for Turning Around a Business (Turnaround ADR). This procedure is occasionally used in out-of-court work-outs. In Japan, in order to validate the turnaround plan for reducing or rescheduling debts in a Turnaround ADR, unanimous creditor approval of the plan is required. However, following the lead of several other legal systems (including the US, the UK, France and various Asian countries (for example, Korea and the Philippines)), METI is considering amending the unanimous creditor approval requirement and replacing it with a super majority rule for Turnaround ADR procedures.

ASIAN COUNTRIES WITH MODERN BANKRUPTCY REGULATIONS BUT LACKING THE MEANS TO OPERATE THEM PROFICIENTLY

The second group of Asian countries are those that have modern bankruptcy regulations, but lack the means to operate them proficiently. China and Vietnam are typical examples of such countries.

Vietnam. In Vietnam, effective from 1 January 2015, the new bankruptcy law (Law No. 51/2014/QH13 on Bankruptcy, enacted on 19 June) replaces the previous bankruptcy law and introduces a number of important changes. For example, under the new law:

- Creditors and employees can file a petition to commence bankruptcy procedures against an enterprise.
- A new concept of asset manager (trustee) for an insolvent entity is introduced.

The reform may increase the number of bankruptcies and rehabilitation proceedings which may in turn help revitalise the Vietnamese economy.

China. In China, after the Enterprise Bankruptcy Law came into effect in 2007, the number of bankruptcy filings has gradually increased. However, some enterprises, especially state-owned enterprises, choose to avoid formal bankruptcy procedures, and instead make use of out-of-court work-outs.

ASIAN COUNTRIES WITH VAGUE BANKRUPTCY PROCEDURES AND OPERATIONS

The third group of Asian countries are those that have both vague bankruptcy procedures and operations. Countries in this group include India, Pakistan, Nepal, and Bangladesh (among others). Bankruptcy procedures in these countries tend to lack sophisticated laws and be operated in an arbitrary manner by courts and administrators. In addition, the shortage of legal specialists is also a problem. For example, in India, there is no single comprehensive and integrated corporate insolvency law to address the needs of an entity in distress.
However, on 29 August 2013 the Companies Act 2013 was enacted in India. The new Act provides guidance for a new insolvency and restructuring framework. The provisions regarding rehabilitation of “sick companies” in the Companies Act 2013 are yet to come into force. It is not clearly known when these provisions will be enforced.

In addition, the time necessary for completion of bankruptcy proceedings is very lengthy. According to the World Bank, it is not uncommon for proceedings to run for periods exceeding three to four years. Therefore, it is far more common to use a method involving the transfer of shares of local subsidiaries or joint companies, than to use insolvency proceedings.

To date there has been little written on international bankruptcy issues relating to Asian bankruptcy procedures. However, this publication acts as a practical guide intended to help global business enterprises better understand insolvency procedures in Asian jurisdictions.

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