



Forum for Asian Insolvency Reform (FAIR)

MAXIMISING VALUE OF NON- PERFORMING ASSETS

*Seoul, Korea
10 - 11 November 2003*

**Inauguration and First stage of the Industrial
Revitalization Corporation of Japan**

by

*Professor Dr. Shinjiro Takagi, Chair,
Industrial Revitalization Commission, Japan*

Inauguration and First stage of the Industrial Revitalization Corporation of Japan

Professor Dr. Shinjiro TAKAGI

1. Outline of the IRCJ as defined in the Basic Policy
2. The IRCJ Law and the Operation Overview
3. Practice of the IRCJ
4. Impact of the IRCJ on revitalizing businesses
5. The First Stage of the IRCJ

The Japanese economy has been in a slump for thirteen years. To spur its economic recovery, Japan has enacted a series of legislation meant to rehabilitate struggling companies, such as the “Financial Revitalization Law”, “Industrial Revitalization Law”, “Civil Rehabilitation Law”, “Corporate Reorganization Reform Law”, the “Special Law for Reorganization of Financial Institutions” and “Laws for Recognition and Assistance of Foreign Insolvency Proceedings”. In addition, the “Guidelines for Multi-Creditors Out of Court Workout” was established, referring to INSOL 8 Principles. Now Japan boasts of having one of the most extensive legal systems for corporate rehabilitation in the world. Nevertheless, the country is still in a long and unforeseeable recession. Under these circumstances, the Industrial Revitalization Corporation of Japan (IRCJ) was established in May, 2003 as one of the last resorts to recover Japanese economical prosperity.

This report was written before my appointment as a chair of the IRC Commission early May, 2003 to reflect my personal views only, and is in no way intended as the official view of the IRCJ.

1. Outline of the IRCJ as defined in the Basic Policy

The Comprehensive Measures to Accelerate Reforms proposed that the IRCJ be established as a key part of aggressively rehabilitating companies and industries, in addition to accelerating NPL disposal, aiming to cut NPLs by half within two years. The Basic Policy (BP) were adopted on this basis, and define the IRCJ and its operation policies as follows:

1. The IRCJ will act as a neutral intermediary in helping companies with excessive debt reorganize themselves when the company is viable but conflict of interests prevent the company and creditors from agreeing on a rehabilitation plan.
2. The IRCJ will intercede in matters that should be resolved by private entities. Therefore, the IRCJ should utilize private initiative as much as possible, promote the development and expansion of loan credit markets and securitization, and foster a market for corporate recovery funds.
3. The IRCJ shall not attempt to prolong a hopeless company’s life. And will help regroup industries with overcapacity in cooperation with governing ministries and agencies and by using the amended Industrial Revitalization Law if necessary.
4. The IRCJ will be financed by government-guaranteed loans. It will be incorporated as a joint stock company, allowing the government’s involvement in setting criteria for financial support and choosing executive directors.

5. The IRCJ will give support to companies classified as “borrowers requiring attention” (including “special attention” and “doubtful” debtors considered capable of rehabilitation). The IRCJ will purchase the loan obligations from the debtor’s non-main banks and draw up a reorganization plan in cooperation with the main bank and the debtor company if the IRCJ determines that more loans can be collected by reorganizing the company than by liquidising it and the reorganization plan agreed on by the main bank and the debtor company is considered feasible.
6. In preparing a reorganization plan, the IRCJ will ask for assistance from private sector experts in corporate restructuring. It will also use statutory procedures for corporate rehabilitation such as the Civil Rehabilitation Law and Corporate Reorganization Law.
7. Debt-to-equity swaps and DIP financing by government-affiliated financial institutions will be used. The IRCJ will be able to give additional loans, inject capital, form trusts and give guarantees to reorganizing and reorganized corporations.
8. The IRCJ will concentrate its purchase of NPLs in the first two years and sell the purchased NPLs and equities acquired via debt-to-equity swap within its five-year life span. In doing so, the IRCJ will strive to minimise the secondary losses taxpayers will ultimately bear.
9. The IRCJ will set fair and transparent standards for the NPLs it purchases. NPLs will be purchased at a market value deemed fair paying due consideration to the reorganization plan. No NPLs should be purchased or sold without approval of the IRC Commission, made up of experts.
10. A reorganization plan must be completed within three years and include measures to improve the balance sheet and profitability of a debtor company so that the debtor company will be able to be re-financed by itself and the IRCJ will be able to sell the loans it purchased. In principle, a plan must set targets that meet the standards stipulated in the Industrial Revitalization Law – standards of productivity enhancement and balance sheet restoration that are described below – for the debtor company to be approved for rehabilitation under the IRCJ scheme. The Industrial Revitalization Law is to be amended concurrently with the adoption of the IRCJ Law. The IRCJ will apply the criteria flexible, ready to make exceptions if the Commission believes there is good reason to do so.
11. A reorganization plan must include measures that enable a debtor company to achieve at least one of the following goals related to productivity improvement at the end of the planned period, which is three years or less:
 - (i) An increase in return on equity (ROE) of more than 2% (if a corporate recovery fund or other company buys the debtor company for the purpose of reorganizing it, cash flow—adjusted return on assets (ROA)—must increase by more than 2%.)
 - (ii) An increase in turnover ratio of tangible assets exceeding 5%.
 - (iii) An increase in added value per employee exceeding 6%.
12. Similarly, a reorganization plan must include measures aimed at achieving all of the following targets in financial health by the end of the three-year period or less:
 - (i) Interest-bearing debt 10 times less than the annual cash flow.
 - (ii) Ordinary income that exceeds ordinary expenses.

2 The IRCJ Law and the Operation Overview

The IRCJ Law provides insight into the workings of the IRCJ. The main points can be summarized as follows:

1. The IRCJ helps individual businesses with viable resources but excessive debt to reorganize by purchasing this debt from financial institutions, thereby ensuring that a healthy financial system is maintained through industrial revitalization and bad-loan disposal.
2. The IRCJ is a business corporation (K.K.) established by approval from the authorizing ministers, which in this case are the prime minister, finance minister, and minister of economy, trade and industry. These ministers must approve the IRCJ's executive appointments, budget plans, and financing (guaranteed by the government). They may use their supervisory position to issue administrative orders requesting reports and inspections of the IRCJ's operations.
3. The Industrial Revitalization Commission (with a membership not to exceed seven and including three or more directors, two of whom must be a representative director and external director) determines whether to extend revitalization support and makes decisions regarding the purchase and disposal of loans. Once a decision has been reached, the commission consults with the authorizing ministers and the ministers administering the relevant industries might make recommendations in light of the extent of the industry's overcapacity and relevant matters. The decision to extend support and purchase loans must meet the publicly disclosed criteria for support.
4. Companies will apply for reorganization support by submitting a business reorganization plan to the IRCJ with their financial institutions (in general, the main bank or banks). Based on the Commission's conclusion, the IRCJ will move quickly to decide whether to support those plans deemed to have a high chance of success. Non-main banks and other financial institutions should decide whether to sell loan claims to the IRCJ (including loan trusts) or accede to the business reorganization plan within the designated period up to three months, and the IRCJ will generally request that these banks temporarily stay on debt collection during this period.
5. The IRCJ will purchase the loans when these financial institutions request the purchase, or when the total sum of loans held by the financial institutions agreeing to the reorganization plan meets the sum necessary for revitalization (in the event that most financial institutions agreed to the purchase or agreed to the reorganization plan). The purchase price will be the appropriate market value decided by the IRC Commission paying due consideration of feasibility of the reorganization plan. The decision to provide support will be retracted if revitalization is not feasible due to the exclusion of financial institutions that do not apply for debt purchase or of financial institutions that hold large amounts of debt but do not agree to the reorganization plan, preventing the plan from reaching the necessary debt sum.
6. If financial institutions provide financing to the targeted company from the time the IRCJ decides to provide support to the time it decides to purchase debt, the super-priority claim of the DIP lender is noted in the reorganization plan, and the financial institution can request that the IRCJ acknowledge the necessity and super-priority claim of this DIP financing. The company may start proceedings for civil rehabilitation or corporate reorganization at a later point (before the IRCJ disposes of the purchased debt). Any unpaid DIP loans should be given priority in the reorganization plans which would be approved in the subsequent rehabilitation or reorganization proceeding. The courts may determine whether the authorization would go against the equitable treatment of creditors, but the courts must keep

in mind that (1) the IRCJ has given their approval to the claim and (2) financial institutions forgave loans according to the terms of the reorganization plan formed in former IRCJ proceeding, so the super-priority claims of DIP lenders will not hurt other creditors (this has set a precedent for the preferential treatment given to the claims of DIP lenders established before the debt transfer in subsequent statutory reorganization procedures.) .

7. The IRCJ can support the revitalization of a company whose debt it has purchased by providing financing, guarantees and capital. It can also review and adjust company operations, provide advice and conduct any other necessary task.
8. The last date for debt purchase is 31 March 2005, and the IRCJ must attempt to transfer or dispose of all purchased debt and/or converted stocks within three years of the purchase decision date. The IRCJ can raise funds by borrowing through government guarantee, and the government will compensate for losses to be incurred by IRCJ's negative net worth at its liquidation.

3 Practice of the IRCJ

The sections of the IRCJ law pertaining to the IRCJ's administrative responsibilities could have been drafted in reference to part of the "Guidelines for Multi-Creditors Out of Court Workout." Referring to these guidelines, the IRCJ's actual responsibilities can be summarized as follows:

1. Companies that are struggling due to excessive debt can draft a reorganization plan with their main bank(s). The company and banks' staff will develop this plan with help or backing from certified public accountants and restructuring advisers. The reorganization plan will encompass both financial and business reorganization, the first achieved by using debt forgiveness and debt-equity swaps to cut interest-bearing debt and increase/decrease capital, and the latter by closing and cutting unprofitable businesses in peripheral divisions, strengthening profitable core divisions, and even splitting up the company, using mergers and affiliations and business transfers. Preparing the draft plan takes from two to three months, and more than 20 staff—including bank and company staff and external specialists—work on the plan. Financial advisers provide help, and the staff look for candidates for sponsors and corporate recovery funds.
2. The main bank and the company hold preliminary discussions with the IRCJ's professional office. The office uses external sources such as restructuring advisers, and follows the advice of members in the IRC Commission as necessary, in reviewing the accuracy of the financial data and the draft's validity, feasibility and economic rationale. Revisions are made as necessary, and the office calls on the advice of certified public accountants, tax accountants, and lawyers as necessary. The office also performs a due diligence process to set the appropriate market value for the debt purchase price. This process requires about 20 staff and a two-month period.
3. Once a reorganization plan with high feasibility is completed, the company and its main bank(s) officially apply to the IRCJ for aid. After consulting with the relevant ministers, the IRC Commission makes a decision without delay on whether to offer revitalization support. Based on this decision, the IRCJ makes its own decision on support, and distributes the plan to the non-main banks, requesting a temporary stay on collections. The IRCJ also asks that the banks decide within a maximum of three months between two choices: whether to apply for debt purchase or to agree to the reorganization plan. The detailed reports prepared by the restructuring advisers and specialists will be used by the relevant ministers in their consultation, and by the commission in making their decision, regarding the prospects for the company's successful revitalization. In other words, a great deal of preparatory work is done out of sight during the period from the prior consultations mentioned in (2) to the application for revitalization support. Most plans that do not seem likely to be successful, despite

revisions made at the review stage, probably never make it to the official application stage. The IRCJ does not publicly release information on plans that make it to the application stage and are not accepted.

4. With the exception of a few creditors that can be excluded without impeding revitalization, the IRCJ purchases the debt when the non-main banks apply for debt purchase or agree to the reorganization plan. The IRCJ withdraws from the decision process if it does not gain the cooperation of the necessary financial institutions, and in this case the companies are likely to go through statutory reorganization procedures. The IRCJ sells the purchased debt within three years of purchase, and during this time it monitors the progress of the plan with the main bank. Any breakdown in the revitalization process will likely result in transfer to statutory reorganization procedures.

4 Impact of the IRCJ on revitalizing businesses

The IRCJ's objective is to help reorganize individual companies—a role normally left to the private sector to conduct on their own initiative. However, my involvement in establishing and administering the “Guidelines for Multi-Creditors Out of Court Workout” has shown me the necessity of the semi-private, semi-governmental IRCJ's involvement in reducing the interest-bearing debt of companies with excessive debt and restoring these companies to health quickly, for private-sector efforts are often insufficient for full-fledged revitalization. In October 2001 the government's economic council issued its “Program to Accelerate Reform,” which aims, among other things, to establish a lot of corporate recovery funds and make DIP financings more popular in Japan at the initiative of the DBJ, after which the Development Bank of Japan (DBJ) received an additional JPY100bn in the FY01 supplementary budget. In 2002 a lot of corporate recovery fund were set up with or without involvement of the DBJ and DIP financing saw increasing use. This is similar to the IRCJ's scheme in that the public sector provides support for corporate and industrial reorganization efforts. Reports state that IRCJ policy does not exclude small and medium-sized enterprises (SMEs) from this program. The IRCJ was given the immense sum of JPY10trn to efficiently rehabilitate enterprises that cannot be left to the private sector, on the premise that the IRCJ was created to complement the Resolution & Collection Corporation (RCC). The revisions in 2001 to the Financial Revitalization Law enabled the RCC to help companies reorganize by buying up their loans, but this alone has not been sufficient, which explains the need for the IRCJ. The IRCJ and RCC should work together to clean up debt-ridden companies and efficiently rehabilitate as many companies as possible. Of course, it will take effective economic policy, and not just the revitalization of individual companies, to resurrect the overall Japanese economy.

1. Limits to relying on private-sector initiative for revitalization

As stated in the BP, ideally the private sector should be able to revitalize corporations with its own efforts, but factors such as the difficulty involved in balancing the interests of creditors require the presence of an institution that can consolidate debts and serve as a neutral mediator to accelerate the revitalization of companies with potential but which cannot be left to the private sector.

In 1999 and 2002 a number of major companies received large amounts of financial aid. Given the worsening asset deflation, the banks' own compliance problems and restrictions posed by taxation, it was probably inevitable, but financial weakness prevented the main banks from extending sufficient support to these companies, as many analysts noted. This indicates the limits of the private sector's ability to rehabilitate companies. According to the IRCJ Law, the IRCJ can provide aid to companies that are deemed likely to recover by following a reorganization plan. Since a great deal of the taxpayer's money will be poured into these companies, the final decision on whether to proffer aid must rest on thorough asset evaluation founded on conservative estimates and a reliable business plan based on realistic projections—it is not enough to simply determine that the company would not necessarily collapse. If the financial profile and revenue improve more than the conservative

assessments initially suggested, the IRCJ could realize gains on a rise in the price of stock obtained through a debt-equity swap.

Although many companies have gone through the statutory reorganization procedures and continue to do so, these procedures inevitably lead to deterioration in corporate value. As such, ailing companies tend not to file for court protection until it is too late for them to be revitalized.

2. Difficulties with main banks in out of court workout procedures

The “Guidelines for Multi-Creditors Out of Court Workout” were established in September 2001 as a tool to facilitate the private sector’s own efforts to revitalize corporations, but it was only used 12 times through the end of July of 2003. The reorganization plans made in out of court workout proceedings under the guidelines provided that companies limit their requests for loan forgiveness to their main and secondary main banks, and ask their tertiary banks only to maintain their credit balance. This was motivated by the fear that the tertiary banks would not agree to requests that losses be spread evenly among the creditor banks and that any attempt at out of court workout would be over before it had started. In an equitable division, the main banks typically take on an amount equivalent to that forgiven by the tertiary banks. Next the company would request aid from its secondary main banks, such as debt forgiveness equivalent to the amount of aid needed from all its creditor banks (including tertiary banks), but this would most likely result in a situation in which the main banks have to take on a larger share of the burden in order to decrease the secondary main banks’ burden enough so that the debt forgiveness scheme is agreed on by all parties. For main banks, this disproportionate burden compared to other banks limits the merits of out of court workout resolution. The December 2002 reorganization plan for Nippon Yakin Kogyo faced so many difficulties that some suspected it would be the last out of court workout case under the guidelines requiring support from secondary main banks.

Less than 10 banks involved in out of court workout cases under the Guidelines at the position of main banks. Although it is merely my own speculation, reasons why other banks did not use the workout proceeding under the Guidelines might be that there is no room to ask secondary and tertiary banks for their cooperation to the loss sharing because banks other than main banks withdrew their loan, or because the main banks were determined to maintain their policy of helping their group companies under their umbrella even in adversity.

Whatever the reason, main banks were required to shoulder almost all burden from October 2002, making it extremely difficult to work out reorganization plans under the guidelines. The only way to rehabilitate companies so that they regain profitability and a healthy financial profile—which is certainly beyond the ability of most banks to accomplish alone—is for the IRCJ to buy up debt from the secondary and tertiary banks and hold three-way discussions with the main bank and company to establish a sound reorganization plan. At this point it was strongly needed for the IRCJ to be set up as soon as possible. Reorganization plans for Seibu Department Store and Hazama Gumi launched in January 2003 have been worked out under the Guidelines. According to Hazama Gumi’s plan, its tertiary banks will be asked for help with half of the financial losses allocated on a pro-rata basis. After the first reorganization plan requiring secondary and tertiary banks to share losses had been worked out, the RCC bought up the non-performing loan assets from those banks as requested.

3. Incentives encouraging applications for loan purchases

In addition to JPY100bn in capital, JPY10trn of funds will be available for the IRCJ for use in revitalizing companies. This will enable the IRCJ to rehabilitate many major corporations, but this certainty is marred by fears that non-main banks might not respond to the IRCJ’s call for offers to purchase debt. However, even in this case the goal will have been achieved if these non-main banks consent to the reorganization plan and provide financial support in the form of debt forgiveness and debt-equity swaps.

The price for the loans will be set at a level commensurate with the business recovery plan, but there is some doubt as to what this will actually mean. Although market value is the usual alternative to book value, it will not be used in this case since the debt will not be traded in the market. The net book value prior to the reorganization plan worked out in agreement with creditors is equivalent to the value of the loan less reserves, but the net book value employed when a reorganization plan is worked out would be equivalent to the loan value less the amount of debt forgiven and the value of stocks gained in a debt-equity swap. Neither of these methods will be used here. Rigid standard would not be appropriate even if referring to the market's valuation methods. The value used will likely be a sum discounted from the face amount depending on the reorganization plan's feasibility, given the amount likely to be recovered in estimated future cash flow. However, the IRCJ will provide aid when it determines that a recovery plan has a high chance of saving the company, so setting a price for the loan purchase that sharply undercuts the loan's face value could shed doubt on the validity of its valuation of the company. Buying up loans at a high price increases the risk of secondary losses, but setting a low price could limit the number of buyers. This is certainly a point of difficulty. Even if they are uncomfortable with the price, non-main banks can agree to reorganization plans for companies they deem capable of recovery, and offer support through debt forgiveness and debt-equity swaps. This kind of participation is enough to efficiently resurrect struggling companies without the IRCJ having to use public money to buy up loans.

4. Possibility of increase in prepackaged statutory reorganizations

Prepackaged statutory reorganization procedures involve the preparation of a reorganization plan that is negotiated and consented on by interested parties including creditors before the company actually files for bankruptcy with the court which has jurisdiction over the case. Prepackaged procedures have certain advantages such as the availability of DIP financing, approval of rehabilitation plan by creditors' majority vote, avoiding power to cancel preferences and fraudulent transfers and rejection of executory contracts.

Convincing creditors other than the company's main bank(s) to forgive debts, allocating losses to the secondary main banks as well and convincing tertiary banks to maintain a credit line for the reorganizing company is an extremely difficult undertaking. Although the main bank and creditor companies may plead with the non-main banks for their cooperation, it takes about a year to gain the agreement necessary for reorganization (a year-and-a-half if preparation time is included), and it is not unusual for the banks to force the reorganizing company to increase the deposits serving as collateral as a condition for their consent. The procedures laid out in the "Guidelines for Multi-Creditors Out of Court Workout" shorten the period—including preparation—to six months (within two or three months of the notice of stand still), but it has not been unusual for some banks to resist cooperation to the last, requiring tremendous efforts to persuade them.

The involvement of the semi-governmental IRCJ will make financial reorganization much easier compared to out of court workout, but even in this case it will be no simple matter to gain cooperation from the creditors accounting for the necessary portion of debt. When the total debt held by the banks agreeing to the plan is less than the total necessary debt, the company will have to give up on the IRCJ's scheme and instead follow procedures for civil rehabilitation or corporate reorganization. Previous cases have shown that out of court workout under the Guidelines involving only financial creditors result in much less damage to corporate value than is typically incurred in the statutory reorganization procedures. This is likely because the news that only financial institutions' debt will be affected relieves trade partners enough for them to continue transactions. The temporary suspension or standstill request made simultaneously with the IRCJ's decision to provide aid will also affect only financial institutions. When there are worries that the necessary number of financial institutions will not agree, the necessary steps regarding trade receivables will be taken during the review period, making it possible to avoid involving general creditors in reorganization plans. Once statutory reorganization procedures start, the general creditors will be protected, as their receivables will be dealt with as minor debt. These measures also minimize the extent of the damage to corporate value, even if the company is forced to undergo statutory reorganization procedures. In this procedure, the

reorganization process begins unless it is clear that the reorganization plan will not be drafted, adopted, or approved, and definite decisions are not made regarding the feasibility of reorganization in the early stages. However, the IRCJ has a team of experts, including external restructuring advisers, conduct a intensive review over a two to three month-period, then the IRC Commission decides to help the debtor corporation only if the Commission is satisfied that proposed reorganization plan should be highly feasible referring to the report made by the experts. This means that the civil rehabilitation and corporate reorganization procedures, which accede to the IRCJ's decision, have a higher chance of success than other cases. Awareness of this further restricts the damage to the company's credit in the eyes of its trade partners, which could ensure that the civil rehabilitation and corporate reorganization procedures run faster and more smoothly. This suggests that conversion to statutory reorganization procedures should not necessarily be avoided. Such a conversion may be made when some banks insist not to agree to the proposed plan, but a good track record of successful reorganization under converted statutory procedures could make it easier to gain banks' cooperation in future IRCJ cases.

Flexible management by the courts has made it easier to use the civil rehabilitation procedures. In December 2002 the Corporate Reorganization Reform Law was enacted, and became effective after April 2003. The extensive revisions include a partial DIP mechanism allowing the current executive officers to be appointed as trustees, more flexible majority criteria for accepting reorganization plans, and the use of fair value in asset assessment and evaluation of collateral, all of which facilitate the application for corporate reorganization procedures (similar to civil rehabilitation). Japan's bankruptcy laws are now among the most user-friendly in the world. The launch of the IRCJ will help to transform Japan's statutory reorganization procedures into tools similar to Chapter 11 bankruptcy procedures in the US.

5 The First Stage of the IRCJ

The Industrial Revitalization Corporation of Japan (IRCJ) was established on April 16, 2003 and started its business operation on May 8 of the same year. After intensive due diligence of the debtors' assets and investigation of the feasibility of the draft reorganization plans made by professional staff of the IRCJ, the Industrial Revitalization Commission (IRC Commission) decided to assist the reorganization of four debtor-corporations on August 28 and September 1.

They are Kyushu Industrial Transportation Corporation (Kyushu Sanko), DIA Construction, Usui Department Store and Mitsui Mine. Kyushu Sanko (KS) and its subsidiaries operate passenger and cargo transportation and other business including travel agencies and hotel operations. KS is an unlisted company with approximately 4000 employees. Should KS go to bankrupt, adverse impact to the regional industrial society would be severe. DIA is a condominium developer doing business in entire Japan and listed in Tokyo Stock Market. Usui Department is a local department store in Koriyama, Fukushima who's shut down would cause a serious decline of the shopping arcade in Koriyama-City which is the biggest city in Fukushima Prefecture. Mitsui Mine (MM) started its coal mining business in 1911 and was the biggest coal mining company in Japan, terminating its coal mining business several years ago. MM and its subsidiaries engage in many kinds of business, including trading of coal, production of cokes, manufacturing machineries, cement plants, cargo transportation and land development. MM is a listed company with more than 3000 employees.

Journalists criticized that the targeted debtor-corporations are smaller than expected in size and they wonder if the IRCJ could carry out its task to recover Japan's economical prosperity through reorganizing many influential distressed corporations with excessive debts. Professional staff members of the IRCJ are working hard, often through the night, on weekends and holidays overnight to investigate the financial status, evaluate assets, draft restructuring plans and other related matters of many candidate debtor-corporations. Regrettably, most of these candidate debtor corporations are small to medium size companies.

I cannot deny that to date banks are hesitant to bring cases to the IRCJ. Minister Takenaka of Financial Service Agency sent letters to banks encouraging more use of the IRCJ recently advised by Minister Taniguchi who is in charge of the IRCJ. Nevertheless, it is not easy to change the banks cautious attitude toward the IRCJ. The IRCJ is able to deal with cases only when banks bring cases in the IRCJ. Without a positive support made of banks, the IRCJ cannot play its role. Why do banks not bring sufficient a number of substantial cases to the IRCJ?

In order to explain the reasons, I have to mention the “main bank” system which is unique in Japanese business society. A main bank used to maintain a special close relationship with a particular business corporation and supply funds to the corporation which may be needed for business operation and additional investments. In addition to the funds, main banks often send managers to the borrower-corporations to assist the debtors’ operation. Although the main bank system was pervasive for a long time in Japan, the financial environment is changing now. Corporations with a good financial reputation are able to raise funds in capital markets and are not relying on main banks. Corporations, who cannot raise money by themselves from the market, have continued to rely upon the main banks. Banks other than main banks, fearing to bear additional non or poor performing loans, tend to refuse to consent to rolling over loans which became due so main banks have to fill the deficiency continuously. Japanese mega banks, losing their power during long prolonged economic recession, have little room to help corporations with huge debts. However, mega banks, who may have indirectly controlled the debtor corporations for years, find it difficult to persuade other banks to share losses on a pro rata basis in an out of court workout process.

In order to accelerate wiping out NPLs and encouraging business revitalization at the same time, the IRCJ was established. The IRCJ will purchase loans from non main banks at the request made by debtor corporations with excessive debts and their main banks, when the IRC Commission is satisfied that their reorganization plans are feasible and equitable. Experienced and talented professional staff of the IRCJ, evaluate assets including good will of the debtor corporations on a discounted cash flow basis using the purchase method, may request the debtor corporations and their main banks to amend the draft reorganization plans to increase amounts of debts forgiveness to avoid possible second failure. This is done before, the IRC Commission examination regarding feasibility of the plans.

Mega banks, who are concerned about losing control of the valuation process, are reluctant to bring large influential cases to the IRCJ. Mizuho Holdings, UFJ Holdings, Sumitomo Mitsui Banking Corporations and Bank of Tokyo-Mitsubishi have now established subsidiaries or divisions specialized to assist borrower corporations’ efforts to rehabilitate. Many regional banks have created similar specialized divisions. Inauguration of the IRCJ played a significant role in stimulating these actions by the banks. I am concerned, however, that these measures may, in some cases, hinder the recognition of appropriate losses in wiping out NPLs and delay Japan’s economic recovery. It is important that the banks not take half measures to reduce their NPLs.

The Japanese government infused 2 trillion Japanese Yen into Resona Bank in July, 2003 and Resona is eager to reduce their NPLs by recognizing their actual value. This may be a good example. We are ready and hope to use 10 trillion Japanese Yen to purchase NPLs, if the banks bring cases in front of us before the end of March, 2005 which is our designated deadline to buy the loans.

As of the end of September, 2003, it is 6 companies in total, as IRCJ decided to assist two more debtor-corporations on September 26.