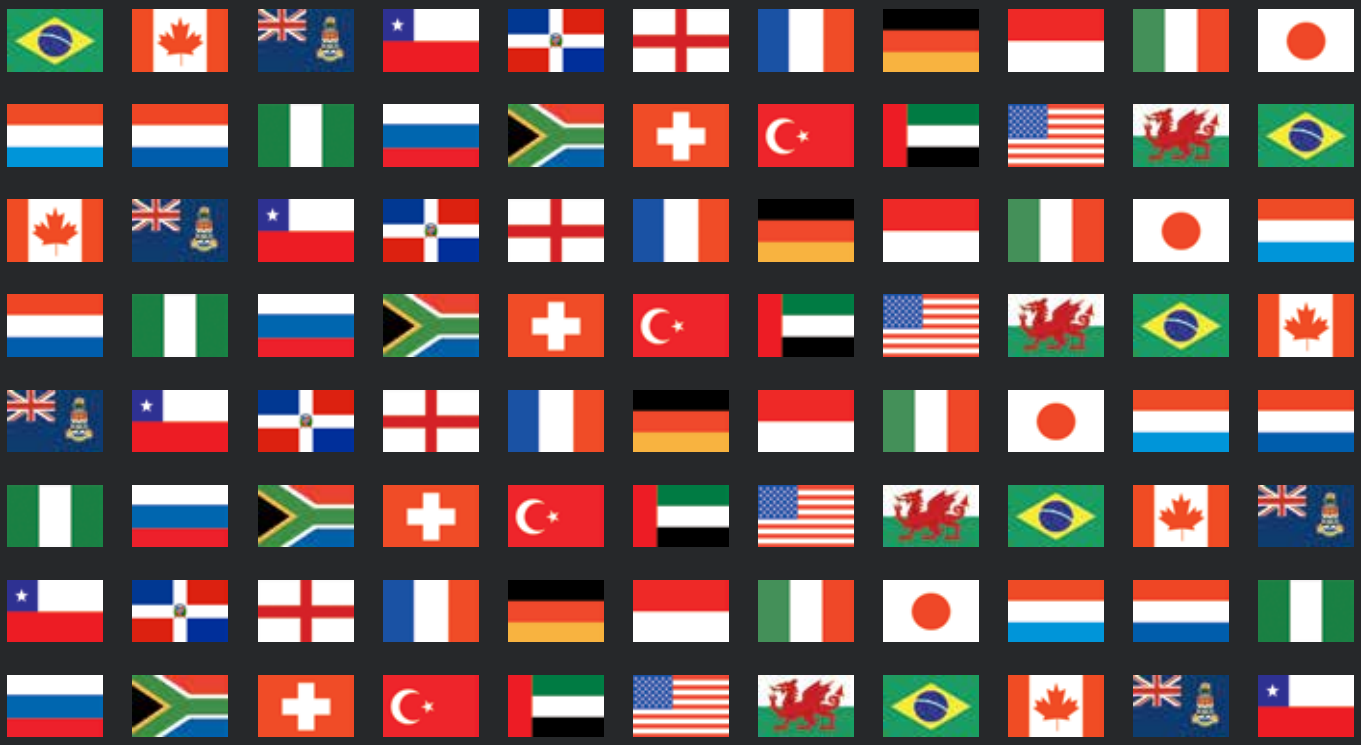
Acquisition Finance

In 20 jurisdictions worldwide

Contributing editors
Ryan Bekkerus, Alexandra Kaplan and Marisa Stavenas



2015

GETTING THE DEAL THROUGH

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Japan

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General structuring of financing

1 What territory's law typically governs the transaction agreements? Will courts in your jurisdiction recognise a choice of foreign law or a judgment from a foreign jurisdiction?

In the case of purely domestic transactions, Japanese law will always govern the transaction agreements. Where the lenders are foreign financial institutions, however, the loan facility agreements may be governed by UK or New York law. If the relevant assets are located in Japan the collateral or security agreements will typically be governed by Japanese law.

Japanese courts will generally recognise and give effect to the decision of parties to have the transaction agreements governed by a foreign law, unless it was found that the application of such laws would contravene the principles of public order and good morals as applied in Japan.

In addition, Japanese courts will recognise any final and conclusive civil judgment for monetary claims (not including monetary claims arising from criminal or administrative sanctions, such as punitive damages, even where such monetary claims take the form of a civil claim) obtained in the courts of a foreign jurisdiction in an action based upon the transaction agreements as a valid judgment and will give effect thereto, provided that:

- the jurisdiction of such foreign court is permitted under Japanese laws or treaties;
- the defendant has received service of process necessary for the commencement of the relevant proceedings, other than by public notice or any method similar thereto, or the defendant has appeared before a foreign court without reserving the right to contest the validity of the service of process, jurisdiction or venue;
- the foreign judgment and the proceedings of the foreign court are not contrary to the principles of public order and good morals as applied in Japan;
- there exists reciprocity between such foreign court's jurisdiction and Japan as to the recognition of foreign judgments; and
- there is no conflicting Japanese judgment on the subject matter.

2 Does the legal and regulatory regime in your jurisdiction restrict acquisitions by foreign entities? Are there any restrictions on cross-border lending?

Generally speaking, there are minimal restrictions on acquisitions by foreign entities in Japan. In the case of certain regulated industries (such as aviation, transportation, telecommunications and the operation of securities exchanges), however, foreign ownership is restricted, typically, up to a one-third or one-fifth ownership interest in the relevant company. In addition, the Foreign Exchange and Foreign Trade Act (FEFTA) requires a foreign acquirer of shares in a Japanese company whose business relates to national security, public order, public security and certain protected businesses (such as agriculture, petroleum, leather, aviation and marine transportation) to file a prior notice to the government and be subject to a 30-day wait period before being able to acquire the subject shares. The competent Japanese authorities may issue a recommendation or order to amend the terms of, or even suspend, the acquisition. The only example to date of a Japanese authority suspending an acquisition occurred in 2008, when The Children's Investment Fund (TCI), a London-based hedge fund, was ordered to refrain from acquiring up to a 20 per cent stake of J-Power, a domestic electricity company that operates power plants, including nuclear power plants, because there was a concern that TCI's shareholding could negatively affect the supply of electricity and nuclear power policy in Japan and, thereby, potentially endanger the public order. FEFTA will also more frequently require ex post facto reports for share acquisitions conducted by foreign investors, but such reports are mere formalities.

There are no restrictions on cross-border lending transactions, except that the licensing requirement (as mentioned in question 6) must be complied with. Further, if the lender is not a financial institution a ex post facto report may also be required under the FEFTA depending on the amount of the loan.

3 What are the typical debt components of acquisition financing in your jurisdiction? Does acquisition financing typically include subordinated debt or just senior debt?

In Japan, acquisition financing is typically structured as senior debt only or a combination of senior debt and mezzanine financing. The inclusion of mezzanine financing is becoming more common in Japan, which is typically structured as subordinated debt or preferred shares. In addition, warrants are sometimes added as a sweetener. While there are examples of subordinated corporate bonds, the securitisation of business assets and seller financing being used in Japanese acquisition financings, such structures are not very common yet. It should also be noted that high-yield bonds have yet to be used for acquisition finance in Japan.

4 Are there rules requiring certainty of financing for acquisitions of public companies? Have 'certain funds' provisions become market practice in other transactions where not required?

In Japan, there is no rule requiring certainty of financing for acquisitions of public companies as required in the UK. When the syndication includes foreign lenders and the LMA format is used for the credit facility agreement, a 'certain funds' provision is used, but such a provision just lists the conditions precedent to the drawdown of loans.

In the case of a tender offer bid being issued for a public target, a document that evidences the existence of funds sufficient to settle such tender offer must be attached to the tender offer registration statement. A credit certificate issued by the lenders is typically used for this purpose. Where a credit certificate is used to evidence the availability of funds, the Financial Services Agency (FSA) requires it to clearly and specifically list the conditions precedent to the drawdown of funds. However, there is no strict restriction as to the type of conditions precedent that may be included, such as the UK certain-funds requirement.

5 Are there any restrictions on the borrower's use of proceeds from loans or debt securities?

There is no statutory restriction on the borrower's use of proceeds from loans or debt securities in Japan.

6 What are the licensing requirements for financial institutions to provide financing to a company organised in your jurisdiction?

For a foreign financial institution to provide loans in Japan as a business, a moneylending licence is required under the Moneylending Business Act, except where the foreign financial institution has a branch office and a foreign bank licence under the Banking Act.

7 Are principal or interest payments or other fees related to indebtedness subject to withholding tax? Is the borrower responsible for withholding tax? Must the borrower indemnify the lenders for such taxes?

Interest payments and other fees payable to non-resident lenders are subject to withholding tax under the Income Tax Act. However, when the foreign lender is acting through a branch in Japan that holds a valid certificate of exemption for withholding tax for foreign corporations or non-residents (article 214 of the Income Tax Act) or certificate of exemption for withholding tax for foreign corporations (article 180 of the Income Tax Act) issued by the relevant tax authorities it will be exempt from withholding tax. Where there is no exemption available to the withholding tax obligations, the borrower will be responsible for such withholding tax. In such cases a tax gross-up provision will usually be included in the credit facility agreement.

8 Are there usury laws or other rules limiting the amount of interest that can be charged?

Interest, commissions and fees payable by the Japanese borrower are subject to the limitations imposed by:

- the Interest Rate Limitation Act under which, among other things, the maximum interest rate for a loan with a principal amount of less than ¥100,000 shall be 20 per cent per annum, a loan with a principal amount of at least ¥100,000 but less than ¥1 million shall be 18 per cent per annum and a loan with a principal amount of at least ¥1 million shall be 15 per cent per annum;
- the Act Concerning Regulation of Acceptance of Contribution, Deposit and Interest, etc, under which, among other things, the imposition of interest at a rate of more than 20 per cent per annum is prohibited and is subject to certain criminal sanctions; and
- the Act on Temporary Measures for Accommodation of Interest, under which, among other things, the maximum interest rate with respect to certain categories of receivables of certain financial institutions may be limited by the order of the Policy Committee of the Bank of Japan, as instructed by the prime minister or the minister of finance of Japan. In addition, under the Moneylending Business Act, a loan agreement made by a person engaged in the money-lending business, as defined therein, will be void if the interest rate stipulated in such loan agreement exceeds 109.5 per cent per annum.

9 What kind of indemnities would customarily be provided by the borrower to lenders in connection with a financing?

Under the form of a term loan published by the Japan Syndication and Loan-Trading Association (JSLA), upon which credit facility agreements are typically based on domestic transactions, the borrower must indemnify the lenders and the administrative agent against any loss, costs and expenses incurred by them due to the borrower's breach of the terms of the loan agreement. In addition, the borrower must indemnify the administrative agent against any loss, costs and expenses incurred by it:

- due to the occurrence of an attachment being made against the loan receivables or the transfer of the loan receivables prior to the distribution of the payment by the administrative agent; and
- in the course of performing the obligations of the administrative agent, to the extent not indemnified by the other lenders.

10 Can interests in debt be freely assigned among lenders?

Interest that has accrued but not been paid may be assigned, but interest that has not yet accrued cannot be assigned separate from the principal.

11 Do rules in your jurisdiction govern whether an entity can act as an administrative agent, trustee or collateral agent?

Under Japanese law, an administrative agent is an attorney-in-fact of the lenders and a collateral agent is an attorney-in-fact of the security holders. The typical role of both agents is not considered to be a regulated business and therefore there are no special rules that govern whether an entity can act as an administrative agent or a collateral agent. A trustee must:

- be registered or have received approval under the Trust Business Act; or
- be a bank and have received approval under the Act on Engagement of Trust Business by Financial Institutions (ie, a trust bank).

However, as mentioned in question 20, securities trusts are rarely used in Japan.

12 May a borrower or financial sponsor conduct a debt buy-back?

A borrower or financial sponsor may conduct a debt buy-back. When a borrower buys back a debt, such debt will be extinguished as a matter of law.

13 Is it permissible in a buy-back to solicit a majority of lenders to agree to amend covenants in the outstanding debt agreements?

The borrower may negotiate with the lenders on amendment of covenants in the outstanding debt agreements. However, it is not common in Japan that the right of such buy-back is provided for in the loan agreement.

Guarantees and collateral

14 Are there restrictions on the provision of related company guarantees? Are there any limitations on the ability of foreign-registered related companies to provide guarantees?

Unlike in EU jurisdictions, there are no statutory financial assistance restrictions in Japan. However, providing guarantees, securities or any other financial assistance to a majority shareholder at the expense of minority shareholders will contradict the general fiduciary duty of directors. Accordingly, wholly owned related companies can provide guarantees without limitation but non-wholly owned related companies can provide guarantees only with the consent of all minority shareholders. There is no special limitation on the ability of foreign-registered related companies to provide guarantees, but if a foreign-registered related company is owned by a Japanese company, the directors of the Japanese company are subject to the same fiduciary duties when the foreign-registered related company provides a guarantee.

15 Are there specific restrictions on the target's provision of guarantees or collateral or financial assistance in an acquisition of its shares? What steps may be taken to permit such actions?

Unlike in EU jurisdictions, there are no statutory financial assistance restrictions in Japan. However, providing guarantees, securities or any other financial assistance to a majority shareholder at the expense of minority shareholders will contradict the general fiduciary duty of directors. Accordingly, for example, in a going-private transaction, the target company cannot provide collateral to the acquisition vehicle (the borrower) until the target company becomes the wholly owned subsidiary of the acquisition vehicle by way of a squeeze-out following the tender offer bid process.

16 What kinds of security are available? Are floating and fixed charges permitted? Can a blanket lien be granted on all assets of a company? What are the typical exceptions to an all-assets grant?

In Japan, acquisition finance lenders will usually take an individual security interest over each type of asset of the target and its wholly owned subsidiaries. The type of security varies depending on the asset type and the financing structure. As opposed to use of a 'blanket lien' in other jurisdictions, this process incurs extra time and cost because the method by which security interests are created and perfected under Japanese law are varied and there are different limitations and restrictions depending on the asset type that need to be considered. In light of these time- and cost considerations and limitations and restrictions, lenders tend to grant exceptions to such all-asset grants. For example, assets that require the consent of a third party to attach a security interest are excluded (eg, leasehold rights, trade receivables). When the payment of a substantial registration tax is required to perfect a security interest (eg, real estate, intellectual property), the requirement for full perfection tends to be exempted. The creation of second priority pledges is often suspended until the full discharge of the senior debt, when the legality and validity of the second priority pledge is in question under Japanese law (eg, inventory, trade receivables).

Floating charges are permitted only for moveables, such as inventory and receivables, such as trade receivables.

A blanket lien over all of the assets of the borrower is called corporate collateral in Japan, but corporate collateral is not used in the context of acquisition finance. One reason is that the use of corporate collateral is limited by statute to securing corporate bonds only and not loans. Another weakness of corporate collateral is that, as a general security interest, it is subordinate to specific security interests. Accordingly, a lender who holds a corporate collateral interest cannot assert priority over a creditor who subsequently obtains a security interest over a particular asset, which makes corporate collateral inappropriate for the purposes of holding a security interest in the context of acquisition finance.

17 Are there specific bodies of law governing the perfection of certain types of collateral? What kinds of notification or other steps must be taken to perfect a security interest against collateral?

The method for creating and perfecting a security interest depends on the type of security interest and the type of assets subject to the security interest.

Stock

Lenders typically create a pledge over shares. When the articles of incorporation of the issuing company provide that stock certificates are to be issued, the execution of a pledge agreement and the delivery of the corresponding stock certificates to the pledgee is required to create the pledge and the continuous possession of such stock certificates by the pledgee is required to perfect the pledge. Usually, the security agent receives delivery of the stock certificates and holds them as proxy for all of the pledgees. When the articles of incorporation of the issuing company do not provide that stock certificates are to be issued and the shares are not listed, the execution of a pledge agreement alone is sufficient to create the pledge and recording such pledge in the share ledger is required to perfect it against third parties. When the shares are listed shares, recording the pledge in the account book maintained at the relevant account management institution is required to create the pledge.

Real estate

Lenders typically create mortgages over the real estate assets owned by the credit parties. The execution of a mortgage agreement alone is sufficient to create a mortgage and, to perfect the mortgage against third parties, such mortgage must be registered.

Receivables

A security interest over receivables may be created by way of a pledge or a security assignment. To create such a pledge or a security assignment, the execution of a pledge agreement or an assignment agreement, as the case may be, is sufficient. There are three ways to perfect a pledge or assignment:

- to send a notice with a notarised date to the third-party debtor;
- to obtain consent with a notarised date from the third-party debtor; or
- to register the pledge or assignment with the competent legal affairs bureau pursuant to the Act concerning Special Exceptions to the Civil Code with respect to the Perfection of Assignment of Moveables and Receivables (the Perfection Act).

Moveable assets

A security interest over moveable assets is typically created by way of a security assignment. To effect a security assignment, the execution of an assignment agreement alone is sufficient. To perfect the security assignment against third parties, the borrower must physically deliver the moveable assets to the security interest holder or declare that it is maintaining possession of the moveable assets on behalf of the security interest holder going forward. As an alternative, the security interest holder may perfect the security assignment by registering the assignment with the competent legal affairs bureau pursuant to the Perfection Act.

Intellectual property

A security interest over intellectual property rights may be created by way of a pledge or a security assignment. For trademarks and patents, the execution of a pledge or assignment agreement and registration of the pledge or assignment with the Patent Agency is required to create the security interest. For copyrights, the simple execution of a pledge or assignment agreement is necessary to create a security interest and the registration of same is only required for perfection against third parties.

18 Once a security interest is perfected, are there renewal procedures to keep the lien valid and recorded?

The registration of an assignment of moveables or receivables under the Perfection Act has an effective period that may be determined by the applicant at the time of the application for registration. Generally, the effective period is set for a term that extends beyond the maturity date of the loan, but if shorter, it is necessary to apply for an extension before the effective period expires.

19 Are there 'works council' or other similar consents required to approve the provision of guarantees or security by a company?

A collective agreement between the employer and the employees may set forth a requirement for approval of a labour union in order for the employer to provide guarantees or security. In Japan, however, such collective agreements are rarely entered into by companies.

20 Can security be granted to an agent for the benefit of all lenders or must collateral be granted to lenders individually and then amendments executed upon any assignment?

In Japan, collateral is typically granted to lenders individually or jointly. In 2008, the amended Trust Act confirmed the validity of security trusts under Japanese law. If a securities trust scheme is used, collateral may be granted to an agent for the benefit of all lenders. However, the security trust scheme, to date, has rarely been used in Japan because it requires extra time and cost and does not provide substantial benefit.

In case of the assignment of loan receivables, the collateral to secure the loan receivables will automatically transfer with the loan receivables to the assignee without any action, pursuant to the Japanese Civil Code. However, an accession letter is typically signed by the assignee to assume the rights and obligations of the assignor under the security documents.

21 What protection is typically afforded to creditors before collateral can be released? Are there ways to structure around such protection?

There is no statutory protection afforded to creditors in connection with the release of collateral.

22 Describe the fraudulent transfer laws in your jurisdiction.

Under the Japanese Civil Code, a creditor may ask the court to rescind any action made by the obligor if such action would 'impair the creditor' (as described below) within the earlier of two years from the date the creditor became aware of such cause for rescission or 20 years following the occurrence of the impugned action. An action 'impairs the creditor' if it will decrease the assets of the obligor to such an extent that the creditor should not be fully satisfied should it exercise its rights. The creation of a security interest on behalf of only some of the existing creditors of a company may be rescinded by an unsecured creditor, but if a new lending arrangement accompanies the creation of such security interest, it will not be rescinded.

Debt commitment letters and acquisition agreements

23 What documentation is typically used in your jurisdiction for acquisition financing? Are short form or long form debt commitment letters used and when is full documentation required?

While finance document forms used by Japanese banks have not been standardised and vary by bank, they share similar language because they are based on the model syndicated loan agreement published by the JSLA. Generally, the use of LMA documents is limited to those cases where one of the lenders is a foreign financial institution and the governing language of the documentation is to be English and is not used for purely domestic transactions.

In Japan, long-form debt commitment letters usually comprise a brief commitment letter, of around five to six pages, to which the substantive terms of the lending arrangement will be attached (generally around 50 to 80 pages).

24 What levels of commitment are given by parties in debt commitment letters and acquisition agreements in your jurisdiction? Fully underwritten, best efforts or other types of commitments?

In Japan, lenders usually commit on a fully underwritten basis in debt commitment letters.

25 What are the typical conditions precedent to funding contained in the commitment letter in your jurisdiction?

The typical conditions precedent to funding contained in the commitment letter are as follows:

- non-alteration of the acquisition structure;
- completion of the equity investment in a certain amount;
- compliance by the borrower with the stated manner in which the funds to be provided by lenders are to be used;
- non-alteration of business projections;
- accuracy of information provided by the borrower;
- obtainment of final internal approval;
- absence of any material adverse change;
- execution of all lending agreements and ancillary agreements in a form and substance satisfactory to the lenders;
- execution of all acquisition agreements and ancillary agreements in a form and substance satisfactory to the lenders; and
- compliance with all of the conditions precedent of the funding set forth in the term sheet.

26 Are flex provisions used in commitment letters in your jurisdiction? Which provisions are usually subject to such flex?

Although not very common, flex provisions are sometimes used in commitment letters. In contrast with other jurisdictions, it is common for only the spread to be subject to such a flex provision in Japan.

27 Are securities demands a key feature in acquisition financing in your jurisdiction? Give details of the notable features of securities demands in your jurisdiction.

Securities demands are not a key feature in acquisition financing and are rarely used in acquisition financing transactions in Japan.

28 What are the key elements in the acquisition agreement that are relevant to the lenders in your jurisdiction? What liability protections are typically afforded to lenders in the acquisition agreement?

In Japan, lenders are usually sensitive to price adjustment provisions, indemnity provisions and the material facts that are to be included in the disclosure letter. No liability protection is provided to lenders in the acquisition agreement.

29 Are commitment letters and acquisition agreements publicly filed in your jurisdiction? At what point in the process are the commitment papers made public?

Where an acquisition involves a mandatory tender-offer bid, an official commitment letter must be filed with the relevant government bureau and such official commitment letter is disclosed through an electric disclosure system (EDINET). However, apart from this, commitment letters are never publicised.

Enforcement of claims and insolvency

30 What restrictions are there on the ability of lenders to enforce against collateral?

Where the grantor of the security interest is subject to corporate reorganisation proceedings (Japanese insolvency proceedings similar to US Chapter 11 proceedings), a secured creditor may not foreclose on collateral outside such proceedings. Where the grantor of the security interest becomes subject to Japanese insolvency proceedings other than the corporate reorganisation proceedings, however, such as bankruptcy proceedings, civil rehabilitation proceedings or the special liquidation proceedings, a secured creditor may foreclose on the collateral regardless of the insolvency proceedings.

31 Does your jurisdiction allow for debtor-in-possession (DIP) financing?

DIP financing is allowed in Japan. DIP financing after the commencement of civil rehabilitation proceedings and corporate reorganisation proceedings (both proceedings are Japanese restructuring-type insolvency proceedings) is automatically treated as a common benefit claim, which is paid, from time to time, in preference to any distribution to the general creditors (it is similar to an administrative expense under the US Bankruptcy Code).

DIP financing, however, is not very common in Japan for a number of reasons, such as the lack of a legal framework for 'super priority' or 'priming liens'.

32 During an insolvency proceeding is there a general stay enforceable against creditors? Is there a concept of adequate protection for existing lien holders who become subject to superior claims?

Once insolvency proceedings have commenced against the borrower, creditors may no longer enforce their claims against the borrower and must comply with the terms of the insolvency proceedings. It is, however, common for the court to issue an order stating that no creditors may enforce their claims against the borrower following the filing of the insolvency proceeding application, prior to the formal commencement of the insolvency proceedings.

There is no concept of 'adequate protection' under Japanese insolvency laws.

33 In the course of an insolvency, describe preference periods or other reasons for which a court or other authority could claw back previous payments to lenders. What are the rules for such clawbacks and what period is covered?

Under Japanese insolvency laws, previous payments to lenders may only be clawed back pursuant to the preference voidance power of the trustee.

Preferences can be voided in the following circumstances:

- the payment is made after the borrower became unable to pay its debts and the lender knows that the borrower is unable to pay its debts or that the borrower has suspended its debt payments;
- the payment is made after the borrower files for insolvency and the lender knows that the petition for the commencement of insolvency proceedings has been filed; or
- the payment is not made pursuant to contractual obligations, such non-obliged payment is made within the 30-day period prior to the borrower becoming unable to pay its debts and the lender knows, at the time of such payment, that the payment will prejudice other creditors.

34 In an insolvency, are creditors ranked? What votes are required to approve a plan of reorganisation?

Ranks of claims

In insolvency proceedings, the priority of the creditors are ranked according to the nature of their claim. The chart below outlines the type of claims under each type of Japanese proceedings in descending order according to priority.

Type of claim	Bankruptcy proceeding	Civil rehabilitation proceeding	Corporate reorganisation proceeding
Secured claim	Right to separate satisfaction	Right to separate satisfaction	Secured reorganisation claim
Common benefit claim	Estate claim	Common benefit claim	Common benefit claim
Preferred general claim	Preferred bankruptcy claim	Preferred rehabilitation claim	Preferred reorganisation claim
General claim	Bankruptcy claim	Rehabilitation claim	Reorganisation claim
Subordinate claim	Subordinate bankruptcy claim	Subordinate rehabilitation claim	Subordinate reorganisation claim

The following is a brief explanation of the general nature of each class of claim:

Secured claim
In bankruptcy proceedings and civil rehabilitation proceedings, the secured creditors may foreclose on or sell the secured property outside the insolvency proceedings. On the other hand, in the corporate reorganisation proceedings, the secured creditors may not foreclose on the secured property outside the insolvency proceedings.

Common benefit claim
Insolvency laws provide for certain types of claims (such as costs, expenses and remuneration for the trustee) which have a common benefit for creditors as 'common benefit claims' in civil rehabilitation proceedings or corporate reorganisation proceedings and 'estate claims' in bankruptcy proceedings. The exercise of this type of claim is not subject to the restrictions imposed in insolvency proceedings, such as discharge, or the amendment of terms and conditions, which may be applied to general claims, and the entire amount of such common benefit claims and estate claims are paid for from the borrower's property, from time to time, as they become due. As such, a creditor who has a common benefit claim or estate claim has the right to a preferred repayment from the borrower's property.

Preferred general claims
Claims against a borrower that are a result of events that occurred, or the grounds or causes of which existed, before the commencement of insolvency proceedings and are secured by a general statutory lien, or any other preferred right, are treated as preferred general claims in insolvency proceedings. For example, wages of employees and certain tax claims fall within the class of preferred general claims.

In bankruptcy proceedings and corporate reorganisation proceedings, a creditor with a preferred general claim cannot exercise its rights outside the insolvency proceedings and can only exercise such rights within the insolvency proceedings. For example, under the corporate reorganisation proceedings, preferred general claims may be subject to deferment and discharge under the reorganisation plan.

On the other hand, in civil rehabilitation proceedings, the exercise of preferred rehabilitation claims is generally not restricted to the actual insolvency proceedings and a creditor with a preferred rehabilitation claim may exercise such rights and collect from the borrower from time to time as the debts become due, outside the proceedings, unless the court expressly suspends the right of creditors to exercise such rights and collect such debts as they become due.

General claims
Claims against a debtor that are a result of events that occurred, or the grounds or causes of which existed, prior to the commencement of the insolvency proceedings and do not fall within any other class of preferred general claims or subordinate claims, will be included in the insolvency proceedings and treated as general claims.

A creditor with a general claim may not exercise such rights outside the insolvency proceedings and can only exercise such rights within the insolvency proceedings. For example, under corporate reorganisation proceedings or civil rehabilitation proceedings, general claims are subject to deferment or discharge under the reorganisation or rehabilitation plan, as the case may be.

Subordinate claims
Other aspects of these claims, such as accrued interest and damages or other penalties arising following the commencement of insolvency proceedings are treated as subordinate claims. In insolvency proceedings, subordinate claims are treated as having a lower priority than general claims.

Approval requirement for rehabilitation/reorganisation plan
A rehabilitation plan under civil rehabilitation proceedings may be approved by an affirmative vote of a majority of the creditors in attendance and the amount of the claims held by these creditors must be at least half of the total amount of the claims for which such voting rights are exercisable.

A reorganisation plan under corporate reorganisation proceedings must be approved by each group of interested parties (eg, unsecured creditors, secured creditors and each group of shareholders; provided, however, that in the event that the borrower is insolvent as of the commencement of the corporate reorganisation proceedings the shareholders will have no voting rights) at a meeting of such group as prescribed under the Corporate Reorganisation Act. At a meeting of the unsecured creditors (ie, those creditors with preferred general claims, general claims and subordinate claims), an affirmative vote of creditors holding at least half of the total amount of the unsecured claims for which voting rights are exercisable is required. On the other hand, at a meeting of the secured creditors, if the proposed reorganisation plan provides for a moratorium on payments, an affirmative vote of creditors holding at least two-thirds of the total amount of the secured claims for which voting rights are exercisable is required. If the proposed reorganisation plan includes provisions that will affect the rights of secured creditors through measures other than a moratorium on payments (eg, a reduction of the secured claims), an affirmative vote of creditors holding at least three-quarters of the total amount of the secured claims for which voting rights are exercisable is required. Finally, when the shareholders have voting rights, at a meeting of the shareholders, an affirmative vote of shareholders holding at least half of the total voting rights of shares that are exercisable is required.

35 Will courts recognise contractual agreements between creditors providing for lien subordination or otherwise addressing lien priorities?

Japanese courts will not recognise contractual agreements between creditors providing for lien subordination or otherwise addressing lien priorities. Under Japanese law, however, the creation of a second priority security interest is permitted and the ranking of such security interest is recognised by the Japanese court. Therefore, in practice, a first priority security interest is created for senior lenders and a second priority security interest is created for subordinated lenders.

In addition, claims that the borrower and creditor agreed to treat as subordinated claims prior to the commencement of insolvency proceedings will be treated in insolvency proceedings as junior to any other claims

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against the borrower. Such claims are referred to as 'contractually subordinated bankruptcy claims', 'contractually subordinated rehabilitation claims' or 'contractually subordinated reorganisation claims' depending on the type of insolvency proceedings.

36 How is the claim of an original issue discount (OID) or discount debt instrument treated in an insolvency proceeding in your jurisdiction?

The face value of the claim (ie, the amount of the claim without any discount) will be treated as the amount of the claim under the insolvency proceeding; provided, however, that there is risk that the Japanese court may recharacterise the claim such that the value of the claim will then be reduced by any such discount.

37 Discuss potential liabilities for a secured creditor that enforces against collateral.

If the secured creditors obtain collateral as a result of the exercise of a security interest, they may be liable for damages related to such collateral as its owner; however, if the secured creditors sell the collateral as a result of the exercise of a security interest, they would not be subject to any such liability.

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