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New regime incorporating majority vote mechanism into out-of-court workout

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Summary

IN SUMMARY

This article introduces and summarises recent trends and developments relating to business turnaround in Japan, with a particular focus on the New Regime enacted in June 2025, which incorporates a majority vote mechanism into out-of-court workouts.

DISCUSSION POINTS

- Factors contributing to the recent trends in insolvency and restructuring in Japan
- Overview of turnaround ADR and the New Regime
- Outlook on the impact of the New Regime on restructuring practices

REFERENCED IN THIS ARTICLE

- Early-Stage Business Restructuring Act
- Turnaround ADR

INCREASE OF INSOLVENCIES

During the covid-19 pandemic, Japan saw a decrease of insolvencies and restructurings partly because of the government's measures to support businesses affected by the pandemic; however, following the end of those measures, the number of insolvencies and restructurings has been increasing. According to Teikoku Databank, 2021 had the lowest level of recorded in-court insolvency cases (6,015 cases) of any year since 1966, but the number increased to 6,376 in 2022, to 8,497 in 2023 and to 9,901 in 2024 (that said, the number has not yet returned to the levels in the aftermath of the 2007–2008 financial crisis).-[1] This trend is anticipated to continue in 2025, since the number of insolvency cases from January to April 2025 increased year-on-year for the four consecutive months, and it appears that several key factors contributing to this recent trend are still present.

Factors Contributing To The Recent Increase In Insolvencies

Japanese Yen Depreciation

The yen had been depreciating over the past few years mainly because the Bank of Japan (BOJ) had maintained its easing of monetary policy. After the yen marked a record low of ¥160 per US$1 in April 2024 for the first time since 1990, the BOJ responded by raising its policy interest rate to 0.25 per cent in July 2024 and to 0.5 per cent in January 2025, marking the highest level in 17 years.

Despite these interest rate hikes, the yen is still relatively weak, hovering between ¥140 and ¥150 per US$1. This prolonged yen depreciation trend has been causing procurement costs to rise because many Japanese companies rely on imports to procure materials. As a result, the cost pressures have weakened the financial positions of numerous businesses, and the rising prices of many commodities to their highest in recent years have dampened not only companies but also consumer household budgets.

Labour Shortages

In Japan, labour shortage has become a serious problem. The fundamental cause of the labour shortage is the continuous and accelerated decline in the working population owing to the low birthrate, the 'super-aged' society and the general policy of not accepting immigrants. Further, the recent application of stricter regulations on overtime work, especially in the construction and transportation sectors, which came into force in 2024, has exacerbated the situation.

The labour shortage has pushed up the cost of hiring new employees and retaining existing ones, and it has even made it difficult to maintain the minimum manpower necessary for business operations, especially of small and medium-sized enterprises (SMEs). According to a survey conducted by Teikoku Databank, the number of insolvencies attributable to labour shortages in 2024 has increased over the past three years (140 cases in 2022, 260 cases in 2023 and 342 cases in 2024),[2] and the number of insolvencies triggered by a lack of successors (mainly with death or disease in founding family management) remains high (476 cases in 2022, 564 cases in 2023 and 540 cases in 2024).[3]

Non-compliance Risks

Another notable driver of corporate distress in recent years has been non-compliance with laws, regulations and other rules or standards. An increasing number of insolvency cases are linked, at least in part, to various forms of misconduct. These include violations related to product safety and testing, breaches of laws (such as cartels and corruption), inappropriate accounting practices and workplace issues such as harassment and other human rights concerns. Such incidents are often reported sensationally in the media, amplifying their reputational impact. According to a survey conducted by Teikoku Databank, the number of insolvencies attributable to 'non-compliance' in 2024 has increased over the past three years (272 cases in 2022, 351 cases in 2023 and 388 cases in 2024).[4]

There may be various background factors behind this trend: (1) there are social expectations that companies must act responsibly by complying with various rules to the extreme details have evolved considerably; (2) the widespread use of social media and online platforms has made it possible for misconduct to spread more quickly and widely than ever before, bringing more public attention to the issues; and (3) the development of whistleblowing systems has made it easier for internal wrongdoing to be exposed.

Other Factors

Although not yet reflected in the 2024 statistics, Trump tariffs announced in April 2025 are already beginning to weigh on the Japanese economy in 2025. In particular, the automotive industry, one of Japan's important industries, will be heavily affected by the tariffs imposed on automobiles and parts. Shifting production to the United States would lead to higher labour and operational costs, while passing tariff burdens onto prices would likely reduce sales. In either scenario, automakers will be forced to restructure their operations globally, causing adverse ripple effects throughout the supply chain from tier 1 suppliers to lower tier suppliers. As an early example of this trend, Nissan Motor Co, Ltd announced a 'Re: Nissan plan' on 13 May 2025 that includes a reduction of 20,000 jobs – equivalent to roughly 15 per cent of its global workforce, along with other deep cost-cutting measures for its turnaround.-[5]

Summary

The Japanese economy has been in a precarious situation, compounded by the uncertainties arising from the factors indicated above. Many enterprises and businesses are already facing or are expected to face serious financial difficulties in the foreseeable future.

INTRODUCTION OF THE NEW ACT

In response to the challenges Japanese companies are currently facing, the Japanese government has introduced a new legislative tool aimed at facilitating early-stage business restructuring. The Early-Stage Business Restructuring Bill was developed through discussions among practitioners, academics, financial institutions and other stakeholders, during which reference was made to pre-insolvency restructuring regimes in Europe, including the United Kingdom's Scheme of Arrangement and Part 26A Restructuring Plan, Germany's StaRUG and France's accelerated safeguard procedure.

The Bill was submitted to the Cabinet in March 2025 and enacted as the 'Early-Stage Business Restructuring Act'[6] (the New Act) in June 2025, which is scheduled to come into force by December 2026. The new regime introduced under the New Act (New Regime) will substantially incorporate a majority voting (in-class cramdown) mechanism into the existing rule-based out-of-court workout procedures. This is intended, at least according to the government's public statements, to mitigate the disadvantages of the out-of-court workouts and facilitate swift and effective business restructuring of financially distressed, or potentially distressed, enterprises.

Although the New Regime includes court involvement and a cramdown mechanism, it is not considered a formal insolvency/restructuring (in-court) proceeding. Unlike traditional insolvency/restructuring proceedings, the New Regime lacks collectivity in a way that it only involves certain types of creditors (ie, financial creditors) and does not provide the tools ancillary to traditional insolvency/restructuring, such as avoidance actions or the ability to assume or reject executory contracts.

Background

Japan offers a variety of restructuring tools, including formal restructuring-type insolvency proceedings (such as civil rehabilitation and corporate reorganisation), as well as several rule-based out-of-court workout frameworks (including the Guidelines for Out-of-Court Workouts, the Guidelines for Business Turnarounds of SMEs (the SME Turnaround Guidelines), turnaround alternative dispute resolution (ADR) and SME vitalisation councils). Despite the recent increase in insolvency cases, over the past decade, rule-based out-of-court workouts have become a preferred choice in turning around or restructuring businesses.[7] This preference is largely because such workouts are more flexible than in-court proceedings and are less detrimental to debtors' businesses as the process does not typically involve trade and other non-financial creditors, does not have to be made public unless the debtor is a listed company and entails less stigma in Japan.

However, out-of-court workouts require unanimous consent of the involved creditors. While this approach worked in the past largely because the creditors had been limited to homogeneous and highly sympathetic Japanese banks and financial institutions, there has been growing concern that as creditors' composition becomes more diverse and global, the unanimous consent approach may no longer work. There also is a possibility of increase in the occurrences of creditor holdouts coupled with features of creditor-on-creditor violence, as a result of which, otherwise viable restructuring plans might be blocked. The government says, these challenges were exemplified by the restructuring of Marelli Holdings in 2022,

where, although over 95 per cent of the creditors agreed to the proposed restructuring plan under the Turnaround ADR, a few dissenting creditors forced the company into an in-court insolvency proceeding (simplified civil rehabilitation).

Discussions of whether to introduce a majority voting mechanism into an out-of-court workout framework to resolve the holdout problem started in 2014. However, concerns about constitutionality had always been raised regarding whether subjecting only a limited group of creditors (namely, financial creditors) to the proceeding and allowing the modification of rights by majority vote over the objection of dissenting minority creditors could amount to a violation of articles 29.1 and 29.2 (property rights) or article 14.1 (equal protection) of the Japanese Constitution.

However, in the course of developing the New Regime in 2024–2025, it was established that the New Regime would not necessarily be unconstitutional. This reflects the growing recognition, developed over the past two decades, that out-of-court workout frameworks targeting only financial claims can be justified on the grounds that they can effectively preserve the debtor's going-concern value and ultimately benefit broader stakeholders.

Turnaround ADR

Overview

Before turning to the details of the New Regime, it is helpful to briefly take a look at the Turnaround ADR – a rule-based out-of-court workout framework that has been well established in practice (particularly for restructurings of large-sized or listed companies) and has served as a foundational model for the development of the New Regime.

Turnaround ADR is a popular rule-based out-of-court workout procedure in which third-party experts coordinate communications between certain types of creditors (typically, financial institutions) and debtors to support the early-stage business revitalisation of debtor companies.

The Japanese Association of Turnaround Professionals (JATP), as a specific certified dispute resolution business operator, is responsible for conducting ADR procedures. There is no limit on the size or industry of debtor companies that can apply to use turnaround ADR. The system can be used by SMEs and larger companies. As it does not involve any court oversight or supervision, no cramdown is available either in class or cross-class, and unanimous consent by the relevant creditors is required to effectuate the debtor's revitalisation plan.

Procedure Outline

At the pre-consultation stage, a debtor contemplating using the procedure is called on to conduct its own due diligence and develop an outline of its business revitalisation plan. The debtor's efforts are surveyed and overseen by a third-party expert, who is also scheduled to be retained by the JATP to serve as the overseeing expert.

If there is a possibility that the proposed plan will be approved, the debtor makes an official application to the JATP. A suspension notice is sent to target creditors (mainly financial institutions), and the first creditors' meeting is convened to appoint a third-party expert as a procedural implementer, who will preside over the process as a third-party professional.

After the first creditors' meeting, the debtor further negotiates and discusses with the creditors the contents of the business revitalisation plan, and the debtor submits the final

version of the business revitalisation plan at the second creditors' meeting, accompanied by a report from the procedural implementer assessing whether the plan satisfies certain requirements including the feasibility and fairness of the plan. Thereafter, the third creditors' meeting is convened, and the involved creditors vote on the plan.

Transition To Other Proceedings

If any creditors disagree with the plan, special conciliation is sometimes used, or depending on the circumstance, a transition to in-court insolvency procedures could occur. In the case of a transition to in-court procedures, to allow for a smooth transition (which, in turn, incentivises relevant parties to do as much as possible within the ADR procedure), the following support measures, among other things, which respect the results and actions taken during the turnaround ADR, have been institutionalised and codified:

- facilitation of priority payment of commercial claims in in-court procedures;
- facilitation of priority payment of bridging loans (pre-debtor-in-possession financing); and
- simplified procedures relating to the expedition of special conciliation procedures.

The concepts listed above were introduced statutorily, rather than just in the JATP's rules, under the amended Act on Strengthening Industrial Competitiveness (the Amendment), which came into effect in June 2021. It has been pointed out that these measures do not fully eliminate the limitations inherent in post-ADR insolvency proceedings. Court proceedings are by nature public, potentially damaging the debtor's business reputation. Moreover, courts retain discretion over whether to grant exceptional priority to trade creditors; if such priority is denied, enterprise value may be impaired. Additionally, there is no guarantee that a sponsor under the out-of-court plan will maintain its support once the case enters an in-court process.

Key Features Of The New Regime

The New Regime appears to share several procedural similarities with the existing Turnaround ADR (its legislative process also suggests that). It is expected that the New Regime maintains key advantages of out-of-court workouts (including non-public process and exclusion of trade creditors), which help mitigate the deterioration of the debtor's enterprise value. The main features of the New Regime are as outlined below.

Scope Of Involved Creditors And Claims

Generally, at least on the face of the current blackletters of the statute, the type of creditors that a debtor can involve and bind under the New Regime is basically only financial institutions, and the type of claims that can be restructured or rescheduled by using the New Regime is only 'financial' claims (ie, loan claims and other claims based on provision of credit). The details of the scope of involved creditors and claims will be clarified in forthcoming ministerial ordinances.

Only unsecured claims are subject to the modification to rights (debt haircut, reschedule, etc) based on the restructuring plan approved under the New Regime (the Plan). As such, only creditors with unsecured claims have voting rights, and the number of voting rights is determined based on the number of unsecured claims. In addition, if there are secured claims, the debtor will likely need to obtain the consent for proposed modification to their rights (rescheduling, reduction of interest rate, etc) from each secured creditor outside the New Regime.

Involvement Of Third-party Organisation

The procedure of the New Regime begins with the debtor submitting an application to a third-party institution designated by the Ministry of Economy, Trade and Industry (METI) (the Designated Institution). The Designated Institution confirms whether the debtor satisfies the requirements to commence the New Regime procedure, including the following requirements: (1) the debtor is, or is likely to become, financially distressed; and (2) it is not apparent that the Plan to be proposed will not be approved.

After confirming the requirements have been satisfied, the Designated Institution notifies all the involved creditors and 'requests' a voluntary standstill (requesting not to enforce their claims nor to exercise any other rights as creditors – the details will be clarified in forthcoming ministerial ordinances).

The debtor must develop and submit the Plan to the Designated Institution, in principle, within six months of the commencement of the proceedings. The Designated Institution examines whether the Plan satisfies certain requirements stipulated by the New Act (eg, absence of violation of laws and regulations, the feasibility of the Plan, satisfaction of the best interest test and any further criteria to be set out in ministerial ordinances). The Designated Institution submits a report outlining the result of the examination above, which will thereafter be submitted to the involved creditors and the court.

As the METI has not yet designated a specific institution as the Designated Institution, it is still uncertain whether the JATP or any other restructuring-related organisations will be appointed as the Designated Institution upon or immediately after the New Regime takes effect in 2026.

Majority Voting And Confirmation By Court

The debtor convenes a creditors' meeting without delay after the receipt of the Designated Institution's report, where the involved creditors vote on the proposed Plan. The requirement for the Plan to be approved is three-quarters or more of the voting rights (which are determined based on the number of unsecured claims). If a single creditor holds three-quarters or more of the voting rights, then a simple majority of all the creditors by headcount is additionally required.

Unlike many foreign restructuring regimes (Part 26A restructuring plan, scheme of arrangement, StaRUG, etc), there is only a single class of unsecured claims (no classification of secured or unsecured claims for voting); therefore, there is no mechanism that allows cross-class cramdown.

The debtor must file with the court for the confirmation of the Plan, which is required for the Plan to be binding (although, if the Plan is approved by the unanimous consent by the involved creditors, the court's confirmation is not required). The court must confirm the Plan unless there is an exceptional circumstance where the Plan or the creditors' meeting process violates laws or regulations, there is apparently no feasibility of the Plan, the Plan was approved by the creditors through unjust means, or the Plan fails to satisfy the best-interest test.

Comparison With Other Countries' Regimes

The New Regime has several similarities with the scheme of arrangement type proceedings adopted in the United Kingdom and other common law jurisdictions and European countries,

particularly in that it is a pre-insolvency procedure that allows a restructuring plan to become binding through creditor majority voting and subsequent court sanction. However, it differs from the scheme of arrangement type proceedings in several important respects. First, as the scope of involved creditors is statutorily defined, there is no room to include trade or non-financial creditors within the process. Second, secured claims are not subject to the mechanism of the New Regime that enables the Plan (including the modification to rights) to be binding by majority vote (and, as such, voting rights are not granted to secured claims). Third, an independent third-party institution is tasked with reviewing and reporting on the feasibility of the Plan and compliance to other requirements.

OUTLOOK

Given that Japan's out-of-court workout practices have developed steadily over the past several decades – and are generally well-regarded by practitioners, financial institutions and other stakeholders – it is expected that the actual implementation of the New Regime will be shaped by existing practices. In this light, it may become a common practical approach for debtors to initially seek unanimous consent from their financial creditors under traditional frameworks and, if a holdout situation occurs, to utilise the majority voting mechanism under the New Regime. For such a strategy to be effective, however, ensuring the seamlessness between the existing out-of-court mechanisms and the New Regime will be essential.

In any case, restructuring professionals and other players or stakeholders should be careful about how the New Regime will affect the existing restructuring practices over time. Further, the details of the New Regime remain to be determined by yet-to-be-publicised ministerial ordinances. Since the actual operations of the New Regime are not yet fully established, practitioners, financial institutions and other stakeholders are required to discuss further how the New Regime should be operated so that the New Regime can be refined into a more usable tool for companies facing, or at risk of, financial distress.

Endnotes

1 ' Bankruptcy Information', Teikoku Databank. ^ Back to section

2 'Bankruptcy Information', Teikoku Databank, '人手不足倒産の動向調査（2024年）', Teikoku Databank (9 January 2025). ^ Back to section

3 ' Bankruptcy Information', Teikoku Databank. ^ Back to section

4 'コンプライアンス違反企業の倒産動向調査（2024年）', Teikoku Databank (24 January 2025). ^ Back to section

5 ' Nissan sets the stage for change with the bold Re:Nissan plan', Nissan Motor Co, Ltd (13 May 2025). ^ Back to section

6 The final version of the New Act (in Japanese) can be viewed at the following link: www.sangiin.go.jp/japanese/joho1/kousei/gian/217/pdf/t0802170332170.pdf.

^ Back to section

7 Notably, the number of cases handled by the SME vitalisation councils, which is an out-of-court workout platform targeting SMEs, has been steadily increasing (4,244 cases in 2021, 6,409 cases in 2022, and 6,787 cases in 2023) ('2023年度に認定支援機関が実施した中小企業再生支援業務（事業引継ぎ分を除く）に関する事業評価報告書', the Organi'ation for Small & Medium Enterprises and Regional Innovation (22 October 2024)) while there are relatively smaller number of cases of turnaround ADR, which is an out-of-court workout platform mainly used by larger or listed companies' restructuring (3 cases in 2021, 2 cases in 2022 and 8 cases in 2023) ('利用状況', the Japanese Association of Turnaround Professionals). The number of restructuring-type insolvency proceedings remains at low levels (for civil rehabilitation, 110 cases in 2021, 92 cases in 2022, and 113 cases in 2023; for corporate reorganisation, 3 cases in 2021, 6 cases in 2022, and 7 cases in 2023) ('令和5年 司法統計年報 1民事・行政編', General Secretariat, Supreme Court). Back to section

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