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Soundings

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The UK Defence Club in Japan

Membership

As the shipping industry in Japan has grown internationally the benefits of being a Member of the UK Defence Club have become increasingly apparent to the Japanese market. The value of the Association's cover and the first class service that is provided was particularly highlighted following the worldwide economic crisis in 2008/2009 and the Association continues to experience a steady growth in its Japanese Membership.

The Japanese Membership is drawn from across the country: Tokyo, Kobe, Osaka, Okayama and Imabari and comprises both ship owners and time charterers representing the vast majority of ocean going ship types.

Service

London Syndicate 1 is responsible for servicing the Association's Japanese Members based in Japan and overseas. The team is led by Paul Sessions and consists of Jacqueline Tan, Mike Bowen, Sean Geraghty and Aki Tsukui. This team of qualified lawyers and mariners offers Members in Japan a full advisory service on all aspects of FD&D issues around the clock. The team in London is supported by a global network of correspondents, lawyers, and experts with extensive experience and knowledge throughout the world and is readily available to support the Association's Japanese Members.

This dedicated team means that the Association is well placed and equipped to guide Members at any stage of their contractual negotiations, and to help find practical solutions to legal problems. The Association assists Members in establishing and defending claims arising out of the operation of their entered ships and has seen an increase in the number of disputes arising in Japan concerning matters

such as S&P, bunker quality, delay/detention of ships, hire and other charterparty claims.

The team has also been widely consulted by the Japanese Membership on topical issues such as piracy and sanctions. It is not only the Association's expertise in assisting Members with complex claims in court or arbitration proceedings but also its first hand "emergency" or "first aid" assistance, given without delay at the outset of any matter, which is so attractive to Members in Japan.

In these uncertain times, it is likely that Members may continue to see disruption to their business operations as the markets are destabilised by poor hire/freight rates and escalating bunker prices. When legal costs have the potential to directly impact on a company balance sheet, the Membership in Japan places great value on the Association's cover and the experienced team available to deliver the best quality service in a cost effective way.



Japanese Rehabilitation Proceedings

1. What does it mean that a company has entered into rehabilitation proceedings?

In Japan there are two types of rehabilitation proceedings, one under the Corporate Organization Act (“COA”) and the other under the Civil Rehabilitation Act (“CRA”). The former is usually applicable to larger companies and the latter to smaller companies or individuals. Whilst the detailed content and implications of the two Acts differ, the key provisions are similar in the sense that both are proceedings designed to ensure the continuation of the business of the company concerned.

As an example of the main differences between the two Acts, proceedings under the COA are referred to as Non-DIP (“DIP” standing for “Debtor in Possession”) where the receiver appointed by the Court will manage and control the company, its assets and debts under the supervision or approval of the Court and the exercise of security rights (such as mortgages) by the creditors is to some extent restricted.

Proceedings under the CRA are known as “DIP” and permit the management of the company that is in place at the time of the commencement of the

proceedings to continue to control the company, its assets and debts under the supervision or approval of a receiver appointed by the Court and, in principle, the exercise of security rights by the creditors is not restricted.

The commencement of rehabilitation proceedings in Japan effectively means that a company has the protection of the Court in the sense that creditors cannot enforce their claims, arrest or attach the company’s assets or ships and that the company concerned cannot repay its creditors without obtaining the approvals of the receiver or the Court.

Once rehabilitation proceedings have been commenced, creditors need to register their claims with the Court within a certain time frame (see Question 3 below) and the company/ the receiver will assess those claims and submit a rehabilitation plan. This usually proposes a process for the settlement of approved claims and may include the reduction of claim amounts and provision for payment in installments.

If the rehabilitation plan is approved by the creditors and the Court, each approved claim will be repaid according

to the plan. The creditors who have priority, such as mortgagees, are dealt with separately.

The company will continue running its business as a going concern under the approval or supervision of the receiver/ the Court during the rehabilitation period.

This process does of course take some time and creditors’ rights under a contract may be affected as explained below.

2. Prior to the commencement of rehabilitation proceedings can a party approach the company to renegotiate some or all of its charterparties?

A party can freely renegotiate with the company before the commencement of rehabilitation proceedings. However, if the conclusion of a settlement agreement or any payment thereunder is made shortly prior to the commencement of rehabilitation proceedings and/or if the outcome of the renegotiation is deemed to prejudice the rights or claims of other rehabilitation creditors (for example, in reducing the assets of the company or in showing preference or providing securities to specific creditors), any settlement could be negated by the company, the receiver or the Court in the subsequent rehabilitation proceedings.

3. What is the procedure to register a claim against a company in the rehabilitation proceedings?

A creditor to the company is in principle required to register its claims with the Court within the period as ordered by the Court, say within one month from the Court order for the commencement of the rehabilitation proceedings. To register a claim, the following documents would be required:

- a) Power of Attorney ("PoA");
- b) Certificate of Corporate Nationality to prove the authority of the person who executes the PoA on behalf of the creditor;
- c) A copy of the charterparty; and
- d) A final statement of account showing the outstanding hire and other sums owing.

A creditor may also wish to register a claim for damages and this is addressed in Question no.6 below.

It is important to ensure that any debt that the creditor may owe to the company is "set off" against the creditor's claims. It should be noted that any set off needs to be made within the period set down for the registration of claims. So, where a creditor has both claims and debts against the company in rehabilitation, even if the creditor would usually have the right to set off its debts against its claim, the creditor would lose its right to do so unless it exercises the right to the set off within the stipulated period. If the creditor fails to do so it could only then recover its claim from the company to the extent of the reduced amount, payable in instalments, whereas it would have to pay to the company the full amount of any debts.

4. Will the receiver be interested in affirming (i.e. maintaining) any outstanding charterparties?

In the case of a long term contract such as a time charterparty, the company/the receiver has the option either to maintain or terminate the contract. The other party to the charterparty can request that the company/the receiver declare its intentions within a certain period. If the company/the receiver does not comply within the specified period, the

charterparty is deemed "affirmed", i.e. the charterparty will be maintained on the same terms and conditions. In practice the company/the receiver may propose to alter some of the terms of the charterparty, such as the hire rate, but the creditor does not have to agree.

The decision whether to maintain or terminate a charterparty is at the sole discretion of the company/the receiver.

If the company/the receiver opts to affirm a time charterparty then all hire payable under that contract would be treated as a "common benefit claim". This means that the hire would be payable in full and without any restriction, such as payment in instalments, under the rehabilitation proceedings.

It is worth noting that under Japanese rehabilitation law, there are two types of creditors' claims: 1) "rehabilitation claims" and 2) "common benefit claims". Generally speaking, the former are claims that arose prior to the commencement of rehabilitation proceedings and are usually to be paid on a reduced basis. Very frequently, less than 10% is paid to creditors. In addition, these claims are usually to be paid in instalments, for example, once a year for four years.

"Common benefit claims" are those that arise after the commencement

of the rehabilitation proceedings and, if accepted, will be paid in full.

If the company/the receiver chooses to terminate a charterparty, only the hire for the period from the commencement of the rehabilitation proceedings up to termination will be treated as a common benefit claim.

5. Following the commencement of rehabilitation proceedings is a Member obliged to maintain a charterparty if hire is not paid? What are the consequences of not maintaining a charterparty?

Before the commencement of rehabilitation proceedings, a creditor may not be paid for hire in full and/or punctually and it may not be paid until a decision as to whether to terminate or affirm the charterparty is made. Whether a creditor is entitled to withdraw or terminate the charterparty by reason of non-payment of hire will need to be assessed on a case by case basis and specific legal advice on the terms and conditions of the charterparty and the governing law should be obtained.

However, as stated above, the company/the receiver has the option to terminate or maintain a charterparty.

[continued overleaf >](#)



Japanese Rehabilitation Proceedings (continued)

A creditor who has a claim for unpaid hire should exercise caution whilst awaiting the decision of the company/the receiver. This is because premature termination of the charterparty by a creditor may place it in breach of the contract if the company/the receiver ultimately elect to maintain it. A premature termination may also prejudice any claim for damages even if the company/the receiver intends to eventually elect to terminate the charterparty. Also, as stated above, the hire for the period from the commencement of rehabilitation proceedings up to the termination by the company/the receiver shall be treated as a common benefit claim.

6. If the receiver of the company in rehabilitation terminates a charterparty, is it possible to claim damages including consequential damages in the rehabilitation proceedings?

The creditor is entitled to claim for damages and is required to substantiate its claim. The extent of the damages recoverable will depend mainly on the governing law of the charterparty and specific legal advice will be required.

7. Assuming that the receiver affirms a charterparty, what happens to it in terms of the rehabilitation proceedings?

In simple terms, the charterparty will continue on the existing terms and conditions and the hire should be paid as a common benefit claim without any reduction or payment in installments.

8. Can steps be taken to arrest assets of the company in rehabilitation proceedings in other jurisdictions?

The protection given to the company in Japanese rehabilitation proceedings is not automatically effective outside Japanese territory. A creditor can potentially enforce its claims by attaching assets or arresting ships outside Japan unless the Japanese rehabilitation proceedings are recognised in the country in question.

9. What is the position concerning a purchase option in a charterparty?

If a charterparty contains a purchase option and the owning company of the ship enters into rehabilitation proceedings then the company/the receiver may choose to terminate the charter, thus preventing the charterer from exercising the option, or the charterparty may be maintained in which case the charterer would be entitled to exercise the option.

If however it is the charterer that commences rehabilitation proceedings, it/the receiver may maintain the charterparty with or without the option being exercised or may terminate the charterparty which will result in non exercise of the option.

If a ship has an outstanding mortgage usually the mortgagee will have the priority over any purchase option under the charterparty.

10. What is the likely timescale and repayment ratio for a repayment schedule under a rehabilitation plan?

The timescale and the payment ratio vary in each case but usually the rehabilitation proceedings or the rehabilitation plan will be finalised only within a few years and in many cases the repayment ratio is at a relatively low figure, often less than 10%.

11. What is the position if the receiver rejects a claim in the rehabilitation proceedings?

When the company/the receiver denies a rehabilitation claim (that is not a common benefit claim or claim that otherwise has priority), the creditor may make an objection thereto by filing a petition for assessment by the Court. The petition needs to be filed with reasoning and supporting evidence within one month from the completion of the inspection of the rehabilitation claims. An assessment order of the Court to determine the acceptance or denial of the claim will be rendered unless the parties reach an amicable settlement.

A creditor who is dissatisfied with an order of the Court may file an appeal within one month.

The comments above are intended to provide a general overview of Japanese rehabilitation proceedings. If however Members become involved in any of these issues then specific legal advice should be obtained and you should also approach your usual Club contact.

The UK Defence Club

Thomas Miller Defence Ltd, 90 Fenchurch Street, London, EC3M 4ST
tel: +44 207 283 4646 fax: +44 207 204 2131
email: tmdéfence@thomasmiller.com web: www.ukdefence.com