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Resolution and Collection Corporation (RCC) - Asset Management Company in Japan

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RCC – Japan

Mallory Dreyer¹

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Abstract

Though the Japanese real estate and stock market bubble burst in the early 1990s, the ensuing financial crisis in Japan did not reach a systemic level until 1997, when four large financial institutions failed in a single month (Nakaso, p8). Because they were heavily exposed to real estate and equity markets, the Japanese banks had a nonperforming loan (NPL) problem, which was prolonged and, according to official estimates, did not peak until 2001 at 8.7 percent of GDP (BOJ 2006, p4). In response, the Japanese government created multiple asset management companies; the Resolution and Collection Corporation (RCC) was the result of the merger of two narrowly focused, semi-governmental agencies and began operations in 1999 (RCC, p12). The RCC was tasked with the purchase of NPLs from both solvent and insolvent financial institutions (DICJ 2008, p68). In 2001, its scope was expanded to include corporate restructuring and revitalization (DICJ 2008, p18). Though there was no specified sunset date for insolvent institutions, the purchase window for solvent financial institutions ended on March 31, 2005 (DICJ 2008, p25). The RCC purchased ¥4,004 billion (approximately \$37 billion USD) in bad debt (book value) at a purchase price of ¥353 billion from solvent institutions by March 2005, and it collected ¥642 billion by March 2008 (DICJ 2005; DICJ 2008, p25). The RCC purchased ¥6,366 billion in assets (estimated ¥29,000 billion book value) from failed financial institutions and recovered ¥7,143 billion by the end of March 2008 (DICJ 2008, p72; Koo, p20). The RCC assisted with debt restructuring for 569 borrowers between 2001 and 2008 (DICJ 2008, p77). Though the RCC is operational as of today, its operations are no longer focused on resolving the 1990s crisis (RCC, p1).

Keywords: asset management company, Resolution and Collection Corporation, RCC, Japan, nonperforming loan, corporate restructuring, corporate revitalization

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Japan – RCC

At a Glance

The Japanese financial crisis of the 1990s was prolonged as banks and the government were slow to acknowledge and respond to a massive nonperforming loan (NPL) problem. In 1998, two asset management companies merged to create the Resolution and Collection Corporation (RCC), which was tasked with the purchase and disposal of NPLs from solvent and insolvent financial institutions. The RCC began operations in 1999, but its operations were limited, as the full scale of the NPL problem was still not recognized.

The government began acting more aggressively to address the NPL problem in 2001 by adding corporate restructuring to the RCC's scope. In 2002, the RCC was able to purchase NPLs from solvent institutions at market value. The deadline to purchase from solvent institutions was March 31, 2005, but no deadline was set for failed institutions. By 2005, the RCC had purchased ¥4,004 billion of loans (book value), approximately \$37 billion USD, at a purchase price of ¥353 billion from solvent institutions and recovered ¥642 billion by March 2008. The RCC recovered ¥7,143 billion on total purchases of ¥6,366 billion (estimated ¥29,000 billion book value) from failed financial institutions by March 31, 2008. The RCC assisted with corporate restructuring of 569 borrowers between 2001 and 2008.

Summary Evaluation

Many observers believe that Japan's banking problems were prolonged in the 1990s and 2000s due to the unwillingness of the government and financial sector to admit the extent of the NPL problem. The RCC, which the government created to address the NPL problem, has been criticized due to its relatively limited scope: it ultimately purchased a total of ¥33 trillion in loans (book value); private economists at the time estimated the NPL problem at ¥100 to ¥250 trillion. Others argue that the RCC was limited in effectiveness as the purchase price offered to solvent financial institutions was often steeply discounted, as the RCC sought to minimize the risk of transferring losses to taxpayers. Others have stated that corporate restructuring was outside of the RCC's value-adding capabilities. However, it has been recognized that the RCC recovered in excess of its purchase price in its disposal of assets from failed and solvent institutions.

Summary of Key Terms

Purpose: “[A]ccelerate the recovery and collection of non-performing loans transferred from failed [and solvent] financial institutions through a fair and transparent process in order to minimize public costs” (DICJ AR 2004, pi).

Launch Dates Announcement Date (Merger):
October 1998
Operational Date: April 1, 1999

Wind-down Dates Expiration Date for Transfers: N/A for insolvent; March 31, 2005 for solvent
Date of Last Asset Disposal: N/A

Program Size Not specified at outset

Usage Solvent: ¥353 billion (purchase price) for ¥4,004 billion (book value)
Insolvent: ¥6,366 billion (purchase price) for an estimated ¥29,000 billion (book value)

Outcomes Solvent: Recovered ¥642 billion on ¥353 billion
Insolvent: Recovered ¥7,143 billion on ¥6,366 billion
Restructuring: 569 borrowers

Management Approach Combination Disposition / Management

Ownership Structure Government-owned

Notable Features Special investigative powers to take on difficult cases such as those tied to organized crime; purchased loans at a steep discount

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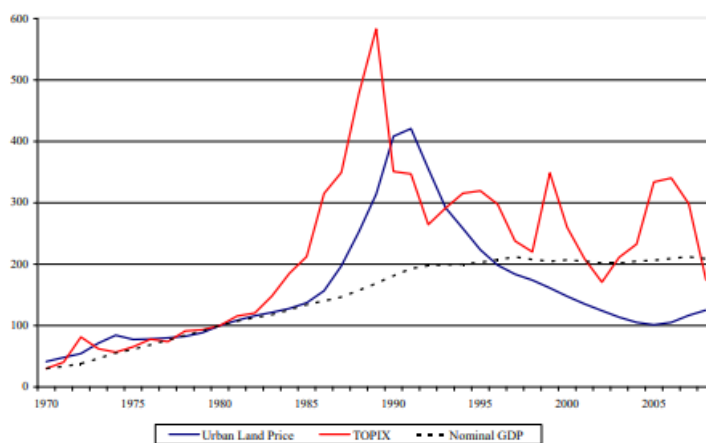
I. Overview

Background

Asset bubble burst and establishment of CCPC (1990-1994)

Japanese real estate and stock market prices tripled in the latter half of the 1980s (Lincoln, p1). The bubble burst in the early 1990s, triggered by interest rate hikes by the Bank of Japan (BOJ), leading to “[a] rapid downturn in speculative investments” which “weakened both demand and asset prices, creating a downward spiral” (Tandon, p8). Within three years, the stock market had lost 60 percent of its peak 1989 value, and land prices decreased by more than half in the following decade (Caballero, p2). The decline in stock and real estate prices had the potential to create large mark-to-market losses for banks and other financial institutions, given their volume of equity holdings and real estate loans (Kanaya, p8).

Figure 1. Stock Price (TOPIX), Urban Land Price, and Nominal GDP (1980=100) from 1970-2007



Note: TOPIX is the price index of the Tokyo Stock Exchange; GDP is gross domestic product.

Source: Tokyo Stock Exchange; Real-Estate Research Institute; and Economic and Social Research Institute (ESRI), Cabinet Office, Government of Japan, websites.

Source: Fujii, p2

During the first years following the collapse of the bubble, financial institution failures were sporadic and limited to smaller institutions (Nakaso, p3). The larger banks and government delayed recognizing the extent of the nonperforming loan problem in the hope that asset prices would return to pre-1990 levels (Kanaya, p22; Fujii, p4). Banks were also slow to write off loans with a low probability of recovery due to the strict tax guidelines for loan loss write-offs, as write-offs were permitted “only after the loan loss amount had been ascertained in bankruptcy or foreclosure proceedings” (Kanaya, p11).

Japanese banks established the Cooperative Credit Purchasing Company (CCPC) in 1993 to assist with the disposal of NPLs, but “the apparent purpose behind its creation was to allow banks to take advantage of tax deductibility for loan write off” (Kanaya, p11). The CCPC dealt only with loans with real estate as collateral. It was established as a private entity with 162

member institutions which provided the initial ¥7.9 billion (approximately \$74 million USD)² in capital as well as the financing for the purchase of bad loans (Packer 1994, p2). Banks could sell loans to the CCPC, which “generated tax benefits for the banks because upon the transfer to the CCPC, the selling banks could recognize losses immediately that reduced their taxes” (Hoshi 2010, p405). Institutions selling a loan to the CCPC had a contingent liability; if there was a significant difference between the purchase price and collections, the difference was charged to the institution; therefore, “the CCPC has recourse to the seller of each loan” (Packer 1994, p3). The first round of purchases in 1993 included 229 loans with a face value of ¥682 billion at a discount of 33.7 percent (Packer 1994, p6). The major banks accounted for the majority of the loans sold to the CCPC (Packer 2000, p147). In the first years of operations, the CCPC was slow to dispose of loans, as it sold only 88 properties by March 1994 (Packer 2000, p146). However, loan disposal accelerated after 1998, and the CCPC was liquidated in 2004 (Hoshi 2010, p405). In total, the CCPC purchased NPLs worth ¥15.4 trillion in face value with ¥5.8 trillion in appraised value (Hoshi 2010, p405).³

Credit cooperative failures and the RCB (1994-1998)

Tokyo Kyowa Credit Union and Anzen Credit Union, two significant credit unions, failed in December 1994 (Nakaso, p4). In 1995, the Bank of Japan created the Tokyo Kyodo Bank (TKB), an asset management company, to assume the assets of the two failed credit unions (Hoshi 2004, p21). In August 1995, the TKB assumed the assets of additional failing credit cooperatives and a failed bank (Nakaso, p5). Private financial institutions provided ¥20 billion in capital, and the BOJ provided ¥20 billion in capital for the TKB (Nakaso, p4). The TKB was reorganized into the Resolution and Collection Bank (RCB) in September 1996 (Nakaso, p7). After the restructuring, the RCB became a 75 percent subsidiary of the DICJ, as it received ¥120 billion in capital from the DICJ (DICJ 2001 AR, piii). Ultimately, the RCB took over the operations of 45 failed banks and credit unions and worked to collect, recover, or sell the nonperforming loans that those institutions had extended (JT 1999a; DICJ 1998, p15).

The jusen companies and the HLAC (1992-1998)

Concurrent with the credit cooperative failures, there was a high level of uncertainty about the quality of lending by the *jusen*, the non-bank housing loan corporations established by banks in the 1970s. The *jusen* moved into higher risk lending in the 1980s following deregulation and increased competition in the home mortgage market (Hoshi 2010, p399). The *jusen* received capital injections in 1993 and committed to rehabilitation plans; however, real estate prices continued to fall, and the Ministry of Finance (MOF), creditors and investors agreed to dissolve seven *jusen* in 1996 (Kanaya, p24). The MOF commissioned a special examination of the *jusen* and determined that 74 percent of their outstanding loans were nonperforming (Kanaya, p24).

² Conversion based on the average yearly exchange rate as of December 31, 2000 (1 USD =107.80 yen) from OFX

³ For more information on the structure of the CCPC, see: Packer, F. (1994) The Disposal of Bad Loans in Japan: A Review of Recent Policy Initiatives. and Packer, F. (2000). The Disposal of Bad Loans in Japan: The Case of the CCPC

In 1996, the Japanese Diet (legislature) established the Housing Loan Administration Corporation (HLAC) (Koo, p10). The HLAC was an asset management company for the *jusen*, and the assets of seven *jusen* companies were transferred to the HLAC in October 1996 (JT 1996). The HLAC was established as a 100 percent subsidiary of the DICJ with ¥200 billion in capital (DICJ 2001 AR, piii). The HLAC was created to dispose of the estimated ¥4.7 trillion of NPLs from the *jusen* companies that it assumed, and the government estimated that the activities would take up to fifteen years to complete (DICJ 1998, p72; JT 1996). The initial estimate of the number of NPLs of the *jusen* companies was approximately 200,000, and there was concern “that as much as ¥1.2 trillion of the loans [would] be unrecoverable” (JT 1996). In addition to assuming the assets of the *jusen*, the HLAC sought civil damages from banks that acted in a criminal manner (JT 1999a).⁴

Increases in NPL volume during the 1990s

During the 1990s, there were an array of factors that led to the NPL problem and its continued acceleration. NPLs were distributed across all types of financial institutions, though the problem was concentrated in real estate, construction, and wholesale and retail trading (Cabinet 2001a). Banks in Japan were reluctant to recognize losses on NPLs during the mid-1990s, as there were strict tax guidelines on write-offs; banks also feared that borrowers would view the write-off as “a signal that the banks had given up on loan recovery” (Kanaya, p11). The main bank system of lending further contributed to the NPL problem. A borrowing firm’s main bank was its primary lender; the main bank was the “quasi-insider monitor” that identified problems before the borrowing firm became insolvent and assisted with business restructuring (Tandon, p93). However, many main banks continued to provide loans to firms, “even when the long-term viability of their borrowers came into question” (Tandon, p93). The continued financing of failing firms, known as ‘evergreening’, is considered a contributing factor to the crisis (Caballero, p2-3). Other macroeconomic trends, such as “the bursting of the asset price bubble, continued weakness of the domestic economy, chronic price deflation and the rising number of business failures and bankruptcies help [to] explain the rise in NPLs” (Fung, p11).

During the 1990s, the government enacted increasingly stringent guidelines to standardize loan classification and disclosure requirements. At the onset of the crisis in the early 1990s, “[l]oan classification rules were lax as related to international best practices”, but the NPL volume increased as the government began to pass legislation to enforce classification standards (Tandon, p129). In addition, loan disclosure requirements were progressively strengthened. The new provisioning policy was based on a bank’s self-assessment of its portfolio, which enabled more flexible provisioning based on the quality of borrowers and their history of default (Nakaso, p18). In 1999, comprehensive requirements for disclosure were introduced, which were considered “among the most far-reaching in the world”

⁴ For more information on the *jusen* crisis, see: Milhaupt, C. & West, M. (2004). The “Jusen Problem”. In *Economic Organizations and Corporate Governance in Japan*: Oxford University Press. <https://www.oxfordscholarship.com/view/10.1093/0199272115.001.0001/acprof-9780199272112-chapter-4>

(Nakaso, p19). The government also sought to further strengthen loan loss provisioning and standardize borrower and asset classification in 2002 (IMF 2003, p6). The progressive strengthening of standards to increase transparency and consistency in reporting is one factor that contributed to the increasing volume of NPLs beginning in 1992.⁵

Though banks were required to provide more transparency about loans and increase loss provisioning, uncertainty remained regarding the total volume of NPLs in Japan. In mid-1995, the official estimate of NPLs was approximately ¥40 trillion (Tandon, p18). However, there were different sources of estimates of the total amount of NPLs in Japan: private estimates, estimates based on bank disclosures and financial statements, and official estimates. As reflected by the fact that “[p]rivate estimates of actual bad loans [were] substantially greater than amounts announced by the banks and the MOF”, there was not a clear understanding of the true scope of the problem, despite the write-offs and reclassification of NPLs (Tandon, p29). Private estimates for bad loans ranged from ¥100 to ¥250 trillion, while the official estimate was ¥36.8 trillion as of 2001 (Lincoln, p7).

Other responses to the escalating crisis

The severity of the crisis became clear with the failure of four large financial institutions in November 1997 (Nakaso, p8). On November 3, 1997, Sanyo Securities, a firm with ¥2.7 trillion in assets, filed an application to begin reorganization proceedings, and the government immediately suspended its operations. Sanyo’s failure “paralysed the entire interbank market,” and Yamaichi Securities failed three weeks later (Nakaso, p8-9). In the case of Yamaichi, the government proceeded with an “orderly wind-down” rather than suspending its operations (Nakaso, p9-10). Hokkaido Takushoku Bank failed on November 17; an assuming bank was found, and the BOJ provided liquidity support. On November 26, Tokuyo City Bank failed; the government released a statement that day reaffirming its commitment to financial stability and assuring deposit protection, as the Deposit Insurance Act had been amended in 1996 to include a temporary suspension of deposit insurance limits (Fujii, p4; Nakaso, p11). In 1998, the Prime Minister announced the nationalization of the Long-Term Credit Bank of Japan and the Nippon Credit Bank; the banks were placed under special public management by the DICJ (Hoshi 1999, p2; DICJ 1999, p10-11).

With the crisis reaching an acute phase, the Diet passed the Financial Function Stabilization Act, which allowed the government to use ¥30 trillion of public funds, ¥17 trillion of which went to protection for depositors of failed banks and ¥13 trillion of which went to bank recapitalization (Nakaso, p11; Fujii, p5). The first publicly funded recapitalization program, which used ¥1.8 trillion, took place in March 1998. However, the injection was “unsuccessful in stabilizing the situation,” and there was a high level of public dissatisfaction in the government’s response to the crisis (Hoshi 2010, p401). The dissatisfaction prompted leadership changes, as the Hashimoto government resigned and a new government led by

⁵ For additional information on loan classification standards, see FSA 2001. Inspection Manual for Deposit-Taking Institutions. https://web.archive.org/web/20060622192021/http://www.fsa.go.jp/en/refer/manual/yokin_e/y00.pdf; Kawai, M (2005). Reform of the Japanese Banking System. https://www.academia.edu/23481809/Reform_of_the_Japanese_banking_system; and Nakaso (2001), p18-19

Keizo Obuchi assumed power (Hoshi 2010, p401). The new government passed the Prompt Recapitalization Act (also referred to as the Early Strengthening Law or the Financial Function Early Strengthening Law) and approved another capital injection worth ¥7.5 trillion (Nakaso, p15), which seemed to calm the market, though “the problem of NPLs persisted and the capital shortage soon reemerged” (Hoshi 2010, p401).⁶

Over the course of the financial crisis in Japan, crisis management and oversight authority changed, and new governmental bodies were established. The Financial Supervisory Agency was established in June 1998, and it took over supervisory powers from the MOF (Kanaya, p31). The Financial Reconstruction Commission (FRC) was also established in 1998 and given the authority to inspect and supervise the banks; it was established as an independent administrative body under Prime Minister to administer the new laws related to bank failures and capital injections (Nakaso, p14). In 2001, the Financial Supervisory Agency and the FRC were reorganized into the Financial Services Agency (FSA), and the FSA became an external part of the Cabinet Office (Fujii, p19). The FSA had “integral responsibility over supervision, inspection, and planning of the financial system” (Hayashi, p502).

There was a strong public outcry against using taxpayer money to resolve the crisis. In response to the *jusen* problem, the government used ¥685 billion of taxpayer money, which led to “public outrage over the repudiation of the promise” not to rely on taxpayer assistance to resolve the crisis (Hoshi 2010, p400). After this, “any reference to the use of public funds [became] almost a political taboo” (Nakaso, p20), and “[t]he legacy of this experience was long lasting because it made the government very reluctant to ask for the much larger sums that would be needed once the troubles of the commercial banks became evident” (Hoshi 2010, p400).

Program Description

The Resolution and Collection Corporation (RCC) was established through the merger of the HLAC and the RCB through an amendment to the Deposit Insurance Act and the Financial Revitalization Act (also referred to as the Financial Function Reconstruction Law). In 1998, the merger agreement was announced, and the RCC began operations on April 1, 1999 (RCC, p12). The RCC was created to “accelerate the recovery and collection of non-performing loans transferred from failed financial institutions through a fair and transparent process in order to minimize public costs”; the RCC could also purchase NPLs from solvent financial institutions “to accelerate the disposal of non-performing loans” (DICJ AR 2004, pi). The RCC assumed the responsibilities of the HLAC and the RCB for managing and collecting the NPLs from the *jusen* and the failed credit cooperatives (Kang, p66). The RCC would continue to pursue legal action against former executives and debtors of failed institutions (Kang, p66). The RCC purchased preferred shares and subordinated debt the institutions receiving capital injections, in accordance with the Prompt Recapitalization Act, though the FRC oversaw the capital injections and determined the underwriting terms of the capital (Nakaso).

⁶ For more information about the capital injections in Japan at this time, see the Financial Function Stabilization Act and the Prompt Recapitalization Act cases written by Vaasavi Unnava (2019)

The RCC was established as a wholly-owned subsidiary of the Deposit Insurance Corporation of Japan (DICJ) (RCC, p2). The government of Japan provided the funding for the RCC, as the DICJ issued government-guaranteed DICJ bonds and injected the proceeds into the RCC (Kang, p66). When the RCC began operations, it had ¥212 billion in capital (Kang, p66). Kohei Nakabo, who served as president of the HLAC from its founding in July 1996, became the president of the RCC (Otake 1999a). The RCC was staffed by the previous HLAC and RCB employees (Otake 1999a), and the RCC had approximately 1,900 employees in April 1999 (Nakaso, p56).

Process for Solvent Institutions

The Financial Revitalization Act granted the RCC the ability to purchase NPLs from solvent banks in addition to failed institutions, though solvent banks were not required to sell their NPLs to the RCC (DICJ 2000, p5; Hoshi 2010, p405). On June 22, 1999, the RCC began accepting applications from the healthy banks willing to sell to the RCC (JT 1999c). These banks were required to file their provisional applications between June 22 and July 9, and the RCC and DICJ reviewed the application, exchanged opinions with the banks, and provided an offer price for the loans (JT 1999c). Banks interested in the offer then filed formal applications to proceed with the purchase. Additional application windows were announced by the RCC over the course of its operations. When the Financial Revitalization Act was enacted in 1998, it designated the authority to the RCC to purchase assets from sound financial institutions through March 31, 2001, but the law was later amended to extend the deadline to March 31, 2004 (DICJ 2008, p25). In April 2003, the period was again extended, and the final deadline was set to March 31, 2005 (DICJ 2008, p48).

Process for Insolvent Institutions

In the case of a failed financial institution, the DICJ, FSA, and courts worked together through the resolution process to ensure a smooth transfer of business to an assuming institution. The institution submitted an application to the DICJ for assistance, and the DICJ determined the financial assistance, which could take “the form of a monetary grant, loan or deposit of funds, purchase of assets, guarantee of liabilities, assumption of financial obligations, subscription for preferred shares and other capital raising instruments, or loss sharing” (DICJ 2008, p44). The purchase of assets would be agreed upon by the failed institution, the assuming financial institution(s) or bridge bank, the RCC, the DICJ, and the FSA. The DICJ released statements detailing the financial assistance given to the failed financial institutions, beginning in 2001. These statements detailed the purchase price and the book value of assets transferred.⁷

Purchase Price

The RCC does not appear to have disclosed the methodology for determining the purchase price offered for NPLs, though it established a multi-stage process to determine the price. To begin the process, a real-estate appraisal was submitted to the RCC with the property valuation; the RCC would then review the appraisal (Packer 2000, p154). Because the RCC

⁷ See DICJ website for press releases detailing the scheme of financial assistance and examples of the transfer of NPLs to the RCC

did not have recourse to the originator bank, it sought to determine an appropriate value for the purchase price (Packer 2000, p154). The RCC, with guidance from the DICJ and the Purchase Price Examination Board (an advisory board of the DICJ governor), determined the purchase price for assets from solvent institutions on a case-by-case basis (Nanto, p10; DICJ 2008, p25). The RCC also sought guidance from supervisory bodies, such as the MOF and the FSA (JT 1999b).

When the RCC was established, it purchased assets at a steep discount to prevent the recognition of losses on its portfolio; this was driven by the heightened political climate and the government's hesitancy to use taxpayer funding for bank bailouts. By October 2001, the RCC had paid an average of 3.8 percent of the original book value for the assets it purchased (JT 2001a). In certain cases, the RCC would pay ¥1 "when purchasing virtually valueless collateral taken on soured loans" which discouraged banks from asking the RCC to buy their NPLs (JT 2001a). Given the discount that the RCC was paying to purchase loans, concerns were raised that banks were not incentivized to sell their NPLs to the RCC. Thus, on January 11, 2002, an amendment to the Financial Revitalization Act was enacted which enabled the RCC to purchase NPLs from "sound financial institutions at market value" (DICJ 2002). Some critics advocated that the RCC be able to purchase NPLs at book value, but this was ultimately unsuccessful, as the RCC sought to avoid recognizing losses that would ultimately be imposed on taxpayers (JT 2002b).

Recovery and Disposal

When the RCC was established, some worried that it would compete with private firms in the debt collection business and crowd them out of the market. However, the president of the RCC stated that the organization would "try to avoid this scenario by specializing in the recovery of loans that 'nobody wants to take,'" such as those connected to organized crime or deemed more difficult to recover (JT 1999a). Because of the DICJ's special investigative powers, the RCC was considered to have an edge over the private sector in cases where the loans were considered difficult to recover (Otake 1999b).

During the first years of operations, the RCC had limited disposal options, as its objective was to "solely recover all of its loans, mainly through repayment or collateral selloff" (Otake 1999a). In 2001, the government actively pursued the expansion of the RCC's scope to accelerate the disposal and resolution of NPLs. The RCC received its trust services license in September 2001, which provided "supplementary measures to dispose of NPLs, which private financial institutions cannot handle" (FSA 2001). The license allowed the RCC to be "entrusted with a portion of the banks' nonperforming loan assets and use them to securitize loans and sell them to investors" (JT 2001b). The Minister of Finance stated that the "approach is expected to expedite an intensive reduction of NPLs still remaining on banks' balance sheets" (FSA 2001). In addition, the RCC adopted bulk sales as a disposal method in 2002 (DICJ 2008, p19).

Political and economic pressure to address the NPL problem escalated as its scope was recognized. The Prime Minister, Junichiro Koizumi, convened a panel to prepare a reform program aimed at fixing the NPL problem. In a speech to the Diet on September 27, 2001, the Prime Minister announced that "in order to expand the functions of the Resolution and

Collection Corporation (RCC), we will introduce more flexibility into the pricing system for nonperforming loan purchase and promote the establishment of a fund for further corporate reconstruction” (Koizumi). The Cabinet called for the RCC to establish a headquarters for corporate restructuring in 2001 “in order to facilitate the rehabilitation of failed companies” (Cabinet 2001b). Thus, the RCC’s activities expanded to include corporate restructuring and rehabilitation, which included debt restructuring and rehabilitation planning, as another method to dispose of and manage NPLs. Legal revitalization cases were those where the RCC would utilize legal proceedings to enforce civil rehabilitation and corporate reorganization. With the consent of financial creditors, the RCC could work “to maintain the livelihood of debtors and rebuild/sustain their business by modifying loan terms” (RCC, p 4). The RCC also used “its trust business functions to support the revitalization of business operators when revitalization cases [were] brought to the RCC by other financial institutions” (RCC, p11).

The minister of the FSA, Heizo Takenaka, also emphasized the importance of resolving the NPL problem. In October 2002, he announced the three-pillared Program for Financial Revival and announced the work schedule in November 2002 (FSA 2002c). One pillar, the “New Framework for Corporate Revival”, promoted the use of the RCC to dispose of NPLs and encouraged the RCC to engage in corporate restructuring. The Program for Financial Revival reiterated the government’s goal to “normalize the NPLs problem in FY 2004 by reducing major banks’ NPL ratio to about half” (FSA 2002b). The Program for Financial Revival further encouraged the RCC to develop a market for loans by accelerating loan sales and strengthening its securitization function (FSA 2002b).

Outcomes

By March 31, 2005, the RCC purchased a total of ¥4,004 billion (book value) of NPLs from 192 solvent financial institutions at a purchase price of ¥353 billion, an approximate 91 percent discount on the book value (DICJ 2005). As of March 2008, the RCC collected a cumulative ¥642 billion on the recovery of these loans (DICJ 2008, p72).

Table 1: Cumulative Total of Assets Purchased from Sound Financial Institutions (as of March 31, 2005)

Institution Type	Number of financial institutions	Principal of claims (¥ billion)	Purchase price (¥ billion)
City banks, long-term credit banks and trust banks	20	2,831.6	287.3
Regional banks	59	572.8	40.4
Regional Banks II	41	434.0	13.7
Shinkin banks and credit cooperatives	72	165.7	11.9
Total	192	4,004.1	353.3

Source: DICJ 2005

For the purchase of assets from failed financial institutions, the RCC acquired a total of ¥6,366 billion (purchase price) of NPLs and recovered ¥7,143 billion as of March 31, 2008

(DICJ 2008, p72). The estimated book value of the NPLs purchased from insolvent institutions is ¥29,000 billion.⁸ Of the ¥6,366 billion in purchases from failed institutions, the RCC purchased ¥4,576 billion from banks, ¥550 billion from Shinkin banks (regional cooperative institutions), and ¥1,241 billion from credit cooperatives (DICJ 2008, p73).

Table 2: Purchase of Assets from Failed Financial Institutions as of March 31, 2008

Category	Amount of purchase (¥ billion)	Cumulative amount of recoveries (¥ billion)
Purchase of assets from failed financial institutions	5,186.5	5,496.4
Purchase of assets from banks placed under special public management (the former Long-Term Credit Bank of Japan and the former Nippon Credit Bank)	1,179.8	1,646.4
Total	6,366.3	7,142.8

Source: DICJ 2008

During the first asset purchase window for solvent banks, the RCC received applications from 39 financial institutions for a total asset purchase of ¥220 billion (Otake 1999b). The DICJ reported that the RCC purchased assets from solvent financial institutions on September 29, 1999 (DICJ AR 2002, pxv). After the first window closed, the president of the RCC announced that he hoped the RCC would eventually buy ¥10 trillion worth of loans and that he was confident more offers would come in the next window (Otake 1999b).

According to the IMF, the RCC had “a minor role in reducing bank NPLs” between its establishment in 1999 and 2002 (IMF 2002, p22). However, with the government’s emphasis on utilizing the RCC as a tool to dispose of NPLs, the RCC began to more aggressively purchase assets. In addition, a 2002 amendment enabled the RCC to purchase NPLs from solvent institutions at market value, making it more attractive for the institutions to sell to the RCC (DICJ 2002). The Minister for Financial Services in 2002 remarked that “as for [the] selling off of loan assets to the RCC, the sales prices have considerably increased to the fair value. The amount of sales has also begun to demonstrate a sign of increase” (FSA 2002a).

In 2001 and 2002, the methods available to the RCC for the disposal and collection of NPLs expanded. The RCC obtained a trust license to securitize NPLs and began to engage in corporate revitalization in 2001. Bulk sales were adopted as a disposal method in 2002 (DICJ 2008, p19). Soon after receiving its trust license, the RCC issued ¥107.4 billion in securities (Kang, p67). According to the DICJ, the liquidation of receivables (book value) by the RCC

⁸ It does not appear that the DICJ has disclosed the total book value of assets purchased from failed institutions. Koo and Sasaki (2010) estimate that the average discount was 78 percent of book value for purchases from failed institutions. Koo and Sasaki use ¥4,885 billion as the total purchase price and estimate that the total book value of acquired assets from failed institutions was ¥22,427 billion. Koo and Sasaki recognize that ¥4,885 billion differs substantially from the ¥6,366 billion reported by the DICJ. In order to arrive at the ¥29,000 billion estimate, we use the estimated discount of 78 percent on the total purchase of ¥6,366 billion. Therefore, the estimated book value for assets purchased by the RCC from failed institutions is ¥29,000 billion.

totalled ¥8,403 billion by the end of March 2008 (DICJ 2008, p19). The RCC disposed of ¥1,562 billion of assets through individual sales, ¥617 billion through securitization, and ¥6,224 billion through bulk sales between 1999 and 2007. The securitization function was utilized between 2001 and 2005, and the bulk sales method was adopted in 2002 and became the primary tool for asset disposal (DICJ 2008, p19).

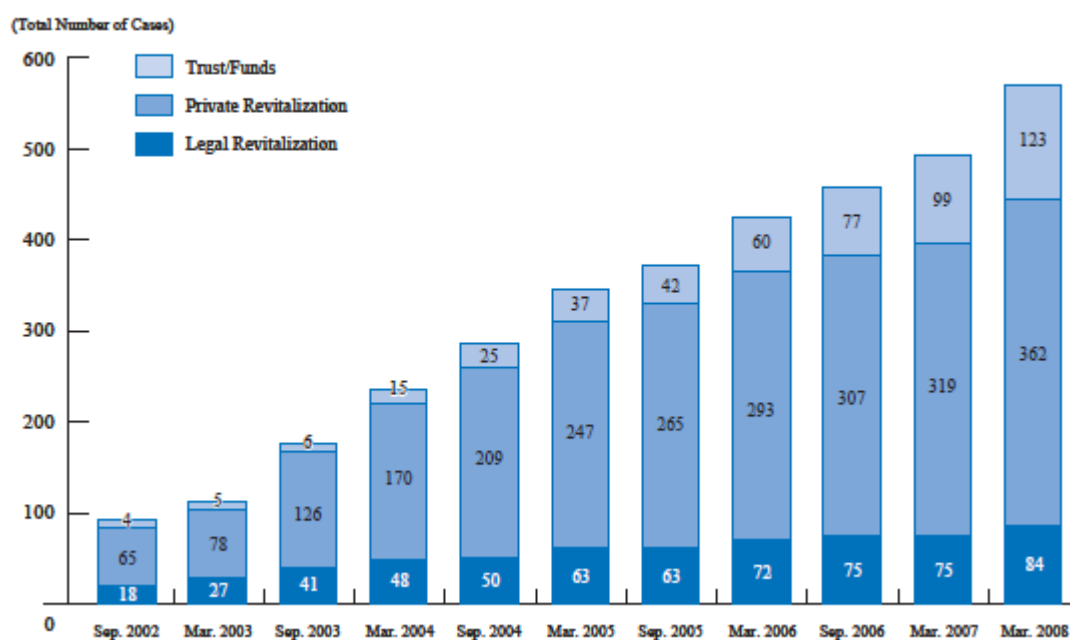
Table 3: Liquidation of Receivables (original book value of claims) by the RCC (in ¥ billion)

Fiscal Year	1999-2000	2001	2002	2003	2004	2005	2006	2007	Total
Individual Sales	95.5	133.9	220.4	359.2	327.4	167.6	122.8	135.5	1,562.3
Securitization	-	32.3	109.6	341.2	56.4	77.4			616.7
Bulk Sales	-	-	263.8	361.8	1,322.7	2,445.1	769.6	1,060.9	6,223.9
Total	95.5	166.2	593.8	1,062.2	1,706.4	2,690.1	892.4	1,196.4	8,403

Source: DICJ 2008

The RCC utilized its corporate restructuring function to reorganize borrowers behind nonperforming loans. Between November 2001 and March 31, 2008, the RCC was involved in 569 cases of corporate revitalization, which included cases of legal revitalization, private revitalization, and privately funded revitalization (DICJ 2008, p77).

Figure 2: Accumulated total number of cases of corporate revitalization by the RCC between 2002 and 2008



Source: [DICJ 2008](#)

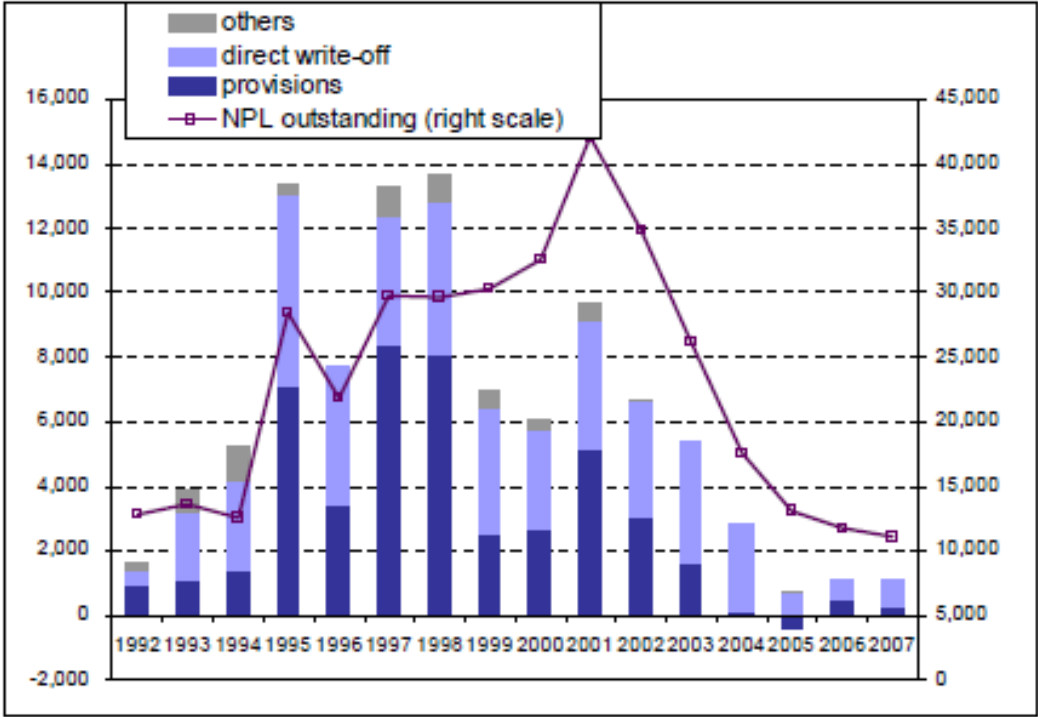
Note: Trust/funds refers to privately funded revitalization

By 2012, the RCC had completed the closure of *jusen* accounts ([RCC](#), p1). The residual assets of the *Jusen* Account, worth ¥11.9 billion, were transferred to the national treasury ([DICJ 2013](#), p35).

In addition, the RCC investigated complaints related to borrowers and lenders. From 1996 to 2008, the RCC investigated 311 cases surrounding auction interference, fraud, extortion, and other misbehaviors. The RCC pursued 124 cases of civil liability by March 31, 2008, for a total amount claimed of ¥125.3 billion ([DICJ 2008](#), p91).

During the first years of the RCC's operations, the full scope of the NPL problem was not fully understood, and the NPL problem accelerated. In 2001, the Cabinet Office stated that the NPL stock continued to increase for two reasons: the NPL definition had been gradually expanded, and the pace at which banks disposed of loans was slower than the pace at which they provisioned new NPLs ([Cabinet 2001a](#)). Because "[t]he government required the banks that received public capital to increase lending" to businesses exposed to the real estate industry, "a new set of nonperforming loans" was created (Hoshi 2010, p402). The ratio of NPLs to total credit exposure at the major banks peaked in 2001 at 8.7 percent. The peak ratio for regional banks was 8.1 percent in 2001 ([BOJ 2006](#), p4). The FSA began to conduct inspections of banks and reported the gap between the banks' disclosures and its own assessment; in the first assessment which evaluated 2000-2001, the FSA found that the gap between the amounts reported by 15 major banks and the FSA's inspection was ¥12.4 trillion ([FSA 2003](#)).

Figure 3: Outstanding NPLs and Losses on Disposal of NPLs (in ¥ billion)



Note: Data are for the end of fiscal year. NPLs are “risk management loans” of all banks, whose definition is slightly different from NPLs based on the Financial Revitalization Law. The numbers referred to in the text are based on the Financial Revitalization Law, which became available from March 1999.

Source: Fujii p4

There were additional policy measures enacted to address the NPL ratio in Japan, such as the continued strengthening of classification and provisioning standards. Capital injections were another key component of the government’s response (Hoshi 2010, p409). In addition, economic recovery is correlated with NPL ratios; as economic conditions improve, firms are more likely to be able to repay debt (Fujii, 3). The BOJ reported in 2006 that “the ratio of NPLs to total credit exposure of the major banks (12 large nationwide commercial and trust banks) declined significantly to 2.9 percent at the end of fiscal 2004, after they achieved the target set by the government of halving the ratio as of the end of fiscal 2001 within three years. It continued to decline to 1.8 percent at the end of fiscal 2005” (BOJ 2006, p4). The BOJ reported that the progress made by the regional banks was not as fast as that made by the major banks. In the 2006 report, the BOJ stated, “The ratio of NPLs at the regional banks (111 local commercial banks) declined to 4.6 percent at the end of fiscal 2005 from 8.1 percent at the end of fiscal 2001” (BOJ 2006, p4). The BOJ attributes the slower decline in the ratio of NPLs at regional banks to the “moderate pace of recovery of the local economies in which the regional banks operate, compared with the recovery of the metropolitan areas” (BOJ 2006, p5). Additionally, the disposal approach taken by regional banks may have been stifled by the “fact that the regional banks tend[ed] to put more focus on maintaining long-term business relationships with borrower firms” (BOJ 2006, p5).

Establishment of the IRCJ

Though the scope of the RCC was expanded in 2002 to include corporate revitalization and restructuring, the Japanese government created another body, the Industrial Revitalization Corporation of Japan (IRCJ), in April 2003, in accordance with the Industrial Revitalization Corporation Law, as subsidiary of the DICJ (DICJ 2008, p69). The IRCJ was established on “the premise that [it would] complement the RCC” (Takagi, p8). According to Shinjiro Takagi, the chairman of the IRCJ, the amendment that expanded the RCC’s scope to include corporate restructuring “[was not] sufficient, which explain[ed] the need for the IRCJ” (Takagi, p8). He framed the two bodies as working in parallel and not in conflict: “the IRCJ and RCC should work together to clean up debt-ridden companies and efficiently rehabilitate as many companies as possible” (Takagi, p8). The IRCJ was established to purchase NPLs from non-main bank lenders; the IRCJ would then use its status as a creditor to work with the borrower’s main bank to restructure debt or assist with corporate revitalization (Hoshi 2010, p404).

The IRCJ was financed by government-guaranteed loans and funded with ¥10 trillion in purchasing power and ¥50 billion in capital (Pohl, p51). It was “incorporated as a joint stock company, [which allowed] the government’s involvement in setting criteria for financial support” (Takagi, p2). The asset purchase window for IRCJ ended on March 31, 2005, and the IRCJ was given guidance to dispose of or manage assets within three years of the purchase date (Takagi, p3). Furthermore, the IRCJ was to “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 lifespan” (Takagi, p3). The IRCJ could purchase loans at market value, while taking the feasibility of the rehabilitation plan into account (IMF 2003, p23). When the IRCJ was established, there was no guidance for how to treat losses (Pohl, p52). Over its lifespan, the IRCJ spent ¥530 billion to purchase ¥970 billion of debt; at the time of its closure in May 2007 (a year earlier than planned), the IRCJ had restructured 41 borrowers with ¥4 trillion in total debt (Hoshi 2010, p405-406). The borrowers came from “a wide range of business sectors,” and the IRCJ “played a role in bridging the gap between private and legal corporate reorganization under a scheme combined with civil rehabilitation procedures to minimize impairment of business value” (DICJ 2008, p69).

II. Key Design Decisions

- 1. At the time of the establishment of the RCC, the Japanese government announced a series of reforms and packages to resolve the escalating financial crisis.**

Over the course of 1998, the Japanese government passed several laws to address the systemic financial crisis. The Financial Function Stabilization Act was passed in February 1998 which made ¥30 trillion available to the government for capital injections and deposit protection (Hoshi 2010, p401). In October 1998, the Diet, the Japanese legislative body, passed the Financial Revitalization Act and replaced the Financial Function Stabilization Act with the Prompt Recapitalization Act (DICJ 2008, p22). The Prompt Recapitalization Act

“stipulate[d] a temporary emergency measure regarding capital injection to financial institutions” (DICJ 1998, p13). The Financial Revitalization Committee (FRC) was also established in 1998 to oversee the bank restructuring process (Kanaya, p32). The government approved two rounds of capital injection: the first, under the Financial Function Stabilization Act, in March 1998 (¥1.8 trillion) and the second, under the Prompt Recapitalization Act, in March 1999 (¥7.5 trillion) (Hoshi 2010, p401-409). The RCC could purchase preferred shares and subordinated debt from financial institutions as a part of the Prompt Recapitalization Act, though the capital injections were overseen by the Financial Revitalization Committee.⁹ The Financial Revitalization Act included the principles for the resolution of failed financial institutions (DICJ 1998, p12). As a part of the Financial Revitalization Act, the HLAC and the RCB were merged to create the RCC, which began operations on April 1, 1999 (Kanaya, p32). Concurrently, the government was in the process of nationalizing the Long-Term Credit Bank and the Nippon Credit Bank (Hoshi 2010, p401).

2. The government expanded the scope of the RCC to include corporate debt restructuring and corporate revitalization in 2001. The government ultimately established a separate asset management company, the IRCJ, with a similar function in 2003.

The scope of the RCC was expanded in 2001 to include corporate debt restructuring and revitalization. Prime Minister Koizumi, in a policy speech to the Diet in 2001, stated that the function of the RCC would be expanded and that a fund for further corporate revitalization would be established (Koizumi). The Front-Loaded Reform Program included a measure to reinforce the disposal of NPLs and stated that the RCC would “establish a headquarters for corporate restructuring in order to facilitate rehabilitation of companies” in November 2001 (Cabinet 2001b). In 2003, the government established another asset management company, the Industrial Revitalization Corporation of Japan (IRCJ), which was established to work with the RCC to address the NPL problem in Japan (Takagi, p8). The IRCJ was given the purpose of restructuring the bad loans it purchased and assisting with the corporate revitalization of borrowers (Takagi, p3). The IRCJ had a purchase window of two years and focused on purchasing bad debt from distressed debtor companies that were viable and likely to be successfully rehabilitated (Takagi, p2).

3. The RCC was established via a merger of two semi-private asset management companies. As a fully owned subsidiary of the Deposit Insurance Corporation, it received its authority in amendments to the Deposit Insurance Act and the Financial Revitalization Act.

The RCC was a fully owned subsidiary of the Deposit Insurance Corporation of Japan (DICJ) (DICJ 2008, p40). The function to manage, collect, and dispose of assets from bankrupt institutions was designated to the DICJ in the Deposit Insurance Act; the DICJ was also designated the authority to take action on specified difficult collection claims, including claims tied to organized crime (DICJ 2008, p48-49; Otake 1999b). The Deposit Insurance Act was amended in 1996 to allow the DICJ to purchase assets from failed institutions as a

⁹ For more information on the 1998 and 1999 capital injections, see the Prompt Recapitalization Act and the Financial Function Stabilization Act cases by Vaasavi Unnava (2019)

method to provide funds to failed financial institutions (Koo, p9). The Financial Revitalization Act was enacted in 1998 and established the RCC, from the merger of the RCB and the HLAC, as a subsidiary of the DICJ (DICJ 2008, p68). Before the RCC began operations, the scope of its authority was expanded to include the purchase, management, collection, and disposal of assets from sound financial institutions, which was delegated in the Financial Revitalization Act (Koo, p9). The DICJ designated debt recovery and real estate management and disposal work to the RCC, which performs these activities “on behalf of the DICJ” (2002 AR, pvi).

Additional legal authority was delegated to the RCC in a variety of measures in the years after its establishment. In 2001, Prime Minister Junichiro Koizumi, established a set of structural reform policies, which included corporate restructuring (Koizumi), and the “Front-Loaded Reform Program” of 2001 stated that the RCC was to establish a corporate revitalization headquarters (Cabinet 2001b). The ability to purchase assets from solvent institutions at market value was delegated in an amendment to the Financial Revitalization Act in 2002 (DICJ 2008, p18). Additionally, the RCC was granted a trust services license to engage in securitization and was given the authority to participate in auctions. The Program for Financial Revival, established by the Financial Services Agency (FSA) and introduced in 2002, further reiterated that the scope of the RCC included corporate restructuring (FSA 2002b). Furthermore, amendments to the Financial Revitalization Act in 2001 and 2003 ultimately prolonged the window for asset purchases from solvent institutions to March 31, 2005 (DICJ 2008, p51).

Table 4. Timeline of Changes to Legal Authority of the RCC

Year	Legal Authority Granted or Extended
1996	<ul style="list-style-type: none"> Revision to the Deposit Insurance Act designating authority to the DICJ to purchase assets from failed institutions (DICJ 2008)
1998	<ul style="list-style-type: none"> Financial Revitalization Act includes merger of the HLAC and the RCB into RCC Authority granted to investigate difficult claims (DICJ 2008)
1999	<ul style="list-style-type: none"> RCC begins operations and able to purchase assets from solvent institutions) (DICJ 2008)
2001	<ul style="list-style-type: none"> Front-Loaded Reform Program and amendment to Financial Revitalization Act designate corporate restructuring function to RCC (Cabinet 2001b) Extension of deadline for purchase from solvent institutions to March 31, 2004 (DICJ 2008) RCC granted trust services license (DICJ 2008)
2002	<ul style="list-style-type: none"> Amendment to Financial Revitalization Law allows RCC to purchase assets at market price (DICJ 2008)
2003	<ul style="list-style-type: none"> Extension of deadline for purchase from solvent institutions to March 31, 2005 (DICJ 2008)

4. The Japanese government framed the RCC as a strong lever to resolve the NPL problem, though there was public uncertainty and speculation.

With the establishment of the RCC, the government projected confidence in its ability to resolve the NPL problem. The president of the RCC was frequently quoted in press releases and articles in the Japan Times. He was seen as a strong leader of the organization (Otake 1999b). When he began to lead the RCC, he stated, “This new job is an urgent and important task since the banks’ blood vessels are clogged with bad loans” (JT 1999a). Upon its establishment, the RCC was deemed to “[signal] the birth of a powerful state-backed organ to collect bad loans” (Otake 1999a). During the first purchase window for solvent financial institutions, the president of the RCC recognized that the total was less than anticipated but was confident that future windows would be more fruitful (Otake 1999b).

However, there was a “divergence between the government’s characterization of the condition of the banking industry and that of outsiders” (Hoshi 2010, p401). There were conflicting messages regarding the scope of the NPL problem in Japan, with private estimates, bank estimates, and official estimates varying in the estimated scale of the problem; in fact, the “official estimates of bad loans were regarded as a ‘lower bound’” of the scope of the NPL problem (Tandon, p18). In a further example of the lack of consensus, IMF directors and government officials were not aligned on the urgency of the crisis. IMF analysts urged the government to take decisive and aggressive action given the scale of the crisis (JT 1999d). However, the statements released by the government contradicted the IMF – in February 1999, a MOF official stated that the financial crisis would be over within a matter of weeks (Hoshi 2010, p401).

In addition, there was public uncertainty and distrust of the government’s reforms and interventions, following the use of taxpayer funding of ¥685 billion for the *jusen* problem in 1996. This assistance was viewed unfavorably by the public, as it reflected the government reneging on its promise not to rely on taxpayer funds to resolve the crisis. After this experience, it became politically unpopular to advocate for programs that would utilize taxpayer funds for bank assistance (Nakaso, p6).

When the government began to expand the scope of the RCC to include corporate restructuring, a trust services license, and the ability to purchase NPLs at market value from solvent financial institutions, the government was presenting a message of confidence in the abilities of the RCC to work towards the objective of resolving the NPL crisis (FSA 2001). There was public speculation surrounding the RCC’s added functionalities, including hope that the RCC would “have the teeth to promote disposal of the banks’ huge bad loans, following in the footsteps of the Resolution Trust Corp” (Kishima).

Furthermore, the government began to more aggressively combat the NPL problem in the early 2000s, with leaders making public statements about the need to address the crisis. Prime Minister Junichiro Koizumi actively spoke about the need to resolve the NPL problem, specifically stating that the RCC would be an important lever to do so (Koizumi). Another key figure in addressing the NPL problem was the FSA minister, Heizo Takenaka, who developed the Program for Financial Revival, which set the goal to resolve the NPL problem by FY 2004

(FSA 2002b). Both Koizumi and Takenaka supported the proactive utilization of the RCC to mitigate the NPL crisis.

5. The DICJ provided governance and oversight of the operations of the RCC, as the RCC was a subsidiary of the DICJ.

The former president of the HLAC, Kohei Nakabo, became the president of the RCC (Otake 1999a). The RCC was staffed by the previous HLAC and RCB employees (Otake 1999a). When the RCC was established in April 1999, it had approximately 1,900 employees (Nakaso, p56). According to an analysis on asset management companies published by the Bank for International Settlements, the RCC had “limited” independence in the legal environment and was not granted special legal protection for staff (Fung, p58).

The DICJ oversaw and provided guidance to the RCC, and the FSA and BOJ provided external governance and oversight (Fung, p56). The DICJ provided the RCC “with the guidance and advice necessary to execute its recovery activities; such as uncovering hidden assets by exercising the right to inspect properties” (DICJ 2004 pvii). The IMF recognized that the FSA, BOJ, DICJ, and RCC all demonstrated “a high degree of transparency” in their operations (IMF 2003, p64). The activities of the RCC were reported by the DICJ, though it does not appear to have published the names of the solvent financial institutions from which it purchased NPLs. The DICJ explicitly published the names of the failed firms receiving financial assistance in press releases and public statements. The releases portrayed the financial assistance scheme, the book value of the assets transferred to the RCC, and the purchase price for the assets.¹⁰

6. The RCC had neither a specified size nor constraints on the amount of NPLs it could purchase.

There were no restrictions placed on the RCC regarding the total sum of NPLs it could purchase (Fung, p60).

7. The RCC was fully publicly funded. The RCC purchased NPLs at a steep discount, making it unlikely that it would recognize losses.

The government of Japan provided all of the funding for the RCC. The DICJ issued government-guaranteed bonds and injected the proceeds into the RCC (Kang, p66). At the time of its initial operations, the RCC had ¥212 billion in capital (Kang, p66). The RCC did not have recourse to the originator banks for the losses incurred when it sold collateral associated with a loan (Hoshi 2004, p21), and there was strong public sentiment to avoid incurring losses (Nakaso, p6). Thus, the RCC purchased assets at a steep discount from book value, on average a 78 percent discount from failed institutions and a 91 percent discount from healthy institutions, making it unlikely that the RCC would recognize losses on the sale or collection of assets (Koo, p9).

¹⁰ See the [DICJ website](#) for examples of the financial assistance schemes for failed institutions

8. The RCC was able to purchase assets from both solvent and insolvent banks and certain non-bank financial institutions.

According to Article 53 of the Financial Revitalization Act, the eligible institutions included: managed financial institutions, agreement successor banks, and special public management banks (Law 132). The definition of ‘financial institution’, as defined in the Deposit Insurance Act, included major, regional and city banks as well as credit unions and credit cooperatives (DIA). Other eligible financial institutions included bridge banks, the Federation of Agricultural Cooperative Associations, and the Federation of Fisheries Cooperative Associations (DICJ 1998, p40). Special public management banks refer to banks such as the Long-Term Credit Bank and Nippon Credit Bank, which were temporarily nationalized banks (Law 132).

9. The RCC could purchase nonperforming and performing loans from eligible institutions.

The types of assets that the RCC could purchase from solvent institutions included loans, suspense payments, interest receivables and accounts receivables for borrowers classified as “bankrupt, de facto bankrupt or in danger of bankruptcy” (DICJ 2002 Purchase Price). Loans that were ineligible included small loans (less than 10 million), loans to public welfare corporations, loans with disputed claims, loans to borrowers undergoing reorganization, loans to non-residents, and loans for overseas real estate (DICJ 1998, p40). For the transfer of assets in the case of a failed institution, the assets eligible for purchase were the assets considered unsuitable for the bridge bank or banks under special management to hold (DICJ 1998, p74-75). The NPL problem was concentrated in real estate, construction, and wholesale and retail trading (Cabinet 2001a). There was no loan size restriction. The DICJ was delegated special investigative powers through the *Jusen* Act, the Deposit Insurance Act, and the Financial Revitalization Act. These special investigative powers supported the RCC’s collection of NPLs, especially uncollateralized loans (DICJ 2001, p5).

10. The RCC acquired NPLs from insolvent financial institutions under the scope of the DICJ’s financial assistance operations.

The RCC was engaged as needed for insolvent financial institutions, as the DICJ was involved in overseeing the financial assistance process. In the case of a failed financial institution, the DICJ, FSA and courts were involved in overseeing and managing the resolution process (DICJ 2008, p54-55). The FSA appointed a financial administrator; if no assuming institution was found, the FSA found a bridge bank (DICJ 2008, p54-55). The failed institution and assuming institution(s) submitted an application to the DICJ for assistance, and the DICJ determined whether to provide assistance. The financial assistance could take “the form of a monetary grant, loan or deposit of funds, purchase of assets, guarantee of liabilities, assumption of financial obligations, subscription of preferred shares, etc. or loss sharing” (DICJ 2008, p44). If there was an assuming financial institution, the assets that the assuming bank did not want were transferred to the RCC. The purchase of assets would be agreed upon by the failed institution, the assuming financial institution(s) or bridge bank, the RCC, the DICJ, and the

FSA (DICJ 2008, p44). The purchase price and book value of assets transferred were disclosed in press releases from the DICJ.¹¹

11. The RCC could purchase NPLs from solvent financial institutions, after the interested banks submitted an application during the purchase window.

For the purchase of assets from solvent financial institutions, the RCC announced the first application window when it began its operations; the application window was from June 22 to July 9, 1999. (JT 1999c). The application window for solvent institutions “as a rule [took] place four times a year,” but the RCC was also able to consult with individual financial institutions on the purchase timeframe if requested (DICJ 2002). After receiving applications, the RCC would evaluate the applications from interested banks and offer a price to the banks; the DICJ provided guidance on the offer price (JT 1999c). If interested, the banks would then submit a formal application to initiate the process and would work with the RCC to coordinate the purchase (JT 1999c). The deadline for purchase was initially set to expire in 2001 but was ultimately extended to March 31, 2005 (DICJ 2008).

12. The RCC had special investigative authority for cases considered difficult to recover, specifically those related to organized crime.

The DICJ supported the RCC in the collection and recovery of assets from “malicious debtors and others” including “obstructed recovery cases involving antisocial forces” (DICJ 2008, p4). Some consider the “antisocial forces”, also called the yakuza, to be a key factor contributing to the size of NPL problem as well as the slow recovery and disposal of NPLs in Japan (LA Times). Estimates for the number of loans related to the yakuza varied significantly, with one estimate at 80% (LA Times) and others at 10% or 30% (Washington Post). Banks and financial institutions made loans to yakuza borrowers, some of which became nonperforming after the collapse of the real estate asset price bubble. In some cases, the yakuza prevented banks from foreclosing on property and prevented auctions, as the yakuza squatted in empty units and buildings (Washington Post). By 2002, 18% of the loans the RCC had purchased were yakuza-related (Bloomberg). The National Police Agency backed the RCC to aid with the seizure of property, and the DICJ established Special Investigation Divisions to enhance the recovery of assets (DICJ 2008, p26). The DICJ “reinforced support for the fair handling of collections in obstructed recovery cases by providing meticulous guidance and advice to the RCC concerning the monitoring and analysis of behaviors of debts in the process of subsequent negotiation on recovery” (DICJ 2008, p28).

13. The RCC’s methodology to determine purchase price was not transparent in the first years of operations; an amendment in 2002 enabled the RCC to purchase assets at market value.

The RCC determined the purchase price for NPLs on a case-by-case basis with guidance from the DICJ and the Purchase Price Examination Board (an advisory body) (Nanto, p10). The Purchase Price Examination Board is an advisory body of the DICJ governor (DICJ 2008, p25).

¹¹ See the [DICJ website](#) for examples of the financial assistance schemes for failed institutions

The Purchase Price Examination Board originally had three members, but it was expanded in 2002 to have five members (DICJ 2002). The RCC did not have recourse to the financial institutions selling the loans; thus, the RCC established a process to ensure the price “reflected fair value” (Packer 2000, p154). The determination of the purchase price was to “[take] into consideration the risk of assets becoming uncollectable and the administrative expenses required for purchase and collection of the assets in question” (DICJ 1998, p40). The RCC established a multi-stage process for pricing the NPLs in which a real estate appraiser submitted a valuation of the property, and the RCC, FRC, and DICJ reviewed and approved the valuation (Packer 2000, p154). In addition, the RCC sought guidance from the MOF and FSA in determining purchase price (JT 1999b). The purchase price also required approval from the Prime Minister, though the Financial Reconstruction Commission granted approval until January 2001 (DICJ 2008, p25). In the first years of operations, the RCC purchased loans at a steep discount, paying an average of 3.8 percent of the original book value (JT 2001a).

The steep discount the RCC paid for loans was considered to be a deterrent to healthy banks interested in selling their NPLs. In a Cabinet Report in 2001, the government recognized that the NPL problem was worsening and stated that “[t]he government will also make the price-setting formula more flexible in order to facilitate purchases of nonperforming loans by the Deposit Insurance Corporation of Japan and the RCC” (Cabinet 2001a). Given the increasing pressure to resolve the NPL problem, the government passed an amendment to the Financial Revitalization Act, effective January 2002, which allowed the RCC to purchase NPLs from “sound financial institutions at ‘market value’” (DICJ 2002). However, some critics believed that this was not enough and advocated that the RCC should purchase loans at book value (JT 2002a, JT 2002c). A cross-party coalition was established to study the proposal, and after analysis, the RCC president announced that he did not support the plan, as the RCC sought to avoid recognizing losses that would be ultimately be transferred to taxpayers (JT 2002b). As another measure to promote flexibility in purchase price, the RCC was given the ability to bid in NPL auctions in 2001 (IMF 2002, p22). Between 1999 and 2005, the RCC’s purchase price of NPLs from solvent institutions was an average of 9 percent of book value (DICJ 2005). According to an estimate, the RCC purchased assets from insolvent institutions at an average of 22 percent of book value (Koo, p9).

14. The RCC initially disposed of loans through sales and collections of NPLs. The tools available to the RCC for asset recovery and disposal were diversified in 2001 and 2002.

The RCC could ultimately utilize the following methods for disposal of NPLs: collection, sales, securitization, and/or operational and financial restructuring (IMF 2002, p20). In its first years of operations, the RCC was limited in disposal methods, and the RCC was slow to dispose of assets (IMF 2002, p22). The RCC received its trust license to securitize nonperforming assets in 2001, after which it began issuing asset-backed securities (Kang, p67). The Program for Financial Revival called for the RCC to accelerate the sales and collections of loans, which led the RCC announce their “Basic Policy concerning the Liquidation and Securitization of Assets held by the RCC”, under which the RCC would “more actively” consider sales and securitization when the methods were economically rational

and advantageous (DICJ 2008, p18). “The RCC adopted a method to sell multiple claims in bulk (bulk sales) through bidding at the end of FY2002” (DICJ 2008, p19). Due to the expanded disposal options, the RCC was more aggressive in its disposal of NPLs between 2001 and 2008; its total balance of debt decreased from ¥5.8 trillion to ¥1.1 trillion (Hoshi 2010, p406).

15. The RCC was entrusted with a corporate revitalization and restructuring function in 2001.

The corporate restructuring function was delegated to the RCC in 2001 through an amendment to the Financial Revitalization Act and the Cabinet Office’s Front-Loaded Reform Program. The Front-Loaded Reform Program called for the RCC to establish a headquarters for financial revival (Cabinet 2001b). The RCC began operations related to corporate restructuring in November 2001 (DICJ 2008, p18). The RCC established the “Corporate Revitalization Study Committee” as an advisory body with the purpose of evaluating the feasibility of each revitalization case (DICJ 2008, p18). The corporate restructuring function was strongly encouraged in the FSA’s Program for Financial Revival in 2002 as well (FSA 2002b). Corporate revitalization could take multiple forms: the RCC was involved in legal revitalization in which it utilized legal proceedings to enforce rehabilitation, and it was involved in cases of private revitalization which involved debt or business restructuring with the consent of other creditors (DICJ 2008, p77). The RCC used its trust license to support the revitalization of firms for which a revitalization case was submitted to the RCC by a different financial institution (RCC, p11). The RCC evaluated cases based on the following criteria: the continuation value of the business, the willingness of the firm to make repayments, disclosure transparency, and the economic rationality for the creditor (RCC, p11). Between November 2001 and March 31, 2008, the RCC assisted with 569 cases of revitalization (DICJ 2008, p18). Overall, the RCC assisted with the restructuring of ¥6.2 trillion in debt (Hoshi 2010, p405-406).

16. The RCC did not have a sunset date for purchases from failed institutions. The deadline to purchase from solvent institutions was initially March 31, 2001, but it was ultimately revised to March 31, 2005.

There was no official sunset date for the RCC, as the RCC continues to operate (with new capabilities and authority) to the present date (Fung, p16, RCC). The deadline for the purchase of NPLs from solvent institutions was initially set for March 31, 2001 and was later extended to March 31, 2005 (DICJ 2008, p51).

III. Evaluation

A significant factor of the environment in which the RCC operated is the definition of nonperforming loans in Japan was initially inadequate and provisioning standards were lax; the authorities gradually revised the framework, but the “lack of adequate provisioning and public disclosure obscured the actual status of the NPLs problem in the financial system and delayed the introduction of much needed comprehensive action” (Nakaso, p18).

In post-crisis analysis, some scholars have argued that the purchase price for NPLs from the solvent banks was too low, which disincentivized these banks from selling to the RCC. Proponents of this argument state that the usage of the RCC was limited as it “[offered] unattractive pricing to banks for the acquisition of NPLs ... owing to political reluctance to recognize financial loss” (Fung, p22). The move to allow the RCC to purchase NPLs at market value was seen as a step in the right direction to accelerate the disposal of bad loans. Takeo Hoshi and Anil Kashyap argue that the RCC case illustrates that asset purchase programs are not sufficient to address bank solvency problems (Hoshi 2010, p412). According to an estimate from Richard Koo and Masaya Sasaki, the RCC was able to buy bad assets at a 78 percent discount to book value from failed institutions and a 91 percent discount to book value from healthy institutions (Koo, p9). In addition, their analysis shows that the “total value of assets purchased by the [RCC from solvent institutions] was an order of magnitude lower than that of assets purchased from failed institutions” which is “a reminder of how difficult it is to remove assets on which large losses must be booked from the balance sheets of healthy institutions” (Koo, p9).

Others have argued that the RCC was not aggressive enough in its purchase and disposal of NPLs and that the RCC should have set performance and time-bound targets for disposal of assets (Kang, p76). Hoshi and Kashyap argue that the RCC was slow in selling off the loans it purchased and essentially operated as a warehouse for bad loans in the initial years of operations (Hoshi 2010, p413). By 2002, the RCC had “played only a minor role in reducing bank NPLs, having so far purchased only ¥1.3 trillion in distressed assets (face value) at an average discount of 96 percent” (IMF 2002, p22). Before 2001, the RCC could only collect or sell individual loans; after 2001, the RCC was able to securitize NPLs, assist with debt restructuring, and utilize bulk sales to dispose of loans. Due to the expanded disposal options, the RCC was more aggressive in its disposal of NPLs between 2001 and 2008; the total balance of debt decreased from ¥5.8 trillion to ¥1.1 trillion and the RCC disposed of many assets for more than the purchase price (Hoshi 2010 p406).

Other scholars argue that the RCC was valuable as it provided the opportunity for banks to remove NPLs from their portfolios in the absence of demand in the market (Fujii, p11). By March 2005, the RCC had purchased ¥4,004 billion of NPLs (book value) from solvent institutions for a purchase price of ¥353 billion, and the cumulative amount of recoveries as of 2008 was ¥642 billion, with no additional purchases made (DICJ 2005; DICJ 2008, p72). The RCC purchased a total of ¥6,366 billion in NPLs from failed institutions and had collected ¥7,143 billion by March 2008 (DICJ 2008, p72).

When the RCC was enabled to engage in corporate restructuring, there was criticism that the RCC lacked the expertise, bandwidth, and resources necessary to effectively restructure corporate debt. Some argued that the RCC “should focus on asset disposal and leave the lead role in corporate restructuring to the private sector” (Kang, p71). With the establishment of the IRCJ, some were concerned that there was no “clear-cut” delineation between the functions of the two bodies; Pohl argues that there were elements of “competition” between the two (Pohl, p52). Hoshi and Kashyap argue that “the division of labor between the RCC and IRCJ [was] not as clear as it is often discussed (Hoshi 2004, p21). However, the RCC was “ultimately involved” in restructuring ¥6.2 trillion in bad debts for 577 borrowers (Hoshi

2010, p405). The authors recognize by assisting with corporate rehabilitation, the RCC began to address the underlying cause of the NPL problem in Japan (Hoshi 2010, p413).

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V. Key Program Documents

Summary of Program

- Summary of the “Front-Loaded Reform Program” – *An overview of the measures taken by the government in 2001 to address economic recovery, including the acceleration of the disposal of NPLs.*
https://japan.kantei.go.jp/policy/2001/economic&fiscal/1026kaikaku-sum_e.html
- Foundation of the Industrial Revitalization Corporation in Japan – *An overview of the Industrial Revitalization Corporation and its operations from its president.*
https://www.iiiglobal.org/sites/default/files/media/The_Industrial_Revitalization_Takagi.pdf
- The effort to stabilise the financial system in Japan: an outline and the characteristics of the programme for financial revival – *An overview of the 2002 Program for Financial Revival.*
<https://bruegel.org/2015/03/the-effort-to-stabilise-the-financial-system-in-japan-an-outline-and-the-characteristics-of-the-programme-for-financial-revival/>
- The Resolution and Collection Corporation and the Market for Distressed Debt in Japan – *A chapter from the 2003 IMF book, “Japan’s Lost Decade: Policies for Economic Revival”, describing the structure and operations of the RCC.*

<https://www.imf.org/external/pubs/nft/2003/japan/index.htm>

Implementation Documents

- Deposit Insurance Act – *A translation of the 1971 Act that established the Deposit Insurance Corporation of Japan.*
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- Purchase Price of Sound Institutions' Assets under Article 53 of the Financial Revitalization Law – *The amendment that enabled the RCC to purchase assets from solvent financial institutions at market price.*
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- Program for Financial Revival – Revival of the Japanese Economy through Resolving Non-Performing Loans Problems of Major Banks – *The FSA program to restore confidence to the Japanese economy by addressing the NPL problem.*
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- Law No 132: Act on the Emergency Measures for Rehabilitation of Financial Functions (1998) – *The Japanese text for the Financial Revitalization Act or the Financial Function Reconstruction Law.*
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- Japan: Regulatory development of the banking resolution regime – *A chapter from the “Research Handbook on Crisis Management in the Banking Sector” which describing the evolution of the regulatory environment and agencies.*
<https://www.elgaronline.com/view/edcoll/9781783474226/9781783474226.00036.xml>
- Obtaining Authorization for Trust Business (In Japanese) – *The announcement that the RCC was granted a trust services license from the MOF.*
https://www.kaisyukikou.co.jp/announce/announce_405.html

Press Releases / Announcements

- Policy Speech by Prime Minister Junichiro Koizumi to the 153rd Session of the Diet – *A speech given to the Cabinet in 2001 by the Prime Minister which covered economic and fiscal reforms.*
https://japan.kantei.go.jp/koizumispeech/2001/0927syosin_e.html
- Japan's Financial Sector Reform: Progress and Challenges – *A 2001 statement from the Minister of Financial Services (FSA) leader reviewing the progress and outlook for the Japanese financial sector.*
<https://www.fsa.go.jp/en/announce/state/p20010903.html>
- Japanese Financial Sector: Progress and Prospect – *A 2002 statement from the Minister of State for Financial Services (FSA) leader reviewing the progress and outlook for the Japanese financial sector.*
<https://www.fsa.go.jp/en/announce/state/p20020920.html>

- Work Scheduled of Program for Financial Revival – A statement from the Minister of Financial Services (FSA) leader, Heizo Takenaka, on the timeline for the Program for Financial Revival.
<https://www.fsa.go.jp/en/announce/state/20021129-2.html>
- Foundation of the Industrial Revitalization Corporation in Japan – A statement from the president of the IRCJ in Japan outlining the IRCJ's policies, laws, and practices.
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- Japan Mob Muddies Real Estate Loan Crisis – A Los Angeles Times article published February 24, 1996, covering the connection of the yakuza on NPLs in Japan.
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- Pile of bad, yakuza-tied debts awaits new president of RCC – A Japan Times article published August 15, 1999, covering the new RCC president and RCC activities to date.
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- Bank Restructuring falls short: IMF – A Japan Times article published September 10, 1999, covering the IMF's reviews and recommendations of the government response.
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- RCC seeks Y900 million in suit – A Japan Times article published February 26, 2000, covering a court suit from the RCC against Hyogo Bank executives.
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