

Global Restructuring & Insolvency Guide

Taiwan

Overview and Introduction

Taiwan, the Republic of China (“**ROC**”), has a codified system of laws. The major codes are the Civil Code, the Criminal Code, the Civil Procedure Code and the Criminal Procedure Code. The content of the codes is drawn from the laws of other countries with similar codified systems, e.g. Germany and Japan, and from traditional Chinese laws. The supreme law of Taiwan is its constitution.

The judicial system is composed of three tiers: the Supreme Court, the High Court and the District Court. Judges decide all cases and there is no provision for jury trials.

In Taiwan, insolvency denotes a state in which a debtor is unable to meet its debts when the debts are due.

Applicable Legislation

There are several mechanisms dealing with insolvency. Articles 282 to 314 of the Taiwan Company Law provide for court-supervised restructuring of potentially viable but insolvent companies. Under the Taiwan Bankruptcy Law, a debtor could be adjudicated bankrupt upon a petition either by the debtor or a creditor when the debtor is unable to repay its debts. If the court declares to cease the reorganisation process of a corporate body, in case the conditions for bankruptcy are met, the court may, *ex officio*, render a ruling to declare the company bankrupt.

While the Taiwan Bankruptcy Law is also applicable to the bankruptcy of an individual, the Consumer Insolvency Procedure Act (the “**CIPA**”) deals with insolvency proceedings for an individual debtor with no business activities or a monthly sales turnaround below TWD 200,000 for five years.

Personal Bankruptcy

Under the Taiwan Bankruptcy Law, individual debtors can be adjudicated bankrupt upon petition by either the debtor or a creditor when the debtor is unable to repay all debts. A debtor who has ceased to make repayments shall be presumed as being unable to pay his debt. Under the interpretation of the court judgments, the definition of “unable to pay his debt” means the debtor’s total debts exceed the total assets. Per the court’s interpretation, in addition to the requirement dealing with one’s inability to settle his debts, there are two more requirements for being declared bankrupt: one, that he has certain assets with which to form a bankruptcy estate and the other, that he owes more than one creditor. Given the above requirements, only a few individuals have so far been declared bankrupt by Taiwan courts.

The CIPA establishes a scheme under which individuals plagued by overdue loans may discharge their debts and improve their financial standing by adjusting their relationship with their creditors. The CIPA allows the debtors to go to court and negotiate a repayment plan with creditors through a binary system of rehabilitation and liquidation procedures.

Eligible Debtors under the CIPA

To be eligible to apply for the CIPA, a debtor needs to meet the following criteria:

- He must never engage in any business activities, or his business monthly sales turnaround is below TWD 200,000 for five years; and
- He is unable, or in danger of being unable, to repay his debts.

Debtors are not eligible to apply for the CIPA under the following circumstances:

- Before the CIPA was enacted (11 April 2008), the debtor successfully negotiated with his creditor banks in accordance with the negotiation mechanism for unsecured consumer loans conducted by the Members of Bankers Association of ROC, unless the debtor had difficulty in performing the negotiated plan through no fault of the debtor.
- After the CIPA was enacted, the debtor successfully negotiated or mediated with his creditor banks in accordance with the CIPA, unless the debtor had difficulty in performing the negotiated plan through no fault of the debtor.

Methods of Debt Clearance

Prerequisite Negotiation

In the case of loans granted by financial institutions, including consumption loans, self-use residence loans, credit card loans or cash card loans, the debtor requests his largest creditor bank in writing for negotiation before he files for rehabilitation or liquidation under the CIPA.

The debt repayment plan that is successfully negotiated with the financial institutions and approved by the court by issuing a ruling can be a title of execution, upon which the financial institutions are entitled to seek compulsory execution if the debtor fails to perform the debt repayment plan.

Rehabilitation

Qualified loans are unsecured or non-preferential consumer loans in an amount less than TWD 12 million.

The debtor proposes a rehabilitation plan that should include repayment in instalments at least every quarter and a rehabilitation term of up to six years, or eight years in exceptional cases. The “exceptional cases” are specified to include: (1) where there are special terms of self-use residence loans in the rehabilitation plan, (2) where the debtor enters into repayment agreements with other secured or preferential creditors, or (3) where the debtor endeavours to make the statutory minimum repayment amounts. When necessary, the debtor may request assistance in preparing the rehabilitation plan from the local government agencies.

Adoption of the Rehabilitation Plan

The rehabilitation plan is adopted at a creditors' meeting.

If the debtor receives a regular salary, practice income or any regular compensation income, and if based on the debtor's income and financial status it can be determined that the debtor has made efforts to repay the debts through the rehabilitation plan, the court shall rule to adopt the rehabilitation plan. The court shall also rule to adopt the rehabilitation plan even when the debtor receives no regular compensation income if there is a guarantor, a person who provides security or another person who is jointly liable for the debts and the court finds the proposed rehabilitation plan is fair.

If the debtor fully performs and completes the rehabilitation plan, the unpaid portion of the debts that have been filed with court and the debts that are not filed with the court are extinguished.

If the debtor fails to perform the rehabilitation plan, the creditors may use the rehabilitation plan as the title of execution to enable them to apply to the court for compulsory execution thereof. The court may, on the application of the debtor, render a ruling to start the liquidation procedure.

If the debtor has difficulty in adhering to the rehabilitation plan through no fault of his own, the court may, at the application of the debtor, rule to extend the rehabilitation plan for less than two years. It is presumed that the debtor has difficulty in adhering to the rehabilitation plan through no fault of his own when the balance of the debtor's disposable income less all necessary living expenses of the debtor and the persons the debtor is legally obligated to provide for is less than the monthly amount payable under the rehabilitation plan for more than three consecutive months. If an extension is impossible, the court may rule to discharge the outstanding debts if the debtor has repaid three-quarters thereof.

according to the plan and if the unsecured and non-preferential creditors have been paid more than they would have been paid in a liquidation procedure. This does not apply to the debts covered by the special terms for the self-use residence loans in the rehabilitation plan.

Liquidation

If the rehabilitation plan is not approved by the creditors at their meeting or if the debtor is unable to pay his debts, the court may rule to start the liquidation procedure on the debtor's application.

Upon termination or completion of the liquidation procedure, the court issues a ruling to discharge the debtor's liability. Such ruling can be revoked within one year if the debtor is found to have concealed his assets or has engaged in any dishonest behaviour in order to obtain the ruling.

If the debtor has salary income, practice income or any other sources of regular income, and if the repayments paid to the unsecured or non-preferential creditors are too low in light of the debtor's disposable income for the two years before the debtor filed for liquidation, the court issues a ruling not to discharge the debtor's liability. However, after issuance of such ruling, if the debtor continues to repay his creditors to the extent that the unsecured or non-preferential creditors receive an amount equal to what they would have been paid in a liquidation procedure, the debtor may apply to the court for a ruling that discharges his liability.

Unless otherwise unanimously agreed to by the unsecured and non-preferential creditors, the court rules not to discharge the debtor's liability if the debtor has already been discharged according to the Taiwan Bankruptcy Law or this CIPA during the past seven years, or if the debtor has been found to have committed dishonesty in order to damage the liquidated assets or circumvent the CIPA.

After the issuance of a ruling not to discharge his liability, if the debtor continues to repay his debts to the extent that every unsecured and non-preferential creditor is paid up to 20% of its debt amount, the court may, on the debtor's application, issue a ruling to discharge the debtor's liability.

Corporate Restructuring and Insolvency

Reorganisations, Restructurings and Work-Outs

Articles 282 to 314 of the Taiwan Company Law provide for court-supervised restructuring of potentially viable but insolvent companies. The corporate reorganisation is intended to assist potentially viable companies to generate sufficient cash flow to meet their debts.

Reorganisation is applicable only to publicly held companies or companies issuing corporate bonds. Reorganisation begins by filing a petition with the District Court with jurisdiction over the registered office of the company that is the subject of the reorganisation. The petition of reorganisation can be filed by any of the following interested parties:

- The board of directors of the company via a resolution passed by a majority vote of the directors present at a meeting of the board and attended by over two-thirds thereof;
- The shareholders of the company who have held at least 10% of the total issued and outstanding shares of the company for at least six consecutive months; or
- Creditors whose claims against the company are equivalent to 10% or more of the total amount of the company's issued and outstanding shares.

Once the petition is received, the court will go through the following procedures before deciding whether to issue an order authorising the reorganisation (the "**Reorganisation Order**"):

- Refer the petition to "competent authorities" seeking their comments on the proposed reorganisation;
- Appoint an auditor to review the company's business and financial status; and

- *Ex officio* or upon the petition of the company or interested parties, determine whether to issue an interim order (“**Interim Order**”) placing limitations on the company/creditors pending its decision on the Reorganisation Order.

The Interim Order cannot exceed a period of 90 days except in case of a reorganisation granted by the court. However, it can be extended for another 90 days upon petition by the company, the interested parties, or at the court’s own decision. By issuing the Interim Order, the court can order the following:

- Withhold/freeze the company’s property (from being disposed of, transferred or sold);
- Limit the company’s operations;
- Limit the company’s performance obligations and other assertion of claims against the company;
- Suspend the proceedings in relation to bankruptcy, composition or compulsory execution against the company;
- Prohibit the transfer of the registered share certificates of the company; and/or
- Investigate the company’s responsible persons for their liabilities for damage to the company and withhold/freeze their personal property.

Within 120 days of receiving the petition of reorganisation and upon referring to the reports and comments from the competent authorities and the auditor, if the court finds that all the statutory requirements were met and that the company is viable, the court will grant the Reorganisation Order. The 120-day period can be extended for another 30 days twice by the court. This effectively means that all bankruptcy proceedings, compulsory execution proceedings and other lawsuits will be automatically suspended.

Once the court issues the Reorganisation Order, it will serve a notice on the competent authority to register the reorganisation. The registration signals to the competent authority that the reorganisation process has begun, after which the court will also assist in:

- Appointing a reorganisation supervisor and manager;
- Giving public notice;
- Informing the creditors with regard to filing their claims;
- Arranging for the interested parties’ committee to be formed; and
- Preparing and approving the reorganisation plan.

In addition to the suspension of legal proceedings mentioned above, the Reorganisation Order effectively grants to a reorganisation manager operating under the supervision of a reorganisation supervisor the right to manage the company’s business and dispose of the company’s properties. This means the normal functions of a shareholders’ meeting, directors and supervisors are suspended.

The creditors will be notified of the dates and place for filing claims and the meeting of the interested parties. All creditors concerned must present all supporting documents and file their claims with the reorganisation manager/supervisor in accordance with the procedures prescribed by the court.

When the filing period expires, the reorganisation manager/supervisor will review the claims and consolidate a list of statutory priority creditors, secured creditors and unsecured creditors (the “**List**”). The List is then reviewed by the court, which will hold a hearing to review the filed claims before preparing a proposed reorganisation plan, which is forwarded to interested parties for their review and approval.

The creditors and other interested parties are entitled to:

- Attend the latter's meeting;
- Review the business and financial condition of the company;
- Comment on the proposed reorganisation;
- Vote on the proposed reorganisation plan; and
- Decide other matters relating to the reorganisation.

The reorganisation plan details the claims that the reorganised company is to be assigned and has to be approved by the interested parties, which consist of shareholders, statutory priority creditors, secured creditors and unsecured creditors, at the meeting of interested parties. At the meeting of interested parties, the voting rights are exercised in groups of shareholders, statutory priority creditors, secured creditors and unsecured creditors, and resolutions shall be adopted by a majority vote of over one-half of the aggregate votes of each group. The number of votes of creditors in reorganisation shall be determined in proportion to the amounts of their claims, and the number of votes of shareholders shall be provided in the articles of incorporation of the company.

Once the reorganisation plan is approved, all debts will be extinguished except for those contained in the reorganisation plan. In addition, any bankruptcy, composition, compulsory execution or other pending litigation involving company property prior to the Reorganisation Order will cease to have effect.

If the Reorganisation Order is not approved, any previous court order issued to withhold or freeze the company's property, limit the assertion of claims or suspend legal proceedings will cease to have effect. Those creditors who have failed to file a claim will have their rights restored and the functions of the shareholders' meeting, directors' meeting and supervisors will resume.

Corporate Insolvencies

Court-Based Insolvencies

The mediation process is governed by articles 6 to 56 of the Taiwan Bankruptcy Law, which provide that the debtor may apply to the court or the local commercial association to settle the debts with its creditors through mediation. However, in practice, the outcome of the mediation is normally unsuccessful as the debtor lacks the assets to satisfy its creditors.

If a corporation is unable to repay its debts, or the court declares an end to the statutory reorganisation process of the corporation, the corporation is likely to face bankruptcy.

Bankruptcy Application

Bankruptcy may be initiated by either the debtor or a creditor when the debtor is unable to meet its debts as they are due. A debtor who has ceased to make repayments shall be presumed to be unable to pay its debts.

If the bankruptcy application is made by the debtor, the debtor must file with the court a report on the status of its assets and a list of creditors. If the application is made by a creditor, it must file a description of the debt owed. Upon receiving the bankruptcy application, the court will begin its investigation and seek the opinion of the debtors, creditors and other interested parties. Although the court is required to accept or reject the bankruptcy application within seven days of receiving it, it can take longer, and the seven-day period is not a statutory deadline.

When an application for bankruptcy is received, the court may, *ex officio* or upon application of the creditors, arrest or detain the debtor or give an order for precautionary measures, such as to freeze the debtor's property from being disposed of, transferred or sold, before the bankruptcy is adjudicated.

After Bankruptcy is Adjudicated

Issuance of a Public Notice and Notification to the Creditors

Once the court adjudicates a debtor as bankrupt, it will appoint a trustee, typically a CPA, lawyer or creditor, to oversee and manage the sale and distribution of the bankrupt's properties. Article 65 of the Taiwan Bankruptcy Law requires the court to issue a public notice informing creditors to report and file their claims with the trustee within a specified period. If the creditors fail to do so, they will not be entitled to repayments from the residual assets of the bankrupt. If the creditors are known to the debtor at the time of adjudication, individual notification must be sent to them informing them of the adjudication. The court will decide on a date for registering the claims. The date, however, must be between 15 days and three months after the adjudication of bankruptcy.

Other than issuing a notice and registering claims, the court is also required to decide on a date to hold the first creditors' meeting to discuss the proposed timeline of the sale of assets and the order of distribution. The first creditors' meeting must be held within one month after the adjudication of bankruptcy.

Trustee's Right to Manage and Dispose of Properties

The bankrupt loses the right to manage and dispose of the properties that constitute the estate. The debtor must turn over books of accounts to the appointed trustee and respond to enquiries that may be raised by the trustee. The operation of the trustee is under close scrutiny by the court and, in practice, the trustee is expected to comply with any reporting duties, often appearing in court twice a week for big cases. The trustee's decision to borrow money for the debtor or make compromises in lawsuits is subject to the consent of the supervisor.

The Bankrupt Estate

The bankrupt estate includes all properties owned by the debtor until the adjudication of bankruptcy and those acquired after the adjudication of bankruptcy, excluding certain items that are necessary for personal use and/or assets that are exempt from compulsory seizure under the ROC Compulsory Execution Laws. Exemptions from compulsory seizure include fuel, food and money, which are necessary for personal use, and sufficient cash to cover the debtor and his co-habitant relatives' living expenses for two months.

According to article 78 of the Taiwan Bankruptcy Law, after the adjudication of bankruptcy, the trustee may request the court to avoid any gratuitous or other onerous transfers that are "prejudicial to creditors' rights" completed prior to adjudication, if such transfers are voidable under the ROC Civil Code. Article 244 of the ROC Civil Code provides that any gratuitous transfer that prejudices a debtor's creditors can be voided by the court and that any non-gratuitous transfers prejudicial to creditors and the debtor who is aware of the prejudice at the time of the transfer can be voided by the court. The claim for revocation in article 244 is extinguished by prescription if not exercised within one year from the moment when the creditor knew of the ground for revocation, or is extinguished after 10 years from the date of doing the act.

Under article 79 of the Taiwan Bankruptcy Law, the trustee may void any provision of security for an existing debt or repayment of any debt before it becomes due, if the provision of security or repayment occurs during the six-month period prior to the adjudication of the bankruptcy.

If the repayment is for any debt after it becomes due, under the interpretation of the Supreme Court judgments, such repayment will not constitute a voidable repayment under article 244 of the ROC Civil Code. The rationale behind this is that although the repayment of the outstanding debt will reduce the assets of a debtor, it also will reduce its liabilities and such repayment will not have any impact on the debtor's financial ability.

Provable Claims under the Taiwan Bankruptcy Law

Article 98 of the Taiwan Bankruptcy Law states that the claims against the bankrupt established prior to the adjudication of bankruptcy shall be obligatory claims provable in bankruptcy (“**provable claims**”), unless the right of exclusion applies. The article requires a creditor to register provable claims with the trustee within a fixed period of time. A creditor has the right of exclusion when he has a pledge, mortgage or lien over the properties of the debtor before the adjudication of bankruptcy. Creditors who have the right of exclusion can exercise their rights without the need to comply with bankruptcy procedures.

Creditors who are also debtors of the bankrupt may set off the claims provided they arose prior to the adjudication of bankruptcy. The provable claims that have not yet become mature will be deemed to have matured upon the adjudication of the bankruptcy.

Distribution of Bankrupt’s Estates

After receiving registration of claims from the creditors, the trustee will prepare a plan of distribution that must be approved by the court and then published for the creditors or other interested parties to consider and raise any objections to. Objections must be raised within 15 days. If no objections are received, the trustee will proceed to divide and distribute the bankrupt’s estate among the creditors who do not enjoy the right of exclusion. The order of repayment is governed by article 112 of the Taiwan Bankruptcy Law, which states that claims subject to the right of priority in the properties of the bankrupt’s estates will be repaid before other creditors. Note that debts that have priority are normally payments required by law. If more than one claim enjoys the same level of priority, repayment will be made *pro rata* to the amounts of the claims.

Close of the Bankruptcy Process

When the court receives notice of the final distribution report from the trustee, it gives a ruling on the closure of the bankruptcy process. Upon the completion of the bankruptcy process, all debts of the bankrupt are discharged and the bankrupt is not liable for any further claims from the creditors unless the bankrupt has been convicted of fraudulent or *mala fide* bankruptcy.

Out-of-Court Mechanisms

Before filing the application for the reorganisation, certain creditors of an insolvent company may enter into a standstill agreement with the debtor for restructuring the debts, under which the creditors agree to refrain from taking legal action against the debtor for a specified period in exchange for the debtor agreeing not to prefer any creditors and usually to give security over all its unsecured assets and to control the expenditures of the debtor.

However, as the standstill agreement will not have a binding effect on a creditor who does not sign the agreement, such a creditor has no obligation to follow the standstill agreement. Therefore, once any creditor takes legal action against an insolvent company, it is unavoidable for other creditors under the standstill agreement to take legal action against the debtor.

Conclusions and Additional Observations

The out-of-court mechanism is seldom workable in Taiwan given that it is difficult to obtain a consensus from all creditors and there is no court order available for preserving the company’s property during the standstill period for avoiding any legal action against the debtor. As such, there is a trend towards court-supervised reorganisation for an insolvent company. Experience reveals that sufficient financial support and financial planning are key elements to the completion of any reorganisation proceedings. As such, recent court judgments on the reorganisation application focus on whether there is any real capital injection plan for an insolvent company. If there is no capital injection plan, the court tends to reject the reorganisation application on grounds that there is no possibility for the company to be reconstructed or rehabilitated through the proceedings.

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