Research on the Procedure Construction of China's Personal Bankruptcy System

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Abstract. Nowadays, the establishment of a nationwide personal bankruptcy system as soon as possible has been a unified view in academic circles. However, the specific setup of this system and the connection and interaction of various supporting systems are still hot issues of academic controversy. From the initial exploration to the continuous prosperity of the local pilot works, the rich pilot experience provides a practical basis for theoretical research. At the same time, new reform trends and changes have emerged in the international frontier legislation. Therefore, this research attempts to give suggestions for the procedural design of the establishment of a national personal bankruptcy legal system in China. Drawing on new experiences and new models domestic and abroad, the selection of personal bankruptcy procedures should adhere to liquidation as the criterion, and attach importance to the role of reorganization, as well as maintain the stability of social and economic order and promote the development and improvement of the legal system.

Keywords: Pre-court reconciliation; Exit mechanism; Individual bankruptcy; Liquidation.

1. Introduction

In February 2019, the "Fifth Five Outline" issued by the Supreme Court listed the personal bankruptcy system as one of the key development tasks. At present, pilot projects of quasi-personal bankruptcy have been carried out all over the country, but the regulations on bankruptcy procedures vary from place to place, and scholars have paid less attention to the issue of procedure selection, and a mature theory of personal bankruptcy and a unified national legal document have not yet been formed.

Under the background of the covid-19 epidemic, employees and investors of small and micro enterprises and individual industrial and commercial households are more likely to encounter economic difficulties. The establishment of a sound and universal personal bankruptcy system is also an important legal guarantee to alleviate their difficulties and meet social needs. Particularly in the context of the covid-19 epidemic, the difficult economic environment requires the establishment of a sound universal personal bankruptcy system for legal protection.

This article will start with the existing local practical experience, combine the perspective of comparative law and the value of procedural legislation, analyze the selection mode of personal bankruptcy procedure in line with the current national conditions of China, and put forward legislative suggestions.

2. The Value of Personal Bankruptcy Proceedings

In order to establish a personal bankruptcy system in line with China's social situation, it is necessary to firstly clarify the legal value pursued by the country's personal bankruptcy law, and further construct specific procedures corresponding to this value.

2.1 Procedural Value Under the Legal Concept

According to Marxist values, value is the meaningful function and attribute of the object to meet the needs of the subject, and the value of law is reflected in the corresponding relationship between people as the subject and law as the object. The needs of people in society are not single, but new needs will continue to grow with the needs that have been met. In order to meet the diverse and developmental needs of the subjects, the value of the law also should be diverse and dynamic, and it is emphasized according to the needs of the development of the times.

Therefore, in order to implement the inclination of the value elements of the law into the legislative practice, the legislator can enhance the orientation of the legal procedure through the reasonable design of the procedure, so as to realize that in the judicial practice, the subject is naturally led to the purpose of promoting value element.

2.2 Analysis of the Value Choice of Personal Bankruptcy Procedure

The general legal value of personal bankruptcy law lies in the purposeful value of pursuing substantive justice and the instrumental value of ensuring the fairness and efficiency of the bankruptcy process. Specifically, personal bankruptcy involves the value balance between the three main subjects of the debtor and the public. Different scholars have different views on these three value choices. The main point of contention is: on the basis of comprehensive consideration of China's national conditions and international frontier legislative achievements, what should be the primary value of personal bankruptcy law procedures. Different emphasis on jurisprudence leads to different designs of individual bankruptcy procedures.

2.2.1 Rebirth

The first value choice is influenced by the American New Beginnings philosophy, which believes that the essence of personal bankruptcy law is a legal system that tolerates failure, focusing on giving "honest and unfortunate" debtors a chance to start over. Personal bankruptcy law should also focus on safeguarding the basic rights and interests of debtors, such as the right to subsistence and development. Based on this value orientation, some scholars advocated restricting debtors from entering liquidation procedures, promoting the application of reorganization procedures, and imposing more relaxed legal restrictions on debtors eligible for reorganization.

2.2.2 Decreased personality

The second value option criticizes the American New Beginnings philosophy, emphasizing that bankruptcy law itself is a "punishing law". Personal bankruptcy was once manifested in the patterns of personal deprivation, liberty deprivation, and depersonalization, and its starting point was humiliating. With the development of modern society, bankruptcy law no longer deprives the right to life and physical integrity, but the bankrupt will still be affected in terms of social activity ability and social credit evaluation.

Some scholars have criticized that rebirthism is currently unable to take root in the soil of China, and should return to the reduction of personality. First, because the economic development models of China and the United States are different, the rebirthism under the American New Beginning philosophy cannot be blindly grafted. Meanwhile, China should avoid the disciplinary background of bankruptcy and construct preventive measures to prevent the abuse of liquidation. If the deconstruction is started when the legal structure is constructed, it is not conducive to clarifying the thinking in the early stage of national legislation on personal bankruptcy. Second, the punitive nature should be emphasized, the legal logic of bankruptcy should be maintained first, and the practical needs of responsibility should be clarified. On the one hand, because the debtor is insolvent, the interests of both parties are unbalanced when entering bankruptcy proceedings. Therefore, bankruptcy liquidation only guarantees the basic survival of the debtor and prompts the debtor to take responsibility for the losses caused by others. On the other hand, the most prominent problem in China's practice is non-payment of debts, and non-debtors urgently need immunity protection. The outstanding phenomenon of debt collection in cases of "difficulty in execution" is one of the main driving forces for the legislation of personal bankruptcy in China.

2.3 The Choice of the Value of Personal Bankruptcy Procedures in China

New Beginnings theory is not acceptable, for it overemphasizes the protection of debtors, but ignores the starting point of bankruptcy law, that is, the protection of creditors' interests. Moreover, this kind of value orientation is contrary to traditional Chinese legal culture and cannot be implemented injudicial practice.

Meanwhile, too much emphasis on punitive is also biased. From the macro perspective of debt cycle changes, society should not uniformly classify debtors who are insolvent as unpardonable and condemned objects. Nowadays, the impact of the environment on natural persons cannot be ignored. Since 2019, many self-employed households have gone bankrupt due to force majeure such as the epidemic. The interests of the debtor, the interests of the creditors, and the public interests seem to be opposed, but in fact, they are essentially the same. Therefore, the personal bankruptcy law should guide the debtors to tide over the difficulties together.

In China, personal bankruptcy procedures should consider the interests of debtors and creditors, and promote the stability of social and public interests under the joint action of the two, so as to achieve a dynamic balance of the three values.

3. The evolution trend of procedure selection from the perspective of comparative law

The common protection of both parties to the debtor and the public interest of society, which is required by legal values, is also the common goal pursued by the personal bankruptcy laws of various countries. However, in different historical stages and national conditions, a variety of program selection models have emerged. Moreover, with the development of the economy and the accumulation of experience, different models are also merging, and new legislative phenomena and reform trends have emerged.

3.1 Inspiration from the “Warren Motion” in the United States

On December 9, 2020, the Consumer Bankruptcy Reform Act of 2020 (the “Warren Act”) was passed by Elizabeth Warren (U.S. Senator, prominent bankruptcy law scholar) and published by De Nadler (Chairman of the House Judiciary Committee) and others to create a new Chapter 10 to establish a new personal bankruptcy process and to repeal the dual-track option of Chapter 7 and Chapter 13 in the current bankruptcy code model.

The legislative framework of the U.S. bankruptcy law has only odd chapters to facilitate the addition of new elements, such as the Warren Motion between the two chapters to amend the law. It provides consumers with a single-entry point, Chapter 10, replacing the dual-track system with a uniform procedure. The bill has been endorsed by organizations such as the Center for Racial and Economic Action, as well as a panel of 74 law professors, attesting to the emergence of a new reform trend. Although the “Warren Motion” has been controversial, its conceptual value and feasibility are worth thinking about and learning.

The Warren Motion replaces a clear institutional design with a combination of liquidation and reorganization, thus becoming more flexible. At the same time, under the institutional design of the Warren Motion, the poor debtors who have the greatest benefits are the debtors, and the debtors who are able to repay the debt bear part of the obligations. As Chairman Nadler noted in an interview, ‘‘The Consumer Bankruptcy Reform Act ensures that the bankruptcy system serves the American people, not just the creditors of large corporations.’’ The institutional framework does not simply protect or limit the debtor as a whole, but rather relieves the pressure on some debtors and takes care of the rights of creditors.

However, it must be noted that whether it is the “minimum payment obligation” or the ultra-short exemption period, it is supported by the national conditions and legislative purposes behind it. Consumer credit is an important part of the U.S. economy, an important tool for expanding domestic demand, and it is precisely the need for consumer credit that eliminates the analysis of acceptable non-luxury spending, and the extremely short exemption period allows debtors to quickly escape from bankruptcy and participate in socio-economic and financial activities, which is also the need of the U.S. economy.

3.2 Changes in German Personal Bankruptcy Procedures

Unlike the United States, Germany's 1999 Bankruptcy Code adds to consumer bankruptcy proceedings, establishing a single-track personal bankruptcy system of compulsory out-of-court settlement and in-court settlement plus liquidation

3.2.1 Changes in the exemption period

When the Bankruptcy Code was amended in 2001, a six-year good conduct period was established. On June 20 2019, the European Commission published the Directive on the Framework for Preventive Restructuring, the Framework for Debt Settlement and Disqualification, and on Measures to Improve the Efficiency of Restructuring, Insolvency and Debt Settlement Proceedings, the EU Directive 2019/1023, which aims to eliminate differences in insolvency laws within the EU . Following this directive, along with the economic pressure brought about by the new crown epidemic, the six years were shortened to 3 years, improving the efficiency of bankruptcy.

3.2.2 Changes to mandatory out-of-court settlements

In 1999, the establishment of compulsory out-of-court settlements was criticized by many scholars, such as cumbersome procedures and increased the burden on debtors. Therefore, the Ministry of Justice and others have repeatedly introduced drafts to try to further modify the procedural settings, such as the 2006 Report of the Ministry of Justice, "Draft Amendments to the Debt Relief Procedure and consumer bankruptcy procedures for the rescue of hopeless debtors", which aims to divert the rescue of hopeless debtors and modify the German personal bankruptcy system.

3.3 Enlightenment from the Trend of Extraterritorial Legislation to the Construction of China's Personal Bankruptcy System

First of all, it can be seen from the legislation and practice of various countries that personal bankruptcy is not only a procedural choice, and its model is not static, but develops with the development of national conditions and practices, and the phenomenon of partial integration of free choice mode and restricted choice mode has emerged. China is in the stage of national legislative exploration of personal bankruptcy, and should learn from countries with mature legislative experience to carry out legal construction based on fully understanding the national conditions and local pilot practices. It is also necessary to realize that the investigation of the model is not once and for all, nor is it static, and it is essential to stand in a dynamic historical perspective and look at the changes in the program model from the perspective of development.

Second, it is necessary to pay attention to protecting creditors' interests and the rights and interests of debtors. Unlike countries with long-term personal bankruptcy practices, China's personal bankruptcy is still in its infancy. In the views of the public, the personal bankruptcy system is contrary to the concept of ‘‘debt repayment’’. Therefore, at the beginning of the system, the protection of the interests of creditors is particularly important, and it takes a certain period of time to transition gradually. In addition, in the face of the significant pressure brought about by the epidemic, the protection of the rights and interests of debtors also needs to be implemented, giving ‘‘honest and unfortunate’’ debtors a chance to breathe.

Finally, safeguarding the rights of both debtors depends on sound procedural settings. Looking at extraterritorial legislation and practice, different models interact with each other, and different legislative tools, debtor diversion models, and exemption periods are used to implement the protection of the rights and interests of both debtors. The most important thing in China's legislation is to establish a sound supporting system, based on China's national conditions, to ensure the right to know and the right to speak of both debtors in the whole stage of the process of selection, to introduce the debtor into the appropriate procedures and stages through the system setting, and to give the judicial staff of the court a clear and feasible judgment standard. After all, A perfect system is more important than a perfect part.

4. The Construction of Personal Bankruptcy Procedure Options

4.1 The Liquidation Procedure is the Basic Criterion

In the author's view, liquidation procedures should not be restricted to prevent abuse. Liquidation proceedings are the basic criteria for the liquidation of debts in bankruptcy for the following reasons:

First, bankruptcy liquidation is a bottom-up measure for debt liquidation. At present, scholars pay too much attention to the saving value of the personal bankruptcy system for debtors. This is not the case, and the construction of a system based on reorganization is not in line with the original intention of the bankruptcy system. As discussed above, the insolvency regime is not a debt-free regime, and the purpose of insolvency is to clear debts. Therefore, the liquidation process is also called the "bottom line benchmark" of personal bankruptcy by scholars.

Second, liquidation is the most traditional and typical procedure in the history of insolvency law. From the practical experience of national insolvency laws, the system that allows debtors to be reborn from debt was relatively late, and in the early stage of the establishment of the bankruptcy system, the liquidation procedure was the most fundamental procedure applicable to the treatment of debts. In the early stage of the development of personal bankruptcy law in China, the liquidation procedure should not be regarded as a supplementary procedure for reorganization, but should be used as a basic procedure.

Third, the punitive significance of the liquidation procedure is conducive to achieving a balance between the rights and interests of both debtors. As mentioned earlier, bankruptcy is not the same as debt forgiveness, and simply substituting the debtor role will shift the bankruptcy system from the perspective of "punishing the debtor and protecting creditors from realizing their claims" to the non-disciplinary doctrine of "protecting the debtor". To establish China's personal bankruptcy system, we must attach importance to the punitive value of liquidation itself, and maintain the severity and finality of the liquidation procedure itself in order to prevent too much tilt towards the debtor and achieve a balance between the rights and interests of both debtors.

4.2 Guiding the Parties to Choose the Procedure through Procedure Setting

On the basis of the liquidation system as the basic principle, we need to compare different procedures to guide the debtor into a more suitable procedure and diverse different types of debtors.

First, in China, which has a large regional difference and a large population, it is not feasible to set a unified calculation formula modeled on the "income test" of the United States. It is wiser to support the parties' independent choice of procedure. In this process, it is necessary to strengthen the participation of creditors, promote the agreement between the two parties through creditors' meetings, and enter a more personalized and effective bankruptcy procedure. Protecting the right to speak of creditors can not only protect the rights and interests of creditors, but also avoid the phenomenon of "indifference" of creditors in subsequent procedures to a certain extent.

Second, the setting of the program is related to the cost of selection, which also affects the choice of the debtor. The author believes that the wisdom of the program setting can also play a role in guiding the parties to choose the procedure. On the one hand, China should guide debtors with solvency into more sustainable reorganization procedures through procedural guidance, such as reducing the cost of access to reorganization procedures, increasing the dividends of reorganization procedures, and adopting simple and direct procedural procedures for appropriate bankruptcy cases. On the other hand, it respects the free will of creditors and debtors, guarantees the right of creditors to object, and realizes efficient and targeted procedural choices through consultation between the two parties.

4.3 Emphasis on Reorganization as a Preventive Procedure

Through the guarantee of systems and standards, the reorganization procedure increases the amount of debt repayment to creditors as much as possible, reducing the impact of debtors on creditors' claims. A certain degree of solvency on the part of the debtor is not a sufficient requirement for the application of the reorganization procedure. If the debtors reach an agreement, the creditor is not willing to extend the repayment period, or the amount of debt repayment obtained through reorganization is lower than the amount available for liquidation, or it may choose to enter the liquidation procedure directly.

The reorganization process is more socially acceptable. The reorganization procedure retains more creditors' claims, and actually takes into account China's debt repayment ideology of "debt repayment and righteousness" since ancient times, which is more acceptable to society, thus enhancing the possibility of law implementation. On the other hand, the reorganization procedure gives debtors who are able to work the opportunity to regenerate, promotes the flow of labor into the market, and maintains the smooth operation of social development.

Therefore, the reorganization procedure is a three-dimensional integration of the protection of the debtor's rights and interests, the protection of the creditors' interests, and the stability of the public social interest. Legislators should attach importance to the construction of reorganization procedures and make them an important preventive judicial procedure in the personal bankruptcy system.

4.4 Setting up Pre-trial Settlements to Relieve Judicial Pressure

At present, the settlement procedure that has been practiced in China is the in-court settlement, and in-court settlement is a bankruptcy procedure that is juxtaposed with reorganization and liquidation. The process requires a court-appointed administrator to help develop the settlement agreement. However, considering the negotiable and liberal nature of the settlement itself, the author believes that the settlement can be used as a preliminary procedure for the parties to choose, and the court only needs to recognize that the settlement agreement is enforceable to achieve the effect of a traditional in-court settlement. At the same time, before entering the bankruptcy procedure, the parties can find non-judicial institutions that provide debt consultation and other matters to conduct property investigations, the formulation of settlement documents, etc., so as to reduce the transactional work into the court and save the resources of the bankruptcy court.

4.5 Establish a Flexible Exit Mechanism

In the author's view, the parties should be allowed to settle at any stage before the declaration of bankruptcy and withdraw from the bankruptcy proceedings. Article 147 of the Shenzhen Regulations stipulates: "In bankruptcy proceedings, if the debtor and all creditors reach a settlement agreement on the disposition of creditor's rights and debts on their own, they may apply to the people's court to terminate the bankruptcy procedure." "This is a major highlight of the Shenzhen Regulations in the design of the bankruptcy procedure system, that is, any procedure and any stage can be compatible with the civil settlement procedure as an exit path, making the procedure have good compatibility." Therefore, it is also necessary to adopt such a flexible exit mechanism in the unified national legislation.

The withdrawal mechanism provides an impetus for the convergence of procedures inside and outside the court. In the process of reaching a settlement, the parties may make full use of the functions of the bankruptcy management institution and the diversified dispute resolution mechanism of the people's court, so that the out-of-court debt mitigation mechanism can be fully developed. In addition, review rules are set up within the judicial process, and the effectiveness of judicial procedures is confirmed through judicial procedures in accordance with the legal requirements, so as to realize the procedural connection between inside and outside the courtroom.

5. Conclusion

In summary, the author puts forward the following suggestions for the procedural design of the establishment of a national personal bankruptcy legal system in China: (1) Firmly take the liquidation procedure as the basic criterion of the bankruptcy law, so that both the debtor and other interested parties can clarify the nature of bankruptcy punishment; (2) Do not set a unified income test, but introduces solvency debtors into the reorganization procedure through procedural settings such as exemption period and behavior restrictions, and diverts debtors; (3) Attach importance to reorganization as a preventive procedure, through the creditor majority meeting system and the best interests standard protect creditors' rights and provide debtors with opportunities for regeneration; (4) Establish a pre-trial settlement mechanism, which only needs the court's approval to be enforceable and reduce judicial pressure; (5) Set a flexible exit mechanism that allows parties to achieve settlement at any stage before the bankruptcy is announced to exit the bankruptcy process.

The socialist legal system with Chinese characteristics is dynamic and open, and the laws of various departments are also developed and updated. At a new historical node, promoting personal bankruptcy legislation is an inherent requirement to improve the legal system and a necessary means to regulate the economic order. The suggestion of completing the selection system put forward in this paper is hoped to become theoretical exploration and research before legislation. This is conducive to fully protecting the legitimate rights and interests of creditors and debtors, assisting the research and exploration of supporting coordination mechanisms, and has important theoretical significance for the construction of a personal bankruptcy system, thereby helping to build a complete modern bankruptcy system and market exit system, and optimize the business environment, and create a good social credit environment.

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