Research on the Implementation Dilemma and Solution Path of Personal bankruptcy Exemption System from the Perspective of Interest Balance *

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Abstract. Under modern bankruptcy law, individual debtors enter bankruptcy proceedings mainly to obtain debt relief. Therefore, the exemption system is not only a part of the Personal bankruptcy system but also plays a core role in the Personal bankruptcy system. However, the debtor's debt relief is based on the consideration of harming part of the creditors' interests in repayment, which poses an ethical challenge to the Personal bankruptcy relief system. Therefore, how to balance the interest relationship between creditors and debtors in the personal bankruptcy exemption system and promote the orderly development of the social market economy, this paper will discuss the model selection, scope of application, inspection period and other aspects.

Keywords: personal bankruptcy, bankruptcy discharge, disclaimer mode, scope of exemption, disclaimer period.

1. Summary

The "Reform Plan for Accelerating the Improvement of Market Subject Exit System" clearly states: "We will study the establishment of a personal bankruptcy system, focusing on solving the problem of joint and several liability of natural persons to guarantees debts arising from enterprise bankruptcy. It is clear that natural persons can be reasonably exempted from liabilities related to production and operation activities due to guarantee and other reasons. We will gradually promote the establishment of a reasonable exemption from liabilities in accordance with the law for eligible consumer liabilities of natural persons, and finally establish a comprehensive personal bankruptcy system." [1] Accordingly, on March 1, 2021, the first national local regulation on personal bankruptcy was issued The Regulations of Shenzhen Special Economic Zone on personal bankruptcy was officially implemented, and on November 8, it announced the ruling of the first Personal bankruptcy liquidation case in mainland China On December 2, 2020, the High People's Court of Zhejiang Province officially released the Guidelines on the Centralized Liquidation of Personal Debts (Personal bankruptcy like) of Zhejiang Courts (for Trial Implementation) Local courts such as Wenzhou City, Zhejiang Province, and Wuxing District, Suzhou City, Jiangsu Province, have also issued implementation plans for personal debt liquidation. The personal bankruptcy system is being innovatively piloted and vigorously developed throughout the country.

1.1. Concept of Personal bankruptcy system

The explanation of the term 'bankruptcy' in economics is a special economic state in which debtors continue to struggle to make ends meet economically. In the legal sense, "bankruptcy" refers more to a legal means and process, that is, a legal system in which the bankrupt debtor declares bankruptcy through the court and repays the debts owed through bankruptcy proceedings.

The term "Personal bankruptcy" is derived from the literal translation of "individual bankruptcy" in Bankruptcy in the United States. Influenced by the differences in social, economic and cultural backgrounds between China and the West, the specific scope of the term "individual" is biased, which leads to the failure to effectively define the scope of application of the personal bankruptcy system. Some people believe that "individual" refers to ordinary natural persons in the general legal sense and commercial natural persons participating in economic activities. Among them, bankruptcy of ordinary natural persons in the general legal sense refers to consumer bankruptcy. Bankruptcy of commercial

natural persons includes bankruptcy of related personal bankruptcy caused by bankruptcy of enterprise legal persons, and bankruptcy of partners or investors and corresponding members caused by bankruptcy of unincorporated economic entities such as partnerships self-employed businesses. According to the relevant provisions of China's Civil Code, "natural person" is a legal concept with strict requirements in China, which is parallel to legal persons and unincorporated organizations. "Natural person" includes ordinary natural persons, individual businesses and rural contract operators. Based on this, it can be found that "natural person" cannot completely cover the personal category and cannot effectively reflect the business attributes of partners and investors. Although personal bankruptcy caused by the bankruptcy of some economic entities is not applicable to enterprise bankruptcy procedures, personal bankruptcy procedures and enterprise bankruptcy procedures are closely related, but there are certain differences from ordinary natural person bankruptcy. This leads to the inability of natural persons to cover all applicable subjects of the personal bankruptcy system, and Personal bankruptcy does not specifically refer to the bankruptcy of natural persons. Based on this, the personal bankruptcy analyzed in this study refers to all bankruptcy subjects including ordinary natural persons and commercial natural persons.[2]

1.2. The concept of bankruptcy exemption system

The exemption system of Personal bankruptcy refers to the system that after the conclusion of the bankruptcy procedure, the honest debtor who meets the legal exemption conditions is exempted from continuing to pay the debts in accordance with the bankruptcy procedure within the legal scope.[3]

After the end of bankruptcy proceedings, there are two ways to deal with the debtor's outstanding debts: one is to adopt an exemption principle, which means to exempt the debtor's insolvent debts in accordance with legal provisions and give them the opportunity to "restart", but it will harm the property interests of creditors; the second is to adopt the principle of irresponsibility, which requires the debtor to pay off all debts. Although this protects the interests of creditors, in practice, debtors often slack off in the subsequent execution process due to excessive debt burden and even transfer property to evade responsibility, ultimately causing greater harm to the interests of creditors. Therefore, most countries currently adopt exemption doctrine in their legislation while setting certain restrictions on debtors' access to exemption.

2. The Significance of Personal bankruptcy Exemption System

2.1. Rebirth for "honest and unfortunate" debtors

With the increasing development of China's market economy, the behavior of individual investment in the market is also becoming increasingly frequent. However, there must be risks in the market, and sometimes losses or even bankruptcies are inevitable. For corporate legal persons, it is still possible to use bankruptcy proceedings to achieve property liquidation and exit the market, but ordinary natural persons and commercial natural persons who bear unlimited liability in economic activities cannot resort to bankruptcy proceedings like corporate legal persons. After investment failure, they often bear the name of "old scoundrel" because they are unable to pay off huge debts. The personal bankruptcy exemption system can help these "honest and unfortunate" debtors, allowing some of their debts to be released after the bankruptcy proceedings are concluded, provided that they comply with the law. This helps them to regroup and hopefully participate in social and economic life while also protecting the interests of creditors to a certain extent. The Federal Court of the United States believes that one of the main purposes of bankruptcy law is to free honest debtors from debt and give them the opportunity to participate in economic life again and create social wealth.[4]

2.2. Realizing fair compensation for creditors

For debtors trapped in debt quagmire, even if the remaining debt is not waived, the likelihood of creditors being able to obtain full repayment is extremely low. They also need to constantly monitor or be vigilant about the debtor's movements, wasting their time and energy. Through the release of

the remaining debt of Personal bankruptcy, it not only frees itself from debt recovery all day long but also prevents the debtor from paying off biased debts. In addition, bankruptcy exemption can encourage debtors to actively cooperate, motivate debtors to actively, truthfully, and comprehensively declare their assets, prevent debtors from transferring or hiding their assets and income, and prevent debtors from making biased payments to individual creditors. This can effectively reduce the cost of creditors' rights protection, resulting in fair payments.

2.3. Solving the problem of "difficult execution"

In 2020, the Supreme People's Court accepted 39347 cases and concluded 35773 cases, and local people's courts and specialized people's courts accepted 30.805 million cases, concluded 28.705 million cases, and concluded 7.1 trillion yuan.[5] It can be seen that the people's courts have achieved breakthrough results in case execution, but there are still some cases facing difficulties in execution. Especially in personal bankruptcy cases, a large number of debtors are unable to execute because of insolvency, which eventually becomes "difficult to execute", which will inevitably damage the credibility of the judiciary in the long run. The emergence of a personal bankruptcy exemption system may be able to solve the problem of "difficult implementation". By providing debtors with hope through debt repayment within a specified period and debt forgiveness upon maturity, they can actively participate in bankruptcy enforcement, and creditors can regain trust in the court, reducing the occurrence of extreme debt reminders. It is helpful for the court to solve the problem of difficult execution in the field of personal bankruptcy and improve judicial efficiency.

2.4. Promoting social-economic development

The personal bankruptcy exemption system is not a way to eliminate the risk of the debtor's investment failure but a risk transfer; that is, the creditor has taken the risk of failure while obtaining the right to receive fair compensation. Similarly, the debtor also has to pay a certain price to obtain residual debt relief, such as limiting high consumption and paying off debts with all income except for necessities of life, to strengthen the debtor's credit security awareness and prevent bankruptcy. It should be recognized that the personal bankruptcy exemption system is not simply to protect the interests of creditors and debtors. Through bankruptcy exemption, a group of individuals with financial failures have been released to society, enabling them to participate in social and economic activities, create social wealth, and reduce the economic losses of all stakeholder. At the same time, bankruptcy exemption can also avoid the economic burden of the debtor's failure to give up life and maintain social stability to achieve sustained and healthy economic and social development, ultimately achieving broader social-economic benefits.

3. The Construction Dilemma of the Exemption System of Personal bankruptcy in China

3.1. The dilemma of choosing an exemption mode

There are currently two legislative models for bankruptcy exemption: automatic exemption and permitted exemption.

Common law countries, represented by the United States and the United Kingdom, adopt the automatic exemption mode; that is, after the debtor has completed the bankruptcy proceedings, there is no need to file an application. After the creditor has been fairly repaid, it will be deemed that the debtor has paid off all debts, and the rest of the debts will certainly be released.[6].

The licensing exemption model refers to the debtor's ability to waive a portion of the debt that can be waived only after obtaining the court's permission. This exemption model mainly exists in civil law countries, and its purpose is to prevent various behaviors of the debtor's fraudulent claims. While protecting the interests of creditors, it can also protect the rights and interests of honest debtors. When the concept of personal bankruptcy is still weak in China, the bankruptcy exemption system is

undoubtedly a huge temptation. Whether the debtor can uphold integrity and actively repay debts is worth considering.[7]

What should be the exemption model in China? From the perspective of the debtor, automatic exemption is clearly superior to permissive exemption, and it is in their best interest to automatically release the debt upon maturity without going through court application procedures. However, the automatic exemption mode will send a negative signal to society that the debtor is easy to get rid of the debt after they owe it, and it will also indirectly encourage the debtor to passively repay the debt, which is obviously not conducive to social and economic stability. Therefore, what kind of exemption mode should be selected is a major problem in the construction of a personal bankruptcy exemption system in China.

3.2. Debtors' Abuse of Debt Relief System Crisis and difficult-to-confirm situations where exemption is not granted

Exemption inspection system is the core issue in personal bankruptcy legislation, and its legal structure includes two parts: exemption conditions and exemption procedures. We should improve the legal structure of the exemption inspection system in China's personal bankruptcy law under the concept of holism and balance of interests.[8]

As China's personal bankruptcy system has not yet been established and the scope of free property is not clear, many dishonest debtors will use the exemption system to escape the prison of debt, seriously damaging the interests of creditors and impeding the harmonious and stable development of social economy. Therefore, defining the scope of application of debt exemption is a key link to improve the personal bankruptcy exemption system.

3.3. Difficulty in limiting the number of times during the debt exemption review period

The final procedure for debt relief is through the exemption period, after which the debtor can completely break away from the debt relationship. The function of the exemption period is not only to examine whether the debtor can re-enter a new production and life after declaring bankruptcy.

With regard to this system, we should see that a short inspection period for bankruptcy exemption may make debtors despise the consequences of bankruptcy, and financial institutions will therefore lend prudently, which will also make it more difficult for the public who are worried about the personal bankruptcy exemption system to accept. Of course, a long period of bankruptcy exemption review is also not advisable, as it may still burden the debtor with heavy life pressure for a long time and even lead to problems such as passive debt repayment and lack of hard work. At the same time, if the number of times the creditor can use this right is not limited, the creditor may maliciously exercise the revocation right, the debtor's property will be threatened, and repeated applications may lead to the abuse of judicial resources.

Therefore, in legislation, how to control its time and frequency is a difficult problem in China's current bankruptcy exemption system. Only by solving this problem can the effectiveness of the debt exemption system be fully realized and the risk of abuse be avoided.

3.4. The Dilemma of National Unified Legislation and the Crisis of Lack of Responsibility Exemption and Supervision System

There are obvious differences in China's economic development, and the construction of the personal bankruptcy system is quite difficult. First, the problem of Personal bankruptcy applicant qualification needs to be solved. If the amount of arrears alone determines whether Personal bankruptcy proceedings can be entered, then there is no unified standard across the country. Second, the construction of supporting facilities is not perfect. Although there are ways explored by the Enterprise Bankruptcy Law, it is different from the personal bankruptcy Law after all. Finally, the pilot project of the Shenzhen Special Economic Zone has not yet achieved phased results, and the lack of practical experience has led to the construction of the personal bankruptcy system being in a stage of crossing the river.

Although the debt relief system is the core system of the personal bankruptcy system, it is also of independent value. Compared with the Personal bankruptcy system, the debt relief system has little difference across the country and is mainly completed by the supervision system. Therefore, to play the role of the debt relief system, it is necessary to establish and improve the operation and supervision system to prevent the debtor from abusing it.

4. Countermeasures for Solving the Difficulties in the Implementation of the Exemption System of Personal bankruptcy

Insolvency exemption is the core of the personal bankruptcy system. In order to solve the problem of difficult execution and optimize the construction of business environment, China should improve the exemption system of personal bankruptcy when formulating the personal bankruptcy law in the future. On the basis of clarifying the origin and theory of the construction of the exemption system of personal bankruptcy, we should put forward the local logic of the system construction in China, including that the legislative concept is not synchronized with the social concept, personal bankruptcy and exemption should be integrated into the unified procedure with different original intentions, and the independent value of exemption in the overall procedure of personal bankruptcy.[9]The ideal path to realize personal bankruptcy exemption control lies in the two-way construction of entity and procedure. In terms of entity construction, in addition to the statutory circumstances and types of debt that are not exempt from liability, detailed provisions should also be made on the examination factors and effectiveness of exemption; In terms of program construction, it is necessary to adhere to the program path of licensing exemption, while specifying the specific steps of the exemption program.[10]

4.1. Adopting a licensing exemption model based on specific national conditions

First, the current personal credit reporting system in China is not yet sound, and traditional concepts are filled with a large number of ideas that tend to protect the interests of creditors, such as "debt repayment, natural justice" and "father debt son repayment". It is obviously difficult for the public to accept the automatic exemption model; Second, the personal bankruptcy exemption system has the dual value pursuit of fair debt repayment and giving the debtor a new life. Under the allowable exemption mode, the court acts as the main body of supervision to supervise the debtor's debt repayment and the creditor's repayment, which can better realize fair debt repayment and avoid the chaos of individual creditors scrambling for the remaining property, violently collecting debt and even negotiating with the debtor to damage the interests of other creditors. Finally, a neutral court as the main body to decide whether to exempt unliquidated debts can avoid the situation in which the debtor uses the personal bankruptcy exemption system to maliciously evade debts and damage the interests of creditors. In summary, it is more appropriate to choose the allowable exemption mode for personal bankruptcy exemption mode in China.

4.2. Clarify situations where no exemption is granted

First, it is necessary to analyze the legislative experience of various countries and clarify the following types of nonexempt debt. Paying taxes according to law is a basic obligation of citizens. If tax debts are exempted, social costs may be transferred unreasonably to the public, which will damage social and public interests. The second is marriage and family debt. If the relief for the debtor allows them to be exempt from the most basic family responsibility, the debt responsibility will be transferred to equally vulnerable parties and society invisibly and even threaten the debtor's spouse and children's right to survival and development, which is obviously not conducive to social stability. The third is penalty debt. The exemption system of Personal bankruptcy is mainly to provide relief for "honest and unfortunate" debtors. As a consequence of illegal crimes, fines and other obligations obviously do not belong to this relief scope.

4.3. Clarification of the exemption period Clarification of the exemption period

We can determine the exemption period based on the specific repayment ratio. For debtors, it can be incentivized to increase the repayment ratio as much as possible to reduce the exemption period. For debtors, being able to obtain a higher proportion of debt repayment to protect their own rights and interests is a balance of interests. In addition, consideration should also be given to the debtor's ability and actual repayment of creditor's rights after the end of the bankruptcy proceedings, and whether to change the debtor's bankruptcy review period can be determined based on their specific performance.

4.4. Response to the Crisis of Debtors' Abuse of the Debt Relief System

First, the debt relief system is based on the declaration of personal bankruptcy, so the debtor must strictly control each stage of the personal bankruptcy declaration procedure. Second, when entering the personal bankruptcy procedure, strictly examine the application qualification of natural persons; in terms of property collection, strengthen the supervision of bankruptcy administrators and creditors; strictly follow the statutory classification in determining the scope of exemption; and reasonably determine the exemption period and improve the protection channels for creditors. Finally, it should be considered how the debt relief system should be arranged in the event of secondary bankruptcy. Although there is no limit on the number of bankruptcies of natural persons, if the debtor's inability to repay repeatedly occurs, the credit of the debtor will be increasingly affected, leading to a social credit crisis and a negative impact on the long-term development of the economy.

4.5. Response to Crisis of Lack of Supervision System

China's personal bankruptcy system has not yet been established, and there are great deficiencies in theory and practice. First, we should establish an information registration and property registration system, include the debtor applying for personal bankruptcy in the information registration system, and then register its property. At the same time, we should give creditors and bankruptcy administrators the authority to supervise and review the information and property registered by the debtor. Second, we should strengthen the construction of the credit supervision system so that the debtor who is dishonest cannot apply for debt relief within a certain period of time or even cannot apply for personal bankruptcy. Finally, we should build a bankruptcy management organization and strengthen the role of personal bankruptcy administrators in personal bankruptcy proceedings.

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