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The Westernization of Chinese Bankruptcy: An Examination of China's New Corporate Bankruptcy Law through the Lens of the UNCITRAL Legislative Guide to Insolvency Law

Steven J. Arsenault*

*Capitalism without bankruptcy is like Christianity without hell.*¹

I. Introduction

On August 27, 2006, the Standing Committee of the National People's Congress adopted the Corporate Bankruptcy Law of the People's Republic of China.² The new bankruptcy law became effective on June 1, 2007³ and replaced the existing enterprise bankruptcy law that was enacted in 1986.⁴ Modeled after Western bankruptcy laws and standards,⁵ the new Corporate Bankruptcy Law is a significant step

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1. Michael Rogers et al., *Airline Turbulence Spreads Across the Land*, FORTUNE, Sept. 29, 1986, at 6 (quoting Frank Borman, former CEO of Eastern Airlines).

2. See Law on Enterprise Bankruptcy (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 27, 2006, effective June 1, 2007) (P.R.C.) [hereinafter Corporate Bankruptcy Law], available at 2006 China Law LEXIS 5574.

3. See *id.* art. 136.

4. Tom Young, *Startling Achievement: Pari Passu for Foreign Creditors and Much More*, INT'L FIN. L. REV., July 1, 2006.

5. See Ann vom Eigen, *China's New Bankruptcy Law Encourages Investment*, 25 AM. BANKR. INST. J. 8 (2006); Mary Swanton, *Bankruptcy: China Passes Its First Unified Bankruptcy Law*, INSIDE COUNSEL, Nov. 2006, at 68. This is not the first time that western bankruptcy law in general, and U.S. bankruptcy law specifically, has been used as the basis for other countries' bankruptcy laws. See also Sandor E. Schick, *Globalization, Bankruptcy and the Myth of the Broken Bench*, 80 AM. BANKR. L.J. 219 (2006). In particular, Chapter 11 of the U.S. Bankruptcy Code served as the basis for

forward in Chinese bankruptcy law. This article begins in Part I with an examination of China's new bankruptcy law through the lens of the UNCITRAL Legislative Guide to Insolvency Law. Part II examines the history of bankruptcy law in China. Part III describes the provisions of the new law, and where appropriate, discusses the similarities and differences between China's new bankruptcy law and the bankruptcy law of the United States ("U.S."). Part IV of this article examines the UNCITRAL Legislative Guide to Insolvency Law and its application to the new Chinese bankruptcy law. Finally, Part V discusses the implications of these comparisons, focusing on improvements of the new law over China's prior bankruptcy law, issues raised by the Legislative Guide comparison, and general areas of concern with China's new bankruptcy law.

II. The History of Bankruptcy Law in China

Bankruptcy law in China was first enacted in 1906 during the Qing Dynasty.⁶ However, the Chinese cultural tradition of non-forgiveness of debts⁷ made the early attempts at bankruptcy law relatively unsuccessful.⁸ Additional attempts to enact bankruptcy legislation in China occurred in 1915 and 1935,⁹ before the rise to power of the Communist Party and the abolition of all pre-existing laws in 1949.¹⁰ The issue of bankruptcy was largely ignored in China until the early 1980s when three articles by Chinese legal scholars led the government to undertake the development of a bankruptcy law appropriate for China.¹¹

amendments to the bankruptcy laws of France, Japan and Korea in recent years. *See id.* at n.1.

6. *See* Feng Chen, *Forward: Chinese Bankruptcy Law: Milestones and Challenges*, 31 ST. MARY'S L.J. 49 (1999); Li Shuguang, *Bankruptcy Law in China: Lessons of the Past Twelve Years*, HARV. ASIA Q., Winter 2001, available at http://www.leggicinesi.it/dottrina/LiShuguang_Bankruptcy.pdf. Both of these articles provide a detailed and very interesting overview of the history of bankruptcy law in China.

7. According to Chinese tradition, "debts incurred by the father shall be assumed by the son." Will Fung, *Policy-Oriented vs. Market-Oriented Bankruptcy: A Tour on the PRC New Enterprise Bankruptcy Law*, 3 CHINA L. REP. 7 (2007), available at <http://meetings.abanet.org/webupload/commupload/IC860000/newsletterpubs/Jan07 CLR.pdf>. In feudal Chinese society, this concept was extended to a grandson, making him responsible for his grandfather's debt or obligation even before he was born. *See* Roman Tomasic & Margaret Wang, *The Long March Towards China's New Bankruptcy Law*, in *INSOLVENCY LAW IN EAST ASIA* 93, 94 (Roman Tomasic ed., 2006).

8. *See Euthanasia For Companies: Chinese Bankruptcy*, *ECONOMIST*, June 2, 2007.

9. *See* Shuguang, *supra* note 6; Tomasic & Wang, *supra* note 7, at 94.

10. *See* Chen, *supra* note 6, at 50.

11. *See id.* at 51.

The result of this process was the enactment of the 1986 Enterprise Bankruptcy Law, which took effect on December 2, 1986.¹² The law was limited, however, in that it applied only to State-owned enterprises, whose debt was largely owed to State-owned banks.¹³ Indeed, one source reports that between the years of 1989 and 1994, Chinese courts accepted only 675 bankruptcy cases.¹⁴ In 1991, the National People's Congress amended Chapter 19 of China's Code of Civil Procedure, providing for a direct basis for handling bankruptcies of non-State-owned enterprises using the repayment procedures specified in the 1986 Enterprise Bankruptcy Law.¹⁵

Bankruptcy law in China was further complicated by judicial interpretations of the Supreme People's Court,¹⁶ regulations governing foreign invested enterprises,¹⁷ administrative regulations issued by the State Council,¹⁸ and local regulations issued by various provinces and municipalities.¹⁹ These multiple layers of bankruptcy law, along with the

12. For an English language translation, see Douglas G. Boshkoff & Yongxin Song, *China's New Bankruptcy Law: A Translation and Brief Introduction*, 61 AM. BANKR. L.J. 359 (1987).

13. See Fung, *supra* note 7.

14. See *id.* at 9.

15. See Shuguang, *supra* note 6; Civil Procedure Law (promulgated by the Standing Comm. Nat'l People's Cong., Apr. 9, 1991, effective Apr. 9, 1991, amended Oct. 28, 2007), ch. XVIII, arts. 199-206 (Procedures for the Bankruptcy and Debt Repayment by Enterprise Legal Persons) (P.R.C.), available at 2007 China Law LEXIS 1904; see also The Company Law (promulgated by the Standing Comm. Nat'l People's Cong., Dec. 29, 1993, effective Dec. 29, 1993, amended Oct. 27, 2005), ch. X, arts. 181-91 (Dissolution and Liquidation of a Company) (P.R.C.), available at 2005 China Law LEXIS 9816 (providing for dissolution and liquidation of a company under specified circumstances).

16. See James H.M. Sprayregen & Jonathan P. Friedland, *The Middle Kingdom's Chapter 11? China's New Bankruptcy Law Comes Into Sight*, 23-10 AM. BANKR. INST. J. 34 (2005); People's Supreme Court, Opinions on Several Issues on the Implementation of the Enterprise Bankruptcy Law of the PRC (for Trial Implementation), 7 November 1991.

17. See Sprayregen & Friedland, *supra* note 16; Measures on Liquidation Procedures for Foreign Investment Enterprises Liquidation Measures (promulgated by the Ministry of Foreign Trade & Econ. Coop., July 9, 1996) (P.R.C.), available at <http://sk2.mofcom.gov.cn/aarticle/chinalaw/investment/200507/20050700176146.html>.

18. See Sprayregen & Friedland, *supra* note 16; State Council Notice on Relevant Issues Relating to the Trial Implementation of Bankruptcy of SOEs in Several Cities (Guofa [1994] No. 59), Oct. 25, 1994; see also State Council Supplemental Notice on Relevant Issues Relating to the Trial Implementation of Bankruptcy, Merger and Acquisition of SOEs in Selected Cities and Employment of Unemployed Workers (Guofa [1997] No. 10).

19. See Sprayregen & Friedland, *supra* note 16; Regulations of Shenzhen Special Economic Zone on Corporate Bankruptcy (promulgated by the Standing Committee of the Second Shenzhen Municipal People's Congress, Nov. 10, 1993, effective March 1, 1994) (P.R.C.), available at <http://www.asianlii.org/cn/legis/gd/laws/rossezocb673>. See also, Xian Chu Zhang & Charles D. Booth, *Chinese Bankruptcy Law in an Emerging Market Economy: The Shenzhen Experience*, 15 COLUM. J. ASIAN L. 1 (2001) (providing

lack of clear guidelines as to enforcement of the bankruptcy law, and combined with a lack of transparency, created a bankruptcy system in China that has been widely criticized as inconsistent and unworkable.²⁰

III. The New Corporate Bankruptcy Law and Comparison to U.S. Bankruptcy Provisions

According to the language of the Corporate Bankruptcy Law, China's new bankruptcy law was "formulated in order to regulate the procedure of corporate bankruptcy, to wind up debts and indebtedness fairly, to protect the legitimate rights and interests of creditors and debtors and to maintain the order of the socialist market economy."²¹ The following is an overview of the provisions of China's new bankruptcy law, with comparisons to U.S. bankruptcy law where appropriate.

A. *The Scope of the New Law*

China's new bankruptcy law applies broadly to all types of business enterprises, including most State-owned²² and non-State-owned enterprises.²³ While reports on early drafts of the new law suggested that partnerships and sole-proprietorships would be excluded,²⁴ both are included under the final version of the law.²⁵ However, these entities are not considered to have "legal person status" and therefore cannot be reorganized; their remedy under the new law is limited to liquidation.²⁶ Likewise, while earlier drafts of the bankruptcy law excluded the bankruptcy and reorganization of financial institutions, such as banks, brokerage firms and insurance companies, the final legislation makes no such differentiation and treats these firms like other business enterprises.²⁷

a comparison of China's national bankruptcy law with the bankruptcy law of the province of Shenzhen).

20. See Sprayregen & Friedland, *supra* note 16; Weijing Wu, *Commencement of Bankruptcy Proceedings in China: Key Issues in the Proposed New Enterprise Bankruptcy and Reorganization Law*, 35 VICT. U. WELLINGTON L. REV. 239, 241 (2004).

21. Corporate Bankruptcy Law, *supra* note 2, art. 1.

22. Excluded from the scope of the new bankruptcy law are approximately 2000 State-owned enterprises designated by the State Council. See Sprayregen & Friedland, *supra* note 16, at n.18. These are primarily business entities engaged in military or mining operations. See *id.*

23. The new Chinese bankruptcy law applies to all "[c]orporate legal persons." Corporate Bankruptcy Law, *supra* note 2, art. 2.

24. See Aleksandrs Rozens, *A Cultural Revolution?*, DAILY DEAL, Aug. 31, 2006.

25. See Sprayregen & Friedland, *supra* note 16, at 60.

26. See *id.*

27. See vom Eigen, *supra* note 5, at 8.

B. *Criteria for and Effects of Bankruptcy Filing*

China's new bankruptcy law provides for a voluntary bankruptcy filing by the debtor or an involuntary bankruptcy filing by a creditor through an application to the People's Court²⁸ in the place of residence of the debtor.²⁹ In order to be eligible to file for bankruptcy under the new law a business entity must either be unable to repay debts that fall due and have insufficient assets to repay those debts in full, or a business entity must be clearly insolvent.³⁰ A debtor meeting those basic filing criteria may submit a bankruptcy application to the People's Court.³¹ The standard applicable to an involuntary filing by a creditor, however, is lower than for a debtor filing: a creditor need merely show that the debtor is unable to repay the debtor's debt.³²

The new bankruptcy law provides three different types of bankruptcy proceedings: reorganization, settlement, and liquidation.³³ All three types of bankruptcy proceedings are available to a debtor filing for voluntary bankruptcy protection;³⁴ however, only reorganization and liquidation proceedings are available to a creditor filing in an involuntary proceeding.³⁵

The criteria set forth for voluntary and involuntary filings in the Chinese bankruptcy law are in contrast to the distinct lack of insolvency criteria under U.S. law. Indeed, under U.S. law, no particular degree of financial distress is required to seek bankruptcy protection, nor is there any requirement of proving insolvency in order to file for voluntary bankruptcy in the U.S.³⁶ Thus, while the scope of companies covered by the new bankruptcy law in China is quite broad, the eligibility criteria for filing for bankruptcy in China is more limited than in the United States.

One significant difference between the bankruptcy proceedings under the new Chinese bankruptcy law and the U.S. bankruptcy law is the effect of filing the bankruptcy case. Under U.S. bankruptcy law, the filing of the bankruptcy petition has significant legal effects. Specifically, the filing of the bankruptcy petition triggers an automatic stay that prohibits, among other things, the commencement or

28. See Corporate Bankruptcy Law, *supra* note 2, art. 7.

29. See *id.* art. 3.

30. See *id.* art. 2. The new Chinese bankruptcy law does not, however, explicitly define the term "insolvent." See *infra* notes 418-24 and accompanying text.

31. See Corporate Bankruptcy Law, *supra* note 2, art. 7.

32. See *id.*

33. See *id.*; see also *infra* notes 125-54 and accompanying text.

34. See Corporate Bankruptcy Law, *supra* note 2, art. 7.

35. See *id.*

36. See *In re Johns-Manville Corp.*, 36 B.R. 727 (Bankr. S.D.N.Y. 1984); *In re Century City, Inc.*, 8 B.R. 25, 31 (Bankr. D.N.J. 1980); *In re Int'l Oriental Rug Ctr.*, 165 B.R. 436 (Bankr. N.D. Ill. 1994).

continuation of judicial or administrative proceedings against the debtor,³⁷ enforcement of any judgment against the debtor or his property,³⁸ any act to obtain possession of the debtor's property,³⁹ and any act to create, perfect or enforce any lien against the debtor's property.⁴⁰ The purpose of the automatic stay is to preserve the status quo of the bankruptcy estate as of the date of the filing⁴¹ and to give the debtor a "breathing spell" from its creditors.⁴² It is also designed to allow a debtor an opportunity to reorganize so that creditors' claims can be satisfied to the greatest extent possible.⁴³ The automatic stay may also prevent a chaotic scramble for the debtor's assets in a variety of uncoordinated proceedings in different courts.⁴⁴ However, even with these safeguards in place for the debtor, a creditor may apply to the bankruptcy court for relief from the automatic stay to allow enforcement proceedings against the debtor or the debtor's property.⁴⁵

Under the new Chinese bankruptcy law, the filing of an application for bankruptcy with the People's Court begins a fifteen day review period during which the court decides whether to accept or reject the filing.⁴⁶ When the application for bankruptcy is made by a creditor, the debtor is notified within five days of the filing and has seven days to contest the filing.⁴⁷ Once the bankruptcy application (whether filed by the debtor or creditor) is accepted by the court, the debtor and all known creditors are notified of the ruling.⁴⁸ However, unlike U.S. bankruptcy

37. See 11 U.S.C. § 362(a)(1) (2006).

38. See *id.* § 362(a)(2).

39. See *id.* § 362(a)(3).

40. See *id.* § 362(a)(4).

41. See *Interstate Commerce Comm'n v. Holmes Transp., Inc.*, 931 F.2d 984, 987 (1st Cir. 1991); *H & H Beverage Distrib. v. Dep't of Revenue*, 850 F.2d 165, 166 (3d Cir. 1988), *cert. denied*, 488 U.S. 994 (1988).

42. See *H & H Beverage Distrib.*, 850 F.2d at 166; *In re Ahlers*, 794 F.2d 388, 393 (8th Cir. 1986), *rev'd on other grounds and remanded*, 485 U.S. 197 (1988), *vacated on other grounds and remanded*, 844 F.2d 587 (8th Cir. 1988); *United States v. Dos Cabezas Corp.*, 995 F.2d 1486, 1491 (9th Cir. 1993); *In re Zinchiak*, 406 F.3d 214, 219 n.2 (3d Cir. 2005); *In re Dawson*, 390 F.3d 1139, 1147 (9th Cir. 2004), *cert. denied*, 126 S.Ct. 397 (2005).

43. See *In re Dawson*, 390 F.3d at 1147; *In re Enron Corp.*, 300 B.R. 201, 211 (Bankr. S.D.N.Y. 2003).

44. See *Farley v. Henson*, 2 F.3d 273 (8th Cir. 1993).

45. See 11 U.S.C. § 362(d)-(g) (2006).

46. The law refers to this decision as "taking cognizance of a bankruptcy application." *Corporate Bankruptcy Law*, *supra* note 2, arts. 10-11.

47. See *id.* art. 10.

48. See *id.* arts. 10, 14. The notification to creditors of acceptance of the bankruptcy filing by the court must include the name of the applicant and the person whose bankruptcy is prayed for, the time when the court took cognizance of the bankruptcy application, the deadline and place for declaring a debt, the name and business handling address of receiver, a statement that debtor(s) of the debtor or person(s) holding debtor's property shall repay debt to receiver or meet receiver's demand for delivery of property,

law, under which the filing for bankruptcy protection triggers an automatic stay of most proceedings and other actions by creditors against the debtor,⁴⁹ under China's new bankruptcy law the acceptance of the bankruptcy application is the triggering event for the automatic stay of creditors' actions against the debtor,⁵⁰ as well as a stay of execution proceedings against assets of the debtor's estate.⁵¹ Moreover, the automatic stay does not prevent continuation of litigation against the debtor indefinitely; it only applies until a receiver is appointed to manage the debtor's property.⁵² In addition, new civil suits can be filed against the debtor even after the bankruptcy is commenced, but only in the People's Court that has jurisdiction over the debtor's bankruptcy proceeding.⁵³ Thus, the protection offered to the debtor under the new bankruptcy law is significantly weaker than the protection a debtor receives under U.S. law.

Once the People's Court accepts the bankruptcy application, all property belonging to the debtor and all property obtained by the debtor thereafter becomes property of the bankruptcy estate and subject to the jurisdiction of the court.⁵⁴ Thereafter, any repayment by the debtor to an individual creditor is invalid.⁵⁵

C. *Participants in Bankruptcy Proceedings*

1. The Debtor

The debtor in a proceeding under the Corporate Bankruptcy Law is assigned a series of responsibilities designed to maintain the status quo and preserve the bankruptcy estate.⁵⁶ Specifically, between the time the debtor is notified that the court has taken cognizance of the bankruptcy proceedings and the conclusion of those proceedings, the related persons⁵⁷ of the debtor have a series of obligations, including the obligation to keep the debtor's property, seals and stamps, books of

the time and place of first creditors' meeting, and other matters of which, in the opinion of the court, creditors should be notified. *See id.* art. 14.

49. *See* 11 U.S.C. § 362 (2006).

50. *See* Corporate Bankruptcy Law, *supra* note 2, arts. 19, 20.

51. *See id.* art. 19.

52. *See id.* art. 20.

53. *See id.*

54. *See id.* art. 30.

55. *See* Corporate Bankruptcy Law, *supra* note 2, art. 16.

56. *See id.* art. 15.

57. The term "related persons" means the legal representative of the debtor, and may include the financial management personnel and other operation management personnel of the debtor. *See id.*

accounts and other documents in their possession and under their management;⁵⁸ to carry out work according to the demands of the People's Court and the receiver and to reply truthfully to questions and enquiries;⁵⁹ to be present at creditors' meetings and reply truthfully to creditors' questions and enquiries;⁶⁰ to not leave their place of residence without consent of the court;⁶¹ and to not take up any new appointments as directors, supervisors or senior management personnel of other enterprises.⁶² In a reorganization proceeding under the new law, the debtor may apply to manage its property and business operations during the reorganization period under the supervision and monitoring of the receiver.⁶³

2. The Creditors

China's new bankruptcy law contemplates that all creditors of the debtor will have a voice in the bankruptcy proceedings.⁶⁴ Specifically, the bankruptcy law provides that all creditors whose debt is confirmed have the right to attend creditors' meetings and vote.⁶⁵ At a creditors' meeting, creditors have the right and duty to examine and verify debts; to apply to the court for the replacement of the receiver and audit the expenses and remuneration of the receiver; to monitor and supervise the receiver; to elect, appoint and replace members of the creditors' committee; to decide on continuation or cessation of the business of the debtor; to pass and adopt a plan or rectification; to pass and adopt settlement agreements; to pass and adopt the scheme for the management of the property and estate of the debtor; to pass and adopt the scheme for conversion of prices or value of the debtor's property and estate in bankruptcy; to pass and adopt the scheme for distribution of the debtor's property in the bankruptcy; and to exercise other duties and powers that, in the opinion of the court, should be performed and exercised at the creditors' meetings.⁶⁶

China's new bankruptcy law also provides for the creation of a creditors' committee to be established in a meeting of all of the creditors who have declared their debts with the People's Court.⁶⁷ The creditors'

58. *See id.* art. 15(1).

59. *See id.* art. 15(2).

60. *See Corporate Bankruptcy Law, supra* note 2, art. 15(3).

61. *See id.* art. 15(4).

62. *See id.* art. 15(5).

63. *See id.* art. 73.

64. *See id.* art. 59.

65. *See Corporate Bankruptcy Law, supra* note 2, art. 59.

66. *See id.* art. 61.

67. *See id.* art. 67; *see id.* arts. 44-58 (summarizing the procedures applicable to the declaration of debts by creditors).

committee cannot have more than nine members and those members must be elected and appointed by, and include, representatives from the creditors themselves and a staff member or representative from the workers' union of the debtor.⁶⁸ The creditors' committee has general powers to monitor and supervise the management of the debtor's property and the distribution of the property of the debtor's bankruptcy estate.⁶⁹ The creditors' committee is required to be notified of significant distributions of the debtor's property, transfers of debts and securities of value from the debtor's property, borrowing and guarantees by the debtor, and other significant events.⁷⁰

These provisions regarding debtors' and creditors' committees are similar in nature to the provisions under U.S. bankruptcy law requiring the establishment of creditors' committees for unsecured creditors and, if the U.S. trustee deems it appropriate, for other creditors as well.⁷¹

3. The Receiver

One of the more important changes under the new Chinese bankruptcy law relates to the appointment of a receiver to manage the debtor's property.⁷² Under the former Chinese bankruptcy law, the liquidation⁷³ of a debtor's assets was carried out under the supervision of a liquidation team, which often included appointees of the local government where the debtor was located.⁷⁴ The result was often a form of local protectionism.⁷⁵ Moreover, under the former bankruptcy law, the liquidation team was not appointed when the court accepted the case, but rather within fifteen days after the court made the adjudication order.⁷⁶ During this potentially long period, there were no supervisors to prevent existing management from misappropriating or mismanaging the debtor's property and assets.⁷⁷

In contrast, under the new Chinese bankruptcy law, the court appoints a professional and independent administrator with broad powers

68. *See id.* art. 67.

69. *See id.* art. 68.

70. *See* Corporate Bankruptcy Law, *supra* note 2, art. 69.

71. *See* 11 U.S.C. §§ 1101-1103 (2006).

72. *See* Corporate Bankruptcy Law, *supra* note 2, arts. 22, 25.

73. Under the former bankruptcy law in China, liquidation was the only form of proceeding available. *See* Sprayregen & Friedland, *supra* note 16, at 60. The new law adds settlement and reorganization options. *See id.*

74. *See id.*

75. *See id.*

76. *See* Charles Booth, *Drafting Bankruptcy Laws in Socialist Market Economies: Recent Developments in China and Vietnam*, 18 COLUM. J. ASIAN L. 93, 116 (2004).

77. *See id.*

to manage the debtor's property and business affairs.⁷⁸ The receiver must be appointed from a list of qualified agencies drawn up by the People's Court, which "include legal and accounting firms and agencies in charge of liquidation."⁷⁹ However, an agency cannot be appointed as receiver if it has an interest in the bankruptcy case or there are other circumstances which make the court believe the agency is not suitable to act as receiver.⁸⁰

Under the new Chinese bankruptcy law the receiver is compensated according to the total value of distributable property of the bankrupt debtor, rather than based on hours worked,⁸¹ in order to encourage the receiver to recover more property of the bankrupt company and further protect the rights of creditors.⁸² In addition, the receiver's compensation and expenses are part of the costs and expenses of the bankruptcy proceeding which receive priority payment status.⁸³

In terms of duties of the receiver, the receiver has the right to decide day-to-day expenses and other necessary expenses of the debtor and the right to manage, distribute and dispose of the property of the debtor's estate.⁸⁴ The receiver also has the right to recover improperly transferred property of the debtor's estate.⁸⁵ Specifically, the receiver has the right to request that the court nullify transactions regarding the debtor's assets committed within one year before the court takes cognizance of the bankruptcy if those transactions involve transfers of property without compensation, transactions at a clearly unreasonable price, provisions of guarantees for debt without property, repayment of debts not yet due, or

78. See Corporate Bankruptcy Law, *supra* note 2, arts. 22, 25. The receiver is required to take over the property, books and records of the debtor; investigate and report on the debtor's property; manage the affairs and day-to-day expenses of the debtor; manage, distribute and dispose of the property of the debtor, and represent the debtor in legal proceedings. See *id.* art. 25.

79. *China Issues Regulation on Selection of Trustees in Bankruptcy*, BUS. CREDIT, June 1, 2007, at 56. See Provisions of the Supreme People's Court on the Designation of Administrators during the Trial of Enterprise Bankruptcy Cases (promulgated by the Supreme People's Court, Apr. 12, 2007, effective June 1, 2007), available at <http://www.lawinfochina.com/Law/display.asp?id=6018&keyword=> (last visited July 28, 2008).

80. See Corporate Bankruptcy Law, *supra* note 2, art. 24(3)-(4).

81. See *China Issues Regulation on Selection of Trustees in Bankruptcy*, *supra* note 79. One commentator suggested that with the new law, "bankruptcy administration will emerge as a new profession in China." Booth, *supra* note 76, at 120 (quoting Wang Weiguo, *Administrator in New Bankruptcy Law in China*, 4 Presentation at the Forum on Agency Reform 2004, available at http://www.iiiiglobal.org/country/china/Administrator_in_new_BL.pdf).

82. See *China Issues Regulation on Selection of Trustees in Bankruptcy*, *supra* note 79.

83. See Corporate Bankruptcy Law, *supra* note 2, art. 41.

84. See *id.* art. 25(4), (6).

85. See *id.* art. 34.

abandonment of debt.⁸⁶ The receiver may also petition the court to nullify any repayment to an individual creditor made within six months before the court takes cognizance of the bankruptcy proceeding while the debtor was insolvent, except where the payment benefits the debtor's property and the bankruptcy estate.⁸⁷ Finally, any action to conceal and transfer the debtor's property for the purpose of evasion of indebtedness, as well as for the purpose of fabrication of indebtedness or admitting false indebtedness, shall be declared invalid.⁸⁸ In each of the above cases, the receiver has the power to recover the debtor's property obtained by such acts.⁸⁹

Failure to carry out the receiver's duties has significant consequences. First, creditors may apply to the People's Court to replace the receiver if the receiver is unable to carry out his duties or if there are circumstances "unbecoming" of the receiver's duties.⁹⁰ Further, if the receiver is not diligent, fully responsible, truthful and honest in performing his or her duties, a fine and civil liability may be imposed.⁹¹

The general structure of the provisions governing the appointment and activities of the receiver under the new Chinese bankruptcy law is similar to the concept of the trustee under U.S. bankruptcy law. Under U.S. law, trustees are appointed or elected in Chapter 7 liquidation cases,⁹² and may be appointed or elected in Chapter 11 reorganization cases.⁹³ In order to be eligible to serve as a trustee in a U.S. bankruptcy proceeding, an individual must be "competent to perform the duties of trustee"⁹⁴ and reside or have an office in the judicial district in which the bankruptcy case is pending.⁹⁵ The trustee has numerous specific powers, rights and duties under the U.S. Bankruptcy law.⁹⁶ In general, the trustee serves as the representative of the bankruptcy estate⁹⁷ and may sue or be sued on behalf of the estate.⁹⁸ More specifically, the trustee may operate

86. *See id.* art. 31.

87. *See id.* art. 32.

88. *See* Corporate Bankruptcy Law, *supra* note 2, art. 33.

89. *See id.* art. 34.

90. *See id.* art. 22.

91. *See id.* art. 130.

92. *See* 11 U.S.C. §§ 701-704 (2006).

93. *See id.* § 1104.

94. *Id.* § 321(a)(1).

95. *Id.* § 321(a).

96. *See, e.g., id.* § 704 (duties of Trustee in Chapter 7 liquidation); *id.* § 1106 (duties of Trustee in Chapter 11 reorganization).

97. *See* 11 U.S.C. § 323(a) (2006).

98. *See id.* § 323(b).

the debtor's business,⁹⁹ subject to the debtor's right to act as a debtor-in-possession in a Chapter 11 reorganization proceeding.¹⁰⁰

D. Management of Bankruptcy Proceedings and Priorities of Claims

1. Submission of Claims

The new Chinese bankruptcy law specifies the procedure to be used by creditors in submitting claims in the bankruptcy procedure.¹⁰¹ The new law's provisions on declaration of debts apply to all creditors who enjoy the debts of the debtor.¹⁰² Once the court takes cognizance of the bankruptcy proceeding, the court determines the time limit in which creditors must declare their debts.¹⁰³ The time limit to declare debts must be between thirty days and three months¹⁰⁴ and creditors must declare their debts within the time limit specified.¹⁰⁵ Creditors must specify in writing the amount of their debts and whether those debts are secured by property, and debts must be supported by relevant evidence.¹⁰⁶ If a creditor fails to declare its debt within the specified time limit, the creditor may make a late declaration before the final distribution of the bankruptcy estate; however, the creditor will not be given any supplementary distribution for earlier distributions already made, and the costs and expenses of examining and confirming the late filing will be the responsibility of the creditor.¹⁰⁷ Moreover, a creditor who fails to declare its debt will not be allowed to exercise the rights of a creditor.¹⁰⁸

Once the declaration of debts is received by the bankruptcy receiver, the receiver is required to keep records of the declarations, scrutinize the debts declared and prepare a statement of debts¹⁰⁹ to be presented at the first creditors' meeting for examination and verification.¹¹⁰ The debtor or creditors may bring suit in the People's Court if either the debtor or creditors disagree with the debts recorded in the statement of debts presented by the receiver.¹¹¹

99. *See id.* §§ 721, 1108.

100. *See infra* notes 137-39 and accompanying text.

101. *See* Corporate Bankruptcy Law, *supra* note 2, arts. 44-58.

102. *See id.* art. 44.

103. *See id.* art. 45.

104. *See id.*

105. *See id.* at 48.

106. *See* Corporate Bankruptcy Law, *supra* note 2, art. 49.

107. *See id.* art. 56.

108. *See id.* art. 56.

109. *See id.* art. 57.

110. *See id.* art. 58.

111. *See* Corporate Bankruptcy Law, *supra* note 2, art. 58.

2. Priorities of Claims in Bankruptcy

One area in which the new Chinese bankruptcy law makes significant improvements over the former Chinese bankruptcy law is in the prioritization of claims in bankruptcy. Under China's former law, employee claims took priority over the claims of secured creditors.¹¹² Thus, employee claims could be satisfied out of a secured creditor's collateral if there were insufficient unsecured assets available to satisfy employees' claims.¹¹³ Under China's new bankruptcy law, claims of creditors holding the equivalent of a security interest in a specific property generally receive first priority to be repaid against that specific piece of property.¹¹⁴ Bankruptcy costs and expenses, consisting of expenses for litigation of the bankruptcy estate; expenses for managing and disposing of the debtor's property; and fees and expenses of the receiver,¹¹⁵ and debts for the common benefit, including debts for contracts entered into by the receiver; debts incurred by management without cause; debts incurred as a result of unjust benefit to the debtor; and costs for personal injury caused by the receiver or the property and estate of the debtor,¹¹⁶ all receive next priority.¹¹⁷ Wages and other funds owed to staff and employees receive next priority, followed by other social insurance expenses owed by the debtor, and, finally, ordinary unsecured debts.¹¹⁸ Where there are insufficient assets to repay the creditors' claims in full within each preference category, the claims are paid pro rata.¹¹⁹

The change in bankruptcy preferences from employees to secured creditors was one of the primary reasons for the long delay in the development and implementation of the new Chinese bankruptcy law.¹²⁰ The term "iron rice bowl" was often used to describe the system of lifelong employment common among State workers in China,¹²¹ and the

112. See John Rapisardi & Deryck Palmer, *Precedent Needed*, 26 INT'L FIN. L. REV. 4 (2007); vom Eigen, *supra* note 5.

113. See Rapisardi & Palmer, *supra* note 112.

114. See Corporate Bankruptcy Law, *supra* note 2, art. 109; Dexter Roberts, *China's New Mantra: Creditors First*, BUS. WK. ONLINE, Aug. 31, 2006, available at http://www.businessweek.com/globalbiz/content/aug2006/gb20060830_421789.htm.

115. See Corporate Bankruptcy Law, *supra* note 2, art. 41.

116. See *id.* art. 42.

117. See *id.* art. 113.

118. See *id.*

119. See *id.*

120. See Rapisardi & Palmer, *supra* note 112.

121. This lifelong employment policy is considered by the government to be the cornerstone of socialism and its guarantee is written into the Chinese Constitution. See Shirley S. Cho, *Continuing Economic Reform*, 19 HASTINGS INT'L & COMP. L. REV. 739, 743-44 (1996).

idea that workers would have a lower priority than creditors in a bankruptcy proceeding was previously unthinkable.¹²² In order to pass the change in bankruptcy preferences a compromise was reached under which a limited but significant exception was included in the new law.¹²³ This exception provides that wages and medical payments and debts for medical, retirement and insurance expenses for employees of the bankrupt entity that were owed before August 27, 2006 receive priority treatment over the secured creditors of the debtor.¹²⁴ With this limited exception, the change in priorities was finally passed and included in the final version of the new bankruptcy law.

E. Types of Bankruptcy Proceedings

China's new bankruptcy law provides for three types of bankruptcy proceedings: liquidation, reorganization and settlement.¹²⁵ All three options are available for a voluntary bankruptcy filed by a debtor; only liquidation and reorganization are available for an involuntary bankruptcy filed by a creditor.¹²⁶ The liquidation provisions are relatively straight-forward, providing for a priority repayment right for secured lenders.¹²⁷ The priority for secured lenders is followed by preferences for wages and other benefits owed to the staff and workers of the bankrupt entity, social insurance expenses owed by the bankrupt entity, and, finally, payments for ordinary unsecured debts.¹²⁸ Payments are made pro-rata within each category of preference.¹²⁹

The settlement proceedings allow a debtor to propose a draft settlement agreement with its creditors.¹³⁰ In order to be adopted, the settlement must be accepted by a majority of the creditors attending a meeting of the creditors, so long as the debt represented by such creditors exceeds two-thirds of the total unsecured debt of the debtor.¹³¹ Once an

122. See Shuguang, *supra* note 6. For a general discussion of the "iron rice bowl" and its transformation in recent years, see Jaeyoun Won, *Withering Away of the Iron Rice Bowl? The Reemployment Project of Post-Socialist China*, 39 *STUD. IN COMP. INT'L DEV.* 71 (2004); Ho-lup Fung, *The Making and Melting of the "Iron Rice Bowl" in China 1949 to 1995*, 35 *SOC. POL'Y & ADMIN.* 258 (2001).

123. See Rapisardi & Palmer, *supra* note 112.

124. See Corporate Bankruptcy Law, *supra* note 2, art. 132.

125. See *id.* art. 7.

126. See *id.*

127. See *id.* art. 109.

128. See *id.* art. 113.

129. See Corporate Bankruptcy Law, *supra* note 2, art. 113.

130. See *id.* art. 95.

131. See *id.* art. 97.

agreement is recognized by the People's Court, it is binding upon both the debtor and all creditors.¹³²

Perhaps the most important feature of the new Chinese bankruptcy law is the addition of provisions allowing for reorganization proceedings.¹³³ Under current bankruptcy theory, reorganizations are considered to be a very valuable alternative to liquidation.¹³⁴ Reorganization is also considered consistent with prevailing international practice.¹³⁵

As discussed above,¹³⁶ under the new Chinese bankruptcy law the debtor may apply to manage its property and business operations during the reorganization period under the supervision and monitoring of the receiver.¹³⁷ This provision is similar to the U.S. concept of a "debtor-in-possession," under which the debtor is allowed to continue in possession of its property and current management is allowed to continue to manage the debtor's affairs.¹³⁸ The U.S. debtor-in-possession has all the rights of a bankruptcy trustee, including the power to continue operations of the debtor's business.¹³⁹

During reorganization proceedings the automatic stay limits the continuation of legal actions against the debtor.¹⁴⁰ The stay includes a suspension of the exercise of security rights by secured creditors against specific property of the debtor.¹⁴¹ However, the new law does provide an exception under which a secured creditor may apply to the People's Court to restore the exercise of security rights where the security may be damaged or its value clearly diminished, resulting in "jeopardy to the rights of the security rights holders."¹⁴² During reorganization proceedings the debtor or receiver may also borrow funds for continuing the debtor's business and may set up guarantees for such a loan.¹⁴³

132. *See id.* art. 100.

133. *See id.* arts. 70-94.

134. *See* Wu, *supra* note 20, at 249.

135. *See id.* (citing Weiguo Wang, Institutional Reasoning in Drafting New Bankruptcy Law of China, Chinese Insolvency Law Symposium: Developing an Insolvency Infrastructure, Hong Kong (Nov. 17-18, 2000), *available at* <http://law.hku.hk/aiifl/events/symposium/papers/wang%20weigu.doc>).

136. *See supra* notes 84-89 and accompanying text.

137. *See* Corporate Bankruptcy Law, *supra* note 2, art. 73.

138. *See* 11 U.S.C. § 1101(1) (2006); *In re* La Sherene, Inc., 3 B.R. 169, 174 (Bankr. N.D. Ga. 1980).

139. 11 U.S.C. § 1107(a) (2006); *see generally* Matter of FSC Corp., 38 B.R. 346, 350 (W.D. Pa. 1983).

140. *See supra* notes 46-53 and accompanying text.

141. *See* Corporate Bankruptcy Law, *supra* note 2, art. 75.

142. *Id.*

143. *See id.*

The reorganization proceedings may be terminated by the People's Court and the debtor declared bankrupt in the event of continued deterioration in the debtor's operation and financial condition with little prospect of recovery, the debtor's fraudulent transfer of assets from the bankruptcy estate, or the debtor's engaging in acts that prevent the receiver from carrying out his duties.¹⁴⁴

The reorganization provisions in the new Chinese bankruptcy law anticipate that either the debtor or the receiver¹⁴⁵ (whichever is operating the debtor's property and business operations)¹⁴⁶ will propose a draft reorganization plan within six months, with a possible three-month extension available from the People's Court.¹⁴⁷ The reorganization plan must include the debtor's business plan, a classification of debts, a debt adjustment scheme, a debt repayment scheme, a time limit for execution of the reorganization plan, a time limit for monitoring and supervision of the execution of the reorganization plan, and other schemes beneficial to the debtor's reorganization.¹⁴⁸ Debts are classified into four categories: secured debts, employee wages and benefits, tax debts, and ordinary unsecured debts.¹⁴⁹ If the reorganization plan is accepted by a majority of each group of creditors representing more than two-thirds of the debts in each category of debt, the reorganization plan will be deemed passed and adopted,¹⁵⁰ subject to the approval of the People's Court.¹⁵¹ Where one or more groups of creditors does not approve the reorganization plan, the People's Court may still approve the reorganization plan if three conditions are met: the debts owed to secured creditors and debts for wages and benefits for employees' retirement and medical expenses must be repaid in full; the repayment ratio for unsecured creditors cannot be lower than would be obtainable in a bankruptcy liquidation proceeding; and the business plan of the debtor must be practicable.¹⁵² Once the reorganization plan is approved by the People's Court, the debtor takes over its business operations in accordance with the plan,¹⁵³ subject to monitoring and supervision by the receiver.¹⁵⁴

144. *See id.* art. 78.

145. One criticism of earlier drafts of the new law was that it did not include the right of creditors to propose competing plans. Sprayregen & Friedland, *supra* note 16, at 60. The final version of the new law also did not include such a provision.

146. *See* Corporate Bankruptcy Law, *supra* note 2, art. 80.

147. *See id.* art. 79.

148. *See id.* art. 81.

149. *See id.* art. 82.

150. *See id.* art. 84.

151. *See* Corporate Bankruptcy Law, *supra* note 2, art. 86.

152. *See id.* art. 87.

153. *See id.* art. 89.

154. *See id.* art. 90.

F. Other Provisions of Interest

1. Legal Liability

One very interesting provision of the new Chinese bankruptcy law is Chapter 11 which deals with legal liability.¹⁵⁵ Indeed, the new law provides a number of provisions regarding legal liability that should be noted. First, the new law provides that the court shall “protect the legitimate rights and interests of the staff and workers of the enterprises involved” and “investigate the legal liability of the operation and management personnel of the bankrupt enterprises in accordance with the law.”¹⁵⁶

Second, the new law provides that the directors, supervisors and senior management personnel who are “in breach of their obligations for being truthful, honest, diligent and responsible”¹⁵⁷ and who cause the enterprise to become bankrupt, bear civil liability and are prohibited from serving in such a role in any enterprise for three years from the conclusion of the bankruptcy proceedings.¹⁵⁸ Fines may be imposed on the debtor’s personnel who fail to attend required meetings,¹⁵⁹ and on the debtor where the debtor fails to submit or submits untrue statements, inventories of indebtedness or debt, and relevant financial reports, or refuses to deliver property, books of accounts and records to the receiver.¹⁶⁰ Finally, where a debtor engages in fraudulent conveyances, sales of assets for less than full value, early repayment or abandonment of debts, or the concealment or misrepresentation of debts, “the debtor’s legal representative and other directly responsible personnel”¹⁶¹ are subject to civil liability for compensation.¹⁶² These provisions are in addition to any criminal liability that might be imposed for criminal offenses.¹⁶³ Thus, the new law includes the significant possibility of civil liability for managers of bankrupt firms. The law is unclear, however, regarding the appropriate standard to be applied and the penalties such managers might face, and it remains to be seen how the courts will interpret and apply these provisions.

155. See *id.* arts. 125-31.

156. Corporate Bankruptcy Law, *supra* note 2, art. 6.

157. *Id.* art. 125.

158. See *id.* This concept is similar to the good faith and fiduciary duty concepts applicable to corporate managers under U.S. law. See Melvin A. Eisenberg, *The Duty Of Good Faith In Corporate Law*, 31 DEL. J. CORP. L. 1 (2006).

159. See Corporate Bankruptcy Law, *supra* note 2, art. 126.

160. See *id.* art. 127.

161. See *id.* art. 128.

162. See *id.*

163. See *id.* art. 131.

2. International or Cross-Border Bankruptcies

China's new bankruptcy law includes a provision directed at international or cross-border bankruptcies.¹⁶⁴ Under this provision, bankruptcy proceedings initiated in China are binding on the debtor's property and estate situated outside China.¹⁶⁵ Thus, the new law specifically provides for extraterritorial application of its provisions.¹⁶⁶ The law also provides that judgments and decisions in foreign courts involving the debtor's property or estate can be recognized by the People's Court in China; however, in order to do so, the People's Court must scrutinize the judgment in accordance with applicable international treaties, and may recognize and enforce such judgments where the court determines that it does not "impair the security and sovereignty of the country and social and public interests or the legitimate rights and interests of the debtors within the People's Republic of China."¹⁶⁷ This language is extremely vague and imprecise, and it is likely to lead to concerns about enforceability of foreign bankruptcy judgments in China. However, these types of issues concerning the enforceability of foreign bankruptcies are part of the problem with international insolvency proceedings in general.¹⁶⁸ As one commentator noted, "international insolvency is an administrative nightmare when no country holds complete jurisdiction over either the debtor, its assets, or its creditors."¹⁶⁹

Under U.S. law, this issue was addressed with the addition of Chapter 15, titled "Ancillary and Other Cross-Border Cases."¹⁷⁰ Under Chapter 15, a petition may be filed for recognition of a foreign bankruptcy proceeding¹⁷¹ and will be recognized by the court as a foreign main proceeding (if pending where the debtor has the center of its main interests) or as a foreign non-main proceeding (if the debtor has an establishment in a foreign country where the proceeding is pending).¹⁷²

164. See Corporate Bankruptcy Law, *supra* note 2, art. 5.

165. See *id.*

166. See *id.*

167. *Id.*

168. See Evelyn H. Biery et al., *A Look at Transnational Insolvencies and Chapter 15 of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 47 B.C. L. REV. 23, 48 (2005).

169. *Id.* (citing M. Cameron Gilreath, *Overview and Analysis of How the United Nations Model Law on Insolvency Would Affect United States Corporations Doing Business Abroad*, 16 BANKR. DEV. J. 399, 402 (2000)).

170. See Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, 108 Pub. L. No. 8, 119 Stat. 23 (Apr. 20, 2005) (codified in scattered sections of 11 U.S.C., 12 U.S.C., 15 U.S.C., 18 U.S.C., and 28 U.S.C.).

171. See 11 U.S.C. § 1504 (2006).

172. See *id.* § 1517(b). The term "establishment" means any place of operations where the debtor carries out a nontransitory economic activity. *Id.* § 1502(2).

Once recognized, the foreign representative is entitled to specified relief, including an automatic stay with regard to the debtor's property within the United States, and the right to act in the same manner as a trustee or a debtor-in-possession in the United States.¹⁷³ These provisions provide specific procedures for recognition of foreign bankruptcy proceedings¹⁷⁴ and specific protections for participants in foreign bankruptcy proceedings where the debtor has property within the United States.¹⁷⁵ The new law in China would certainly benefit from similar provisions.

IV. The UNCITRAL Legislative Guide on Insolvency Law

A. Overview

In June 2004, Working Group V ("Insolvency Law") adopted the text of the UNCITRAL Legislative Guide on Insolvency Law ("Legislative Guide").¹⁷⁶ The United Nations General Assembly passed a resolution accepting the Legislative Guide on December 16, 2004.¹⁷⁷ The acceptance of the Legislative Guide concluded more than a decade of work that began in 1992 as part of the UNCITRAL Congress entitled "Uniform Commercial Law in the 21st Century."¹⁷⁸ Specifically, the Legislative Guide arose from a 1999 proposal that UNCITRAL should "undertake further work on insolvency law, specifically corporate insolvency, to foster and encourage the adoption of effective national corporate insolvency regimes."¹⁷⁹

The purpose of the Legislative Guide is to assist in the establishment of an efficient and effective legal framework to address insolvency issues of debtors.¹⁸⁰ It is intended to be a reference source for national authorities and legislative bodies when preparing new laws and regulations and in assessing the need to review and update existing insolvency laws and regulations.¹⁸¹ The Legislative Guide focuses on

173. See 11 U.S.C. § 1520(a)(1)-(4) (2006).

174. See *id.* §§ 1515-1517.

175. See *id.* § 1522.

176. See UNCITRAL, Legislative Guide on Insolvency Law at iii, U.N. Sales No. E.05V.10 (2005) [hereinafter Legislative Guide], available at http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf.

177. See G.A. Res. 59/40, U.N. Doc. A/Res/59/40 (Dec. 16, 2004).

178. See Presentation by Jenny Clift, Senior Legal Officer and Head, Technical Assistance and Coordination, United Nations Office of Legal Affairs, UNCITRAL Legislative Guide on Insolvency Law, Forum on Asian Insolvency Reform 1-2 (Apr. 27-28, 2006, Beijing, China, available at http://www.oecd.org/document/15/0,3343,de_2649_34845_38177487_1_1_1_1,00.html (last visited July 22, 2008)).

179. Legislative Guide, *supra* note 176, at iii.

180. See *id.* at 1.

181. See *id.*

insolvency proceedings against a debtor engaged in economic activity, rather than individuals not engaged in economic activity.¹⁸²

The Legislative Guide is not intended to be a model law,¹⁸³ in that it does not provide a single set of model provisions to address critical issues; rather it is designed to assist the reader to evaluate different available approaches and choose the one most suitable in the particular national or local context.¹⁸⁴

The first part of the Legislative Guide focuses on key objectives of an effective and efficient insolvency system.¹⁸⁵ Under the Legislative Guide, any insolvency system should aim to achieve certain objectives in a balanced manner, regardless of the specific provisions chosen to implement the design of the particular insolvency law.¹⁸⁶ The specific goals identified by the Guide are as follows:

1. Provision of certainty in the market to promote economic stability and growth
2. Maximization of values of assets
3. Striking a balance between liquidation and reorganization
4. Ensuring equitable treatment of similarly situated creditors
5. Provision of timely, efficient and impartial resolution of insolvency
6. Preservation of the insolvency estate to allow equitable distribution to creditors
7. Ensuring a transparent and predictable insolvency law that contains incentives for gathering and dispensing information
8. Recognition of existing creditor rights and establishment of clear rules for ranking priority of claims
9. Establishment of a framework for cross-border insolvency.¹⁸⁷

The second part of the Legislative Guide identifies core provisions that should be addressed in an effective and efficient insolvency law.¹⁸⁸ These core provisions are logically divided into six broad categories:

182. *See id.*

183. A "model law" is a legislative text recommended to states for enactment, with or without modification. *See* Clift, *supra* note 178, at 3. Thus, a model law proposes a comprehensive set of legislative solutions to a particular problem and the language to be enacted into a national law. *See id.*

184. *See* Legislative Guide, *supra* note 176, at 2. Thus, the Legislative Guide differs from a model law in that the Legislative Guide is not intended to be enacted into national law as such; rather, the Legislative Guide outlines the core issues and provides recommendations that provide specific guidance on how those legislative provisions might be drafted. Clift, *supra* note 178, at 3.

185. *See* Legislative Guide, *supra* note 176, at 9.

186. *See id.* at 10.

187. *Id.* at 10-14.

188. *See id.* at 37.

Application and Commencement;¹⁸⁹ Treatment of Assets on Commencement of Proceedings;¹⁹⁰ Participants;¹⁹¹ Reorganization;¹⁹² Management of Proceedings;¹⁹³ and Conclusion of Proceedings.¹⁹⁴ Some of the more important features of each of these categories are discussed separately below.¹⁹⁵

B. *Application and Commencement*

Under this first category, the Legislative Guide addresses issues relating to debtor eligibility and jurisdiction¹⁹⁶ and commencement of insolvency proceedings.¹⁹⁷

1. Eligibility and Jurisdiction

With regard to eligibility, the Legislative Guide suggests that an insolvency law should govern insolvency proceedings against all debtors that engage in economic activities, including natural or legal persons, including State-owned enterprises, and including both for-profit and not-for-profit enterprises.¹⁹⁸ Further, entities excluded from the application of an insolvency law should be limited and clearly identified.¹⁹⁹

In terms of jurisdiction, the Legislative Guide provides that an insolvency law should identify which debtors have sufficient connection to the state to be subject to its insolvency law, including consideration of whether a debtor has its “centre of main interests” in the state or has “an establishment” in the state.²⁰⁰ The Legislative Guide also suggests that an insolvency law should define the court that has jurisdiction over the commencement and conduct of insolvency proceedings.²⁰¹

189. *See id.* at 38.

190. *See* Legislative Guide, *supra* note 176, at 75.

191. *See id.* at 161.

192. *See id.* at 209.

193. *See id.* at 249.

194. *See id.* at 281.

195. The entire Legislative Guide is nearly 400 pages long; thus, by necessity, a complete and exhaustive discussion of each of these categories is not possible. I have therefore selected representative portions of each section for this discussion based upon my perception of the provisions that are most important.

196. *See* Legislative Guide, *supra* note 176, pt. two, I.A., at 38-44.

197. *See id.*, pt. two, I.B., at 45-67.

198. *See id.*, recommendation 8, at 44.

199. *See id.*, recommendation 9, at 44.

200. *Id.*, recommendation 10(a)-(b), at 44.

201. *See* Legislative Guide, *supra* note 176, recommendation 13, at 44.

2. Commencement of Insolvency Proceedings

The Legislative Guide provides detailed guidance concerning provisions dealing with the commencement of insolvency proceedings, including a recommendation that the law specify that the debtor or any of its creditors should be permitted to make an application for commencement of insolvency proceedings.²⁰² The criteria set forth in the Legislative Guide allow either debtor filing or a creditor filing if the debtor either is or will be generally unable to pay its debts as they mature, or if the debtor's liabilities exceed the value of its assets.²⁰³ The Legislative Guide also provides that the law should specify that where a debtor files an application for commencement, either the application for commencement will automatically commence the insolvency proceedings or the court will promptly determine whether the commencement standard has been met and, if so, commence insolvency proceedings itself.²⁰⁴ Likewise, when an application is filed by a creditor, the debtor should be given notice of the filing and an opportunity to respond by contesting the application, consenting to the application, or, where the application seeks liquidation, requesting the commencement of reorganization proceedings.²⁰⁵ The law should provide for a requirement of and means for the delivery of notice of commencement of insolvency proceedings.²⁰⁶ The notice should include information concerning submission of claims, the procedure and form requirements for submission of claims, the consequences of failing to submit a claim, and information concerning verification of claims.²⁰⁷ Finally, the insolvency law should direct the court to dismiss proceedings if, after commencement, the court determines that the proceedings constitute an improper use of the insolvency law, or the debtor was ineligible or did not meet the commencement standard at the time of commencement of the insolvency proceedings.²⁰⁸

C. *Treatment of Assets on Commencement of Proceedings*

The second category of Part Two of the Legislative Guide identifies provisions dealing with specific aspects of the treatment of the debtor's assets after insolvency proceedings are commenced.²⁰⁹ The significant

202. *See id.*, recommendation 14, at 64.

203. *See id.*, recommendations 15(a)-(b) and 16(a)-(b), at 64-65.

204. *See id.*, recommendation 18(a)-(b), at 65.

205. *See id.*, recommendation 19(a)-(b), at 65.

206. *See* Legislative Guide, *supra* note 176, recommendations 22-23, at 66.

207. *See id.*, recommendation 25(a)-(d), at 66-67.

208. *See id.*, recommendation 27(a)-(b), at 67.

209. *See id.*, pt. two, II, at 75-159.

issues identified include the assets of the insolvency estate,²¹⁰ the protection and preservation of those assets,²¹¹ the use and disposal of assets,²¹² post-commencement finance issues,²¹³ and avoidance proceedings.²¹⁴

1. Assets Included in the Estate

Recognizing that “the need to identify, collect, preserve and dispose of the debtor’s assets” is “[f]undamental to insolvency proceedings,” the Legislative Guide attempts to identify the assets included in the insolvency estate.²¹⁵ Specifically, the insolvency law should specify that the estate includes assets of the debtor, determined by reference to the relevant applicable law and reading the term “asset” broadly to include property, rights and interests of the debtor, including the debtor’s rights and interests in third-party-owned assets.²¹⁶ The estate should also include assets acquired after commencement of the insolvency proceedings and those recovered through avoidance and other actions.²¹⁷

2. Protection and Preservation of Assets

The second item in this category deals with the protection and preservation of the assets of the insolvency estate.²¹⁸ Of critical importance to the protection of the assets of the insolvency estate is the imposition of a stay preventing creditors from commencing actions to enforce their rights through legal remedies and continuing actions already under way against the debtor.²¹⁹ In this regard, the Legislative Guide provides that an insolvency law should specify that on commencement of insolvency proceedings, actions or proceedings concerning the assets of the debtor and the rights, obligations or liabilities of the debtor are stayed;²²⁰ that actions to make security interests effective against third parties and to enforce security interests are stayed;²²¹ that execution or enforcement against assets of the estate is

210. *See id.*, pt. two, II.A., at 75-83.

211. *See* Legislative Guide, *supra* note 176, pt. two, II.B., at 83-103.

212. *See id.*, pt. two, II.C., at 104-13.

213. *See id.*, pt. two, II.D., at 113-19.

214. *See id.*, pt. two, II.F., at 135-55.

215. *Id.*, pt. two, II.A.1. ¶ 1, at 75.

216. *See* Legislative Guide, *supra* note 176, recommendation 35(a), at 82.

217. *See id.*, recommendation 35(b)-(c), at 82.

218. *See id.*, pt. two, II.B., at 83.

219. *See id.*, pt. two, II.B.2., at 83.

220. *See id.*, recommendation 46(a), at 101.

221. *See* Legislative Guide, *supra* note 176, recommendation 46(b), at 102.

stayed;²²² that the right to terminate any contract with the debtor is suspended;²²³ and that the right to transfer, encumber or otherwise dispose of any asset of the estate is suspended.²²⁴ The insolvency law may provide for clearly stated exceptions to the application of the stay.²²⁵ The stay should remain in effect until the court grants relief from the stay, a reorganization plan is adopted (in reorganization proceedings), or a fixed time period expires (in liquidation proceedings).²²⁶ The grounds for relief from the stay should include a showing by a secured creditor that the encumbered asset is not necessary to a prospective reorganization or sale of the debtor's business, that the value of the encumbered asset is diminishing without adequate protection,²²⁷ and in a reorganization proceeding, that a reorganization plan is not approved within any applicable time limits.²²⁸

3. Use and Disposition of Assets

The third item in this category deals with the use and disposal of assets by the estate.²²⁹ Specifically, the Legislative Guide indicates that an insolvency law should permit the use and disposal of assets of the estate, including encumbered assets, in the ordinary course of business.²³⁰ Use and disposal of assets outside the ordinary course of business should also be permitted where creditors are given adequate notice of the disposal and the opportunity to be heard in court.²³¹ Moreover, the insolvency representative should be free to sell an encumbered asset free and clear of any encumbrance, outside the ordinary course of business,²³² as long as the insolvency representative gives notice of the proposed sale to the holder of the encumbrance,²³³ the holder is given the opportunity to be heard by the court where they object to the proposed sale,²³⁴ relief from the stay has not been granted,²³⁵ and the priority of interests in the

222. *See id.*, recommendation 46(c), at 102.

223. *See id.*, recommendation 46(d), at 102.

224. *See id.*, recommendation 46(e), at 102.

225. *See id.*, recommendation 47, at 102.

226. *See* Legislative Guide, *supra* note 176, recommendation 49(a)-(c), at 102-03.

227. Adequate protection can be provided by appropriate measures that may include cash payments by the estate, provision of additional security interests, or such other means as the court determines. *See* Legislative Guide, *supra* note 176, recommendation 50(a)-(c), at 103.

228. *See id.*, recommendation 51(a)-(c), at 103.

229. *See id.*, pt. two, II.C., at 104.

230. *See id.*, recommendation 52(a), at 111.

231. *See id.*, recommendations 52(b), 55, at 111-12.

232. *See* Legislative Guide, *supra* note 176, recommendation 52(b), at 111.

233. *See id.*, recommendation 58(a), at 112.

234. *See id.*, recommendation 58(b), at 112.

235. *See id.*, recommendation 58(c), at 112.

proceeds of the sale of the asset is preserved.²³⁶ The “insolvency law should specify methods of sale for sales conducted outside the ordinary course of business that will maximize the price obtained for assets being sold,”²³⁷ should permit the urgent sale of an asset without prior approval of the court or creditors where the asset is “perishable, susceptible to devaluation or otherwise in jeopardy,”²³⁸ and “should require any proposed disposal of an asset to a related person to be carefully scrutinized before being allowed to proceed.”²³⁹

4. Post-Commencement Financing

The fourth item in this category deals with post-commencement financing and emphasizes the importance of providing a source of funds for the debtor’s continued operation, particularly in the context of a reorganization.²⁴⁰ Because of this need, the insolvency law should facilitate and provide incentives for post-commencement financing where it is determined to be necessary for the continued operation or survival of the debtor’s business or the preservation or enhancement of the value of the estate.²⁴¹ These provisions should determine the priority given to post-commencement finance, ensuring it is at least ahead of ordinary unsecured creditors,²⁴² and “should enable a security interest to be granted for repayment of post-commencement finance, including a security interest on an unencumbered asset” or “a junior or lower-priority security interest in an already encumbered asset of the estate.”²⁴³ However, the Legislative Guide does provide protection for existing secured creditors, providing that a security interest to secure post-commencement financing should not have priority ahead of an existing security interest in the same assets unless the existing secured creditor agrees,²⁴⁴ or the court authorizes the creation of a senior security interest provided certain criteria are met,²⁴⁵ including “the existing secured creditor is given the opportunity to be heard,”²⁴⁶ “the debtor can prove it

236. *See id.*, recommendation 52(d), at 112.

237. Legislative Guide, *supra* note 176, recommendation 57, at 112.

238. *Id.*, recommendation 60, at 113.

239. *Id.*, recommendation 61, at 113.

240. *See id.*, pt. two, II.D.1., ¶ 94, at 113-14.

241. *See id.*, recommendation 63, at 118.

242. *See* Legislative Guide, *supra* note 176, recommendation 64, at 119.

243. *Id.*, recommendation 65, at 119.

244. *See id.*, recommendation 66, at 119.

245. *See id.*, recommendation 67, at 119.

246. *Id.*, recommendation 67(a), at 119.

cannot obtain the finance any other way,”²⁴⁷ and “the interests of the existing secured creditor will be protected.”²⁴⁸

5. Avoidance Proceedings

Finally, this category deals with avoidance proceedings, in recognition of the possibility that during the time period between the debtor becoming aware of the likelihood of a bankruptcy filing and the actual commencement of the proceedings, both debtor and creditors may take steps that have the effect of creating an unfair disadvantage for ordinary unsecured creditors.²⁴⁹ Thus, the Legislative Guide provides that “an insolvency law should include provisions that apply retroactively to and are designed to overturn transactions, involving the debtor or assets of the estate, and that have the effect of either reducing the value of the estate or upsetting the principle of equitable treatment of creditors.”²⁵⁰ Specifically, three types of transactions should be avoidable: transactions intended to defeat, delay or hinder the ability of creditors to collect claims by putting assets beyond the reach of creditors or otherwise prejudice the interests of creditors;²⁵¹ undervalued transactions, in which the debtor transferred an interest in property or undertook an obligation in exchange for a nominal or less than equivalent value or for inadequate value, at a time when the debtor was insolvent or in a transaction that resulted in the debtor becoming insolvent;²⁵² and preferential transactions, in which a creditor obtained more than its pro rata share of the debtor’s assets at a time when the debtor was insolvent.²⁵³ These transactions may be avoided if they occurred during a “suspect period” specified in the insolvency law.²⁵⁴ The insolvency law should also specify the time period in which an avoidance proceeding may be commenced²⁵⁵ and the elements to be proved in order to avoid a particular transaction.²⁵⁶

247. Legislative Guide, *supra* note 176, recommendation 67(b), at 119.

248. *Id.*, recommendation 67(c), at 119.

249. *See id.*, pt. two, I.F.1., ¶ 148, at 135. As the Legislative Guide suggests, the debtor, for example, may be tempted to hide assets from creditors, incur artificial liabilities, make asset transfers to relatives and friends, or pay certain creditors to the exclusion of others. *See id.* Creditors may also take strategic action to place themselves in an advantageous position relative to other creditors. *See id.*

250. *Id.*, recommendation 87, at 152-53.

251. *See id.*, recommendation 87(a), at 153.

252. Legislative Guide, *supra* note 176, recommendation 87(b), at 153.

253. *See id.*, recommendation 87(c), at 153.

254. *See id.*, recommendation 89, at 153. A “suspect period” is a specified time that “is calculated retroactively from a specified date, being either the date of application for, or commencement of, the insolvency proceedings.” *Id.*

255. *See id.*, recommendation 96, at 154.

256. *See id.*, recommendation 97, at 154.

D. Participants

The third category in Part Two of the Legislative Guide deals with the rights and responsibilities of the various participants in an insolvency proceeding.²⁵⁷ Significant parts of this category are dedicated to the debtor,²⁵⁸ the insolvency representative,²⁵⁹ and creditors.²⁶⁰

1. The Debtor

With regard to the debtor, the Legislative Guide indicates that “the insolvency law should clearly specify the debtor’s obligations in respect of [the] insolvency proceedings.”²⁶¹ The debtor’s obligations should include an obligation “to cooperate with and assist the insolvency representative to perform its duties,”²⁶² to provide accurate and complete information relating the debtor’s business,²⁶³ including lists of transactions occurring prior to commencement that involved the debtor or its assets,²⁶⁴ ongoing legal proceedings,²⁶⁵ assets and liabilities,²⁶⁶ debtors and their obligations,²⁶⁷ and creditors and their claims;²⁶⁸ and to cooperate with the insolvency representative to take control of the estate and cooperate in the recovery of assets.²⁶⁹ The insolvency law should also specify the role of the debtor in the continuing operation of debtor’s business during the insolvency proceedings, recognizing that a variety of approaches are possible.²⁷⁰ These approaches include the debtor retaining full control of the business²⁷¹ (similar to the debtor-in-possession concept under U.S. law),²⁷² limited displacement with the debtor operating the business on a day-to-day basis subject to supervision of an insolvency representative,²⁷³ or “total displacement of the debtor from any role in the business.”²⁷⁴ Finally, “the insolvency law should

257. See Legislative Guide, *supra* note 176, pt. two, III., at 161-207.

258. See *id.*, pt. two, III.A., at 161-73.

259. See *id.*, pt. two, III.B., at 174-89.

260. See *id.*, pt. two, III.C., at 190-205.

261. *Id.*, recommendation 110, at 172.

262. Legislative Guide, *supra* note 176, recommendation 110(a), at 172.

263. See *id.*, recommendation 110(b), at 172.

264. See *id.*, recommendation 110(b)(i), at 172.

265. See *id.*, recommendation 110(b)(ii), at 172.

266. See *id.*, recommendation 110(b)(iii), at 172.

267. Legislative Guide, *supra* note 176, recommendation 110(b)(iv), at 172.

268. See *id.*, recommendation 110(b)(v), at 172.

269. See *id.*, recommendation 110(c), at 172-73.

270. See *id.*, recommendation 112, at 173.

271. See *id.*, recommendation 112(a), at 173.

272. See *supra* notes 139-40 and accompanying text.

273. See Legislative Guide, *supra* note 176, recommendation 112(b), at 173.

274. *Id.*, recommendation 112(c), at 173.

permit the imposition of sanctions for the debtor's failure to comply with its obligations under the insolvency law."²⁷⁵

2. The Insolvency Representative

The Legislative Guide uses the term "insolvency representative" to refer to the person responsible for administering the insolvency proceedings, sometimes referred to as "administrator," "trustee," "receiver," or "judicial manager," among other terms.²⁷⁶ The Legislative Guide indicates that "the insolvency law should specify the qualifications and qualities required for appointment as an insolvency representative," as well as "grounds upon which a proposed insolvency representative may be disqualified."²⁷⁷ The "insolvency law should require the disclosure of a conflict of interest, a lack of independence or circumstances that may lead to a conflict of interest or lack of independence"²⁷⁸ by either a proposed insolvency representative²⁷⁹ or persons proposed for employment by the insolvency representative or the estate,²⁸⁰ and should establish a mechanism for determining the compensation of the insolvency representative and establishing priority for its payment.²⁸¹ The mechanism for selecting and appointing an insolvency representative should be specified and may include "appointment by the court; by an independent appointing authority; on the basis of a recommendation by creditors or the creditor committee; by the debtor; or by operation of insolvency law where the insolvency representative is a government or administrative agency or official."²⁸²

In terms of duties, the Legislative Guide indicates that an insolvency law should specify that "the insolvency representative has an obligation to protect and preserve the assets of the estate"²⁸³ as well as the consequences for failing to properly perform such duties and any related standard of liability imposed.²⁸⁴ Grounds for removing the insolvency representative should include "incompetence, failure to perform or failure to exercise the proper degree of care in performance of

275. *Id.*, recommendation 114, at 173.

276. *See id.*, pt. two, III.B.1. ¶ 35, at 174.

277. *Id.*, recommendation 115, at 188. The specified qualities include "integrity, independence, impartiality, requisite knowledge of relevant commercial law and experience in commercial and business matters." *Id.*

278. Legislative Guide, *supra* note 176, recommendation 116, at 188.

279. *See id.*, recommendation 116(a), at 188.

280. *See id.*, recommendation 116(b), at 188.

281. *See id.*, recommendation 119, at 188.

282. *Id.*, recommendation 118, at 188.

283. Legislative Guide, *supra* note 176, recommendation 120, at 188-89.

284. *See id.*, recommendation 121, at 189.

its powers and functions;”²⁸⁵ “inability to perform;”²⁸⁶ “lack of a particular or specialized qualification required by a specific case;”²⁸⁷ “engaging in illegal acts or conduct;”²⁸⁸ “conflict of interest or lack of independence that would justify removal;”²⁸⁹ or a change in the function of the insolvency representative.²⁹⁰

3. Creditors

The last part of this section of the Legislative Guide addresses the interests of creditors participating in the insolvency proceedings.²⁹¹ The Legislative Guide provides that an insolvency law should specify that both secured and unsecured creditors are entitled to participate in insolvency proceedings and should identify what that participation may involve.²⁹² The insolvency law should also “specify the matters on which a vote of creditors is required and establish the relevant eligibility and voting requirements,” specifically requiring that creditors “vote on the approval or rejection of a reorganization plan.”²⁹³ The insolvency law may require a first meeting of creditors within a specified time period after commencement²⁹⁴ and should facilitate active creditor participation through a creditor committee (or multiple creditor committees where their interests are diverse), special representative or other mechanism for representation.²⁹⁵ The insolvency law should also establish a mechanism for appointment of a creditor committee, which may include selection by creditors or appointment by the court or an administrative body.²⁹⁶ The insolvency law should specify the rights and functions of the creditor committee,²⁹⁷ which may include providing advice and assistance to the insolvency representative,²⁹⁸ participating in development of a plan of reorganization,²⁹⁹ receiving notice of and being consulted on matters in which their class has an interest,³⁰⁰ the “right to

285. *Id.*, recommendation 122(a), at 189.

286. *Id.*, recommendation 122(b), at 189.

287. *Id.*, recommendation 122(c), at 189.

288. Legislative Guide, *supra* note 176, recommendation 122(d), at 189.

289. *Id.*, recommendation 122(e), at 189.

290. *See id.*, recommendation 122(f), at 189.

291. *See id.*, pt. two, III.C., at 190.

292. *See id.*, recommendation 126, at 203.

293. Legislative Guide, *supra* note 176, recommendation 127, at 203.

294. *See id.*, recommendation 128, at 203.

295. *See id.*, recommendation 129, at 203.

296. *See id.*, recommendation 132, at 204.

297. *See id.*, recommendation 133, at 204.

298. *See* Legislative Guide, *supra* note 176, recommendation 133(a), at 204.

299. *See id.*, recommendation 133(b), at 204.

300. *See id.*, recommendation 133(c), at 204.

hear the insolvency representative at any time,”³⁰¹ and “the right to be heard in the proceedings.”³⁰² Finally, the insolvency law should exempt creditor committee members from liability for their actions in such capacity “unless they are found to have acted fraudulently or to be guilty of willful misconduct,”³⁰³ and it should “specify the grounds for removal of members of a creditor committee and provide for their replacement.”³⁰⁴

E. Reorganization

The fourth category in Part Two of the Legislative Guide deals with reorganization.³⁰⁵ Both the elements of the reorganization plan and the process of approval and confirmation of the plan are discussed in detail.

1. Elements of a Plan of Reorganization

The Legislative Guide provides that the insolvency law should specify that a plan of reorganization may be proposed on or after the making of an application to commence insolvency proceedings or within a specified time after such application.³⁰⁶ The plan should be accompanied by a disclosure statement enabling those entitled to vote on the reorganization plan to make an informed decision about the plan.³⁰⁷ The disclosure statement should include a summary of the plan,³⁰⁸ information regarding the financial situation of the debtor,³⁰⁹ “non-financial information that might have an impact on the future performance of the debtor,”³¹⁰ a comparison of the treatment of creditors by the plan and what they would receive in liquidation,³¹¹ “the basis upon which the business would be able to keep trading and could be successfully reorganized,”³¹² information showing that “adequate provision has been made for satisfaction of all obligations included in the plan,”³¹³ and “information on the voting mechanisms applicable to approval of the plan.”³¹⁴ At a minimum, the reorganization plan itself

301. *Id.*, recommendation 133(d), at 204.

302. *Id.*, recommendation 133(e), at 204.

303. Legislative Guide, *supra* note 176, recommendation 135, at 205.

304. *Id.*, recommendation 136, at 205.

305. *See id.*, pt. two, IV., at 209-47.

306. *See id.*, recommendation 139, at 234.

307. *See id.*, recommendation 141, at 234.

308. Legislative Guide, *supra* note 176, recommendation 143(a), at 234.

309. *See id.*, recommendation 143(b), at 234.

310. *Id.*, recommendation 143(c), at 234.

311. *See id.*, recommendation 143(d), at 234.

312. *Id.*, recommendation 143(e), at 234.

313. Legislative Guide, *supra* note 176, recommendation 143(f), at 235.

314. *Id.*, recommendation 143(g), at 235.

should identify each class of creditors and the treatment provided for each;³¹⁵ “detail the treatment of equity holders;”³¹⁶ “detail the terms and conditions of the plan;”³¹⁷ “identify the debtor’s role in implementation of the plan;”³¹⁸ “identify those responsible for future management of the debtor and supervision of the implementation of the plan;”³¹⁹ and “indicate how the plan will be implemented.”³²⁰

2. Approval and Confirmation of the Plan

The insolvency law should establish a mechanism for voting on approval of the reorganization plan,³²¹ with creditors separately classified according to their respective rights and with each class entitled to vote separately,³²² and with all creditors and equity holders that are in the same class offered identical treatment.³²³

The Legislative Guide recognizes two different approaches to confirmation of a plan that has been approved by creditors.³²⁴ In some insolvency laws, “approval by a requisite majority of creditors is all that is required for the plan to become effective,” while in other insolvency systems, court confirmation of the plan is required in order for the plan to become effective and binding.³²⁵ In an insolvency law where court confirmation of an approved plan is required, the court should be required to confirm that the requisite approvals have been obtained and the approval process conducted properly;³²⁶ that “creditors will receive at least as much under the plan as they would have received in liquidation, unless they have specifically agreed to receive lesser treatment;”³²⁷ that the plan does not contain provisions that are contrary to the law;³²⁸ that administrative claims and expenses will be fully paid;³²⁹ and that if a class of creditors voted against the plan, that class will receive full recognition of its ranking under the insolvency law and the distribution to that class under the plan conforms to that ranking.³³⁰ Where no court

315. *See id.*, recommendation 144(a), at 235.

316. *Id.*, recommendation 144(b), at 235.

317. *Id.*, recommendation 144(c), at 235.

318. Legislative Guide, *supra* note 176, recommendation 144(d), at 235.

319. *Id.*, recommendation 144(e), at 235.

320. *Id.*, recommendation 144(f), at 235.

321. *See id.*, recommendation 145, at 235.

322. *See id.*, recommendation 148, at 235.

323. *See* Legislative Guide, *supra* note 176, recommendation 149, at 235.

324. *See id.*, pt. two, IV.A.8, ¶ 56, at 226.

325. *Id.*

326. *See id.*, recommendation 152(a), at 236.

327. *Id.*, recommendation 152(b), at 236.

328. *See* Legislative Guide, *supra* note 176, recommendation 152(c), at 236.

329. *See id.*, recommendation 152(d), at 236.

330. *See id.*, recommendation 152(e), at 236.

approval is required, the insolvency law should permit parties in interest, including the debtor, to challenge the approval of the reorganization plan based on specified criteria.³³¹ Those specified criteria include: whether the grounds for approval by a court were satisfied,³³² and whether there was a claim of fraud.³³³ In the case of a claim of fraud, the insolvency law should specify a time limit for bringing such a challenge calculated by reference to the discovery of the fraud,³³⁴ the party that may bring such a challenge on the basis of fraud,³³⁵ and the Court should hear the challenge.³³⁶ The insolvency law should also provide a mechanism for supervising the implementation of the reorganization plan, which may include “supervision by the court, by a court-appointed supervisor, by the insolvency representative, or by a creditor-appointed supervisor.”³³⁷ Finally, the insolvency law should provide that the court may convert the reorganization to a liquidation³³⁸ where a plan is not proposed within any time limit allowed,³³⁹ a plan is not approved,³⁴⁰ an approved plan is not confirmed by the court if required,³⁴¹ an approved plan is successfully challenged,³⁴² or “there is substantial breach by the debtor of the terms of the plan or an inability to implement the plan.”³⁴³

F. *Management of Proceedings*

The next portion of Part Two of the Legislative Guide deals with management of the insolvency proceedings.³⁴⁴ Included in this section is the treatment of creditor claims³⁴⁵ and the priorities and distribution of proceeds.³⁴⁶

1. Treatment of Creditor Claims

With regard to the treatment of creditor claims, the Legislative Guide provides that an “insolvency law should specify that claims that

331. *See id.*, recommendation 153, at 236.

332. *See id.*, recommendation 153(a), at 236.

333. Legislative Guide, *supra* note 176, recommendation 153(b), at 236.

334. *See id.*, recommendation 154(a), at 237.

335. *See id.*, recommendation 154(b), at 237.

336. *See id.*, recommendation 154(c), at 237.

337. *Id.*, recommendation 157, at 237.

338. *See* Legislative Guide, *supra* note 176, recommendation 158, at 237.

339. *See id.*, recommendation 158(a), at 237.

340. *See id.*, recommendation 158(b), at 237.

341. *See id.*, recommendation 158(c), at 237.

342. *See id.*, recommendation 158(d), at 237.

343. Legislative Guide, *supra* note 176, recommendation 158(e), at 238.

344. *See id.* at 249.

345. *See id.*, pt. two, V.A., at 249-66.

346. *See id.*, pt. two, V.B., at 266-76.

may be submitted include all rights to payment that arise from acts or omissions of the debtor prior to commencement of the insolvency proceedings.”³⁴⁷ The law should indicate whether secured creditors are required to submit claims³⁴⁸ and should provide that similarly ranked creditors are treated equally with respect to the submission and processing of their claims whether they are domestic or foreign creditors alike.³⁴⁹ The law should also specify the consequences of failing to submit a claim in a timely manner.³⁵⁰

Once a creditor claim is filed, the insolvency representative should be able to admit or deny any claim, in full or in part,³⁵¹ and a creditor whose claim is denied should be able to request the court to review their denied claim.³⁵² Claims by related persons should be subject to particular scrutiny, and, where justified,³⁵³ “the voting rights of the related person may be restricted,”³⁵⁴ “the amount of the claim of the related person may be reduced,”³⁵⁵ or “the claim may be subordinated.”³⁵⁶

2. Priorities and Distribution of Proceeds

The second part of this section of the Legislative Guide deals with priorities and distribution of proceeds in insolvency proceedings.³⁵⁷ The insolvency law should specify the classes of creditors affected by the insolvency proceedings and the treatment of those classes in terms of priority and distribution,³⁵⁸ and should identify the order in which claims are to be satisfied from the estate.³⁵⁹ It should also specify that secured claims are to be satisfied from the encumbered asset in either liquidation or reorganization proceedings.³⁶⁰ Finally, the insolvency law should specify that claims other than secured claims are ranked in the following order: “administrative costs and expenses,”³⁶¹ “claims with priority,”³⁶²

347. *Id.*, recommendation 171, at 264.

348. *See* Legislative Guide, *supra* note 176, recommendation 172, at 264.

349. *See id.*, recommendation 173, at 264.

350. *See id.*, recommendation 175, at 264.

351. *See id.*, recommendation 177, at 265.

352. *See id.*, recommendation 181, at 265.

353. *See* Legislative Guide, *supra* note 176, recommendation 184, at 266.

354. *Id.*, recommendation 184(a), at 266.

355. *Id.*, recommendation 184(b), at 266.

356. *Id.*, recommendation 184(c), at 266.

357. *See id.*, pt. two, V.B., at 266-76.

358. *See* Legislative Guide, *supra* note 176, recommendation 185, at 275.

359. *See id.*, recommendation 186, at 275.

360. *See id.*, recommendation 188, at 275.

361. *Id.*, recommendation 189(a), at 275.

362. *Id.*, recommendation 189(b), at 276.

“ordinary unsecured claims,”³⁶³ and “deferred claims or claims subordinated under the law.”³⁶⁴

G. *Conclusion of Proceedings*

The final section of the Legislative Guide relates to the conclusion of the insolvency proceedings.³⁶⁵ Under this section, where natural persons are eligible as debtors, the issue of discharge of those debtors from liability for pre-commencement debts should be considered.³⁶⁶ In particular, any debts excluded from discharge and any conditions attached to the debtor’s discharge should be kept to a minimum and should be clearly set forth in the insolvency law.³⁶⁷ Finally, the insolvency law should specify the procedures by which the insolvency proceedings will be closed.³⁶⁸

V. Implications of the Comparisons: Improvements and Shortfalls of the New Law

A. *Improvements of the New Law Over China’s Prior Bankruptcy Law*

The new Chinese bankruptcy law makes significant improvements in China’s bankruptcy system in several important areas, including the expanded scope of the law,³⁶⁹ increased transparency,³⁷⁰ and more workable priorities of interests in bankruptcy.³⁷¹ Each of these areas is discussed in more detail below.

1. Expanded Scope

The new law significantly expands the scope of enterprises to which bankruptcy is available and the types of bankruptcies available.³⁷² The new law applies to all business enterprises, including both State-owned and non-State-owned enterprises,³⁷³ creating a unified national bankruptcy law. The significant increase in the number of private

363. Legislative Guide, *supra* note 176, recommendation 189(c), at 276.

364. *Id.*, recommendation 189(d), at 276.

365. *See id.*, pt. two, VI, at 281-86.

366. *See id.*, recommendation 194, at 285.

367. *See id.*, recommendations 195, 196, at 285.

368. *See* Legislative Guide, *supra* note 176, recommendations 197, 198, at 286.

369. *See* Corporate Bankruptcy Law, *supra* note 2, arts. 2, 70-94.

370. *See id.* arts. 22-29.

371. *See id.* arts. 109, 113-15.

372. *See id.* art. 2 (providing that the corporate bankruptcy law applies to all corporate legal persons).

373. *See supra* notes 22-25 and accompanying text.

enterprises demonstrates the need for this type of broad-based bankruptcy law.³⁷⁴ The unified coverage of non-State-owned businesses is a significant improvement over the old piece-meal system that created significant legal and administrative uncertainty, particularly for foreign investors.³⁷⁵ Moreover, the new law is structurally an improvement over the former system, which is described as “a quilt of laws, regulations and directives” that “overlap and contradict each other in some respects.”³⁷⁶

The addition of reorganization as an option for bankrupt entities is likewise a significant improvement under the new system. As discussed above, reorganization is considered a very valuable alternative to liquidation and is in accordance with international bankruptcy procedures.³⁷⁷

2. Increased Transparency

The new law provides a much more transparent process for bankruptcy proceedings, with the bankruptcy being directed by an independent administrator rather than a group of government officials and interested parties.³⁷⁸ In the past, a very low level of bankruptcy cases in China was the result, at least in part, of low regard for or belief in judicial power in China.³⁷⁹ As one commentator suggested, many creditors in China were well aware that bankruptcy cases were really decided by the government, not by the courts.³⁸⁰ The transparency and independence provided by the new system should inspire significantly more confidence and trust in the system.³⁸¹

3. Priorities in Bankruptcy

The change in priorities of interests in the bankruptcy proceedings is a very significant improvement. With a limited exception,³⁸² the new

374. See Immanuel Gebhardt & Kerstin Olbrich, *New Developments in the Reform of Chinese Bankruptcy Law*, 12 AUSTL. J. CORP. L. 109, 110 (2000); Ronald W. Harmer, *International Insolvencies: Colloquium: Insolvency law and Reform in the People's Republic of China*, 64 FORDHAM L. REV. 2563, 2574 (1996) (indicating in both articles that there are significantly more private enterprises than state-owned enterprises in China).

375. Neil McDonald, *It's About Time*, 25 INT'L FIN. L. REV. 52 (2006).

376. Pauline Ma, *A New Chinese Bankruptcy System Made for Business or for the State?*, 11 AUSTL. J. CORP. L. 192, 195 (2000).

377. See Wu, *supra* note 20, at 249.

378. See Ma, *supra* note 376, at 206.

379. See *id.*

380. See *id.*

381. See Charmian Kok, *China's New Bankruptcy Law to Boost Investments: Survey*, BUS. TIMES SING., July 31, 2007.

382. See *supra* notes 124-25 and accompanying text.

corporate bankruptcy law gives secured creditors priority over employees in the distribution of assets, a significant (and potentially politically sensitive)³⁸³ change in the bankruptcy law in China. This change is in marked contrast to the provisions of the former bankruptcy laws, in which creditors' claims were generally subordinate to the claims of workers and other "local" creditors.³⁸⁴ The change in priorities significantly increases protections for secured creditors and is much more in line with the bankruptcy provisions in Western systems.³⁸⁵

B. Issues Raised by the Comparison to the Legislative Guide

A comparison of the provisions of the new Chinese bankruptcy law with the provisions of the Legislative Guide discussed above provides some interesting insights. While the new Chinese bankruptcy law conforms to the Legislative Guide in many respects, there are some areas in which the new law differs significantly from the recommendations in the Legislative Guide.³⁸⁶ This portion of the article will discuss the issues raised³⁸⁷ by this comparison.

1. Jurisdiction

In terms of jurisdiction, the Legislative Guide provides that an insolvency law should identify which debtors have sufficient connection to the state to be subject to its insolvency law, including consideration of whether a debtor has its "centre of main interests" in the state or has "an establishment" in the state.³⁸⁷ As the Legislative Guide indicates, in many cases no issue as to the applicability of the relevant insolvency law will arise because the debtor will be a national or resident of the state and will conduct its economic activities in that state.³⁸⁸ In cases where there is an issue concerning the debtor's connection to the state, the Legislative Guide indicates that there are a variety of approaches that may be taken, including the "centre of main interests" test used under the UNCITRAL

383. See *supra* notes 115-25 and accompanying text.

384. See Young, *supra* note 4.

385. See 11 U.S.C. § 507 (2006).

386. In many areas, the new Chinese law is in accord with the provisions of the Legislative Guide. Rather than repeating the provisions of the Chinese law that agree with the Legislative Guide, I have limited my discussion to areas of difference; thus, if the new Chinese law is not identified as being inconsistent with a particular provision of the Legislative Guide, the reader may assume it is consistent with the Legislative Guide's provisions in that area.

387. Legislative Guide, *supra* note 176, pt. II.A.2, ¶12, at 41.

388. See *id.*

Model Law on Cross- Border Insolvency,³⁸⁹ the “establishment” test, and the “presence of assets” test.³⁹⁰

The “centre of main interests” test looks to the place of the debtor’s registered office (or habitual residence in the case of an individual) unless it can be shown that the debtor’s centre of main interests is elsewhere.³⁹¹ The “establishment test” looks to whether the debtor has an establishment (meaning a place where the debtor carries out a non-transitory economic activity) within the relevant jurisdiction.³⁹² Finally, the “presence of assets” test allows jurisdiction if the debtor has assets within the state without requiring that the debtor have a centre of main interests in the state.³⁹³ While any of these tests could be an appropriate choice, the UNICTRAL Model Law on Cross-Border Insolvency and the European Council (EC) Regulation No. 1346/2000 of 29 May 2000 both use the “centre of main interests” test.³⁹⁴

The new Chinese law, however, does not contain any such provision. It seems to assume that an entity involved in a Chinese bankruptcy proceeding will already be subject to the laws of the Chinese courts.³⁹⁵ The new Chinese law would be stronger and clearer if it included a jurisdictional provision identifying the level of contact by the debtor required to file a bankruptcy proceeding in China.

2. Disposition of Assets and Post-Commencement Financing

The Legislative Guide suggests that an insolvency law should include provisions permitting the use and disposal of assets in the ordinary course of business³⁹⁶ and outside the ordinary course of business where creditors are notified and given the opportunity to be heard in court.³⁹⁷ Such sales should be subject to provisions that will maximize the price obtained for assets being sold, whether the sale is by auction, or if more profitable, by private sale.³⁹⁸ The insolvency law should also permit urgent sales in certain circumstances, including where the asset is “perishable, susceptible to devaluation or otherwise in jeopardy.”³⁹⁹

389. *See id.*, pt. II.A.2.a, ¶ 13, at 41.

390. *See id.*, pt. II.A.2, ¶ 12, at 41.

391. *See id.*, pt. II.A.2.a, ¶ 13, at 41.

392. *See* Legislative Guide, *supra* note 176, pt. II.A.2.b, ¶ 15, at 42.

393. *See id.*, pt. II.A.2.c, ¶ 17, at 42.

394. *See id.*, pt. II.A.2, ¶ 12, at 41.

395. *See, e.g.*, Corporate Bankruptcy Law, *supra* note 2, art. 3, (providing that “[b]ankruptcy cases shall be under the jurisdiction of the People’s Courts *in the place of residence of the debtor*” (emphasis added)).

396. *See supra* note 230 and accompanying text.

397. *See supra* notes 231-239 and accompanying text.

398. *See* Legislative Guide, *supra* note 176, pt. II.C.2.b, ¶¶ 79-80, at 106.

399. *See supra* note 238 and accompanying text.

The Legislative Guide recognizes that the debtor must have access to funds in order to continue its operations and that continued operation is critical both in a reorganization proceeding and in a liquidation proceeding where the business is to be sold as a going concern.⁴⁰⁰ Because of this need, the Legislative Guide suggests that an insolvency law should include detailed provisions concerning post-commencement financing, including specific provisions detailing the priority given to post-commencement financing,⁴⁰¹ specifying that a security interest may be granted for repayment of such financing,⁴⁰² and specifying that such financing should not have priority over an existing security interest in the same assets unless certain requirements are met.⁴⁰³

The new Chinese bankruptcy law does not discuss in any detail provisions for disposition of assets of the estate of the debtor and the need for post-commencement financing by the debtor beyond the general provisions that allow the receiver to manage, distribute and dispose of property of the estate⁴⁰⁴ and borrow funds and setup guarantees for the loan.⁴⁰⁵ More detailed provisions on these issues would assist the receiver in better protecting and maximizing the value of the bankruptcy estate.

3. The Receiver and the Creditors' Committee

Further, the new Chinese bankruptcy law does not cover a number of provisions recommended by the Legislative Guide dealing with the participants to the bankruptcy proceedings. Specifically, the Legislative Guide suggests that a bankruptcy law should obligate the insolvency representative to protect and preserve the assets of the estate.⁴⁰⁶ The new Chinese law could be read to imply such an obligation in its provision providing the receiver with a general obligation to manage the debtor's property,⁴⁰⁷ but it does not explicitly require it. The Legislative Guide also suggests that the grounds for removing the insolvency representative be spelled out in detail, including, among other things, failure to exercise the proper degree of care in performance of its powers and functions, inability to perform, engaging in illegal acts, and conflicts of interest or lack of independence.⁴⁰⁸ The new Chinese law indicates that creditors

400. See Legislative Guide, *supra* note 176, pt. II.D.1, ¶ 94, at 113.

401. See *supra* notes 240-43 and accompanying text.

402. See *supra* note 243 and accompanying text.

403. See *supra* notes 244-48 and accompanying text.

404. See Corporate Bankruptcy Law, *supra* note 2, art. 25(4), (6).

405. See *id.* art. 75.

406. See *supra* note 283 and accompanying text.

407. See Corporate Bankruptcy Law, *supra* note 2, art. 25(6).

408. See *supra* notes 286-90 and accompanying text.

may petition the People's Court to remove the receiver if it is unable to carry out its duties,⁴⁰⁹ but it does not specify the grounds or the standards the court should apply.

The Legislative Guide also provides that members of the creditors' committee should be exempt from liability for their actions as committee members, except in the case of fraud or willful misconduct, and that the law should identify the grounds for a committee member's removal and replacement.⁴¹⁰ The new Chinese law does not provide such protection, nor does it specify the grounds or standards that should be applied in removing and replacing members of the creditors' committee.

4. Claims by Related Persons

The Legislative Guide provides that claims by related persons, whether in a family or business context, should be subject to particular scrutiny.⁴¹¹ In particular, the Legislative Guide suggests that an insolvency law should consider a mechanism to identify the types of conduct involving related persons that may give rise to suspicion and deserve special attention.⁴¹² Examples of such situations include transactions with the related person while the debtor is severely undercapitalized (such as a loan by an office holder of the debtor when debtor's company is undercapitalized and continues to trade without sufficient funds to pay creditors) and transactions involving evidence of self-dealing (such as a principal agreeing to a compensation package six months before the bankruptcy filing and then filing a claim for such compensation in the succeeding liquidation proceeding).⁴¹³ In these cases, the amount of the claim may be reduced and made subordinate to the claims of other classes of creditors, or "the voting rights of such creditor may be restricted with respect to certain issues" such as the selection of the insolvency representative.⁴¹⁴

The new Chinese bankruptcy law does not address this issue at all. In the interests of achieving the highest degree of transparency possible, the new law should include a provision addressing the scrutiny to be applied to related party claims. Under U.S. bankruptcy law, dealings between an insider and a debtor are subject to strict scrutiny, and with regard to a claim by the insider, the burden is on the insider to show the

409. See Corporate Bankruptcy Law, *supra* note 2, art. 22.

410. See Legislative Guide, *supra* note 176, recommendations 135-36, at 205.

411. See *supra* notes 353-56 and accompanying text.

412. See Legislative Guide, *supra* note 176, pt. two, V.A.3.f.ii, ¶ 48, at 262.

413. See *id.*

414. *Id.*, pt. two, V.A.3.f.ii, ¶ 48, at 262-63.

“inherent fairness and good faith” of a challenged transaction.⁴¹⁵ A similar provision should be considered for China’s bankruptcy law.

5. Conclusion of Proceedings and Discharge

Finally, the Legislative Guide provides that at the conclusion of bankruptcy proceedings, the issue of discharge of natural debtors from liability should be addressed, and that any debts excluded from discharge and any conditions attached to the debtor’s discharge should be clearly set forth.⁴¹⁶ While the new Chinese law might be read to imply that discharge of indebtedness occurs, it is not clear whether or not the discharge of debts will in fact occur, what standard the court must apply, or the procedure to follow for such discharge to occur.

C. General Areas of Concern with the New Law

In addition to the specific issues raised by the above comparison to Legislative Guide provisions, a number of areas of concern with the new law should be addressed.

1. Criteria for Recognizing Bankruptcy Filings

While the new Chinese bankruptcy law requires that the People’s Court recognize a bankruptcy filing,⁴¹⁷ it does not specify the criteria the court is to use in making that determination. Is the court simply examining the status of the debtor to be certain that the filing criteria for a bankruptcy application are met? Or is the court’s examination for some other purpose, such as assuring that the filing is not an improper use of the bankruptcy proceedings? The purpose of the court’s review and the criteria the court should apply are not identified in the new law.

Likewise, the new bankruptcy law does not define the term “insolvent,” one of the key criteria for the availability of a voluntary bankruptcy filing by a debtor.⁴¹⁸ The lack of a definition for this term is important because the term has different meanings in different contexts. For example, under U.S. corporate law, insolvency is determined under either a balance sheet test, where a firm is insolvent if its liabilities

415. *In re All-American Auxiliary Ass’n*, 95 B.R. 540, 544, (Bankr. S.D. Ohio 1989).

416. *See supra* notes 365-68 and accompanying text.

417. *See Corporate Bankruptcy Law, supra* note 2, arts. 10-12.

418. The provisions detailing the criteria for determining insolvency were also unclear in earlier drafts, which required proof of “bad management and the incurring of heavy losses” leading to an “inability to discharge matured liabilities.” *See Harmer, supra* note 374, at 2575. This standard was criticized as “unclear, vague and open to disagreement.” *Id.*

exceed its assets,⁴¹⁹ or an equitable insolvency test, where a firm is insolvent if it cannot pay its debts as they become due in the ordinary course of business.⁴²⁰ The determination of insolvency can be very difficult because it depends on accounting calculations which are far from static.⁴²¹

On the other hand, in finance literature a firm's insolvency is measured in a different way: a firm is considered insolvent if it cannot pay its bills when due without undue distress—that is, without resorting to selling illiquid assets at a significant loss of value.⁴²² This focus on the practical effects of a firm's inability to pay bills is substantially similar to the first element of eligibility under the new Chinese law—the inability to repay debts that fall due.⁴²³

The term insolvency and what it means in the context of Chinese business operations must be more clearly defined. As some commentators suggest, Chinese courts are heavily dependent both politically and financially on the Chinese government and therefore may be subject to pressure, particularly with regard to State owned enterprises.⁴²⁴ These potential concerns over lack of transparency and misuse and misapplication of the process⁴²⁵ are not satisfied by such a general lack of criteria and guidance.

2. Exception for Certain Employee Expenses

While the new system of priorities applies generally to claims under the new Chinese bankruptcy law,⁴²⁶ there is a potentially significant exception to this revision of bankruptcy priorities. As discussed above,⁴²⁷ wages and medical payments and debts for medical, retirement

419. See Cory Dean Kanderstin, *The Duty to Creditors in Near-Insolvent Firms: Eliminating the "Near-Insolvency" Distinction*, 60 VAND. L. REV. 1235, 1244 (2007).

420. See *id.*

421. As one commentator points out, "given the malleability of accounting figures, reasonable people may disagree on when a firm is insolvent in fact, especially under the balance sheet test, which relies on a comparison of accounting figures." *Id.*

422. For a discussion of the liquidity of a firm and relevant solvency measures, see STEPHEN A. ROSS, RANDOLPH W. WESTERFIELD & BRADFORD D. JORDAN, *FUNDAMENTALS OF CORPORATE FINANCE* 57-62 (7th ed. 2006).

423. See *supra* note 203 and accompanying text.

424. Wu, *supra* note 20, at 244.

425. An earlier draft of the new bankruptcy law allowed the court to declare the debtor bankrupt whenever it discovered that the debtor had failed to pay off debts due, which, when combined with the lack of the possibility of a reorganization, led some commentators to suggest that this could lead to liquidation of businesses that could have been rescued and that such powers increase the opportunity for corruption and other abuses. Gebhardt & Olbrich, *supra* note 374, at 114. These same concerns are equally applicable to the lack of criteria and guidance under the new law.

426. See *supra* notes 112-24 and accompanying text.

427. See *supra* notes 120-24 and accompanying text.

and insurance expenses for employees of the bankrupt entity that were owed before August 27, 2006 receive priority treatment over the secured creditors of the debtor. While this provision is limited in scope to debts that were already in existence prior to the new bankruptcy law, the recognition that such debts can be given priority over secured creditors' claims is likely to concern many creditors. Moreover, many large, State-owned enterprises are believed to have large liabilities that fall within the scope of this exception.⁴²⁸

3. Ambiguity of Cross-Border Insolvency Provisions

While the new Chinese bankruptcy law does provide a procedure for the recognition and enforcement of foreign bankruptcy judgments in China,⁴²⁹ the standards the court must apply are vague and ambiguous. In order for the Chinese court to recognize judgments and decisions of a foreign court involving the debtor's property, the Chinese court must scrutinize the judgment in accordance with applicable international treaties, and may recognize and enforce the judgment where the court determines that it does not "impair the security and sovereignty of the country and social and public interests or the legitimate rights and interests of the debtors within the People's Republic of China."⁴³⁰ While the inclusion of provisions in the new law concerning recognition of foreign bankruptcy is an improvement over earlier drafts,⁴³¹ it is still inherently vague and sufficiently ambiguous to be cause for significant concern regarding the enforceability of a foreign bankruptcy judgment in the courts in China. The addition of a provision similar to the U.S. cross-border insolvency provisions under Chapter 15⁴³² would be very useful and would boost creditor confidence in the Chinese bankruptcy system.

4. Administration of the Law in Practice

Finally, it is too early to tell how the new Chinese bankruptcy law will be administered in practice.⁴³³ While the new law makes significant strides in terms of coverage and transparency, those who have observed China's efforts to implement and enforce intellectual property laws⁴³⁴

428. See McDonald, *supra* note 375.

429. See Corporate Bankruptcy Law, *supra* note 2, art. 5.

430. *Id.*

431. Earlier drafts adopted a territorial approach to international bankruptcy, under which procedures of bankruptcy outside China were not effective with regard to the debtor's property within China. See Gebhardt & Olbrich, *supra* note 374, at 121.

432. See *supra* notes 170-75 and accompanying text.

433. See generally McDonald, *supra* note 375.

434. See generally Robert C. Bird, *Defending Intellectual Property Rights in the BRIC Economies*, 43 AM. BUS. L.J. 317 (2006); Frank Lin, *Piracy In China: Identifying*

know that enacting the legislation and creating a workable system from the legislation are two very different things.

VI. Conclusion

The adoption of the Corporate Bankruptcy Law is a significant step forward in Chinese bankruptcy law. While the new law is not perfect and does have some areas in which improvement is needed, it broadly expands the scope of coverage under and the transparency of Chinese bankruptcy. Moreover, the new law brings much of Chinese bankruptcy law in line with modern bankruptcy theory, particularly in the area of priorities in bankruptcy. In many respects, the new law is in accord with the suggestions and recommendations of the UNCITRAL Legislative Guide to Insolvency Law. In those areas where it is not, and in those areas where the law is weak, including the definition of insolvency and the ambiguity of cross-border insolvency provisions, modifications to the new law would be useful.

The new Corporate Bankruptcy Law is a good indication that China's economic reforms are strong and continuing. The statement at the beginning of this article that "capitalism without bankruptcy is like Christianity without hell"⁴³⁵ is quite accurate, and the new law is a significant addition of a set of consequences for China's private enterprises.

The Problem And Implementing Solutions, 14 CURRENTS: INT'L TRADE L.J. 83 (2005); Peter K. Yu, *From Pirates to Partners: Protecting Intellectual Property in China in the Twenty-First Century*, 50 AM. U. L. REV. 131, 139 n.37 (2000); Gregory S. Feder, *Enforcement of Intellectual Property Rights in China: You Can Lead a Horse to Water, But You Can't Make it Drink*, 37 VA. J. INT'L L. 223, 241-42 (1996).

435. Rogers, *supra* note 1.

