

Research on the Theoretical Basis of Limitations on Personal Bankruptcy Exemptions

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Abstract: The exemption system is the core of modern personal bankruptcy law, but it should be clear that the bankruptcy exemption is not a system that exclusively serves the debtor, but it is the result of balancing the interests of the creditors, the debtor and even the whole society, so it is indispensable to construct the personal bankruptcy exemption system and to make certain limitations on the exemption. The theoretical analysis of the limitation of personal bankruptcy exemption is carried out by elaborating on the theory of debtor cooperation, humanitarian theory and social utility theory. The theory of debtor cooperation is based on the background that the society encourages the bankrupt to cooperate actively and severely cracks down on malicious debts, when it comes to humanitarianism, the personal bankruptcy exemption legislation obviously changes from creditor standard to pay equal attention to the interests of creditors and debtors, and increases the obligation for creditors to respect the survival and development of debtors and protect the personal dignity of debtors. Then the theory of social utility shows that creditor's rights should be subject to the overall interests of society and be restricted. The legislation of individual bankruptcy has changed from individual standard to social standard, and the understanding of the legislature on individual bankruptcy has gradually deepened.

Keywords: Personal Insolvency; Insolvency Exemptions; Limitations on Exemptions; Debtor Cooperation; Humanitarian; Social Utility

1. Introduction

Personal insolvency exemption refers to a legal system that exempts an "honest and

cooperative" insolvent from the responsibility of continuing to discharge his debts. In comparative law countries as well as some regions of China, there have long been personal bankruptcy and its exemption system legislative practice. The United Kingdom, the United States, Germany, Japan and other countries have made detailed provisions on the commencement conditions and procedures of personal bankruptcy, as well as the conditions and limitations of exemption from liability. From the implementation of the Shenzhen Special Economic Zone Personal Bankruptcy Regulations in 2021 to the economic "rebirth" of the debtor in China's first personal bankruptcy case in June 2023, it means that the implementation of the personal bankruptcy system in China is feasible, but regrettably, there are problems with the application of restrictive clauses of the exemption system and the legal practice of the pilot regions, such as Zhejiang, Guangdong and Shandong. Unfortunately, there are problems in the legislation and judicial practice in the pilot areas such as Zhejiang, Guangdong, Shandong, etc., such as the contradiction between the applicable limitation clauses of the exemption system and the system of civil law, the uncertainty of the authority of the license exemption, the excessively long period of exemption, the exempted types of debts, and the lack of exemption. In order to solve the practical problems in these specific areas, it is necessary to return to the theoretical basis of personal bankruptcy exemption limitations and the necessity to examine them.

2. Theoretical Basis for Limitations on Personal Insolvency Exemptions

The theoretical basis of exemption limitation has a fundamental impact on the design system of personal bankruptcy exemption system in China, and the biggest obstacle encountered in the implementation of the exemption system in

the Shenzhen Bankruptcy Regulations is the public's concern about debt evasion. Therefore, it is necessary to limit the exemptions and understand the integration of multiple concepts behind the personal bankruptcy exemption limitations, so as to construct the personal bankruptcy exemption limitations norms suitable for China's national conditions.

2.1 Debtor Cooperation Theory

The theory of debtor cooperation was first introduced by our scholar Zou Hailin in 1994 from the spirit of British legislation[1]. The core essence of the theory is to maximize the interests of creditors by exempting debtors from liability in exchange for their cooperation, i.e., their greater willingness to cooperate with the procedure to alienate property. The theory of debtor cooperation only grants exemptions to debtors who are willing to cooperate, viewing the granting of exemptions to debtors as a temptation to induce debtors to cooperate with creditors and insolvency administrators as much as possible in insolvency proceedings to enhance the efficiency of the debtor's asset locating, collection and liquidation work[2]. If the debtor is willing to cooperate, the exemption will be granted, and vice versa, it will not be granted. Undoubtedly, the cooperation of debtors is closely related to the increase of creditors' interests, because debtors who are willing to cooperate play a crucial role in increasing the size of assets available for distribution and reducing the administrative costs of distribution, which enables creditors to obtain the maximum distribution of property at the moment and obtain real satisfaction[3].

The foregoing is the ideal performance in insolvency proceedings of an honest debtor who obtains exemptions, but not all debts can be exempted, and the theory of debtor cooperation goes some way to answer the question of why exceptions to exemptions, limitations on exemptions, should be carefully considered. We have to consider the limitations of the exemptions to a degree, the debtor cooperation theory for limiting personal bankruptcy exemptions is a balancing art, in general, creditors would like to see the personal bankruptcy exemptions harshly limited, in order to not only get a real discharge in the present, but also get a subsequent discharge in the future when the debtor's property condition improves. Whereas

too many restrictions on personal bankruptcy exemptions are clearly unfriendly to debtors, why should debtors cooperate if exemptions are not available for most debts? Therefore, the theory of debtor cooperation should balance the interests of creditors and debtors when guiding the limitation of exemptions, and enhance the willingness of both parties to cooperate, so that the bankruptcy exemptions can play their proper role.

2.2 Humanitarian Theory

Although the debtor cooperation theory can provide the original impetus for the personal bankruptcy exemption limitation legislation, it is not difficult to see that the center of gravity of the theory is still to serve the interests of creditors, the early personal bankruptcy legislation in the United Kingdom is pervaded by overprotection of creditors and overprotection of creditors, such as indefinite imprisonment of the debtor, however, in addition to leaving the debtor with a heavy burden of debt and pain, this approach does not does not compensate creditors for their losses and has no other benefits. With the historical evolution of the personal insolvency system, the legislative orientation of the personal insolvency system has changed, with legislation gradually seeking to strike a balance between the protection of the debtor and the creditors and taking into account the debtor's right to life and development, a change that has been influenced mainly by humanitarian theories.

Humanitarian theory affirms and promotes the intrinsic self-worth of the debtor, and it considers it a humanitarian imperative to pull the deeply indebted out of their crushing debt and into normal existence and development[4]. The automatic exemption doctrine in U.S. bankruptcy law functions to compel creditors and other members of society to forgive the insolvent. Forgiveness does not mean that the injured party can be restored, but the exemption has a restorative function for both creditors and debtors. First, the detailed examination and review of the debtor's personal and property affairs in bankruptcy restores the sense of imbalance in the minds of creditors who have been left unsettled by the exemption, and second, the transformative power of the bankruptcy process protects the debtor's self-esteem[5], enabling him or her to

regain the strength to become a productive member of society, whose self-reliance reduces the depletion of society's scarce resources. Bankrupt debtors are already vulnerable members of today's creditworthy society, and treating them with "an eye for an eye, a tooth for a tooth" will inevitably ignite the fires of evil in their hearts and trigger social unrest; conversely, showing them enough respect and concern will motivate them and promote social healing.

Although modern bankruptcy law is not only a guarantee of a sound credit system, it is also a humane law in the history of the code. However, historical experience has shown that not all bankruptcy debtors are persons of good morals. Since the creditor under the humanitarian theory has to be benevolent, the debtor must also have good morals and be of good character. Social experience tells us that complete humanitarianism is not desirable, because an immoral debtor is not worthy of the exemption qualification, if because of complete humanitarianism to let the bankruptcy debtor to get away with it, then it is unacceptable to the creditors, will inevitably damage the interests of the creditors, and exacerbate the phenomenon of the bankruptcy debtor to evade the debt, if the impunity has become a common phenomenon, the moral hazard will be unanticipated increased The moral hazard will increase unanticipatedly if impunity becomes a common phenomenon. Even in the United States, where exemptions are minimized, it is impossible for debtors to obtain unlimited exemptions. Thus, the law must properly interpret humanitarian theory to play a role in identifying immoral debtors. In short, humanitarianism is never about unlimited exemptions; what it really seeks is to minimize the limits of exemptions so that as many "honest but unfortunate" debtors as possible can rebuild their finances, and that is its true value.

2.3 Social Cost-benefit Theory

The social cost-benefit theory was firstly introduced into China by Professor Zeng Erxiu in 2000 and discussed[6], which mainly verifies that the exemption is more conducive to the promotion of social well-being by comparing the social costs and benefits of exemption with those of non-exemption, and also emphasizes the necessity of restricting the

exemption of bankruptcy.

Bankruptcy exemptions can give debtors the courage to take risks, thus stimulating market vitality, while exemption limitations can remind debtors to remain rational. Bankruptcy exemptions can provide natural persons engaged in commercial activities with a minimum level of protection, preventing the debtor from falling into an impossible situation as a result of bankruptcy. If personal bankruptcy is not allowed to be exempted from liability, it means that after a debtor suffers from bankruptcy once, it is very likely that his or her life will be shrouded under the cloud of debt disputes in the future, and he or she will be devastated, and he or she will no longer have the courage and confidence to rise again and return to a normal life at an early date, which will cause society to lose a labor force that can create wealth. Moreover, if the debtor will not be exempted from liability, he or she will resist bankruptcy filing out of shame, not to mention actively cooperating with creditors and administrators to promote the operation of bankruptcy proceedings. Bankruptcy law hopes that through the exemption to stimulate the debtor's spirit of commercial adventure, promote economic innovation, but in the case of unlimited bankruptcy exemption, the debtor may be overconfident in the future economic market, too objective to the business risk[7], at this time, the cost of exemption is higher than the benefit of the exemption, in this case to give the debtor exemption is obviously too irrational, the limit of bankruptcy exemption to correct the irrational mechanism.

Bankruptcy exemption limitations also help prevent bad faith debt avoidance. On the surface, the non-exemption doctrine may seem to safeguard the interests of creditors, but the real situation may be more than that. Upon hearing of the non-exemptions, the debtor may maliciously conceal his solvency and make up for his debts by tearing down the east wall and causing further deterioration of his property, and by the time a large number of creditors come to collect the debts, it will be difficult for them to settle the debts, thus wasting the energies and resources of the two parties. Bankruptcy exemption as a means to solve the debt problems of both parties in one package, so that both parties can focus on new business operations[8], while allowing both parties to get relief, but also integrates the overall

resources of the community, and promote social prosperity and stability. However, there is no doubt that if such a good thing as exemption falls on a bankrupt who is maliciously indebted, such a person will surely intensify his efforts to evade debts, and then the good theory of exemption from bankruptcy will be in vain, therefore, it is necessary to limit such a situation outside the scope of exemption from bankruptcy.

3. Justification of Personal Bankruptcy Exemption Limitations in China

The practice of personal bankruptcy exemption limitation in China is still in the initial exploration stage, but the general conclusion from the scholars' research is that personal bankruptcy is no longer a purely moral issue and bankruptcy debts should be allowed to be exempted. Preventing the bankruptcy procedure from being reduced to a channel for debtors to evade debts has always been a concern of legislators, and is also related to the confidence of the community in the personal bankruptcy system[9]. This viewpoint is justified in the unique national conditions of China, and the current lack of a systematic and comprehensive understanding of the concept of personal bankruptcy exemption by the masses inevitably creates a serious moral hazard for the society[10]. Although some scholars study the relationship between bankruptcy exemption and "debt evasion" and elaborate that the exemption will not become a tool for debtors to evade debts, but only a small number of professionals will have such an objective and systematic understanding, and there is still a gulf of practical proof that is still missing from the hearts of the people, and the judicial practice is based on the scientific legislation as a prerequisite, so it is particularly important to emphasize the importance of restricting personal bankruptcy exemption at the legislative level. Therefore, it is particularly important to emphasize on the legislative level to limit the personal bankruptcy exemption. The evolution process of the leniency and severity of bankruptcy exemption limitations in various countries has proved that the personal bankruptcy exemption limitations are the choices of a variety of theories working together.

4. Concluding Remarks

To sum up, when China carries out the legislation on personal bankruptcy exemption limitations in the future, it should not only consider the appropriateness of the bankruptcy exemption system and the status quo of China's social development, but also skillfully deal with the heterogeneity between the viewpoint of "repaying the debt is a matter of course" in the traditional culture and the "fresh start" concept of existing bankruptcy exemption. The heterogeneity between the traditional culture's viewpoint of "repaying debts and paying money" and the existing bankruptcy exemption concept of "starting over" is skillfully dealt with, and the path of bankruptcy exemption restriction is constructed under the guidance of diversified exemption concept. "The life of law is always not logic, but experience", bankruptcy and exemptions should be understood and accepted by the public in real cases, therefore, the most appropriate approach in China is to integrate the concept of multiple exemptions and balance the interests of many parties, so as to be widely recognized in the practical implementation.

The purpose of personal bankruptcy is not only to pool property and make collective liquidation, but also to safeguard the right to survival and development of the bankrupt debtor and his or her co-living members, and to maintain stable and healthy development of society. Not only should creditors be subject to compromise in the overall interests of society, but bankruptcy exemptions should also operate under appropriate restrictions in order to balance conflicting interests.

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