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Different Statues- On the Necessity of Separate Legislation of Personal and Corporate Bankruptcy Law

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Abstract: Within the framework of the existing bankruptcy legal system, there are a series of differences in the classification of bankruptcy law in various states, such as New Zealand, Australia and Canada. The focus of this "classification" is "whether it is necessary to distinguish between the the legal provisions of the personal bankruptcy and corporate bankruptcy in terms of legislation and justice, which is also one of the hot topics in legal circles. At least for now, a popular trend seems to be to dismiss such "distinction", which is "looking the insolvency legal system as a whole". If we just observe it from the perspective of legal logic, this view has its rationality on a certain extent. However, as long as we combine the legal theory with the practice, we will find that there are a series of crucial differences between personal and corporate bankruptcy both at the theoretical level and in the approach of reasoning when coping with the relevant cases (for example, corporate bankruptcy needs to be differentiated based on the size of the enterprises, personal bankruptcy should consider the basic survival of the debtor in addition to the repayment of the debts.) Such crucial differences make it impossible to forcibly unify these two (personal and corporate bankruptcy law) in one legal system; Otherwise, on the one hand, there will be the unnecessary costs of re-legislation. On the other hand, it will also cause unnecessary to the parties (whether individuals or enterprises) and judges to make judgments in judicial practice. Therefore, based on the above opinions, the essay will demonstrate the distinctions between personal and corporate bankruptcy law, with the aim of explaining a conclusion: personal bankruptcy and corporate bankruptcy are two completely different systems; Therefore, in terms of legislation, not only should these two not be unified, but also needs to be further distinguished on the basis of the existing law.

Keywords: Bankruptcy Law; Corporate Bankruptcy; Personal Bankruptcy; SMEs (Small and Medium-Sized Enterprises); Debtor`s Basic Survival

1. Introduction

With the introduction of Corporations Amendment (Corporate Insolvency Reforms) Bill 2020, the request for "radical revolution of insolvency law" seems to become more and more popular in Australia. Under this trend, there is an issue that is constantly being raised by a lot of organizations and scholars, namely: the unification of personal and corporate bankruptcy law. (For example, Professor Mason mentioned "the need for a comprehensive review with proper regard to the structure of the modern Australian economy", as well as "the importance of Australia looking at insolvency as a whole"[1], Furthermore, Minter Ellison questioned the so-called fragmentation in insolvency system, in addition, a view with potential tendency was also expressed by the Australian Restructuring Insolvency and Turnaround Association (ARITA) : The division between personal and corporate insolvency was the primary cause of unnecessary complexity in system.[2]) According to the above point of view, it can be seen that the integration of a legal system, specifically, the fusion of personal and corporate insolvency provision seems to be a general trend. Therefore, in this realistic background, this essay will critically analyze the differences and the connections between the personal and corporate insolvency law from multiple perspectives (more specifically, the legislative theory and the judicial practice perspective). Then, all the discussion and examples raised in this paper are used to try to prove a conclusion that basically opposite to the individuals and organizations mentioned above, which is: personal bankruptcy and corporate bankruptcy are two "racing cars on different tracks". In other words, they are two completely different legal systems. Therefore,

not only should they not be unified directly, but on the contrary, the differences between those two should be further emphasized in legislation and judiciary level on the existing basis. To prove this point, this paper will demonstrate the analysis from three perspectives, the general structure is as follows.

2. "What" Fundamental Theories

The fundamental theories related to this essay mainly refer to the conceptual differences between personal and corporate bankruptcy, which can be divided into the following two aspects:

1) Causes result in bankruptcy are different:

For corporate bankruptcy, the reasons for this outcome are relatively simple:

a) The company is unable to pay off the debts which are due, and all assets cannot repay all debts.

b) The company does not repay the debts that about to expire and it can be presumed that the company is evidently insolvent. (such as a long-term operating loss without any significant improvement)

However, for personal bankruptcy, the reasons regarding that are more complicated, which can be generally divided into three categories according to the behavior of the individuals:

a) Joint bankruptcy: The so-called "joint bankruptcy" means the "personal bankruptcy" because of the bankruptcy of an enterprise, more specifically, is a situation that individuals incur the debts of a bankrupt company due to some reasons (for example, directors are personally liable for company`s debts as a result of insolvent trading), and they become bankrupt because of their inability to repay these debts.

b) Operational bankruptcy: Unlike "joint bankruptcy", the "operational bankruptcy" refers to a circumstance that during the course of a natural person engaging in business activities with his or her own name (individually-owned businesses), the person becomes insolvent due to business failure; or a situation when a person goes bankrupt because of the failure during the process of personal investment activities. (such as buying stocks)

c) Daily consumption bankruptcy: Compared with the above two, this type of bankruptcy is easier to comprehend, which means that a person become bankrupt due to improper daily consumption, such as credit card overdraft or inability to repay the loan that used for daily living.

From the above comparison, it can be seen that the causes of personal and corporate bankruptcy obviously cannot be classified in the same sphere and the reasons about personal bankruptcy are more complex. This is mainly because as a subject, natural people have more freedom than enterprises thus they(person) are able to carry out more diverse activities.

2) The consequences of bankruptcy are different:

a) Corporate bankruptcy: Regardless of any company, as long as it goes bankrupt, its subject qualification will inevitably be extinguished. Because the fact, bankruptcy, is enough to demonstrate that the company has lost the ability to operate normally, and the company, without any operating capacity, has no social value to continue to exist.

b) Personal bankruptcy: Personal bankruptcy is totally different. We can say that a bankrupt company are "dead"; however, the subject status of natural person will not be eliminated because of bankruptcy, but keep its existence. Therefore, more factors should be considered about personal bankruptcy than corporate. For corporate bankruptcy, no rights should be created, instead it should act to ensure that the rights that exist are vindicated to the extent possible. [3] Nevertheless, regarding personal bankruptcy, in addition to protect the legal interests of creditors, from the perspective of human rights, the basic survival of an insolvent individual in society should also be noted. For example, for a bona fide natural person, whether it is necessary to keep a part of property to maintain the expenses for his daily life.

In summary, there are some profound distinctions between personal and corporate bankruptcy in theoretical level, so it seems unrealistic to completely unify these two legal systems. On the contrary, the separate legislation for personal and corporate bankruptcy should be further emphasized according to the existing differences between these two.

3. "Why" Existing Arguments

1) Two views contrary to this essay:

Regarding the separate legislation of personal and corporate bankruptcy, there are some controversies in society, among which the most popular objections are the following two:

Firstly, two separate regimes will incur unnecessary complexity costs (costs include the difficulty for some small and medium-sized

enterprises (SMEs) to comprehend the insolvency system, as well as the legal costs involved in the process of handling bankruptcy cases), this "unnecessariness" has a negative impact on both creditors and debtors;

Moreover, some SMEs in Australia actually have a mixture of personal finance and corporate finance; therefore, two separate systems will lead to hesitation or chaos in the court's legal application and jurisdiction when dealing with such bankruptcy cases.[4]

2) Analysis about the first view:

The first opinion is originated from the statistics and conclusions by Australian Financial Security Authority (AFSA). (Average debt for a business-related personal insolvency is $830,502, approximately 5.8 times larger than the average debt in a non– business–related insolvency ($141,733); Small businesses, AFSA wrote, 'frequently lack the resources and expertise to effectively understand and navigate complex and, in particular for small creditors, costly insolvency systems'[5]) The above reflection does reflect the current situation of some SMEs facing bankruptcy. However, this view has the following logical flaws:

a) The knowledge of the insolvency system is not directly determined by the size of the enterprise. In other words, the focus of AFSA`s conclusion is not on "lack the resources and expertise to 'understand', but on 'navigate' the system". Therefore, the "unnecessary complexity costs" mentioned in the view is not the result of separate legislation, but the existing insolvency system`s failure to take into account the realities faced by SMEs. Thus, to solve this problem, it is essential to formulate more targeted provisions for SMEs in terms of corporate bankruptcy legislation.

b) The issue mentioned by the first view cannot be solved just by unify insolvency legislation literally. The reason is that when facing bankruptcy cases, the subjects are not only the SMEs, but also purely bankrupt individuals who have no relation with company. Furthermore, in addition to the theoretical differences, there are also obvious distinctions in the trail ideas about personal and corporate bankruptcy in terms of judicial practice. The details are as follows.

Corporate bankruptcy: Regarding corporate bankruptcy, when making judgments, courts mainly use the "creditor`s perspective" in reasoning the case. The "creditor`s perspective" means starting from the creditor`s interest and giving priority to judging "how to reasonably distribute the debtor`s property to ensure the legitimate interests of creditors are maximized". This kind of "perspective" is reflected in many aspects of trial. For instance, when the liquidator seeks a "shelf order" from the court under s588FF(3) of the Corporations Act 2001 (Cth) ("The court may treat some transactions carried out by insolvent company before liquidation as "voidable transactions" according to the "shelf order"; in general, the granting of shelf order requires consideration of the specific facts of the case.), if the purpose of the liquidator seeking for the extension of shelf order`s time is just to decide an appropriate time to bring proceedings, then in order to save costs, the court have no obligation to conduct a preliminary enquiry of the merits of the case. In other words, although the potentially voidable transactions cannot be checked, the court may still grant an extension. This view was supported by Federal Court of Australia in a case judgment made in March 2024. The above facts means that the court broaden the scope of application of the "shelf order`s extension", which can give the liquidator more adequate time to confirm the debtor`s voidable transactions and increase the chance that the debtor`s property be divided by creditors, thereby ensuring the creditor`s losses can be compensated to the greatest extent. It can be seen from these facts that when dealing with corporate bankruptcy cases at the judicial level, the attention to creditors` interests is in a high position.

Personal bankruptcy: Personal bankruptcy is completely different. In judicial practice, unlike corporate cases, the so-called "debtor`s perspective" is mainly used when handling personal bankruptcy cases. The meaning of "debtor`s perspective" is reasoning the entire case from debtor`s interest and before determining a specific plan for the distribution of creditors` interests, priority is given to the actual financial situation of the debtor. (such as whether it is truly insolvent; whether there is an opportunity to discharge bankruptcy in short-term.) This "perspective" can also be reflected in some aspects. For example, Federal Court of Australia recently emphasized that among the three situations that bankruptcy was automatically discharged at the end of the three-year-period according to s149 of the Bankruptcy Act 1966 (Cth), the day when the "situation" occurs is not counted within the three-year-

period. This allows bankrupt person to better understand the deadline of automatic discharge of bankruptcy and manage their relationship with the trustee properly, such as jointly dealing with property attached to the trustee. In addition, Federal Court of Australia also confirmed that when coping with personal bankruptcy cases, the mental health of insolvent individuals (For example, whether the person has suffered from serious mental illness due to bankruptcy) should be taken into consideration in the judgement. This is an obvious difference compared with corporate bankruptcy cases; because judgments about corporate bankruptcy cases usually do not consider the negative impact of debtor. The importance of bankrupt "natural persons" during the trial of personal bankruptcy cases can also be seen according to these facts.

From above discussion, it can be concluded that in addition to conceptual differences, there are also obvious distinctions in judicial level between personal and corporate bankruptcy, and the "judicial-level differences" are actually reasonable. Because for an enterprise, the relationship between creditors and debtors is relatively clear; therefore, when courts dealing with such cases, it is important to focus on how the debtor`s property can be paid equitably among all creditors. No matter how unfortunate debtors are; creditors with good faith are always innocent victims. As for personal bankruptcy, as mentioned above, the complexity of "natural person" leads more costs when courts dealing with personal bankruptcy cases. What is more, the minimum living security of insolvent individuals should be taken into consideration as well. This is very complicated. Therefore, when facing personal cases, the courts should consider debtor`s perspective first and rigorously confirm the debtor`s actual situation. On the one hand, it may save judicial costs; On the other hand, it also embodies the humanity that is indispensable to the law. Therefore, the personal and corporate bankruptcy are two "totally different systems". The separate legislation dose not incur unnecessary costs; it is a choice that has to be made after considering the inherent distinctions between these two on both theoretical and judicial level. Although the USA, which formally unified bankruptcy legislation, recognizes the substantial differences between them.

3) Analysis about the second view

Regarding the phenomena mentioned in the second view, which is proposed by World Bank, even if it does exist in fact, it alone is not enough to overthrow the existing "separate legislation". The reason is as follows.

Sometimes, the so-called "mixture" of personal and corporate property does not a helpless choice for SMEs to maintain their normal business activities, but a chaotic situation they make on purpose, with the aim of increasing the difficulty of judging and liquidation, thereby evading some debts. For example, some people may conceal the actual assets of their insolvent companies which would be available for distribution to creditors by conducting some false transactions (such as the loan that is never intended to be repaid). More directly, the feature of these "false transactions" is the true intention of the parties in the "transactions" is obviously inconsistent with the apparent content of the "transactions". Moreover, the performance of the debt will not be delayed of impeded without such transactions. This type of "false transaction" can be executed by debtor on his own, or by debtor and trustee in collusion. Therefore, to protect the creditors` interests, courts usually need to order the debtor to explain the abnormal accounts with the request of creditors. The "false transaction" will be determined as long as the debtor cannot provide convincing reasons, then the legal effect of the "false transaction" will not be admitted. This opinion is illustrated by the judgement of Federal Court of Australia in March 2024. According to these facts, attention needs to be paid to such situation where some SMEs deliberately intermingle their personal and corporate property. Moreover, the phenomena (false transaction) can be avoided validly by separating legislation of personal and corporate bankruptcy scientifically. Because according to the current regulation, there are two organizations (liquidator administrated by ASIC and bankruptcy trustee administrated by AFSA) supervise the manager of SMEs at simultaneously when SMEs facing bankruptcy. This regime, on the one hand, can assist them to distinguish personal and corporate property more accurately to go through the bankruptcy. On the other hand, it can also reduce the chance of debtor making false representation to infringe the creditors` interests. In addition, about the SMEs and their legal representatives who apply the voluntary bankruptcy, the legislation can also confirm a regime that presumes the enterprises (or individuals) constitute "malicious bankruptcy"

then refuse their application under some circumstances to protect the debtors and creditors with good faith. (Malicious bankruptcy means debtors try to evade debts by applying bankruptcy, or creditors apply for the debtor`s bankruptcy to destroy the debtor`s business reputation.) However, the unification of legislation, means the unification of regulatory agency, as well as the standards of judging personal and corporate bankruptcy. This will reduce the supervision of debtors and the chance of debtors "making a profit in troubled situation" may increase.

4. "How" Possible Solutions

According to the "existing arguments" mentioned above, possible solutions, in other words, the general directions about personal and corporate bankruptcy legislation, can be considered from the following perspectives:

1) Personal bankruptcy

a) Provision about rejecting bankruptcy:

Regarding the situation that individuals use "bankruptcy" to get rid of debts, such as the deliberate mixing of personal and corporate property mentioned above, the regulation of China can be referred, in other words, denying the application for voluntary bankruptcy of natural persons under some circumstances, such as debts incurred due to illegal consumption (like purchasing illegal drugs); as well as avoiding debts by false representation (like "false transaction" mentioned above), hindering the litigation process and hindering the realization of creditors` interests.

b) Mandatory consideration about debtor`s basic survival

After personal bankruptcy, the identity of natural person still exists; therefore, the fundamental survival of debtor needs to be noticed. For example, if an insolvent individual with good faith indeed faces the dilemma in maintaining daily lives, the state should consider subsidizing some relief funds or forgiving some debts. Moreover, in addition to material life, the mental health of bankrupt person should be considered as well. As mentioned above, when a person facing bankruptcy suffers severe psychological pressure, the court has the responsibility to investigate the casual relationship between the "bankruptcy" and debtor`s "mental status". If the relationship can be proved, the court "must" consider the debtor`s mental health when making judgments and claims "the state has the obligation to ensure the health and welfare of a bankrupt or his or her family". This reflects respect for basic human rights.

2) Corporate bankruptcy

About corporate bankruptcy, considering the SMEs that have no choice but mixing personal and corporate property for operating, a more appropriate approach compared with spending a lot of costs unifying legislation is to publish the "amendment" specifically to deal with this situation on the basis of current regime. More directly, a more target bankruptcy system for SMEs needs to be formulated on the premise of separating the legislation of personal and corporate bankruptcy system, while preventing fraud by some SMEs. The details are as follows.

a) Limit the rights of liquidators and further optimize the position of SMEs when facing liquidation.

As mentioned above, liquidators can directly apply the extension of "shelf order" under some circumstances. This is unfair to some SMEs with limited funds and energy, because it will increase their pressure when facing bankruptcy. If too many legal transactions are revoked, the enterprises may lose the capacity to compensate their employees while paying off debts. In addition, if the scope of the extension of the "shelf order" is too board, the entire bankruptcy process will be delayed, which will also make the procedure that should convenient become cumbersome. Therefore, in order to improve the efficiency and take care of SMEs, it is necessary to consider limiting the ability of liquidators to propose voidable transactions sometimes. According to the Corporations Amendment (Corporate Insolvency Reforms) Bill 2020 announced by Australia, the time limit for proposing avoidable transactions has been shortened from 6 months to 3 months in terms of simplifying liquidation procedure. This is the "procedural reform". On this basis, adding "substantial reform" should be considered, which is: for SMEs, when the liquidator applies to the court for the "shelf order", the liquidator is responsible for proving the "avoidable transaction" at any time. In other words, the liquidator must try to demonstrate that the transaction applied for revocation is illegal, such as it constitutes fraud, or if not cancel, the interests of creditors will suffer significant losses, and so on. Otherwise, the liquidator cannot apply for the "shelf order". This will actually limit the scope of avoidable transactions for SMEs facing

liquidation, reduce the unnecessary pressure exerted by the current regimes on SMEs, so as to encourage them to rally as soon as possible.

b) Encourage negotiation between parties, let the court support forced mediation when necessary.

Considering the complicated situation faced by SMEs in the bankruptcy process, mainly including the hesitation of the court to apply Corporations Act or Bankruptcy Act, and the fact that SMEs needs to face two (or more) supervisory agencies, in order to better achieve the purpose of eliminating debts, it is recommended that court "release" the power to deal with specific situations of bankruptcy cases and encourage creditors and debtors to reach negotiation agreements on their own. More specifically, if in a specific bankruptcy case, both creditors and debtors can be presumed with good faith and diligent to fulfil their obligations, then the court can consider giving the power to handle the bankruptcy agreement to parties themselves (such as confirming a reasonable restructuring plan), rather than just holding the power of making judgments. In other words, the court should take the responsibility of a "mediator" rather than an "arbiter". The reason is that a healthy bankruptcy legal relationship, should not be a "zero sum game" between creditors and debtors; it is about reaching a result that is acceptable to all parties in terms of repaying debts with the joint efforts of both creditors and debtors. To accomplish this aim, the experience of Canada can be referred, which is under some circumstances, authorizing the court to force creditors and debtors to negotiate then create a mediation by themselves. For example, when the debtors indeed with good faith and are trying their best to resolve the issues regarding debt through fair negotiation, but the creditors still keep silence and reject to respond, or do anything that helpful to improve the situation, when this happens, in order to save costs, the court may force such creditors to appear in court and mediate with debtor. A series of potential positive effects will be brought by applying this regime. If the mediation fails, it will not cause actual losses to creditors or debtors; however, as long as an acceptable mediation agreement is created, it will obviously conductive to the realization of the debt`s restructuring plan. On the one hand, this regulation can protect the legitimate interests of creditors; on the other hand, it can also reduce the financial pressure of debtors, encouraging the debtors to get out of the trouble faster, thereby reactivate the so-called "dead end" of bankruptcy. In addition, there is one thing needs to be noted: forcing "a mediation agreement" can only force the act of "mediate" itself. Nevertheless, the court cannot interfere with the specific content of the agreement.

c) In bankruptcy cases, giving the experienced employees the right to express their opinions.

In terms of fraud prevention, as mentioned above, considering the situation that some SMEs intermingle personal and corporate property on purpose to avoid their debts does exist, it is recommended to strengthen the internal supervision of the enterprises (debtors) themselves. More specifically, it is to broaden the scope of applying bankruptcy, which currently can only be filed by creditors or debtors, permitting the experienced employees within the debtor`s company who disagree the specific situation of bankruptcy to raise their objections. Because compared with the courts, or other external people, the experienced employees usually have a more accurate judgment on the actual operating conditions of the indebted enterprise, as well as whether there is a chance of turning the losses to profit. Therefore, to prevent the appearance of avoiding debts deliberately, the law should give experienced employees reasonable freedom to participate in bankruptcy cases. Moreover, in order to increase the enthusiasm of employees to take part in the supervision, companies should pay attention to the "experience" of employees and do not deny their work easily, such as when the new employer denies the work or the original employer`s employees, the court ought to refute it, and the court has the obligation to consider the effect on employees when they are hearing the bankruptcy-related cases. If this regulation is established, it will also be helpful to reduce the situations that debtors cheat creditors in addition to mix their property, like the internal fraud within the debtor, which is, company`s directing mind conduct the fraudulent acts within the scope of his or her authority, then resulting in the losses of creditors. Under this circumstance, if experienced employees can be given the right to object to such behavior, the interests of both creditors and employees will be protected validly.

To sum up, the legislative directions that can be considered in the future regarding personal and corporate bankruptcy are obviously different. The personal bankruptcy regime should pay

more attention to the characteristics of the "natural person" identity; while the corporate bankruptcy regime needs to notice the actual situation of SMEs.

5. Conclusion

All in all, whether in the theoretical level, the judicial practice, or in terms of the direction for progress in the future, personal and corporate bankruptcy cannot be classified into the exactly same field. Therefore, not only should they not be unified directly, but on the contrary, these two regimes should be further distinguished on the existing basis.

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