

**The Bankruptcy Law in China:
Under-utilization and Reasons Behind**

A Thesis

Submitted to the

Stanford Program in International Legal Studies

At the Stanford Law School

Stanford University

In Partial Fulfillment of the Requirements

For the Degree of

Juridical Science Master

By

Xiao-gang Wang

May 1999

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Abstract

This thesis focuses on the Enterprise Bankruptcy Law of the People's Republic of China (Trial Implementation) (the "1986 Bankruptcy Law"), its textual stipulations, its instrumental application and under-utilization, and concludes with suggestions for future reforms.

This thesis starts with a brief review over China's economic reform since the 1980s. Following the successful agricultural reform in the countryside, China started a new round of more dramatic reform in the public industrial sector beginning in 1984. As the reform progresses, bankruptcy came to the forefront as the state hoped it would force the SOEs either to improve their management or face the specter of bankruptcy.

The reality shows, however, that the law has not achieved its proposed goals. Empirical research reveals that government has applied it selectively rather than automatically. The recent Guangdong International Trust and Investment Company ("GITIC") bankruptcy case shows how the law is being used by the central government to recentralize the country's financial control. Empirical study also reveals that the law is also being selectively used to help the government restructure the country's industrial structure.

The reasons behind this failure of application include both technical impediments inherent to law (such as the defects in commencement proceedings, loopholes in the

choice of liquidators which allow local favoritism, and problems with exoneration for negligence), and political-economic constraints in the post-reform Chinese socio-political environment (such as the existence of rigid price control and the lack of unified accounting rules and professional CPAs, local protectionism prevalent in the judicial system, and the government's fear of labor unrest that would follow a widespread implementation of the bankruptcy law, etc.).

The bankruptcy law's under-utilization has profound implications for the rule of law and legal reform in China. As part of China's modernization strategy, many other modern business laws have been introduced into China within the past decades. They have experienced problems similar to the 1986 Bankruptcy Law. The underlying reasons for these problems of implementation are found within China's modern transition, as communist ideology clashes with economic liberalization. When there is a conflict, the priority is usually given to maintaining political stability, leaving modern Western statutes as abstract stipulations on dusty books.

Reform of the public sector and bankruptcy law have gone hand in hand since 1986. The same institutional impediments that limit the bankruptcy law's application also restrict economic reform. Therefore, for successful application of the 1986 Bankruptcy Law, the inefficiencies of the public sector must be solved first. After discussing the weakness of the corporatization in bringing about improvements in economic efficiency, the thesis concludes that more dramatic reform of the economy is required to make the bankruptcy legislation meaningful: privatization of state enterprises.