

NEW COURTS ON THE BLOCK: A COMPARATIVE ANALYSIS OF BANKRUPTCY
LAW IN CHINA AND THE UNITED STATES

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Abstract

This paper examines the factors impacting utilization of China's Enterprise Bankruptcy Law (“EBL”). After a decade of underutilization, the EBL has experienced a significant increase in filings over the past decade. Utilizing legal formalism as an analytical framework, this paper conducts a comparative legal analysis with the United States Bankruptcy Code and analyzes historical data to explain the EBL’s use. The findings reveal that although there are substantial textual differences between the bankruptcy laws, the recent surge in EBL applications correlates more strongly with the establishment of specialized bankruptcy courts in China. This suggests that the choice of venue, influenced by the availability of these specialized courts, may be a key driver behind the increased use of bankruptcy filings. The paper concludes by highlighting the limitations of the current data and calls for more detailed, micro-level case studies to further explore the dynamics affecting bankruptcy law applications in China.

Keywords: Bankruptcy, China, legal formalism.

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INTRODUCTION

Over the past four decades, China has experienced a productivity miracle. It has sustained nearly ten percent annual GDP growth and lifted over 800 million people from poverty. This accounts for nearly three-quarters of global poverty reduction during this period (World Bank 2022). However, China's GDP growth has slowed for the past decade. In response, economists at the World Bank have highlighted the need for reforms in China's bankruptcy laws as a potential engine for future growth (Brandt 2020). Similarly, the Supreme People's Court of China has emphasized the importance of promoting and enhancing domestic bankruptcy laws to support economic transitions (Ren, Xu, Liu, and Wei 2023).

Bankruptcy laws are critical in determining the fate of financially distressed entities and their impact on the broader economy. In the United States, the U.S. Bankruptcy Code is a cornerstone of the economic system. This framework underpins the dynamic principle of 'creative destruction', crucial for long-term economic vitality and innovation. It is utilized by entities ranging from individuals to major corporations and plays a vital role in facilitating economic resilience and adaptation through structured processes for reorganization and liquidation (Mrockova 2020, 190). Established over a century ago and continuously refined, the U.S. Bankruptcy Code serves as a global benchmark for its comprehensive approach (Schick 2006, 219).

In 2006, China enacted its landmark Enterprise Bankruptcy Law ("EBL"), which was designed to align the national bankruptcy system with international standards. The EBL came into force in 2007 and introduced a unified legal framework applicable to all types of enterprises, both state-owned and private (Bendapudi 2008, 211). It established clear insolvency procedures,

providing a predictable and orderly resolution process similar to the Chapter 11 provisions of the United States (Lee and Ho, 165). Additionally, the EBL improved protection for creditors and employees by prioritizing the payment of unpaid wages and social security contributions and enhancing creditor rights to ensure more equitable asset distribution.

However, despite these advancements, the following decade saw a decline in the number of bankruptcies in China compared to the period before the law was passed. Moreover, the ratio of bankruptcies to the total number of companies in China was significantly lower than that observed in other countries such as Russia, England, or Germany (Mrockova 2020, 190). Compared to the United States, the rate of bankruptcies in China was 200 times lower than expected (Zhang 2018).

This paper argues that textual differences between the EBL and U.S. Bankruptcy Code can explain the infrequent application of the EBL. In various legal domains, China employs a legal formalism approach – a judicial philosophy that mandates strict adherence to the letter of the law in decision making (Kennedy 2001, 8634). Utilizing legal formalism as an analytical lens, this paper identifies six major textual differences between the EBL and U.S. Bankruptcy Code to explain the lower incidence of bankruptcies in China. These differences are the filing criteria, insolvency requirements, automatic stay provisions, debtor-in-possession (“DIP”) procedures, reorganization plan timelines, and control of venue; each can contribute to the disparity in bankruptcy rates observed between the two countries.

Further, the paper examines recent bankruptcy data from both China and the United States to evaluate these textual divergences more critically. In particular, data reveal the EBL becomes used at a rapidly increasing rate after 2015 and surpasses the number of corporate

bankruptcies in America by 2020. This paper posits that while earlier reforms such as differences in DIP protocols and reorganization plan timelines under the EBL have not substantially influenced bankruptcy rates, the control of venue, which may be a proxy for specialized bankruptcy courts, appears to be a more significant factor.

In exploring if legal formalism is an appropriate theoretical framework for bankruptcy in China, this paper contributes a comprehensive comparison of major textual differences between the U.S. Bankruptcy Code and China's EBL. For practitioners, understanding these differences provides crucial insights for companies considering bankruptcy proceedings in China. This comparative analysis is particularly valuable for managers in multinational corporations, aiding in navigating the complexities of bankruptcy laws across different jurisdictions.

The remainder of this paper is organized as follows: Section 2 presents a literature review which highlights bankruptcy studies and legal formalism. Section 3 outlines the research methods used in this paper. Section 4 presents the key textual differences between the U.S. Bankruptcy Code and Chinese EBL, as well as statistics about bankruptcies in the United States and China. Section 5 discusses the implications of these results. Section 6 concludes the paper with a summary of findings and potential directions for future research.

LITERATURE REVIEW

This literature review will first provide an examination of global bankruptcy studies, with a particular focus on the U.S. Bankruptcy Code as a widely adopted model in various legal jurisdictions. It will review a range of methodologies employed to study the law, from qualitative assessments to quantitative analyses. Next, the literature review will transition to the Chinese context and highlight unique challenges posed by the lack of robust bankruptcy data. This

section details efforts by scholars to navigate and interpret the sparse data landscape in China. Lastly, this review discusses the application of legal formalism as a theoretical lens for understanding Chinese law more broadly, with specific attention to its use in legal interpretations during the 20th and 21st centuries.

Global Bankruptcy Studies

Within global bankruptcy studies, the United States Bankruptcy Code is a critical paradigm for scholars studying bankruptcy. The frequency and availability of robust data from the United States has resulted in numerous studies exploring both qualitative and quantitative aspects. For example, in France (Cafritz and Gillespie 2005, 41), Japan (Matsushita 2006), and the Netherlands (Raaijmakers 2001), analyses of the respective national laws consistently reference the influence of the U.S. Bankruptcy Code. Furthermore, comparative studies like those by Bohanon and Plouffe (1999) on Mongolia and Manganelli (2010) on Italy directly analyze the texts of the laws to underscore differences with the U.S. Bankruptcy Code.

In addition to these qualitative comparisons, researchers have utilized a diverse range of methods to measure the impact of bankruptcy laws. This is an especially difficult task given that there are many external and immeasurable factors which contribute to the enforcement and impact of the law. Hotchkiss (1995) and Bris et al. (2006) examined instances where firms repeatedly filed for Chapter 11 to study if too many firms are preserved under U.S. bankruptcy provisions. In another approach, Chang and Schoar (2006) studied judge assignment to determine that judges with a pro-creditor bias tend to be more efficient in their rulings. Antill (2021) provides a model of bankruptcy based on similar judge assignment. Additionally, Eraslan

(2008), employed game theory to estimate the significance of the liquidation value in bankruptcy negotiations.

Quantitative comparative studies also extend to evaluations of other nations' bankruptcy frameworks in relation to the U.S. Bankruptcy Code. Thorburn (2000) explored the Swedish auction-based bankruptcy system, and concluded it was faster and minimized deviations from the absolute priority rule compared to Chapter 11 in the United States. Conversely, Ravid and Sundgren (1998) found that the Finnish bankruptcy system is less efficient when compared with Chapter 11 in the United States.

Chinese Bankruptcy Studies

Increasingly, quantitative research is being conducted on Chinese bankruptcy law. The first significant data set, encompassing 930 bankruptcy cases from 2007 to 2015, was manually compiled by Zhang (2018) using archives from The China People's Court Daily. Since 2014, millions of Chinese court judgements have been digitized, which has also enhanced data accessibility (Liebman, Roberts, Stern, and Wang 2022). Using China's "National Corporate Bankruptcy Information Disclosure Platform," Li and Ponticelli (2022) created a dataset of 2815 bankruptcy cases from between 2011 to 2020. Additionally, many courts have developed their own online bankruptcy platforms and populated them with regional court filings (Austin and Lin 2020, 5). Despite these efforts, data remains sparse as local courts fail to disclose more than 60% of their legal opinions (Zhuang, Wong, Yi, and Zhang 2022).

Therefore, in contrast to the United States, where quantitative research on the bankruptcy law is well-developed, studies on Chinese bankruptcy law remain predominantly qualitative. Patel (2009) and Bufford (2007) have explored the overarching structural similarities between

Chinese and American bankruptcy laws. Conversely, Woodward Jr. (2008) delineates four significant textual differences between the two laws. In the decade after the EBL's promulgation, scholars began to observe the EBL was seldom used in practice. To explain this, Jiang (2014) provides a comprehensive comparative analysis of Chinese and U.S. bankruptcy laws. Since then, another decade has passed, and the EBL in China has continued to develop. Economically advanced regions, such as Shenzhen and Zhejiang, have reported approving more bankruptcies and have also begun to resolve them faster (Steele et al. 2018, 678). Thus, there is a gap in the literature for a qualitative study of differences given changes in the EBL and its usage.

Moreover, recent scholarly work has pursued qualitative explanations for the limited adoption of the EBL that extend beyond its text. Mrockova (2021) adopts a societal-level perspective, suggesting that implementation lags in China compared to the United States are influenced by societal biases against bankruptcy. Ruilian et al. (2022) attribute bankruptcy inefficiencies to political pressures, while Li and Ponticelli (2022) as well as Steele et al. (2018, 672) point to judge education and political interference as key factors. These impacts underscore the need for further research to reconcile these factors and clarify their impact on their adoption of the EBL.

Legal Formalism in China

In China, legal formalism is a judicial philosophy that emphasizes strict adherence to legislated rules and limits the scope of judicial interpretation. This concept has profoundly influenced the Chinese legal system since the 1950s and continued through the 1980s. It has shaped Chinese legal education, as judges recall learning to equate "justice" with "formalism" (Lubman 1994, 320; Potter 2000, 210).

Over time, the acceptance of legal formalism has varied. Potter (1994, 338) defines formalism as “an approach that emphasizes doctrinal consistency” and acknowledges that in the 1990s, it was criticized. More recently, Luo (2021, 916) observes that formalism remains widely used in contemporary Chinese law. Today, “the core of legal formalism is adjudication based on rules. In the context of legal interpretation, formalism emphasizes textual reading of rules” (Luo, 916).

This historical and doctrinal backdrop of legal formalism in China has two implications for this paper. First, the entrenched nature of formalism in Chinese legal education and practice provides a valuable lens through which to examine the EBL. It suggests that formalism, as a long-established method of interpreting laws in China, can offer insights into how the EBL has been understood and implemented within judicial and commercial contexts. Second, despite its widespread application in interpreting other areas of commercial law, formalism has yet to be thoroughly applied to the EBL in terms of bankruptcy proceedings (Potter 2000, 210). This gap highlights an opportunity to employ formalism as an analytical lens to analyze the EBL. Through this lens, textual differences can explain the relatively low incidence of bankruptcy filings since the law's enactment.

METHODS

Textual Analysis

This paper adopts the theory of legal formalism as its primary analytical framework to explore the textual differences between China's Enterprise Bankruptcy Law (EBL) and the U.S. Bankruptcy Code. That is, this paper argues that differences in the law will directly affect its utilization. To operationalize this theory, this paper follows the comparative approach utilized by

Manganeli (2010) and utilized by Bohanon and Plouffe (1999) in their cross-cultural bankruptcy study. They first explain the U.S. Bankruptcy Code, then explain Italian or Mongolian law, respectively, and conclude by resolving major textual differences between the two. This paper first explains the U.S. Bankruptcy Code, then it explains the EBL, and lastly it focuses on identifying and analyzing major textual divergences between the two legal documents. Given the substantial difference in length—the U.S. Bankruptcy Code spans over 700 pages, while the EBL comprises only 136 articles—the U.S. code is inherently more comprehensive (United States Code, 1978; State Council, 2006). For instance, the U.S. Bankruptcy Code includes provisions for personal bankruptcy, a concept notably absent in Chinese law. Given the quantity of differences between the two laws, this paper will report textual differences also examined in existing literature. Through this method, this paper will assess the most important potential impacts on the observed decline in the usage of the EBL.

Aggregate Statistics

Furthermore, this paper incorporates aggregate statistics from the American and Chinese governments to better contextualize the usage of the EBL in its second decade. Since its adoption in 2007, the EBL has been periodically clarified to align with international standards. Interpretive rulings by the Supreme People’s Court of China in 2011 and 2013, and further clarifications in 2019, have sought to enhance understanding and application of the EBL (Bufford, 2017, 14). Amidst an ongoing debt crisis in critical sectors like real estate, the Supreme People’s Court is actively revising the EBL (Ren et al. 2023). Hence, modern usage of the EBL may differ significantly from the prior decade.

Data for China is extracted from the Gazette of the Supreme People's Court of the People's Republic of China (“Gazette”). For each year, the Gazette publishes a table of all court cases accepted, resolved, and ongoing within the nation. These cases are then subdivided into legal categories. Prior to 2017, the Supreme People’s Court of China would announce the number of bankruptcies accepted for the year (Lin, 2018); since 2017, the Gazette has separated out bankruptcies and compulsory liquidations in its statistical bulletin reports. Figures from prior to 2017 are those recorded by Lin; figures after 2017 are also bankruptcy acceptances reported by the Gazette. All year-on-year changes are the author’s calculations.

Information about the U.S. Bankruptcy Code was sourced from the United States Courts database. This database offers granular data including categorizations by chapter, nature of debt, county, and reporting period (quarterly and yearly). For consistency with the Chinese data, this paper considers annual bankruptcy data of businesses filing for either liquidation (“Chapter 7”) or reorganization (“Chapter 11”). Chapter 7 is included because the U.S. Bankruptcy Code allows direct filings for liquidations. In contrast, the EBL statistics separate compulsory liquidations from the umbrella “bankruptcies” statistic, which is comprised of voluntary liquidations and reorganizations. In China, debtors first file for bankruptcy and may be liquidated if reorganization is unsuccessful (Lin, 2018). To calculate the total number of bankruptcies for each year, the author added the number of Chapter 7 and Chapter 11 cases for each year.

Data from regional databases in China, while theoretically available, were not used in this paper. First, these databases are typically incomplete. Zhuang et al. (2022) indicates that approximately 60% of cases aren’t filed in these databases. For the “National Corporate Bankruptcy Information Disclosure Platform” used by Li and Ponticelli (2022), more than 90% of cases were not uploaded and those which were displayed a strong bias towards shorter cases.

Second, there is no convenient mechanism to access the data. Liebman et al. (2022) collected information from more than one million cases with a database from Henan province, but the collection required a team of computer scientists to scrape the data for 18 months. The extensive resources and time required to collect or further process this data to include only EBL cases would have been infeasible for this paper. Therefore, the analysis is limited to the readily available national aggregate bankruptcy data.

RESULTS

U.S. Bankruptcy Code

The US Bankruptcy Code, codified in Title 11 of the United States Code, serves as the principal federal law governing bankruptcy and insolvency proceedings in the United States (United States Code). It is designed to apply to both individuals and corporations and provides a legal framework to address debt and insolvency issues across various sectors.

The structure of the Bankruptcy Code is organized into several chapters. Chapters 1 (“General Provisions”), 3 (“Case Administration”), and 5 (“Creditors, the Debtor, and the Estate”) are foundational. These chapters outline general procedures and principles that apply universally across all types of bankruptcy cases. These chapters define the basic concepts, administrative processes, and roles of key stakeholders involved in bankruptcy proceedings (United States Code).

The remaining chapters are tailored to distinct bankruptcy scenarios: 7 (“Liquidation”), 9 (“Adjustment of Debts of a Municipality”), 11 (“Reorganization”), 12 (“Adjustment of Debts of a Family Farmer or Fisherman with Regular Annual Income”), 13 (“Adjustment of Debts of an

Individual with Regular Income”), and 15 (“Ancillary and Other Cross-Border Cases”). To better understand the EBL, the key chapters of the U.S. Bankruptcy Code are Chapters 7 and 11. In Chapter 7, both individuals and businesses dissolve their operations, and a trustee is appointed to liquidate the debtor's non-exempt assets to pay off creditors. Liquidation is often used by those who need a straightforward way to discharge overwhelming debts.

Conversely, Chapter 11 focuses on corporate restructuring. It is designed predominantly for corporations, although individuals can file under this chapter under certain circumstances (United States Code). Chapter 11 allows businesses to continue operations while reorganizing their debt structure, which can include renegotiating terms with creditors, selling off parts of the business to raise funds, or restructuring operations to regain profitability. The objective is to enable the survival of the business, preserve jobs, and ensure that creditors receive a better repayment through the reorganized plan than they would through a liquidation process.

Enterprise Bankruptcy Law

The Chinese Enterprise Bankruptcy Law (EBL), which replaced the 1986 bankruptcy law, marked a significant advancement in China's approach to bankruptcy. The 1986 law contained 43 articles across six chapters and had several limitations (Boshkoff and Song 1987). It only applied to state-owned enterprises, the law focused on determining faults rather than survival, and it placed employees at the top of the creditors' ranking (Wei, 2014).

In contrast, the EBL is a comprehensive framework which addresses both state-owned enterprises and private companies (Lee and Ho 2010, 149). It contains 136 articles across 12 chapters and encompasses a broader scope of applications and modernized principles (State Council 2006). The EBL allows for both voluntary and involuntary reorganization and adopted

more flexible procedures in a manner closely aligned with international practices (Arsenault 2008).

Like the United States Bankruptcy Code, the EBL is organized into several chapters. Chapters I (“General Provisions”), II (“Application and Acceptance”), III (“Administrator”), IV (“A Debtor’s Property”), V (“Expenses for Bankruptcy Proceedings and Debts Incurred for the Common Good of Creditors”), VI (“Declaration of Claims”), VII (“Creditors’ Meeting), XI (“Legal Liability”), and XII (“Supplementary Provisions”) outline general procedures that apply for all types of bankruptcy cases.

The remaining chapters are tailored to specific bankruptcy scenarios.

Chapter VIII (“Reorganization”) mirrors U.S. Chapter 11 in which a financially distressed entity can reorganize its operations and debts. The bankruptcy administrator must develop a reorganization plan approved by the court and creditors holding two-thirds of the debt value. If the debtor's situation worsens, or in cases of malfeasance, the case may be converted to liquidation. This type of bankruptcy accounts for approximately 20 percent of all cases in China (Austin and Lin 2020, 10).

Chapter IX (“Compromise”) is unique to the EBL and without a direct U.S. counterpart. It involves a court-approved voluntary settlement between the debtor and unsecured creditors, aiming for a "harmonious resolution." It requires acceptance by over half of these creditors, representing at least two-thirds of unsecured debt. If the compromise fails, the case is converted into liquidation. Because of its exclusion of secured creditors and the absence of ongoing supervision post-agreement, this approach is rarely used (Austin and Lin 2020, 12).

Chapter X (“Liquidation”) mirrors Chapter 7 of the U.S. Bankruptcy Code. The bankruptcy administrator manages the debtor’s assets and formulates a liquidation plan that, if approved by creditors, is executed to distribute proceeds. This pathway is the most common, representing approximately 80 percent of bankruptcy cases in China. Typically, unsecured creditors recover 10–15 percent of their claims (Austin and Lin 2020, 13).

Major Textual Differences

This paper conducts a detailed comparative analysis of the textual elements of the US Bankruptcy Code and China's EBL to uncover nuanced similarities and differences. While there are several overarching similarities, such as both parties being able to initiate bankruptcy, the option for reorganization and liquidation, claim priority, creditor committees, and the ability to enforce a cramdown, key distinctions delineate the operational frameworks within each jurisdiction. A table summarizing the following differences is presented in the Appendix.

1. Ease of Filing

The US Bankruptcy Code simplifies the initiation of bankruptcy proceedings, as described in 11 U.S.C. Section 301, as it automatically treats the commencement of a voluntary case as an order for relief. Conversely, Chinese law requires debtors to file an application for revival or liquidation which can take up to 15 days for a court response (EBL Articles 7, 8, and 10). This waiting period therefore creates friction in using the EBL compared to the U.S. Bankruptcy Code.

2. Insolvency Requirements

The requirements for declaring bankruptcy differ notably between the US and China, particularly in the interpretation and application of insolvency tests. In the US, although insolvency is not a strict legal requirement, companies often must pass the "cash flow test" to file for bankruptcy. (Lee and Ho 2010, 153). This test assesses whether mandatory cash outlays exceed incoming cash flows, indicating financial distress. In contrast, Chinese law requires a company to demonstrate insolvency through the "balance sheet test," which involves showing that liabilities exceed assets (EBL Article 2). This accounting-based approach creates frictions to using the EBL by placing a stricter, quantifiable threshold on insolvency.

3. Automatic Stay

The implementation and scope of the automatic stay in bankruptcy proceedings also showed a significant divergence between the two countries. An automatic stay facilitates an organized process of debt negotiation protected from creditor actions. In the US, 11 U.S.C Section 362 states that the automatic stay is triggered immediately upon filing a bankruptcy petition. This stay is effective globally and halts all collection activities, thereby ensuring the equal treatment of creditors and preventing the dissipation of the debtor's assets. Conversely, in China, an automatic stay does not take effect until the bankruptcy application is officially accepted by the court (EBL Article 16). This delay can lead to a "creditor race," as creditors attempt to secure their claims against the debtor's assets before the stay is enacted, potentially undermining an equitable resolution of claims and deterring bankruptcy applications.

4. Debtor-in-Possession (DIP)

In the US, the concept of a Debtor-in-Possession (DIP) is fundamental, especially under Chapter 11. When a company files for bankruptcy, it can continue to operate its business and

manage its assets without appointing an external trustee. This arrangement is authorized under 11 U.S.C. 363(c)(1), which allows the debtor to conduct business transactions in the “ordinary course” of business. The debtor retains the powers of a trustee, including the ability to negotiate leases, dispose of assets, and enter transactional agreements while under the oversight of the bankruptcy court.

In contrast, in Chinese bankruptcy proceedings, DIP is not the default practice. Typically, an outside administrator is appointed to take over business operations once a bankruptcy petition is accepted (EBL Articles 13, 17, 18). Article 73 does allow for the possibility of a DIP arrangement, where the debtor may continue to operate the business under certain conditions. However, this method is not widely used (Austin and Lin 2020, 24). In addition, when DIP is permitted, it operates under the supervision of the appointed administrator, which makes the autonomy of the debtor significantly less than that in the American system (Steele et al. 2018, 682). This results in a scenario in which the debtor's management is closely overseen, which can make debtors less willing to file for bankruptcy (Bufford 2017, 8).

5. Reorganization Plan

The process and timelines for filing a reorganization plan vary between the US and China. Under 11 U.S.C. 1121(c)(3), a debtor is afforded an exclusivity period of 120 days to file a reorganization plan. Following this period, creditors have 60 days to review and object to the plan, provide feedback, or propose modifications. If the debtor fails to propose a plan within 120 days, creditors may propose alternative reorganization plans.

In contrast, Chinese bankruptcy law mandates a more rigid timeframe for reorganization. According to the EBL, the debtor or bankruptcy administrator has between six and nine months

after the petition is accepted to propose a reorganization plan (Austin and Lin 2020, 8). If a plan is not proposed within this timeframe, the reorganization case must be converted into a liquidation case, leading to the end of business operations and the sale of assets. Although a quicker bankruptcy may seem as though it would increase the efficiency of bankruptcies, the greater chance of liquidation would result in fewer bankruptcies than in the United States.

6. Control of Venue

The venue for bankruptcy filings also differs. In the United States, corporations can file for bankruptcy in any jurisdiction where it conducts business, has assets, or is incorporated if it has been established there for at least 180 days prior to filing (Woodward Jr. 2008). This flexibility allows debtors to choose jurisdictions that may offer more favorable interpretations of bankruptcy laws or more experienced courts.

In China, Article 3 requires that bankruptcy proceedings occur in jurisdictions where the debtor is domiciled. Given the influence of legal formalism in China, this appears consistent with the idea that all judges will interpret the law to the text and therefore companies should not expect preferential treatment. However, for companies with multinational stakeholders, this limitation may reduce the company's willingness to file for bankruptcy in China.

Contemporary Trends in U.S. Bankruptcy Code and EBL Usage

In addition to the textual differences, this paper also evaluated bankruptcy trends over time. Table 1 delineates the historical trajectory of bankruptcy cases accepted by courts in mainland China from 1998 to 2023, excluding the Special Administrative Regions of Hong Kong and Macau. The analysis of the bankruptcy data, as illustrated in Table 1, reveals several

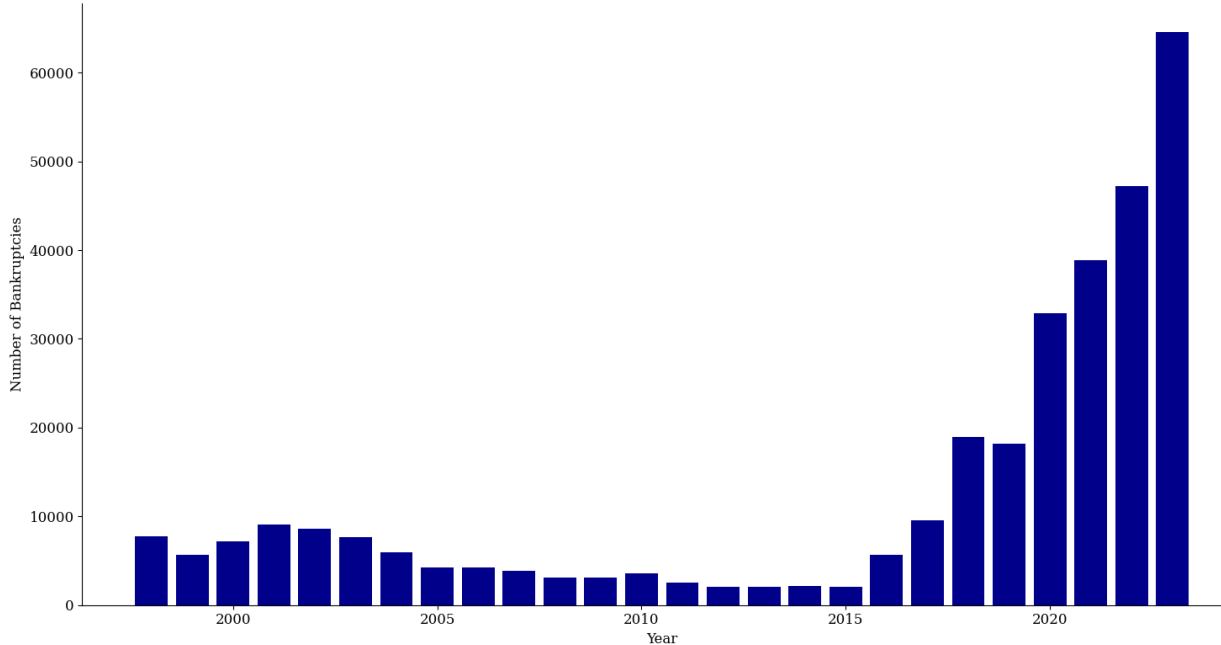
noteworthy trends. Most strikingly, 2016 marked a dramatic upsurge in the number of bankruptcy cases, with a 175.1% increase from the previous year. This significant rise coincides with a period of legal reforms in China which may have contributed to the ease and accessibility of filing for bankruptcy. For instance, in 2016, China established its first specialized bankruptcy court (Cheung 2016). This increase is quantified in Table 1 by annual percentage change and visually depicted in Figure 1.

Table 1. Total Number of Bankruptcy Cases Accepted by Courts in Mainland China

Year	Bankruptcies	% Change in Bankruptcies
1998	7746	-
1999	5622	-27.4%
2000	7219	28.4%
2001	9110	26.2%
2002	8615	-5.4%
2003	7673	-10.9%
2004	5928	-22.8%
2005	4238	-28.5%
2006	4253	0.4%
2007	3817	-10.2%
2008	3139	-17.8%
2009	3128	-0.4%
2010	3567	14.0%
2011	2531	-29.0%
2012	2100	-17.0%
2013	2088	-0.6%
2014	2159	3.4%
2015	2058	-4.7%
2016	5665	175.1%
2017	9542	68.4%
2018	18950	98.6%
2019	18174	-4.1%
2020	32900	81.0%
2021	38847	18.1%
2022	47251	21.6%
2023	64567	36.7%

After 2016, the data in Table 1 also shows consistent double-digit percentage increases in bankruptcy filings year over year, reflecting a trend that warrants further. These increases, such as the 98.6% rise in 2018 followed by consistent growth until 2023, illustrate a marked shift in the bankruptcy landscape in China.

Figure 1. Total Number of Bankruptcy Cases Accepted by Courts in Mainland China



Moreover, in 2017, the Gazette began releasing more granular data. Data on compulsory liquidations has improved, which provides insights into creditor-led company liquidations. Table 2 incorporates this data and extends the analysis from 2017 onwards. The table reveals an evolving relationship between bankruptcies and compulsory liquidation, with the latter exhibiting significant growth. Table 2 also analyzes the volume of bankruptcy filings with compulsory liquidation cases and presents a ratio of bankruptcies to the aggregate of

bankruptcies and compulsory liquidations. Notably, the ratio of bankruptcies to the total of bankruptcies and compulsory liquidations decreases from 88.7% in 2017 to 65.8% in 2023, highlighting the increasing prevalence of creditor-initiated compulsory liquidations over the period. This comparison is shown in Figure 2, underscoring the prevalence of bankruptcy within the Chinese legal framework. The data suggest that while bankruptcies are predominant, compulsory liquidations are increasing at a more rapid pace. This aligns with typical outcomes in emerging economies (Li and Ponticelli 2022).

Table 2. Total Number of Bankruptcy and Compulsory Liquidation Cases Accepted by Courts in Mainland China

Year	Bankruptcies	Compulsory Liquidation	Ratio of Bankruptcies to Total
2017	9542	1219	88.7%
2018	18950	2785	87.2%
2019	18174	3113	85.4%
2020	32900	5798	85.0%
2021	38847	9615	80.2%
2022	47251	28491	62.4%
2023	64567	33577	65.8%

Figure 2. Proportion of Bankruptcies to Compulsory Liquidations in Mainland China

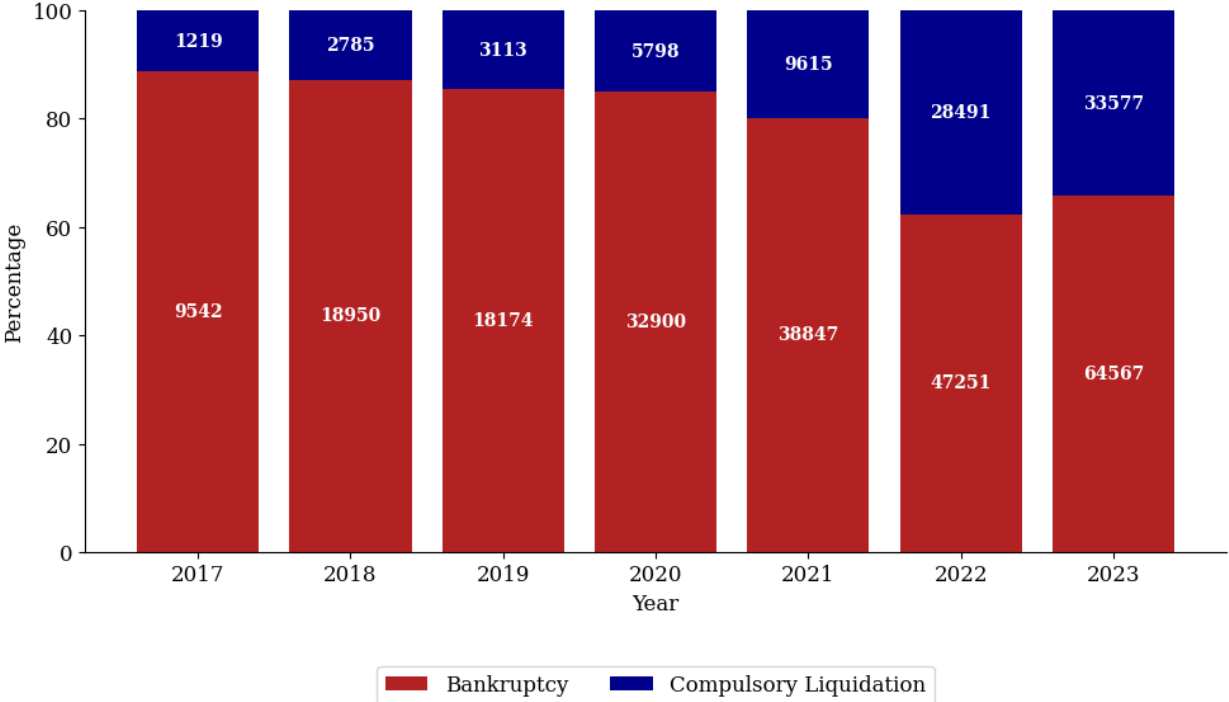


Table 3 and Figure 3 reveal distinctive bankruptcy trends in the United States that are not seen in China. For instance, there was a sharp increase in filings in 2009, with total cases reaching 55,645. Since 2009, bankruptcy filings demonstrated a consistent decline over the years. This trend suggests a recovery and stabilization of the economic landscape, alongside possible improvements in financial and business practices over time. This also suggests that the business cycle in China and the United States may be out of sync, or that China’s lack of EBL usage is due to another factor.

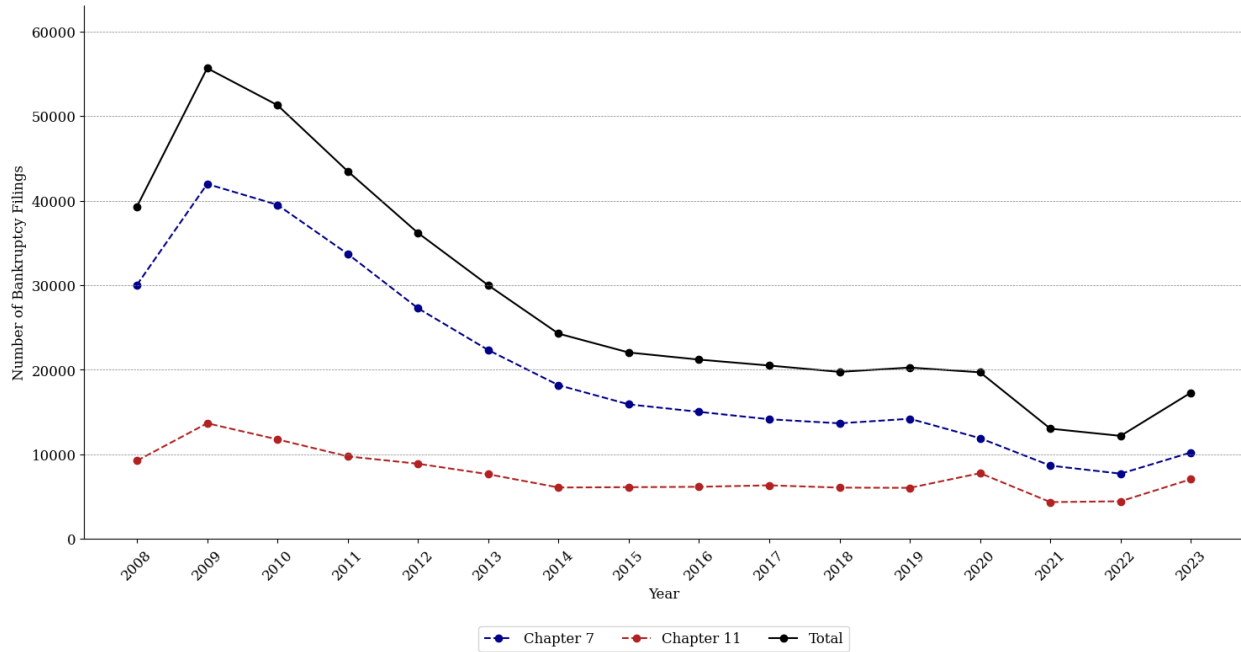
Throughout the observed period, Chapter 7 cases consistently outnumbered Chapter 11 reorganization cases. This indicates a stronger inclination towards liquidation among distressed firms, potentially signifying that businesses facing fiscal difficulties opted to cease operations rather than restructure. While the U.S. showed a spike followed by a decline corresponding to

economic recovery phases, China displayed a steady increase in bankruptcy filings, which suggests differing impacts of economic conditions or legal frameworks on bankruptcy practices.

Table 3. Total Number of Chapter 7 and 11 Cases in the United States.

Year	Chapter 7	Chapter 11	Total
2008	30034	9259	39293
2009	41962	13683	55645
2010	39501	11778	51279
2011	33698	9772	43470
2012	27274	8900	36174
2013	22334	7660	29994
2014	18184	6093	24277
2015	15917	6130	22047
2016	15033	6174	21207
2017	14157	6350	20507
2018	13678	6078	19756
2019	14215	6052	20267
2020	11919	7786	19705
2021	8678	4366	13044
2022	7728	4465	12193
2023	10229	7070	17299

Figure 3. Total Number of Chapter 7 and 11 Cases in the United States.



DISCUSSION

Textual Discussion

Using the lens of legal formalism, the results section highlights significant textual differences between the EBL and U.S. Bankruptcy Code. In the United States, businesses experience greater certainty in the bankruptcy process, as indicated by the immediate effect of an automatic stay upon filing. This contrasts sharply with the EBL, which requires applicants to endure a 15-day waiting period. Such procedural rigidity in China is consistent with a legal system grounded in legal formalism, which prioritizes adherence to clear, predefined standards over procedural flexibility. This contributes to bankruptcy's barrier in China as related to ease of filing, insolvency requirements, and the implementation of automatic stays.

Further, businesses in the United States benefit from increased autonomy. Notably, the DIP system allows debtors to retain control over daily operations in bankruptcy. In contrast, an outside administrator typically assumes control in China. In addition, the U.S. Bankruptcy Code offers a comparatively lenient timeframe to submit a reorganization plan and does not compulsorily convert reorganization into liquidation if a consensus with creditors is not reached. The relative lack of flexibility therefore could explain why bankruptcies are less common in China.

The option to choose the venue for bankruptcy filings in the United States also highlights the flexibility of the American system. This does not align with the principles of legal formalism observed in China, as strict venue rules and timelines reflect a commitment to doctrinal consistency. These formalistic elements likely contribute to the lower incidence of bankruptcy filings in China following the enactment of the EBL

The formalist approach, while aiming to ensure consistency and predictability in legal applications, may inadvertently hinder effective resolution of bankruptcy cases. This is particularly limiting in a globalized business environment as multinational stakeholders may find the restrictive venue controls in China a significant barrier to effective judicial recourse. Such constraints on venue selection can deter filings, especially among international firms that are accustomed to more accommodating bankruptcy practices elsewhere or domestic firms with executives trained abroad.

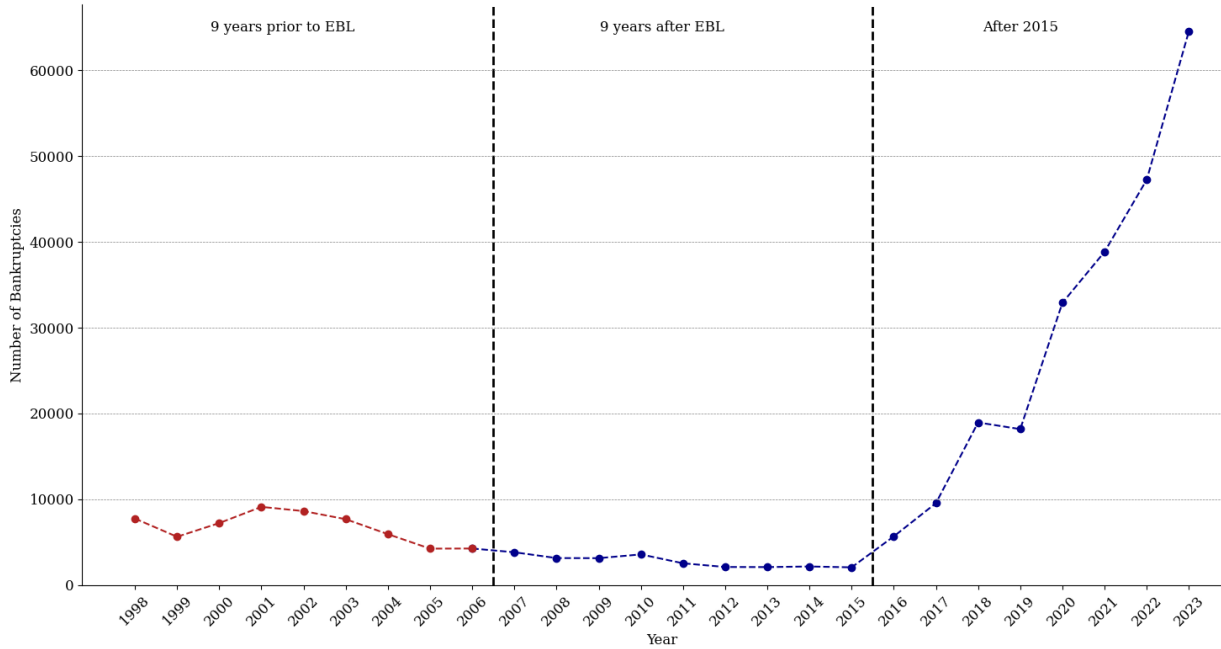
Contemporary Trends in U.S. Bankruptcy Code and EBL Usage

Given the textual differences identified and potential explanation for Chinese bankruptcy rates, it is important to align these results with contemporary data. Figure 4 illustrates the

trajectory of bankruptcy filings in China from 1998 to 2023, segmented into three distinct periods. The red line represents the years prior to the promulgation of the EBL and the blue line represents the years after the promulgation of the EBL. The vertical black dashed line on the left marks the promulgation of the EBL. As scholars have noted, there was a notable lack of bankruptcies prior to the EBL, and a similarly notable lack of bankruptcies in the nine years after the EBL was promulgated where bankruptcies decreased on average (Jiang 2014).

The data, however, changes dramatically after 2015, as indicated to the right of the second vertical black dashed line where there is a substantial increase in filings. This sudden surge raises questions about the factors contributing to this change. Three potential explanations can be: global economic factors, legal changes, and legal realism. First, it is plausible that bankruptcies are impacted by broader economic trends such as global financial crises, and therefore would correlate with the rise in bankruptcy filings. Second, if legal adjustments were made to the EBL around 2015, this could potentially explain the sudden increase in filings. And, third, if there were no significant amendments to the EBL itself or external economic issues during this period, this could suggest a limitation in the applicability of legal formalism to explain bankruptcy filings in China. Rather, it could indicate other, less formalistic legal principles such as legal realism are a better analytical lens to interpret Chinese laws.

Figure 4: Trends in Bankruptcy Filings in China Before and After the Implementation of the Enterprise Bankruptcy Law

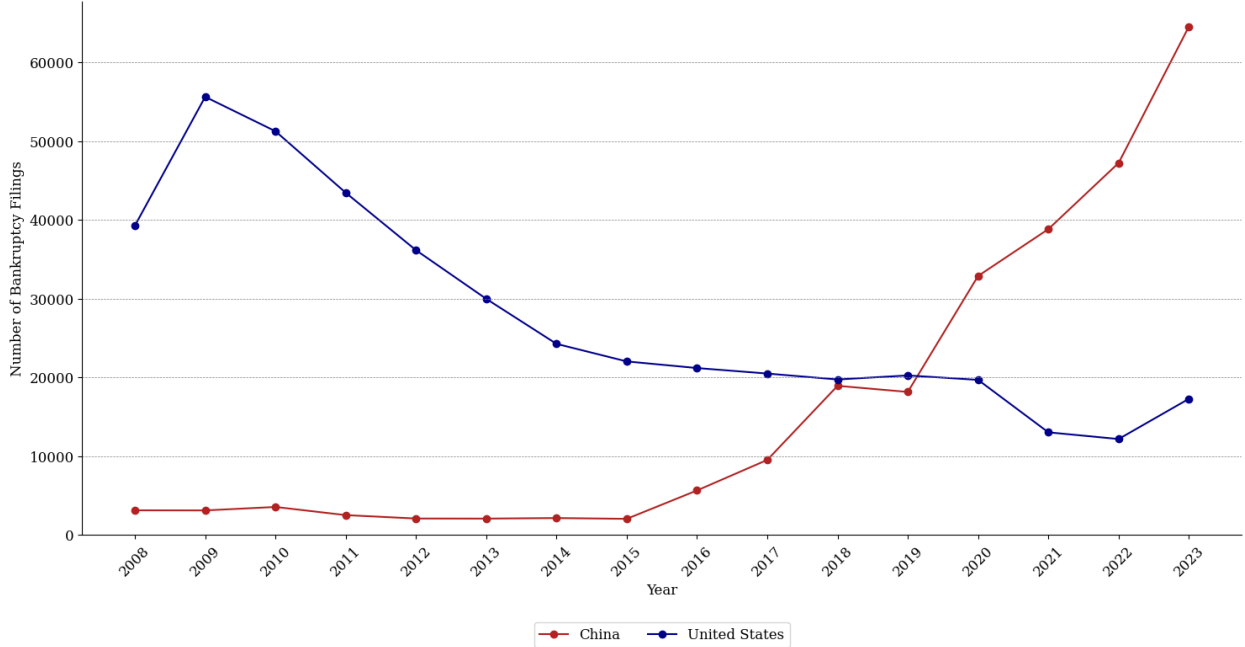


To better understand potential global economic impacts, Figure 5 depicts the total number of corporate bankruptcies in the United States and China from 2008 through 2023. If a global shock caused China’s increase in bankruptcy rates, a similar effect should be seen in the United States. Instead, the graph illustrates a stark divergence in bankruptcy trends between the two countries, with the United States exhibiting a cyclical pattern and China showing a continuous upward trajectory post-2015.

In the United States, bankruptcy filings peaked sharply in 2009, likely a direct result of the global financial crisis that began in 2008. Subsequent years saw a steady decline in filings, reflecting a gradual recovery from the crisis. The cyclical nature of these trends in the United States suggests that bankruptcy filings are responsive to broader economic cycles and market dynamics, rather than being strictly influenced by changes in the legal framework. In contrast,

China’s trend does not follow a global economic pattern but instead begins a significant and sustained increase from 2015 onwards. This suggests that the factors influencing Chinese bankruptcy filings may be predominantly domestic rather than global. The steady rise in filings, despite the absence of a corresponding global financial crisis during this period, suggests potential legislative changes or shifts in the enforcement or interpretation of bankruptcy laws within China. Granted, a critical limitation of this analysis is that it relies on aggregate data. To understand if there are particular courts or types of business resulting in the increased bankruptcy rates in China, more granular data would be required.

Figure 5: Bankruptcy Filings in the United States and Accepted Bankruptcy Cases in China.



Textual Discussion Revisited

Given the divergence in bankruptcy rates in the United States and in China, this paper will revisit the textual discussion to see if any changes occurred in China around 2015 to the laws.

1. Ease of Filing

The historical reluctance of Chinese courts to accept bankruptcy applications, as noted in Article 12, has introduced a significant level of uncertainty into the bankruptcy process. This was particularly challenging for businesses seeking legal avenues for debt resolutions. Reforms in 2011 addressed this issue by allowing filings to escalate to a higher judicial level if ignored, thereby reducing bottlenecks at the initial filing stages (Bufford 2017, 18). Further, this change reflects a shift towards a more debtor-friendly approach within the Chinese legal framework. These changes could be consistent with the data shown if there was a lagged implementation. Otherwise, ease of filing may not have as much explanatory ability for China's bankruptcy rates.

2. Insolvency Requirements

Changes in 2011 also adjusted the landscape regarding insolvency requirements. With the introduction of judicial discretion in the assessment of insolvency, courts have been granted more flexibility in interpreting insolvency beyond strict financial metrics (Bufford 2017, 16). This shift towards judicial discretion introduces a layer of subjectivity but also allows for a more nuanced consideration of each bankruptcy case. It is noteworthy that these changes do not entirely correlate with the observed spike in bankruptcy filings, suggesting that other factors, possibly economic or regulatory, may also influence these trends. However, the shift from formalism to judicial discretion could indicate the analytical lens of legal formalism is incorrect in the context of Chinese bankruptcy.

3. Automatic Stay

The clarification provided by the second judicial interpretation in 2013 marked a significant development in the handling of automatic stays. This interpretation mandates that all claims against a debtor's post-filing must be processed within the bankruptcy court (Bufford 2017). This change ensures centralized, consistent handling of claims and protects the debtor from disparate actions across various jurisdictions, thereby reinforcing the protective aspects of the bankruptcy process and mitigating the risk of a creditors race. This change occurred later than the previous two changes, but this change alone does not explain the continued spike in Chinese bankruptcies year after year.

4. Debtor-in-Possession (DIP)

Despite the clarification in 2019 regarding the application and implementation of DIP, its actual usage remains largely unchanged. These guidelines have clarified when and how a DIP can be implemented, yet it appears that the practical application of DIP in bankruptcy cases has not shifted significantly. This stagnation might suggest cultural or institutional hesitancy to fully embrace this approach, possibly due to concerns over debtors' ability to manage their affairs effectively post-filing. Given the lack of change, DIP is unlikely to explain why the frequency of Chinese bankruptcies have increased over time.

5. Reorganization Plan

The process for filing a reorganization plan has remained unchanged. While Covitz et al. (2006) suggests that improving the timing of reorganization plans could potentially improve bankruptcy rates, no change has been implemented in China. In addition, the liquidation component of this law remains unchanged.

6. Control of Venue

The jurisdictional requirement for bankruptcy proceedings to occur where a firm is registered could have hindered a business' ability to seek more favorable judicial environments. Given the lens of legal formalism, these environments may be preferential for reasons external to the law, such as greater capacity or throughput. Thus, the introduction of specialized bankruptcy courts in 2016 marks a significant development in mitigating these limitations (Cheung, 2016). While these courts do not alter the geographic constraints, they improve the quality and consistency of bankruptcy proceedings available to geographies through specialized judicial expertise.

In the United States, the bankruptcy system operates with specialized courts staffed by judges who possess specific expertise in bankruptcy law. This specialization facilitates more informed and consistent decisions across cases, enhancing the predictability and reliability of bankruptcy proceedings. In contrast, China traditionally handled bankruptcy cases in civil courts, which may not have had the same level of specialization (Li and Ponticelli, 2022). Only in major cities have specialized bankruptcy courts been established, leading to potential inconsistencies in the application of bankruptcy laws across different regions. This disparity can affect the efficiency and fairness of proceedings.

The recent surge in bankruptcy filings in China, increasing to levels 30 times higher than those observed in 2015, indicates a pivotal shift in the landscape. This increase coincides with the expansion of specialized bankruptcy courts (Cheung 2016). Further, more specialized bankruptcy courts have opened after 2016, which could explain the continued increases in bankruptcies each year (Li and Ponticelli 2022). The timing suggests that these judicial and legal

enhancements may be contributing significantly to the maturation of China's bankruptcy system. However, although the correlation with these judicial and legal developments is evident, without data clarifying the proportion of cases allocated to special courts and civil courts, there is a lack of direct causal evidence. Li and Ponticelli suggest the ratio may be one-to-one but are extrapolating from a limited sample. Nonetheless, the gradual establishment of specialized courts may be fostering a more robust and efficient bankruptcy system in China, aligning it more closely with international practices seen in systems like that of the United States.

CONCLUSION

This paper has explored the textual differences between China's Enterprise Bankruptcy Law and the United States Bankruptcy Code through the analytical lens of legal formalism. This paper also combined data from China and the United States to better understand how bankruptcy trends have changed in the past decades. In revisiting the textual changes to the EBL, it is reasonable to claim that the modifications to ease of filing, insolvency requirements, automatic stays, debtor-in-possession (DIP) protocols, and reorganization plans have not significantly altered the EBL in ways that would likely lead to the dramatic increase in bankruptcy filings observed since 2015. It's possible that the effects of earlier reforms were delayed, only becoming apparent as firms gradually adjusted to the changes in the legal landscape. This lag could explain the timing of the surge in filings, aligning it with broader acceptance and understanding of the reforms among the business and legal communities. Still, while these elements have undergone revisions, the timing and one-off nature of these changes do not sufficiently correlate with the continued spikes in bankruptcy cases to serve as definite causal factors.

The introduction of specialized bankruptcy courts in 2016, however, emerges as a more plausible contributor to this trend. These courts, by offering a more specialized and presumably efficient forum for handling bankruptcy cases, may have reduced barriers to filing and thus encouraged an increase in bankruptcy applications. This shift suggests that while the formal control of venue, has not changed, the practical effect of these courts opening have impacted control of venue. That is, control of venue is serving as a proxy variable for broader accessibility of specialized bankruptcy courts.

Given this development, there is not yet a compelling reason to reject legal formalism as an analytical lens for understanding China's bankruptcy laws. Legal formalism can still provide valuable insights into how laws are interpreted and applied, particularly in a system where rule-based adjudication prevails. However, the increasing role of specialized courts indicates a shift towards a more pragmatic approach in specific contexts, which may eventually warrant a reevaluation of the strict formalist perspective.

To make causal claims about the drivers behind the rise in bankruptcy filings in China, it is imperative to access more detailed, micro-level data. Such data would enable a deeper analysis of the specific changes and their impacts, helping to disentangle the influences of legal reforms from other economic or regulatory factors. Future research can focus on collecting and examining case-level data across different regions and sectors. This approach would provide insights into how individual courts interpret and apply the reformed laws, and the resultant effects on bankruptcy outcomes.

Furthermore, exploring areas not extensively covered in this paper could enrich the understanding of bankruptcy within China's broader legal and economic framework. Personal

bankruptcy law, although not currently implemented in China, represents the majority of bankruptcy in America. This is a significant gap in the legal landscape and could influence future reforms. Additionally, the role of financial institutions under the EBL and the implications of cross-border trade issues in bankruptcy proceedings are critical areas that require further investigation. These topics not only broaden the scope of research but provide testing opportunities for the applicability of legal formalism in related contexts.

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APPENDIX

Table 4. Summary of Textual Differences

Aspect	US Bankruptcy Code	Chinese Enterprise Bankruptcy Law (EBL)
Ease of Filing	Simplified initiation; filing automatically treated as an order for relief (11 U.S.C. Section 301).	Requires debtors to file an application and wait for court acceptance; potential for non-acceptance of applications (Articles 7, 8, 10, 12).
Insolvency Requirements	Insolvency not strictly required; "cash flow test" often used (companies must show cash outlays exceed incoming cash flows).	Insolvency mandatory, demonstrated via "balance sheet test" (liabilities exceed assets, Article 2); subject to judicial discretion.
Automatic Stay	Immediate upon filing, global in effect, stops all collection activities (11 U.S.C. Section 362).	Only effective after court accepts bankruptcy application, potentially leading to creditor races (Article 16).
Debtor in Possession (DIP)	Standard practice; debtor manages business as "debtor in possession" with trustee powers (11 U.S.C. 363(c)(1)).	Not default; an administrator typically takes control, though DIP is possible under supervision if allowed (Articles 13, 17, 18, 73). Courts generally reluctant to approve DIP.
Reorganization Plan	Debtor has 120 days of exclusivity to propose a plan, with a subsequent 60-day period for creditor feedback; creditors can propose plans if debtor fails (11 U.S.C. 1121(c)(3)).	Six to nine months to propose a plan post-petition acceptance; failure to propose leads to liquidation (specific citations needed).
Control of Venue	Flexible; can file where business is conducted, where assets are located, or where incorporated, if established 180 days prior to filing.	Must be filed where debtor is domiciled, centralizing proceedings to local jurisdiction.