

The Discussion on the Possibility of the Combination of Liquidation Obligor System and Liquidator System

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Abstract: When a company requires liquidation, the Chinese law has divided the individuals responsible into liquidation obligor, who are responsible to start the procedure and liquidators as those who execute liquidation. However, this mechanism may not only lower the efficiency of liquidation [1], but also provide an opportunity for certain shareholders to transfer risks as well as an escape from their responsibilities. The liquidation obligor system and the liquidator system are different steps of the same procedure. Moreover, the two systems have a share in common in their stipulations on the identity and the responsibility of the related individual, it is possible that the combination of the two systems can solve some of the problems existed.

1. The history of liquidation obligor

Liquidation in China was firstly explained in 1993 that it can be executed by three different groups: the company member, the court at the request of creditors and department concerned when the company was dissolved by administrative reasons according to the Company Law. There were no regulations on liquidation beforehand except for a principle regulation.

The law later held company members responsible for liquidation regardless of the reason in 2005. However, the Company Law said nothing about who should be responsible to start the liquidation until 2008.

The liquidation obligor system that aims to solve the problem was created by Judicial Interpretation Section II on the Company Law in 2008 and was specified in 2013 by Guidance Case 9. The system was finally made clear in 2017 as it was included in article 69 in General Provisions of Civil Law

The history of the liquidation obligor system has made it clear that this system is more of a solution to a flaw in the original Law [2] than the law that's based on historical background or irrefutable logic.

2. Problems that liquidation obligor system creates

It can be concluded from the history that the Chinese Company Law did not expect companies that were dissolved by administrative reasons to dissolve willingly and therefore gave the power to "department concerned". However, it did not specify the identity of "department concerned" [3] and the effort to explain it as the business administration department is doubtful [4].

In the face of this dilemma, the later version of Company Law has created the responsibility-based liquidation obligor system in favor of the creditors. Alongside the solution, it created the first problem-liquidation obligor is reluctant for liquidation since the law didn't protect their rights as much. In practice, it's often the small companies that are easy to confuse the corporate personality and are forced to dissolve that rely on this system. Liquidation obligor is possible not to notify creditors or start liquidation so that they may escape from joint responsibility or debt [5].

Another problem is the moral risk this system brings. According to Guidance Case. 9 and Judicial Interpretation Section II on the Company Law, liquidation obligor is required to take joint responsibility when important files or ledgers are missing or destroyed. Some creditors may take advantage of this system by asking for joint compensation or even prevent liquidation from

happening. On the other hand, since liquidation obligor includes all shareholders as liquidation obligors, it allows some shareholders to deliberately destroy the files and use the rule of joint responsibility, sometimes even cooperate with creditors to transfer risk [6]. In the end, the system that was originally made as a supplement to liquidator has been more emphasized and relied on than the liquidator, created an order-reversed situation.

Another problem that worth mentioning is that while the identity and obligations of liquidation obligors are cleared, it's blended with the liquidator system to some degree, making the dealing a bit hasty towards situations when the files and ledgers are missing or destroyed. According to Judicial Interpretation Section II on the Company Law, the obligations of liquidation obligor, which is to start liquidation procedure and safekeeping the property, ledgers and important files, is supposed to be lifted once liquidator takes over [7]. Yet it did not state it clearly and had no mention of the lasting period of liquidation obligor. Furthermore, it did not speak of whether liquidation obligors are obligated to make sure the liquidation is done. This makes it possible that if the files, ledgers are found missing after the liquidator takes over, liquidation obligor is still held responsible and forced to compensate.

Likewise, the blurring of the difference between liquidation obligors and liquidators can also be made clear since Judicial Interpretation Section II did not have the same legal principle basis when regulating the same group due to similar reason-article 18(1) is based on tort liability [8] while article 18(2) is based on the personality of legal persons [9]. This further proves that liquidation obligor lacks rigorous professional logic.

3. Similar stipulations of other countries

In other countries that adopt Continental Law Systems, liquidation obligors and liquidators are actually combined, avoiding the problems above while making sure liquidation can start when requested.

The Japanese Company Law stipulates in article 478 that the liquidator of a limited company should be appointed in the order of company directors, the ones appointed in the constitution of the company, the ones appointed by the general meetings of shareholders. The court is also allowed to appoint a liquidator in request of a person of interest or the justice minister. This system not only is practical since it has considered the situations where the liquidator is nonexistent or unqualified, but also shows respect for corporate autonomy as well as the rights of creditors.

The British Bankruptcy Law is also worth taking a look since it also emphasized the role of the decision-making department during liquidation. The British Law stated that when the company is dissolved voluntarily by company members, directors can issue an announcement 5 weeks before the dissolution agreement is approved. If directors don't announce that the company can pay off all its debt within 12 months, the liquidation will be led by creditors. Meanwhile, directors will face the penalty of imprisonment or fine if they seek to escape debt by issuing a false announcement. Though Britain has no compelled regulations on liquidators' identity, its restraints on directors and the promise to allow creditors to lead the liquidation ensure the protection on the interest of creditors.

4. The possibility of combining liquidation obligor and liquidator

Liquidation aims to protect the interest of the creditors as well as company members. Therefore, China named those who could take control of the company, which accordingly owes fiduciary duties of care and loyalty to the company and its shareholders [10], as the possible candidate for liquidation obligor and liquidators [11].

Meanwhile, since the resolution of the meeting can't be approved without controlling shareholders' consent, it can be interpreted that controlling shareholders, as a candidate of liquidators of the company, authorized related individuals or agencies to liquidation on his behalf. In other words, liquidation obligors and liquidators are aimed to govern the same group of people and protect the same legal interest, creating a reduplication.

The logical order of the two systems should also be taken into consideration. If the liquidator group is consist of shareholders of companies with limited liability, controlling shareholders or directors of limited companies, who are also obligated to act as liquidation obligor, then in fact, these very people of interest appointed themselves. If the limited company appoints other agencies for liquidation, then in fact it's an act of authorization. This logic sequence of the two systems has made it unnecessary to use two different systems to regulate a single and complete procedure.

Therefore, considering the current execution of these two systems, the combination of the two may serve as a plausible solution to avoid existing liquidation problems.

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