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Necessity and Feasibility Analysis of Establishing a Priority for Reorganization Financing Claims in China

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Abstract: The Supreme People's Court has issued the *Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the People's Republic of China (III)*, which defines reorganization financing claims as common benefit debts. The claims of the reorganization financier shall be paid only in priority to ordinary bankruptcy claims, but shall be subordinated to secured claims. However, the practice of judicial reorganization financing has shown that even if the debt of reorganization financing is classified as common benefit debts, it is still not enough to enhance the investment confidence of financiers. To ensure the safety and profitability of financing, restructuring financiers often require their claims to be granted super-priority status, which is clearly established in the US Bankruptcy Code and falls within the DIP (debtor-in-possession) financing regime applicable to bankruptcy reorganizations. Although the practice of reorganization financing in China has shown similar needs to the US DIP financing regime, China's laws have not yet made a clear response to this. What is particularly crucial is that the positioning of priority in China's current legal system has been ambiguous for a long time, which has brought fundamental difficulties to the creation of priority in reorganization financing. In view of this, this article attempts to deconstruct the conditions for the existence of financing priority through structural functionalism theory. Based on this, it analyzes the necessity and feasibility of establishing debt priority rights for reorganization financing in China at the current stage.

Keywords: Bankruptcy priority; Reorganization financing; Mutual benefit debt; Interest balancing

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1. Introduction

Although Article 42 of the Enterprise Bankruptcy Law of the People's Republic of China (hereinafter referred to as the "Enterprise Bankruptcy Law") defines the scope of common benefit debts, there is still no consensus on whether debts incurred after bankruptcy acceptance become common benefit debts. Article 2 of the Supreme People's Court's *Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the People's Republic of China (III)* (hereinafter referred to as "Judicial Interpretation III of the Bankruptcy Law") defines reorganization financing claims after bankruptcy acceptance as common benefit debts. It clearly states that such claims have priority over ordinary bankruptcy claims and are subordinate to secured claims in terms of repayment. However, the priority of repayment has not significantly boosted the investment confidence of restructuring investors. For example, in the restructuring case of Shanghai Yuehe Real Estate Co., Ltd., among the beneficial bond debt investors introduced by the management team, three-quarters of the investors required that their common benefit debts be granted super-priority status in repayment.

There has been widespread controversy in the theoretical community regarding the priority of debt repayment in reorganization financing. Some scholars advocate drawing lessons from the priority rules of American creditor's rights. That is, on the basis of defining "loans payable for the debtor's continued business in the reorganization procedure" as "common benefit debts," a super-priority claim is constructed to give priority to such debts over existing secured debts [1]. Some scholars also believe that we can learn from the US DIP financing regime and establish a hierarchical priority system for financing in China [2]. Under the principle of priority in the effectiveness of property rights, if the priority right is property rights, according to the principle of statutory property rights, any priority right not provided by law does not have priority effect; If the priority right is a creditor's right, and the property right and priority right coexist on the same subject matter, the property right should have priority over the priority right. To fully realize the function of priority in dealing with conflicts of rights, treating priority as property rights seems to be the only way out. But if not restricted, the creation of rights guided by the principle of statutory property rights will inevitably impact the existing rules of rights order in China. Therefore, some scholars emphasize that the debt repayment plan in reorganization cannot break through the principle of absolute priority [3]. This principle emphasizes the importance of the order of settlement of various rights in the reorganization process to safeguard the interests of interest groups opposing the reorganization plan. Some scholars have pointed out that if the secured party cannot obtain better treatment than the liquidation procedure through the reorganization procedure, then the reorganization procedure is not necessary for the secured party [4]. Some American scholars believe that DIP financing priority will reduce the repayment amount of other unsecured debts, which not only violates the principles of fairness and efficiency in reorganization procedures, but also hinders the stimulation of investor supervision of debtors [5]. Therefore, this article attempts to deconstruct the functional structure of the priority of reorganization financing and clarify the basis on which the priority of reorganization financing depends. Based on this, it examines the necessity and feasibility of establishing priority rights for reorganization financing in China.

2. The applicability of structural functionalism analysis path

2.1. Controversy over the priority of reorganization financing claims

DIP financing priority in the United States grants different levels of priority to financiers based on the difficulty of financing. The US Bankruptcy Code stipulates that in general, financiers have a priority repayment right over ordinary creditors or equivalent to management fees; If funds cannot be raised, the debtor may provide a position for the financier that is superior to the compensation of management fees, or set up guarantees for it; If no funds have been raised yet, the debtor may create new guarantees for the financing party on the property that has already been secured, and enjoy super priority. The legislative experience in the United States has proven that financiers have a need for priority rights. However, there is currently significant controversy in China regarding whether the priority of debt reorganization financing should be considered as a new type of right. The contradiction manifests in the following two aspects:

On the one hand, the academic community has a vague understanding of the concept of "priority." According to the size of the extension of priority, the academic community has formed two views: narrow priority theory and broad priority theory.

The narrow priority theory holds that the concept of priority has a relatively small extension and only needs to be explained for a specific part. The identification features of this special part are either property rights features [6], or creditor's rights features [7]. Therefore, the theory of property rights holds that priority for compensation is the only type of priority, and therefore priority is a typical security right. The theory of fictitious property rights holds that before the law directly gives priority to the repayment of a special debt, the right is actually a debt [8]. The theory of creditor's rights holds that under the legal system of dividing property and debt, priority rights do not require possession or registration, which inevitably conflicts with the principle of public disclosure of property rights. Moreover, the existing priority rights in China are unpredictable and difficult to publicize, so the priority repayment of priority rights only comes from the creditor's rights [9].

The generalized priority theory holds that priority attributes are the core criteria for determining priority [10]. When there is a conflict of rights, priority refers to the statutory right of civil rights that can be realized before other rights based on direct legal provisions or agreements between the parties. This should include statutory priority for compensation, priority for purchase, priority for leasing, and priority for contracting [11]. It is meaningless to distinguish whether priority is a property right or a creditor's right. The theory of independent rights holds that priority is an independent civil right with priority for compensation [12]. The effectiveness theory holds that priority cannot exist independently and can only exist by attaching to specific types of rights. Therefore, priority is a special effectiveness that places the realization of a certain type of right first [13]. The theory of relief rights holds that priority is a remedial right, and its essence is a legal method of protecting rights [14].

On the other hand, there is a fairness dilemma in considering the priority ranking of financiers. From the perspective of incentivizing the financing of restructured enterprises, improving the recoverability of financing loans can protect the interests of financiers; From the perspective of the guarantee system, the interests of existing secured creditors should be protected during the bankruptcy liquidation of enterprises. However, the total amount of assets of the restructured enterprise is constant, and when there are creditors involved in reorganization financing, their priority order should be carefully considered. Following the requirement of legal stability, creating corresponding equity hierarchy rules may be a feasible solution. However, there are still many controversies in the academic community regarding the basis for the creation of equity hierarchy rules. Some scholars believe that rights are equal and there is no hierarchical relationship between them [15]. Some scholars also believe that the hierarchy of rights is significantly reflected in the division between basic rights and ordinary rights [16]. The author believes that even if the status and opportunities between subjects are equal, it is difficult to bring equal benefits to all rights holders due to differences in their established objective conditions and abilities [17]. Due to the uncertainty of the legal nature of priority rights, the balance of interests between the priority holder and the guarantor of restructured financing claims may be a balance between interests of different natures, that is, the balance of heterogeneous interests. Unlike homogeneous interests, which can be quantitatively compared numerically, measuring heterogeneous interests poses a challenge of commonality.

Isaiah Berlin advocates value pluralism. He believes that every value is objective, and there is no single, completely reasonable registration or ranking of human values. Berlin regards the incompatibility and irreconcilability between "goodness" and "goodness" as the core problem of contemporary philosophy [18]. In the case of a failed reorganization of a company leading to bankruptcy liquidation, different secured claims can be compared over time, and it can be concluded that the first registered mortgage A is paid off before the later registered mortgage B. The reason why mortgage rights A and B can be compared is that they are of the same type. They can demonstrate order through registration and have universality. It can be seen that the measurement of homogeneous interests can easily find a certain parameter as the basis for balancing and choosing between them. However, the presentation of heterogeneous interests seems to be a dilemma. When a reorganized enterprise moves toward bankruptcy liquidation, should the law optimize the reorganization financing channel by sacrificing the interests of secured creditors? Or should the law sacrifice the interests of reorganization financiers to uphold the security system, and sacrifice the future of the reorganized enterprise to stabilize secured transactions and the efficiency of enforcing security rights? In handling this dilemma, the law can only favor one side or the other, and cannot achieve a balance between the two. Thus, the priority right of reorganization financing claims and the security right face a “ public degree dilemma.”

2.2. Overview of structural functionalism analysis path

The Structural Functional Theory (AGIL) proposed by Talcott Parsons is regarded as the most complete systemic theory of structural functionalism by the structural functionalist school. Parsons believed that any system is composed of four subsystems, namely the economic system, the political system, the social community, and the cultural model hosting system [19]. Meanwhile, these four secondary systems each undertake four functions that are fundamental to the existence of the system (as shown in **Table 1**) [20]. These four basic functions are [21]:

1. Adaptation (hereinafter referred to as “A”): The system obtains the necessary resources from the environment through various means in order to sustain itself. In the social system, this function is performed by the economic system.
2. Goal attainment (hereinafter referred to as “G”): The system has the ability to mobilize resources to achieve its goals. In the social system, this function is carried out by the political system.
3. Integration (hereinafter referred to as “I”): The system must coordinate its various internal parts to become a functional entity. In the social system, this function is performed by the social community.
4. Latency pattern maintenance (hereinafter referred to as “L”): The system has the ability to record its original operating mode. Even if the system is forced to interrupt, recording can ensure that the system can resume normal operation when restarted. In the social system, this function is performed by the cultural model hosting system.

Table 1. Social system and function

Subsystems	Function	Social structure category
Economic system	Adaptation (A)	Role
Political system	Goal attainment (G)	Community
Social community	Integration (I)	Standard
Cultural model hosting system	Latency pattern maintenance (L)	Value

It is worth noting that these four secondary systems can be correspondingly divided into smaller systems, undertaking lower-level functions. In Parsons’ view, the more progressive the society is, the more levels the model divides downward [22]. As shown in **Figure 1**, human behavior is influenced by the behavioral organism system, personality system, cultural system, and social system. The operation of the social system cannot be separated from the combined effects of economy, politics, culture, and law. As the legal system continues to be divided downward, the bankruptcy system, as a complete system, should also have adaptive functions, goal attainment functions, integration functions, and pattern maintenance functions. After Parsons proposed the theory of structural functionalism, Robert K. Merton further introduced the concept of distinguishing between explicit and implicit functions. The explicit function is the objective consequence expected and recognized by the participants, while the implicit function is the objective consequence that the participants did not expect. As people’s awareness increases, latent functions will gradually transform into explicit functions, making people aware [23]. The explicit function is divided into adaptive function, goal achievement function, integration function, and pattern maintenance function.

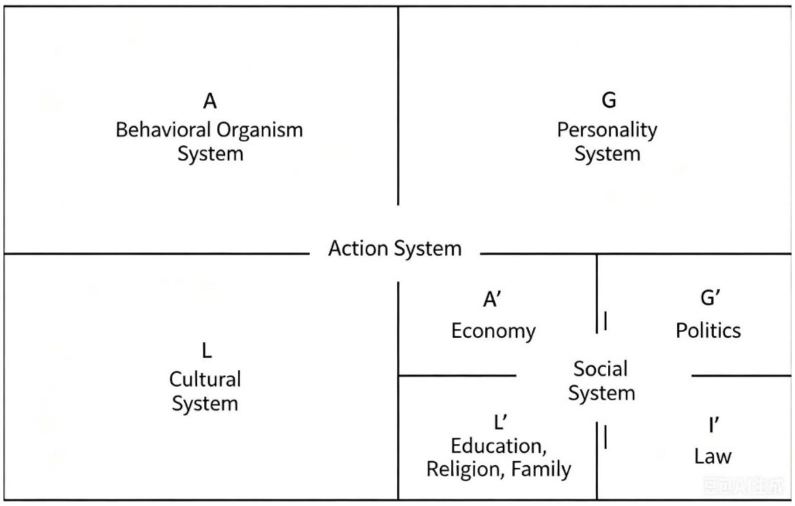

Figure 1. Functional structure of social system

2.3. The feasibility of functionalist analysis path

Richard Rorty proposed a solution to the problem of universality in measuring heterogeneous interests: reducing all problems to political issues, setting aside philosophical, moral, and religious debates, and viewing "imagination" as the best path to moral progress, making people value democratic consensus more than anything else [24]. Upon closer examination of the origin and development of priority within and outside the domain, it is not difficult to find that priority is always intertwined with politics.

In the civil law system, priority originated from Roman law. Roman priority is called a priority mortgage. Unlike other legal mortgages, Roman priority is not determined by the order in which the rights are established, but by the qualifications of the creditor, which is an exception to the principle of "priority of rights before the other." Roman priority includes three types: first, the statutory mortgage of national taxes; second, the legal mortgage right on the wife's dowry; third, the legal mortgage obtained by creditors to assist debtors in preserving or improving real estate [25]. The emergence of legal mortgage rights for national taxation mainly reflects the public welfare concept of prioritizing public over private. Modern philosophers Marx and Engels believed that taxation is a form of redistribution of surplus products or surplus value by the state [26]. But in ancient Rome, taxes were not something that the state arbitrarily demanded from residents, and residents did not pay taxes to the state based on unilateral obligations. This is because the state needs to provide services that guarantee residents' satisfactory lives. Based on the concept of back-and-forth transactions, the state levies taxes on residents, such as war expenses [27]. At the same time, during the period of the Roman monarchy, the treasury and the imperial treasury divided the public finances of Rome into two, and as the emperor's position became stronger than that of the Senate, the imperial treasury became increasingly important. Therefore, when the Imperial Treasury was a creditor, Roman law stipulated that the debtor's entire property was used to guarantee the tax claim of the Imperial Treasury [28]. The emergence of legal mortgage rights on wives' dowries aims to improve women's family status and protect them from the harm of husbands' arbitrary abandonment. In ancient Rome, dowry was the property that a woman brought with her when she got married. This property was not only a compensation for the loss of inheritance rights due to marriage, but also an important symbol of legal marriage and not concubinage [29]. With the continuous expansion of Roman territory, there was a phenomenon of moral decline in society, and the number of divorces continued to rise. During this period, women were deeply troubled by their husbands' arbitrary divorce, and some even used marriage to defraud women of their property. After Ushitini realized that the dowry should belong to the wife, he stipulated that in order to guarantee the woman's right to claim the dowry, the woman had a general mortgage right over the man's property, which had priority over other mortgages [30]. The emergence of legal mortgage rights on real estate is based on Rome's emphasis on the social value generated by real estate. In the view of Roman jurists at that time, building structures or planting plants on land was an expansion and increase of the ownership of the principal thing (which Roman law considered to be the land) [31]. In other words, if the debtor does not receive payment from the creditor, the debtor's real estate will inevitably be damaged, or its value cannot be increased; that is, the ownership of the main property will shrink and remain unchanged. The debtor benefits entirely from the creditor's payment, and based on the principle of fairness, the creditor should be given priority in repayment.

The priority system flourished in France. The French priority system not only inherited French customary law and Roman statutory law, but also abolished some feudal privileges and shackles. Its priority makes it the best superstructure for the development of capitalism. In the French Civil Code promulgated in 1804, priority can be divided into general priority and special priority. The former are the rights of creditors to obtain priority repayment from the value of the debtor's general property. It has two forms: the general priority over movables, which takes all movables as the subject matter, and the priority over movables and immovables, which takes all movables and immovables as the subject matter. The latter are the rights of creditors to obtain priority repayment from the value of the debtor's specific property. It also has two forms: the special priority over movables, which takes specific movables as the subject matter, and the priority over immovables, which takes specific immovables as the subject matter. The specific priority rights of movable property include: rent for houses or land, pledge rights, storage fees for goods, purchase price of movable property, hotel expenses, and debts for official misconduct; The creditor's rights that enjoy priority over real estate include: the sale price of real estate, real estate purchase loans, inheritance debts, worker wages, and worker wage payment loans. According to the specific provisions of priority, the relatively disadvantaged party in the transaction may have the right to receive priority compensation for specific assets. However, among the proletariat, except for construction workers who have priority in terms of wages, the other proletariat has nothing. From this perspective, the original intention of priority is not to solve the livelihood problems of the proletariat, but to appease the extremely poor workers and make them sell their labor force for long-term exploitation by capitalists. It can be seen that the priority of France only consolidated the achievements of the French Revolution and solidified the position of capitalism in France.

The mapping of priority to the politics of various countries provides the possibility for structural functionalist analysis. Zweig and Kötz regarded functionalism as the fundamental research method of comparative law in their "General Theory of Comparative Law" [32]. They pointed out that the problems faced by the laws of every society are essentially the same. Various legal systems solve these problems in different legal forms but with similar functions, so function is the starting point and foundation of all comparative law [33]. Marxism holds that historical development always spirals upwards. In other words, although the priority of each country is a reflection of its politics, it deals with the balance of heterogeneous interests that are currently prominent in society. Throughout the long course of human history, these issues of balancing interests have always been similar, so the functions of priority among countries should be similar. In addition, in the process of determining the priority of debt reorganization financing in China, the generalization of the basis of rights argument makes it difficult to unify the logical value measurement, resulting in various controversies [34]. Considering that the structural functional theory pursues the overall balance and harmony of society, this theory can be applied to discuss the functional role of debt priority in reorganization financing in a multiple "relationship," avoiding focusing solely on individual value judgments. Therefore, we can understand the function of DIP financing priority in the United States from the perspective of structural functionalism, in order to find a solution to the "fairness dilemma" between China's restructured financing debt and secured debt.

3. Functional analysis of debt priority in reorganization financing

3.1. Functional analysis of DIP financing priority

According to Section 364 of the US Bankruptcy Code, US DIP financing regime roughly divides financing priority into three levels: at the first level, if the trustee is able to finance in a non-secured form, there is no need for court authorization, and the debt can be considered as priority for bankruptcy management expenses. At the second level, if the trustee is unable to obtain financing in the manner of the first level, the court may allow claims arising from reorganization financing to rank senior to administrative expenses in the distribution order, or may set up guarantees on the debtor's unsecured assets; Or set up secondary guarantees on the property that the debtor has a secured burden on. At the third level, if the custodian fails to raise funds in the aforementioned manner and has provided sufficient protection for the original guarantor, the court may allow the setting of priority or consistent priority guarantees on the secured property, which is called super priority. It can be seen that the original intention of the designer of DIP financing priority in the United States was to solve the problem of corporate reorganization financing. The repayment order of financing debts ranges from bankruptcy management fees to super priority. Based on the design intention and practical performance of DIP financing, it can be found that DIP financing priority has the following obvious functions.

3.1.1. Reasonable allocation of capital for adaptive functions

Tracing back to its origins, the establishment of DIP financing priority rules in the United States originated from the equitable takeover case of railway companies. Since 1870, the panic caused by economic crises has affected railway companies. A large number of American railway companies have experienced bond interest defaults. However, neither redemption nor direct liquidation can address the debt crisis of the railway company. Because the total liquidation value of railway tracks sold to different creditors is much lower than the operational value of railway companies that own the network. Therefore, restructuring debt while maintaining operations is the most efficient solution for secured bondholders, ordinary creditors, and railway company shareholders. In order to achieve this goal, the judicial practice of "equitable takeover" relying on judicial power endorsement was born in the absence of written law as a basis. When an American railway company is in financial crisis and defaults on its creditors, any creditor can request the court to appoint a manager to take over the railway company [35]. After the manager takes over, the first dilemma they face is insufficient funds to maintain operations. To address this issue, the US court grants the manager the authority to issue a takeover certificate in specific circumstances. The content of the takeover certificate is to guarantee the creditor's rights with all the assets of the railway company, and these creditors' rights have priority over other creditors of the railway company, even over existing secured creditors. The debt of the takeover certificate is the embryonic form of DIP financing priority [36].

Studies have shown that the more effective capital redistribution is, the less impact the economy will have during the depression phase [37]. From this, it can be seen that in the context of multiple economic crises, the establishment of DIP financing priority in the United States is guided by efficiency. Its specific manifestation is that economic benefits play a prominent role in "key debt," and then the assets of the enterprise are redistributed with a super-priority claim to protect "key debt" and reduce the negative impact of economic crises.

3.1.2. The realization of objective implementation functions is essentially fair

"Super priority" is only the appearance of DIP financing priority, while the "fairness and impartiality" of the restructuring plan is the goal of this priority. In bankruptcy liquidation proceedings in the United States, bankruptcy priority is referred to as the absolute priority rule. This rule stipulates that priority creditors are satisfied before unsecured creditors, whose claims are higher than those of equity holders [38]. One characteristic of the reorganization process in the United States is the overturning of the absolute priority rule [39]. Some scholars have pointed out that the reversal of absolute priority rules may be accompanied by the injection of new capital by old shareholders, which is usually the only possibility for companies to restart. The reversal of absolute priority rules has been described as a feature of US bankruptcy law that benefits debtors. This indirectly indicates that legislators do not need to restructure procedures based on economic purposes to protect the rights of equity holders.

In the US Bankruptcy Code, the provision that fully embodies the reversal function of reorganization proceedings is Section 1129 (b) (1), whose core concept is "fairness and impartiality." In the case where the debtor's property is limited, according to the different nature of the creditor's rights, their repayment must have a sequence. Although the development of the market economy requires the private law system to be centered on autonomy of will, its premise is equal status and equal opportunities in order to promote effective competition in the market [40]. However, in reality, there are objective differences between civil subjects in terms of risk tolerance, information acquisition ability, social status, and other aspects [41]. Autonomy of will can only achieve formal fairness. So the restructuring plan cannot only focus on protecting individual rights and interests. Regarding the question of whether the court should approve a restructuring plan that creditors refuse to accept, Section 1129 (b) (1) of the US Bankruptcy Code proposes a mandatory approval system. This system requires that the mandatory approval of the reorganization plan should be "fair and equitable" for any dissenting and impaired voting group. It can be seen that substantive fairness is the core goal of the restructuring plan. Because the DIP financing priority is a sufficient condition for the smooth implementation of the reorganization plan, while safeguarding the legitimate rights and interests of both the debtor and the creditor, the seemingly unfair legislative norms essentially reflect the fairness and efficiency of the reorganization process. Therefore, DIP financing priority is also aimed at achieving substantive fairness.

3.1.3. The integration of functions and the harmonization of US DIP financing regime and exclusive rights system

Exclusive right is the proper name of the bankruptcy law of civil law countries for the secured creditor's right to individual liquidation in bankruptcy proceedings. The "Bartner Principle" established by the United States Supreme Court aims to coordinate the relationship between bankruptcy law and private law norms. Without conflicting with the core values and legal policies of bankruptcy law, bankruptcy law should respect and maintain the content of private law entity norms [42]. Based on this principle, the US bankruptcy law should try to fill in the substantive norms of bankruptcy law with private law substantive norms as much as possible. Therefore, although the US bankruptcy law does not directly provide for the system of exclusive rights, it stipulates that secured creditors have priority over most ordinary creditors in bankruptcy proceedings, which is similar to the legal effect of exclusive rights. This priority provision maintains the priority of security rights, but reduces the amount available to pay other creditors, becoming an obstacle to restructuring corporate financing. In this context, DIP financing priority has had a profound impact on the order of secured claims and has a significant guiding role in the behavior of restructuring financiers and potential guarantors. To some extent, it has played a role in reconciling US DIP financing regime with the exclusive rights system. This is specifically manifested in the following two aspects.

On the one hand, DIP financing priority protects the interests of financiers. The initial purpose of DIP financing priority is to protect the interests of restructuring financiers and reduce their investment concerns. If the restructuring of the enterprise fails, the lowest repayment order of the financier at this time is equivalent to the bankruptcy management expenses. In US bankruptcy law, bankruptcy management expenses include bankruptcy expenses and common benefit debts. After the secured debt is settled, the bankruptcy management expenses are first settled. Therefore, because DIP financing priority is generally in the second or higher order of repayment, even if the company's restructuring fails, the interests of the financiers are protected to the greatest extent under existing conditions. Financing parties can focus solely on investing in restructuring enterprises, which not only saves companies on the brink of danger but also promotes the effective circulation of idle funds.

On the other hand, DIP financing priority guarantees the fundamental interests of security rights. In order to attract financing, DIP financing priority in the United States provides corresponding preferential treatment to financiers to reduce investment risks caused by uncertain restructuring prospects and alleviate their worries. Among the three levels of DIP financing priority, the priority of the first two levels will not affect the repayment order of existing security rights. However, super-priority claim at the third level completely subverts the existing liquidation rules of bankruptcy law and is detrimental to the interests of existing secured creditors. Therefore, the application of super-priority claim must comply with the principle of full protection: One is to compensate the secured creditor, and the amount of compensation is equal to the amount of loss in the value of the creditor's collateral; the second is to provide additional guarantees or set guarantees on other property; thirdly, if it is found that the protection is not sufficient in the future, the creditor who has suffered the loss is given the right to claim the common benefit cost [43]. It can be seen that preferential treatment of financiers is not allowed at the expense of the interests of existing secured creditors. The DIP financing priority still guarantees the basic interests of security rights, which is in line with the purpose of the exclusive rights system.

3.1.4. Value transmission of pattern maintenance function

As mentioned earlier, the prototype of DIP financing priority in the United States was the debt of proof of takeover. The debtor of this debt is limited to the railway company. On the premise of recognizing the importance of reorganization financing in maintaining the operation of the railway company, the court authorizes the priority of the debt in the takeover certificate on the grounds that the railway company has public value. From this, it can be seen that the priority basis of the debt of proof of takeover lies in the priority of public interest. The financing priority based on the proof of takeover debt is the result of value judgment, integrating corresponding values into bankruptcy practice, promoting people to peacefully accept the possible damage to the rights and interests that are forcibly arranged, and completing the value orientation of society as a whole. On the one hand, the formation of financing priority is not based on the existence of absolute priority rights or a determined level of rights, but requires the participation of value judgment to strengthen the legitimacy and rationality of its content increase or decrease; On the other hand, financing priority is a policy choice made by the United States based on its own national conditions in a special economic environment [44]. Therefore, financing priority brings the values within the policy to every corner of society, laying a sufficient ideological foundation for the birth of DIP financing priority.

3.2. The significant function of debt priority in reorganization financing

Creating a completely new right undoubtedly requires a considerable cost. For example, if the priority of reorganization financing claims is positioned as a statutory security interest, it will inevitably lead to the incomplete implementation of various principles of property rights and become a mere formality. Since we have paid the risk cost, we inevitably hope to achieve higher returns. The establishment of debt priority rights for reorganization financing in China is certainly aimed at enabling it to play its due role. Based on the explicit functions of DIP financing priority in the United States, the author believes that China's debt priority for reorganization financing has the following four explicit functions:

3.2.1. Redistribution of benefits

The US bankruptcy law rearranges the interests of employees, tax authorities, fishermen, and farmers. It grants special treatment to landlords and business partners. It gives a specific priority position to parties to executory contracts. It rearranges the priority of beneficiaries of statutory liens in bankruptcy. It treats creditors who lend to consumers differently from those who lend to businesses. It treats general creditors and creditors with claims for contemporaneous exchange differently from other unsecured creditors. It also treats banks with the right of setoff differently from banks without that right. This US bankruptcy priority list has hinted to us that bankruptcy laws classify creditors based on their financial status. Scholars have directly pointed out that these are all about the choices of distribution and redistribution [45].

In China's bankruptcy law, the interests of workers, social insurance authorities, tax authorities, and guarantors are also distributed. According to Article 113 of the Enterprise Bankruptcy Law, in the event that the debtor is unable to repay all debts, the order of property distribution is: (1) Bankruptcy expenses and joint benefit debts; (2) Labor debt; (3) Social insurance premiums and tax claims; (4) Ordinary bankruptcy claims. According to Article 109 of the Enterprise Bankruptcy Law, the exclusive rights holder has the priority right to receive compensation for specific assets. Once China establishes a priority right for debt reorganization financing debts, the newly added financiers will inevitably break the aforementioned distribution order and redistribute benefits in the face of limited assets of the restructuring enterprise.

3.2.2. Implementing the principle of fairness

The principle of fairness in the Enterprise Bankruptcy Law includes fair treatment of all stakeholders such as secured creditors, employees, insurance and tax authorities, financiers, and ordinary creditors; The narrow principle of fairness only includes the provisions in Article 1 of the Enterprise Bankruptcy Law that contain the term "fairness," specifically referring to the fair settlement of creditor's rights and debts. The principle of fairness serves as a powerful tool to break the deadlock in the game between multiple parties with interests. It adhered to a basic rule in the "restructuring," which is to expand the quantity of existing assets. Under the concept of bankruptcy liquidation, the property of the bankrupt debtor is a fixed and unchanging guarantee, resulting in a zero sum game in the approval process of the restructuring plan. But the essence of corporate restructuring is to expand the cake before distributing it, aiming to ease conflicts of interest. Therefore, the principle of fairness in reorganization considers how to increase the debtor's assets and then increase the interests of stakeholders. Therefore, the priority of reorganization financing serves as the starting point for the implementation of the restructuring plan. It should adhere to the principle of fairness and not simply and roughly distribute bankruptcy assets equally, ignoring the crucial role of financiers in the process of "optimizing stock and expanding increment."

3.2.3. Coordinating bankruptcy law and private law entity norms

China has gradually formed a basic consensus to fill the substantive norms of bankruptcy law as much as possible with private law substantive norms while drawing on foreign experiences such as the "Bartner Principle" [46].

In Chinese civil law norms, property rights have priority effect [47]. In the bankruptcy liquidation procedure, the priority effect of claims priority is maintained, and secured claims have the highest priority for repayment on specific assets. The vast majority of countries in the world have accepted the ranking arrangement of secured debt under bankruptcy law. In the *Guidelines on Effective Bankruptcy and Creditor/Debtor Systems* issued by the World Bank, the guarantee system is regarded as an important system for maintaining the good operation of the market economy. Because determining performance enhances creditors' investment confidence, the law should clarify priority rules and minimize or eliminate priority over security rights as much as possible [48]. However, some scholars still question the proposition that "property rights are superior to creditor's rights." Some scholars believe that this proposition mistakenly simplifies the question of which priority to realize between two creditor's rights into a comparison between security interests and creditor's rights [49]. Some scholars also believe that property rights and creditor's rights are not on the same object, and there is no opportunity for conflict to arise [50]. Formally, the bankruptcy law stipulates that the secured interest holder has the highest priority for repayment due to enjoying exclusive rights. This obviously highlights the comparison between creditor's rights on the same object and weakens the comparison between property rights and creditor's rights. In this situation, the priority of reorganization financing debts should have the ability to coordinate the tense relationship between bankruptcy law and private law entity norms, rather than exacerbating conflicts.

3.2.4. Inheriting core values

Marx once said that if "ideas" are separated from "interests," they will definitely make a fool of themselves [51]. During the period of social transformation and rapid development of the market economy in China, economic interests often determine the value judgments of the subjects [52]. In the debt relationship of reorganization, economic interests are the fundamental reason for the mutual exclusion of reorganization subjects. If the restructuring of the enterprise fails and enters bankruptcy, based on the existence of the bankruptcy exemption system, it is not important for the debtor to choose which plan to repay all creditors; For creditors, the priority of repayment is the key to whether their debt can be realized when the debtor's assets are insufficient to cover the debt. The value judgment of each subject is based on their own needs, interests, and goals. If legislators or judges only make value judgments from the perspective of a single creditor, they will find that no creditor's claim should be abandoned. Only the dominant values in society can guide the direction of value judgments.

With the development of modernization, values that are compatible with the modern market economy have flooded into Chinese society and been widely accepted. The foundation of the existence of traditional Chinese values has been challenged, but as Gustav Le Pen said, although traditional values are incomplete, their power is still very strong [53]. The value of prioritizing private rights is increasingly widely accepted in bankruptcy reorganization debt conflicts. The traditional values born from agricultural civilization will not disappear, but will become more prominent. Although bankruptcy tax claims give way to worker claims, they still have priority over general claims in terms of repayment. Therefore, in order to implement the priority of reorganization financing debts in China, it should have the function of inheriting and developing the core socialist values of China.

3.3. The potential function of debt priority in reorganization financing

The prominent functions that China's debt priority rights for reorganization financing should possess include redistributing benefits, realizing the principle of fairness, coordinating bankruptcy law and private law entity norms, and inheriting core values. The question is, who determines the degree of "reasonableness," "fairness," "coordination," and "transmission" here? Values are the premise of legal logic. Whether values are established or not can be tested by non-legal logic [54]. Some scholars believe that the bankruptcy priority stipulated by empirical laws in different countries has broken through the principle of equal creditor rights, which is actually the result of logic compromising policies [55]. David Easton argued that the meaning of policy is the authoritative distribution of social values [56]. Therefore, as a new type of right, the priority of reorganization financing claims has to face the problem of not allowing certain people to enjoy certain things and allowing certain people to possess them.

The key to accepting the priority of debt reorganization financing by all stakeholders is whether it is the result of balancing human rationality to the maximum extent possible. Enjisch and Larentz believe that the provisions in legal traditions and international conventions originate from legal reality [57]. In the process of transforming from legal reality to legal provisions, legislators use a utilitarian way of thinking. The so-called utilitarian way of thinking refers to first determining that the result is the maximization of "good," and then developing from "good" to "just." Utilitarianism reduces various considerations in ethical life into a single value thinking mode, extracts a pattern from the understanding of public rationality, and then imposes this pattern on individuals to obtain the justification for the so-called consensus explanation [58]. From this perspective, the utilitarian way of thinking continuously dilutes the rich ethical resources in the modern world. Unlike the traditional legal model that follows utilitarianism, the creation of debt priority rights for reorganization financing is based on people's trust in legislators. Given that all human activities contain the motivation to maximize subjective utility, even seemingly irrational altruistic behavior can be explained by maximizing benefits. Therefore, the function of resolving conflicts of rights through debt priority in reorganization financing is to maximize human rational ability and suppress human irrationality in the process of weighing reasonable interests. In response to the issue of fairness between restructured financing debt and secured debt, attention should be paid to individual justice. Differentiated treatment should be given to different categories of parties, and the maximum utilization of limited property should be achieved. As some scholars have pointed out, in practical aspects such as legal application, as long as abstract propositions are transformed into concrete situations, the measurement of reasonable interests is feasible [59].

4. Analysis of the necessity and feasibility of establishing priority rights for reorganization financing debt

Based on the analysis above, a socially accepted debt priority for reorganization financing should have "4+1" functions. There are four explicit functions (redistributing benefits, implementing fairness principles, coordinating bankruptcy law and private law entity norms, and inheriting core values), as well as one implicit function (resolving conflicts of rights). The key to whether the priority right of reorganization financing claims can be established in China is whether its "4+1" functions can be smoothly performed in specific reorganization cases.

In the restructuring case of Shanghai Yuehe Real Estate Co., Ltd., three-quarters of the joint benefit bond investors demanded that their joint benefit bonds enjoy super-priority claim repayment rights. Creditors with property collateral express opposition. Therefore, the management team proposed that the mortgagee be given priority in receiving compensation based on the value of the bankruptcy property on the date of acceptance of the bankruptcy proceedings. After the completion of the project's continuation, there will be a value-added portion between its sales revenue and the property value on the date of bankruptcy acceptance, and the co beneficial creditors will receive priority compensation for the value-added portion. This proposal has been confirmed by Article 51 (1) of the Interpretation of the Supreme People's Court on the Application of the Civil Code of the People's Republic of China on the Guarantee System (hereinafter referred to as the Judicial Interpretation on the Guarantee System). In this way, a hypothetical proposition is obtained: "If the value of the property increases after reorganization, then the joint benefit creditors will receive priority compensation for the increased value." At this point, the "appreciation of property value after restructuring" is a sufficient and necessary condition to constrain the emergence of "priority rights for reorganization financing debt." However, it is unknown whether the property value of the enterprise will increase after restructuring, which makes the emergence of priority rights for reorganization financing debt not inevitable and greatly reduces the attractiveness to restructuring investors. Therefore, whether this constraint can be eliminated is an important support for proving the establishment of priority rights for reorganization financing. By analyzing the function of debt priority in reorganization financing, it is proven that "property value appreciation after restructuring" is not a necessary condition for "debt priority in reorganization financing."

Taking the conflicts of interest arising from the reorganization of real estate enterprises as the analysis sample, using the theory of interest measurement [60], a game table of interests between common interest bond investors and property secured creditors is constructed (as shown in **Table 2**), which can clarify the functional content of the priority of reorganization financing claims.

Table 2. Interest game between investors of mutual benefit bonds and creditors with property guarantees

Select the object of protection	Result					
	Party interests		Group interests		Institutional interests	Social public interests
	Common benefit debt investors	Property security right holders	Group interests of common benefit debt investors	Group interests of security right holders	Guarantee system	National policy : optimize the business environment
Common benefit debt investors	√	×	√	×	×	√
The person with property security right	×	√	×	√	√	√

Explanation: "√" indicates legal protection, "×" indicates no legal protection.

From the above table, it can be seen that if the law protects the interests of joint interest bond investors, the interests of the guarantee system will not be protected, while the social public interest will be protected. On the contrary, if the interests of property security rights holders are protected, both institutional interests and social public interests can be protected. Based on this result, it is necessary to establish a debt priority for reorganization financing, but there is still a lack of feasibility. Next, we will discuss these separately.

4.1. Analysis of the necessity of creating priority rights for reorganization financing debt

4.1.1. Priority rights for debt reorganization financing can allocate capital reasonably

After the real estate enterprise enters bankruptcy proceedings, whether from the perspective of protecting the interests of creditors, realizing the utility of land resources, or maintaining the survival of the real estate enterprise, reorganization is the procedure that maximizes the interests of all parties. On the one hand, fully utilizing idle funds to improve the success rate of restructuring; On the other hand, successful financing will not reduce the amount of unsecured debt repayment, but can instead protect the repayment interests of unsecured creditors by reducing the possibility of the enterprise going bankrupt and liquidation. Therefore, the priority of reorganization financing claims has the function of rational allocation of capital.

4.1.2. Priority rights for debt reorganization financing to achieve substantive fairness

The priority of reorganization financing claims is a breakthrough in the principle of equality of creditors, and it also breaks through the current priority rules of security rights. The guarantee system is one of the important systems in the substantive norms of private law in China. The priority of reorganization financing is different from the current bankruptcy priority, inferior to secured claims, but seeks the highest priority position. However, considering the act of injecting incremental funds into unfinished projects, it is a high-risk investment behavior. It is necessary to provide investors with corresponding preferential treatment. The DIP financing priority in the United States grants restructuring financiers better guarantee rights, establishes a comprehensive financing hierarchy system, and sets the priority authority of financiers in hierarchical levels [61]. This hierarchical system recognizes the differences in financing methods and risk levels among financiers. Comprehensively considering the situation of financiers and other creditors in the context of corporate restructuring and making differentiated arrangements is substantive fairness in the outcome.

4.1.3. Priority rights of debt reorganization financing are transmitted through top-down values

The priority of reorganization financing and the guarantee system are both promoting corporate financing. The priority of reorganization financing is to leverage stagnant funds, while the guarantee system is to maintain the flow of healthy funds. But in terms of form, the priority of reorganization financing is consistent with the values conveyed by the guarantee system. Both are guided by maximizing the welfare of corporate stakeholder groups, following the logic of win-win cooperation among stakeholders, and achieving corporate reorganization financing [62]. Therefore, the priority of debt reorganization financing has the function of transmitting values, and the content of values is consistent with the guarantee system.

4.2. Feasibility reflection on establishing priority rights for reorganization financing debt

4.2.1. The priority of reorganization financing claims cannot be coordinated between bankruptcy law and civil code

There is a clear inconsistency between the provisions of the Civil Code on security interests and the priority of reorganization financing claims. The highest priority position sought by the priority of reorganization financing does not conform to the principle of party autonomy, and may even directly lead to a decrease in the repayment rate of the guarantor. Scholars have found that both the theory of "creditor power" and the theory of "information determination" determine to what extent the private credit system can provide loans to the outside world. The former refers to the more convenient it is for creditors to recover loans or obtain collateral, the more willing they are to lend [63]. The latter refers to lenders being more inclined to lend to borrowers they are familiar with [64]. Meanwhile, studies have found that in underdeveloped countries and regions with incomplete laws, the operation of credit markets relies on information sharing; Countries and regions with relatively complete legal systems pay more attention to improving bankruptcy systems and safeguarding the rights of post-bankruptcy creditors [65]. Therefore, prioritizing the protection of the interests of property secured creditors is more conducive to the development of China's credit market. The priority of reorganization financing does not have the function of coordinating bankruptcy law and private law entity norms.

4.2.2. The priority of reorganization financing claims is not the optimal solution to resolve conflicts of rights

The priority right of debt reorganization financing does not have the function of resolving conflicts of rights. According to the theory of balancing interests, since protecting the interests of common interest bond investors is in line with the country's policy of optimizing the business environment, and the guarantee system hinders the restructuring of real estate enterprises, it is necessary to break through the guarantee system and prioritize the protection of the interests of common interest bond investors. But protecting the interests of the secured party is beneficial to both the security system and the optimization of the business environment. The 'Access to Credit' indicator is one of the top ten indicators in the World Bank's Global Business Environment Assessment. There are four secondary indicators, namely the Legal Rights Strength Index, Credit Information Depth Index, Credit Registration Institution Coverage, and Credit Institution Coverage. To achieve the prosperity of the credit market, it is not only necessary to improve the protection of creditors' rights, but also to perfect the credit information sharing mechanism. China is a developing country, and the most effective way to improve the credit market environment should be to perfect the credit registration system. At present, significant progress has been made in the improvement of China's legal system. In this critical period, it neither conforms to the principle of "first come, first served," nor does it give priority to reorganization financing in the publicity system, which will impact the gradually improved information sharing mechanism and is not conducive to the score of the "access to credit" index. Therefore, protecting the interests of property security rights holders is the "maximum net benefit" solution to protect the public interest.

In summary, the functions of debt priority in reorganization financing are necessary for current social development, so the establishment of debt priority in reorganization financing is reasonable. However, the debt priority for reorganization financing does not fully possess the "4+1" function that is accepted by society as a bankruptcy priority. For example, it lacks coordination between bankruptcy law and civil code, as well as in resolving conflicts of rights, so the creation of debt priority rights for reorganization financing cannot pass the tests of necessity and feasibility.

5. Other paths for smooth reorganization financing channels

With the rapid development of social technology, new types of rights will continue to emerge. The closed hierarchy rules are difficult to ensure the reconciliation of rights conflicts that have not yet emerged. Priority is a legal tool that adapts to the development of social relations and serves as a "regulator" for resolving conflicts of rights. However, it is not the universal key to resolving conflicts of rights. Based on the previous test results, it is not a correct choice to fully entrust the legislative idea of establishing a super-priority claim for reorganization financing to market regulation in the current difficulty of financing for restructuring enterprises. We can try to think from the perspective of investors. At the practical level, the types of investors include financial investors and strategic investors. The former prefers to invest in short-term arbitrage of enterprises. The latter focuses more on long-term returns and has advantages in technology, management, and talent, which can promote the restructuring and upgrading of the enterprise's industrial structure. At the legislative level, there are no strategic investors among the entities identified in the Enterprise Bankruptcy Law. Therefore, from the perspective of non-market regulation, alleviating the financing difficulties of restructuring enterprises can be achieved by improving the protection of the rights and interests of financial investors and strategic investors in different types.

Financial investors focus on business performance, and their capital injection behavior is essentially speculative activity. Although from a microeconomic perspective, investing in restructuring enterprises, especially non-listed companies, often does not fully align with the economic self-interest of a single economic organization and appears to be irrational. But from a macroeconomic perspective, investors can interact and communicate with the bankruptcy administrator through the bankruptcy reorganization case information network to obtain the remaining operational value of the reorganized enterprise. Therefore, the information disclosed by restructured enterprises is the least dissipated and most efficient investment indicator. Operating value refers to the social and economic benefits that an enterprise can create in its continuous operation. The standard for encouraging corporate restructuring is that the operational value of the restructured enterprise is higher than the value of bankruptcy liquidation. We take the restructuring case of Lifan Technology (Group) Co., Ltd. (hereinafter referred to as "Lifan Technology") as an example. Lifan Technology was the top enterprise in Chongqing's motorcycle export value before the restructuring. Due to the gradual decline in business performance, a large number of debts could not be repaid and faced bankruptcy reorganization. Subsequently, the financial investor Liangjiang Fund introduced by Lifan Technology is a state-owned investment fund. The reason why Lifan Technology can attract government funding is due to its rich operational value. It involves the local government's fiscal revenue, regional industrial development, and maintaining social stability. As rational investors, financial investors should have a certain level of risk tolerance. Therefore, starting from the principle of economic self-interest, the protection of the rights and interests of financial investors should focus on improving the information disclosure system of restructured enterprises and providing reliable investment indicators for financial investors.

Strategic investors focus on the layout of the market. They expect to have a certain degree of discourse power in the enterprise, participate in daily business management, and obtain strategic investment returns in the industry. Unlike financial investors who only invest cash flow, strategic investors not only need to invest capital, but also need to invest advanced technology and management to promote the adjustment and upgrading of the company's product structure and industrial structure. This is because strategic investors focus on optimizing and expanding their own business through restructuring, so the core of strategic investment is the "strategic synergy effect." Reorganized enterprises that can trigger "strategic synergy effects" have a natural appeal to strategic investors. Improving the information disclosure system for restructured enterprises can enhance the efficiency of strategic investors in discovering investment targets. But there are boundaries to the industrial expansion brought about by strategic investment. Strategic investment restructuring of enterprises carries expansion risks, and the information disclosure system cannot provide a bottom line for such risks. Under the current bankruptcy law in our country, it is more appropriate to give new financing the status of joint benefit debt. Some scholars have mentioned that common benefit debts are not a super-priority claim and cannot be superior to security interests. However, the security interest is restricted in the reorganization process, and the mortgagee cannot freely realize the collateral. The efficiency of realizing benefits of common benefit debts is stronger than that of security interests [66]. In other words, common benefit debts can protect the exit rights of strategic investors, reduce their investment concerns, and promote their investment in restructuring the enterprise. However, it is worth noting that the Interpretation of the Enterprise Bankruptcy Law (III) clearly stipulates that new loans shall refer to the relevant provisions of common interest bonds. In terms of context, financial investment is included, but the amount invested in the form of equity, technology, or management is not clearly defined. Thus, there is still a lack of protection for the rights and interests of strategic investors, and the co-benefit bond financing model needs further improvement.

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