

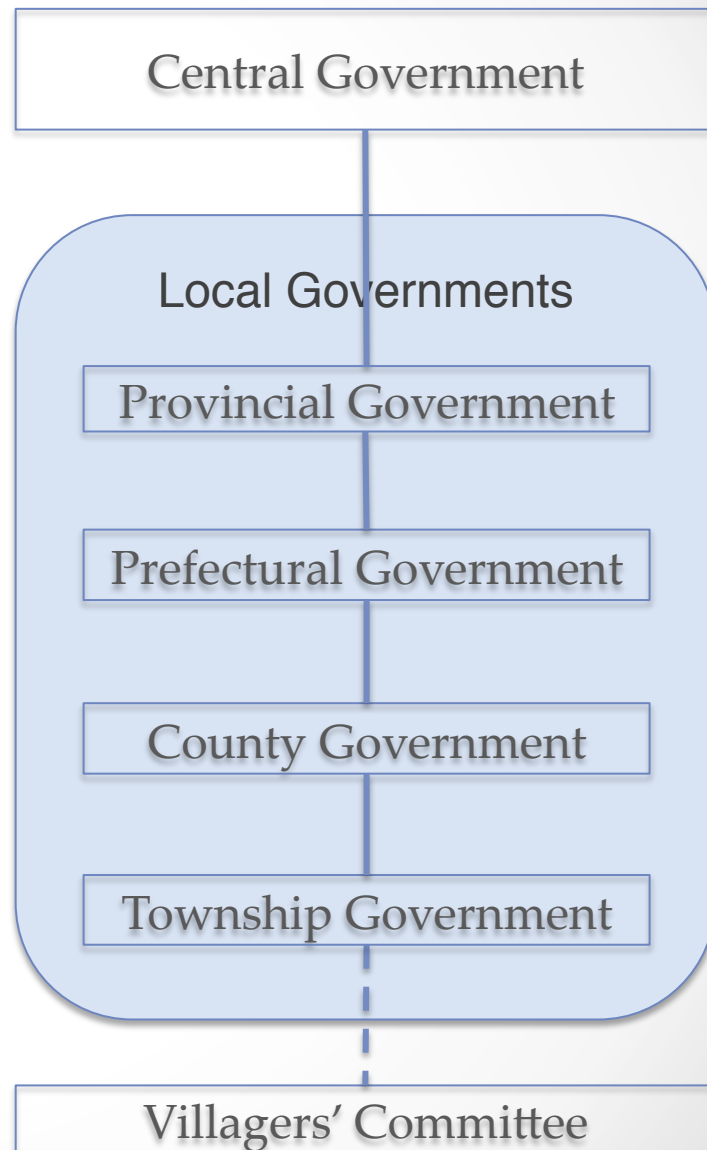
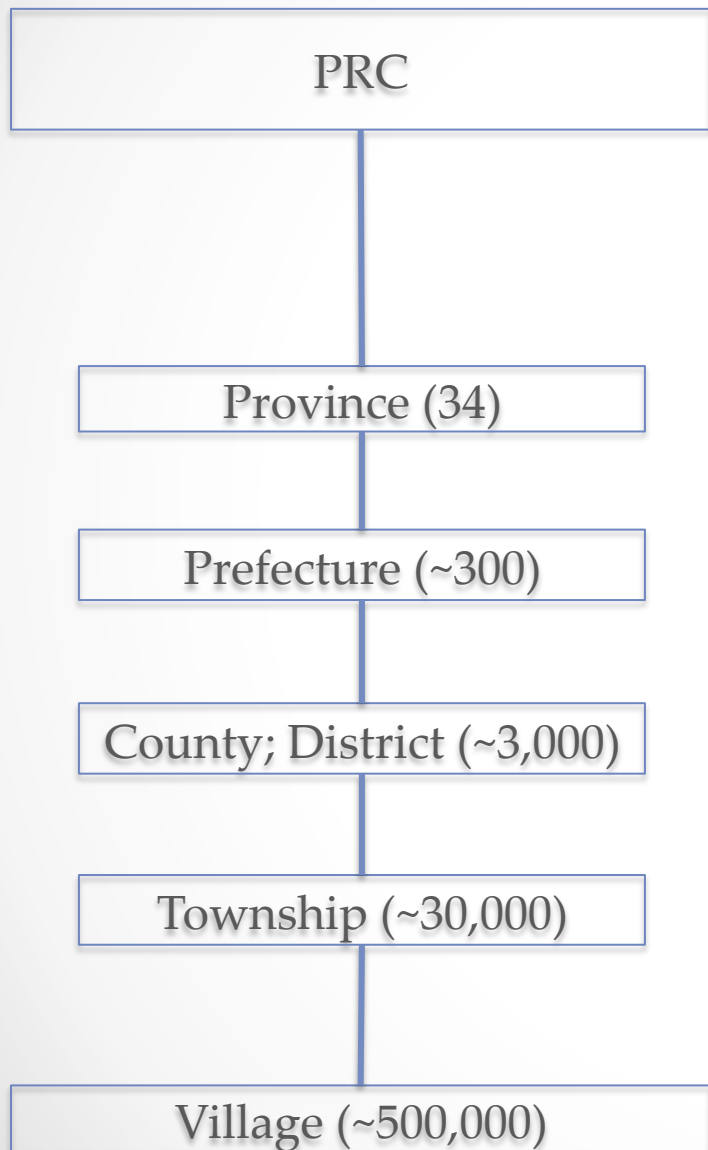
11.S945 Urbanizing China

# Financial and Land Institutions in China

Liyan Xu, Jinhua Zhao

9/16/2013

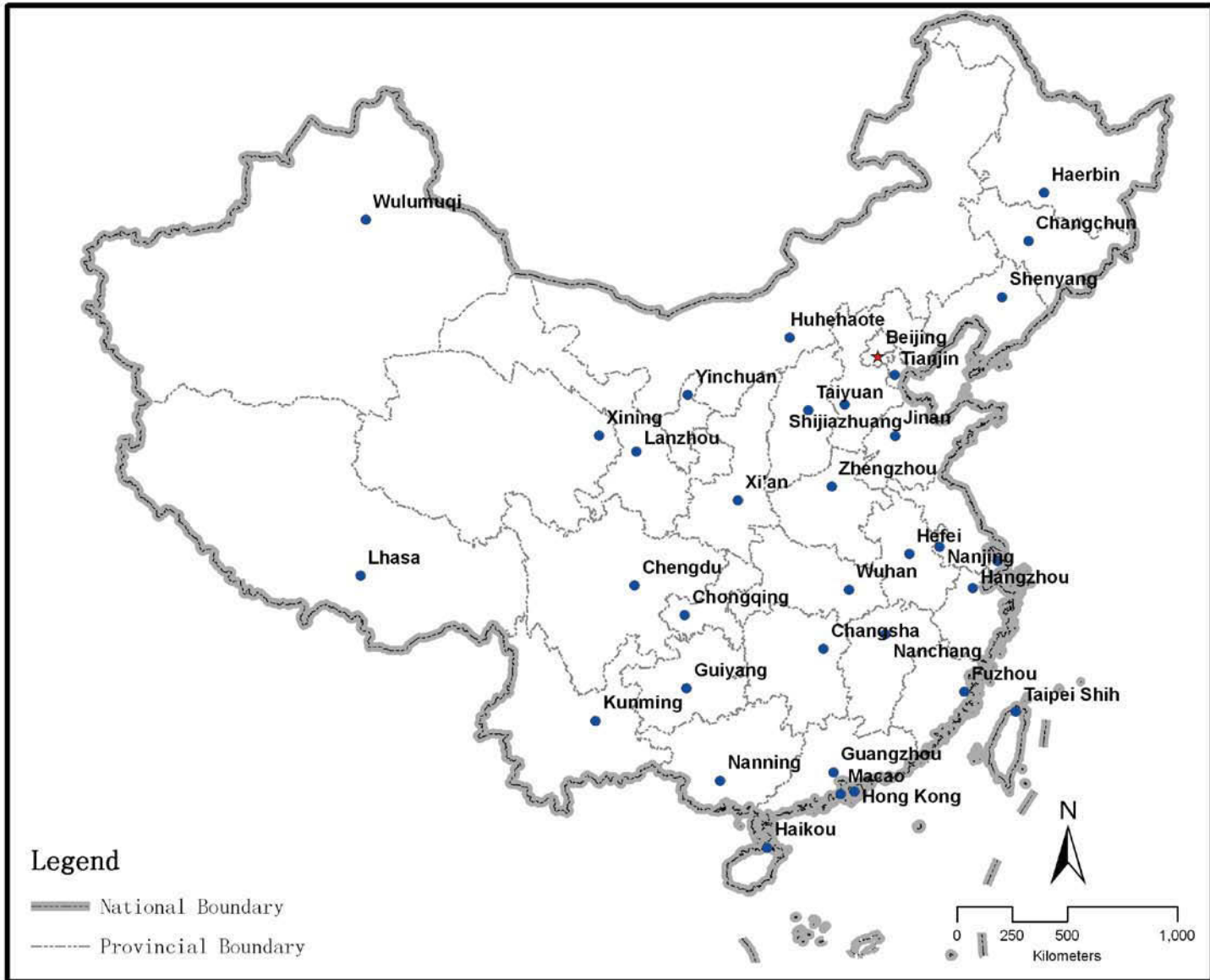
# Basic Structure of Governance in China



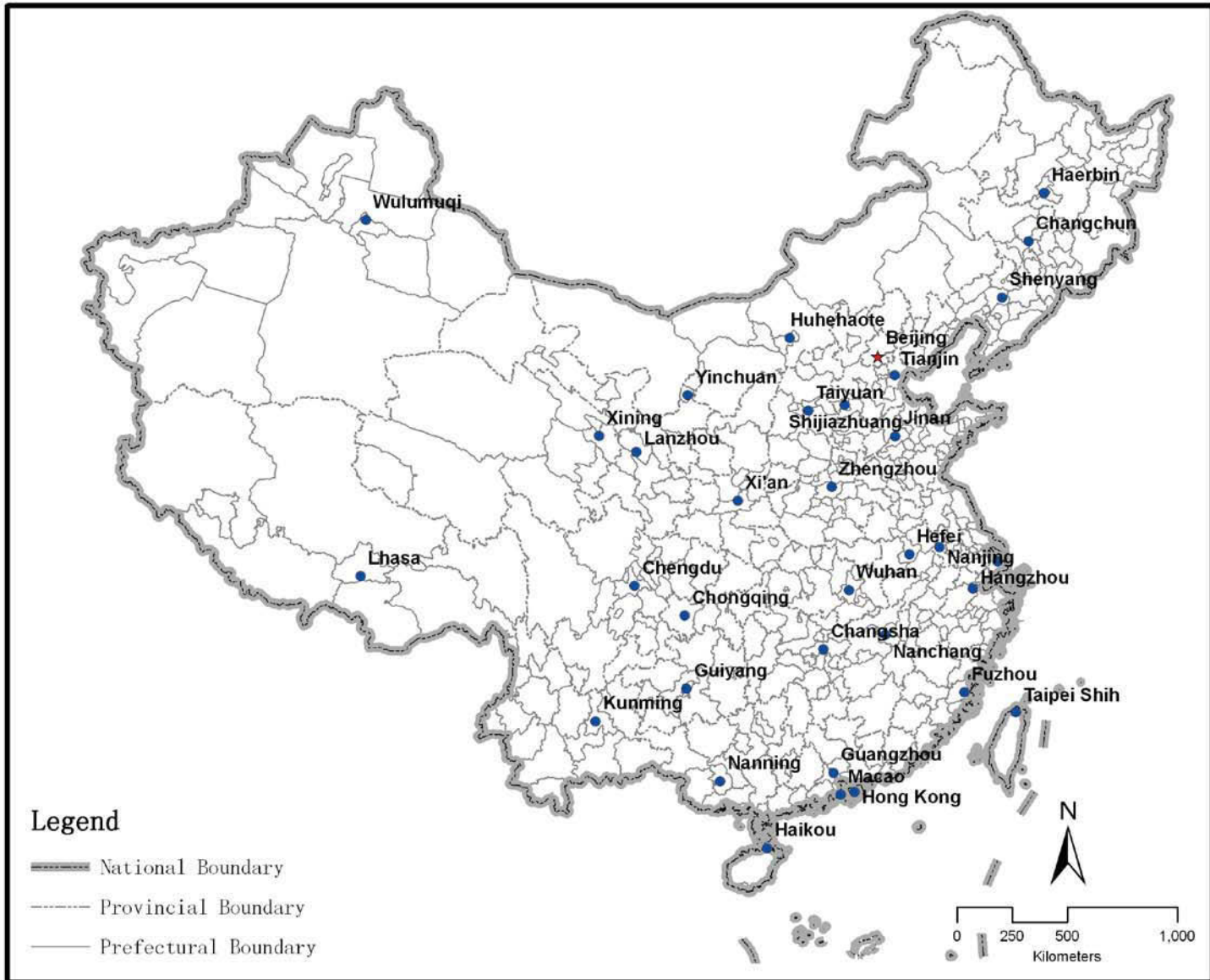
# Country



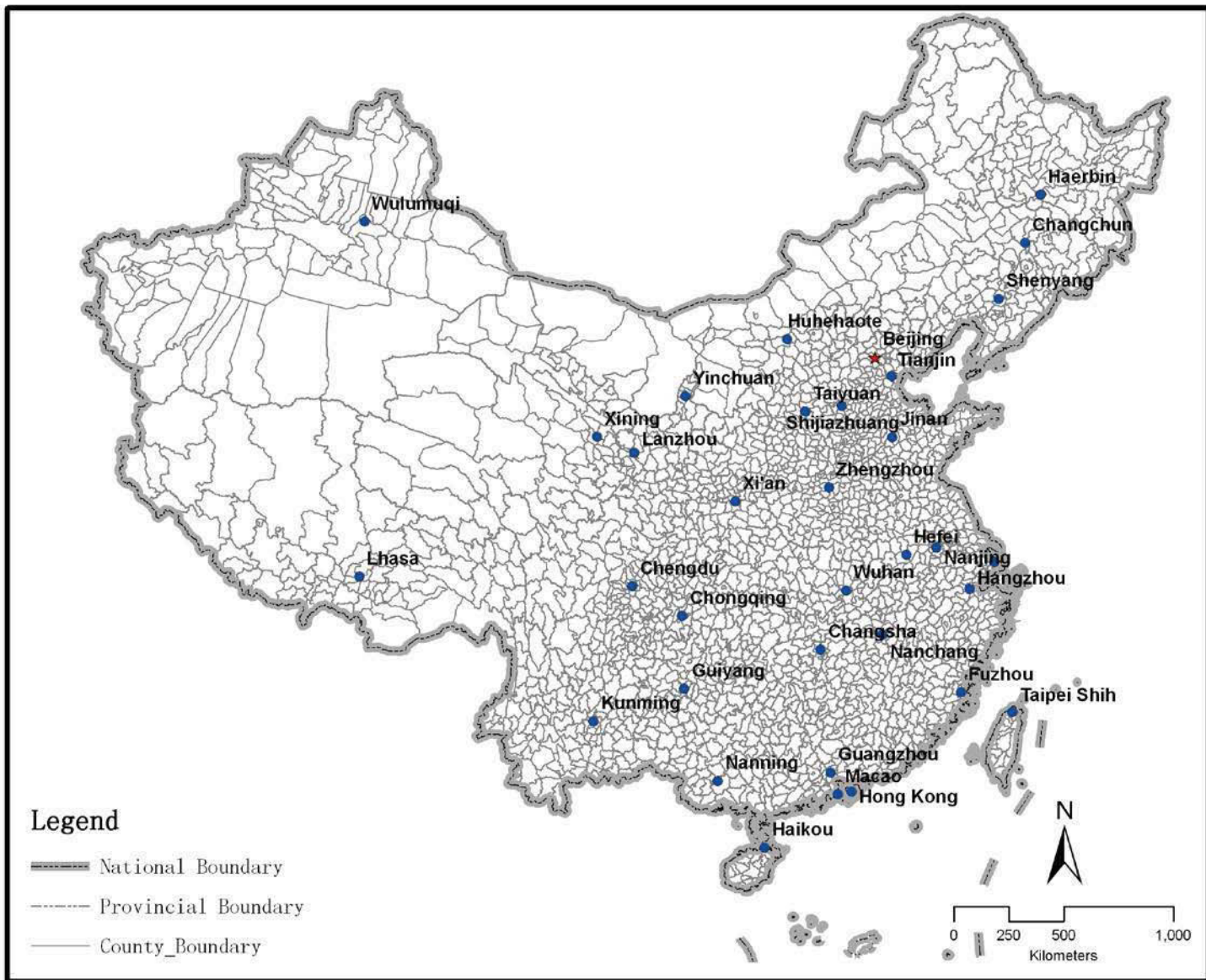
# Provinces



# Prefectures

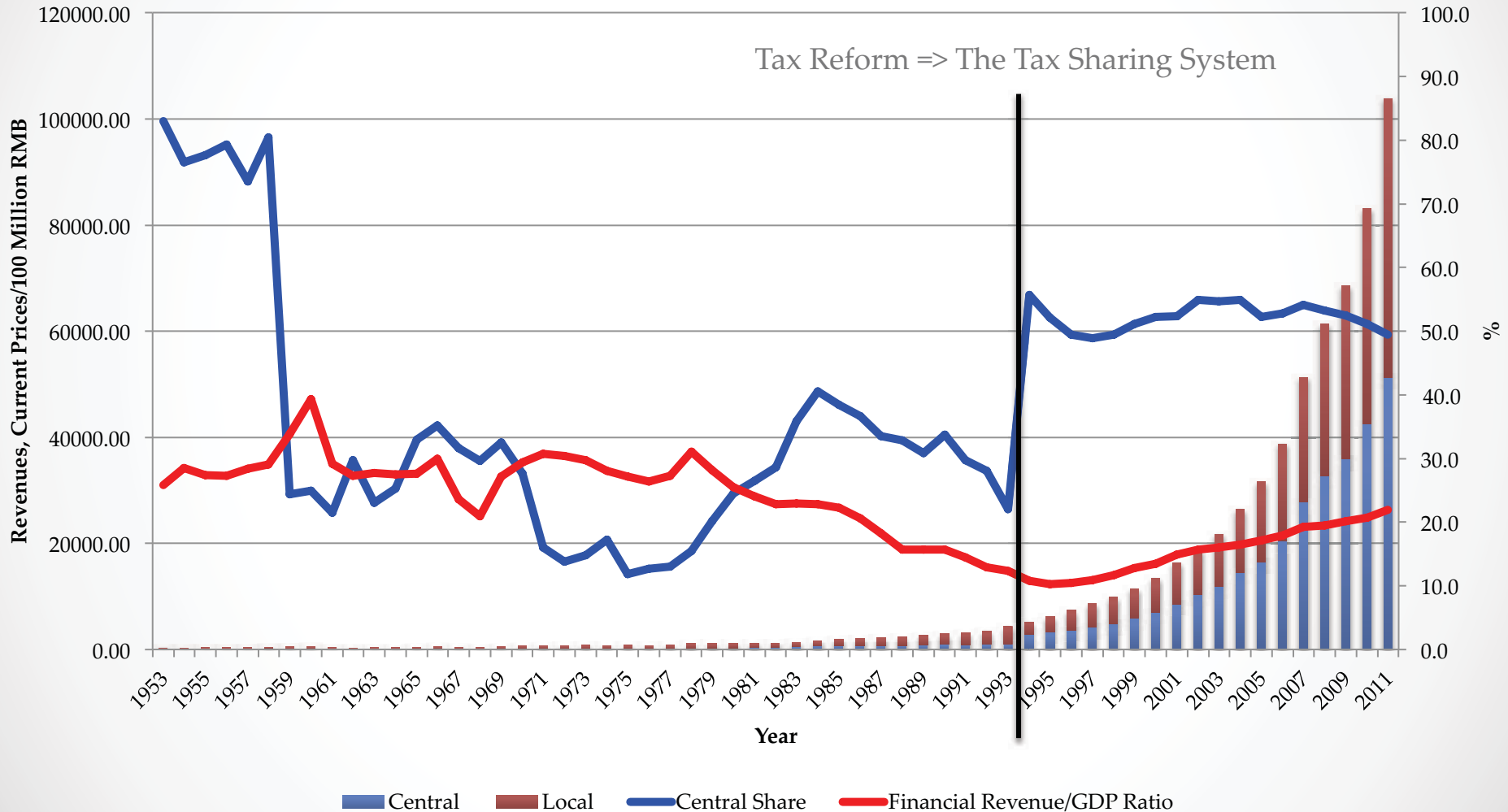


# Counties



# Basic Facts of China's Public Finance

## Public Finance in China 1953-2011



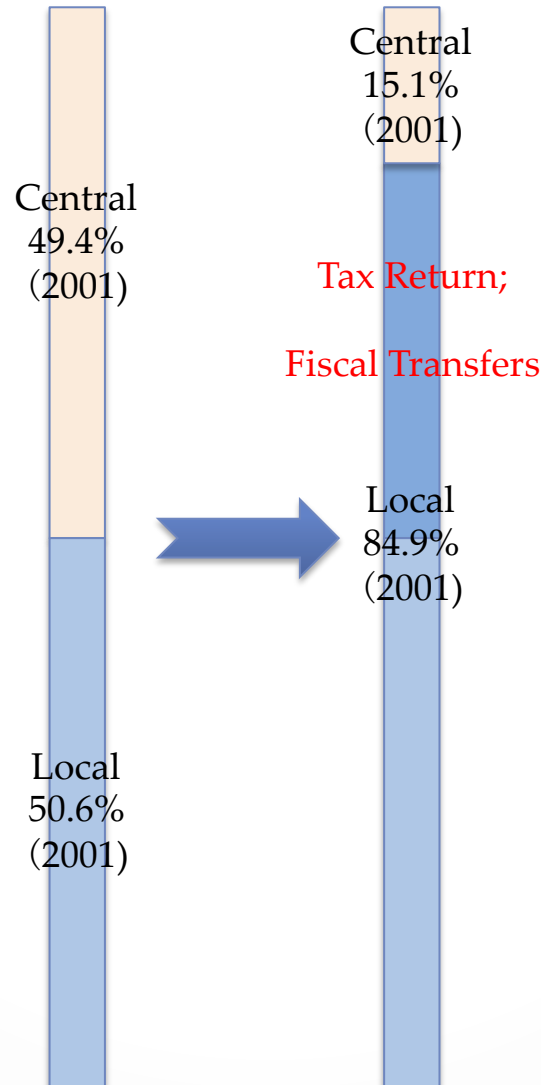
# Fiscal Federalism with Chinese Characteristics

## Income

- |                  |  |
|------------------|--|
| To Central Gov't | <ul style="list-style-type: none"> <li>• Tariff;</li> <li>• Profit from designated State-run firms;</li> <li>• Sea Oil Tax;</li> </ul> |
|------------------|--|

- |                              |  |
|------------------------------|--|
| Shared Revenue Sources (C/L) | <ul style="list-style-type: none"> <li>• VAT(75/25);</li> <li>• Income tax/40);</li> <li>• Stamp tax on securities transactions (97/3);</li> </ul> |
|------------------------------|--|

- |                |  |
|----------------|--|
| To Local Gov't | <ul style="list-style-type: none"> <li>• Business tax;</li> <li>• Other resource tax;</li> <li>• Other stamp tax;</li> <li>• Vehicle&amp;Boat tax;</li> <li>• Contract tax;</li> <li>• Tobacco tax;</li> <li>• Urban land use tax;</li> <li>• Land VAT;</li> <li>• Property tax;</li> <li>• <b>Land grant fees;</b></li> </ul> |
|----------------|--|



## Expenditures

- |                    |  |
|--------------------|--|
| From Central Gov't | <ul style="list-style-type: none"> <li>• Central gov't operating;</li> <li>• Defense;</li> <li>• Diplomatic expenditures;</li> <li>• T-Bill payments;</li> </ul> |
|--------------------|--|

- |                                       |   |
|---------------------------------------|---|
| Shared Expenditures (Primarily Local) | <ul style="list-style-type: none"> <li>• Law enforcement;</li> <li>• Health care;</li> <li>• Agriculture;</li> <li>• RID;</li> <li>• Universities;</li> <li>• Infrastructure investment;</li> </ul> |
|---------------------------------------|---|

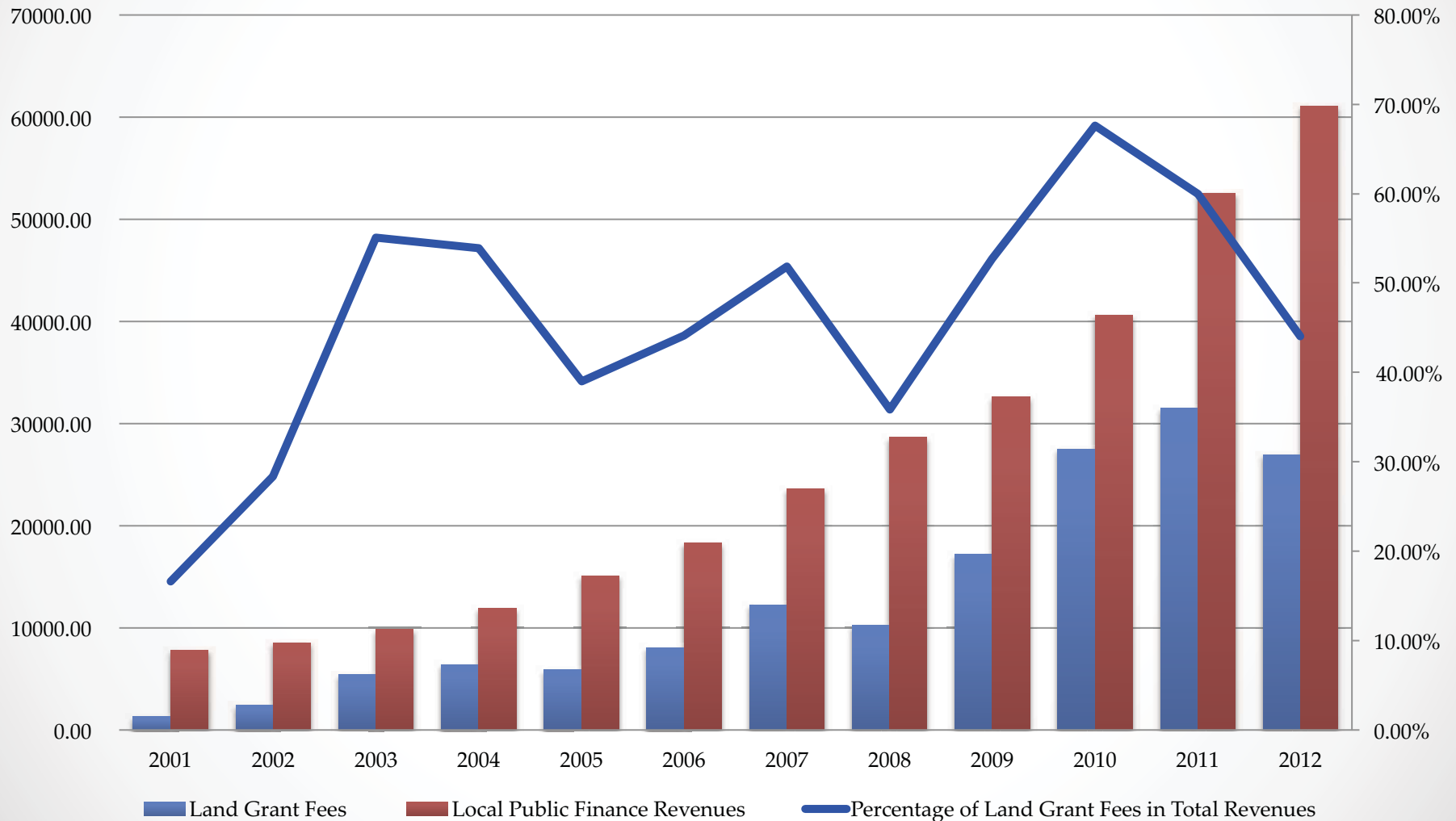
- |                  |  |
|------------------|--|
| From Local Gov't | <ul style="list-style-type: none"> <li>• Local gov't operating;</li> <li>• Compulsory Education;</li> <li>• City maintenance;</li> <li>• Militia;</li> </ul> |
|------------------|--|



# Financial Crisis of Local Governments

- Fiscal gap for local governments
  - Mismatch between revenues and expenditure obligations
- Absence of other financing vehicles
  - Local governments cannot raise taxes w/o the central government's permission
  - Until very recently, they cannot issue debts either
- => Financial Crisis
- Solution: extra-budgetary revenues <- land grant fees (long-term land development rights lease)

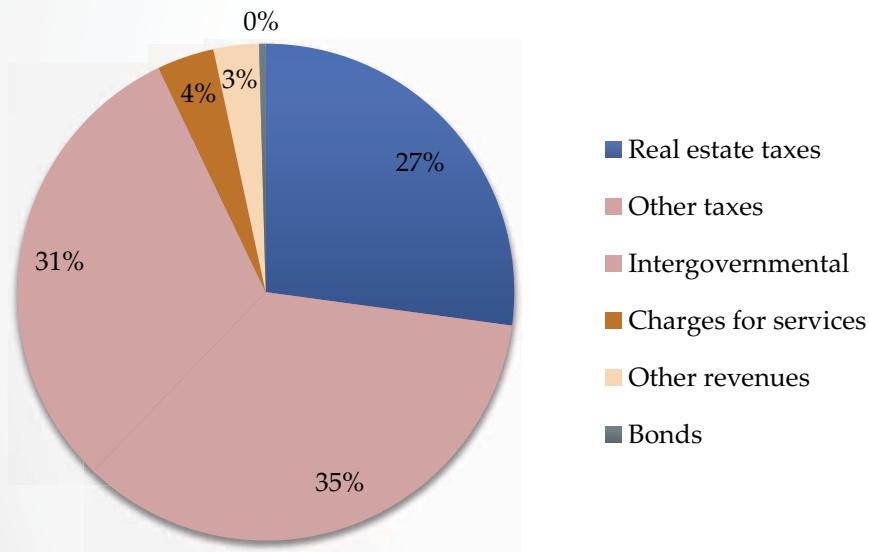
# “Municipal Land Finance” in China



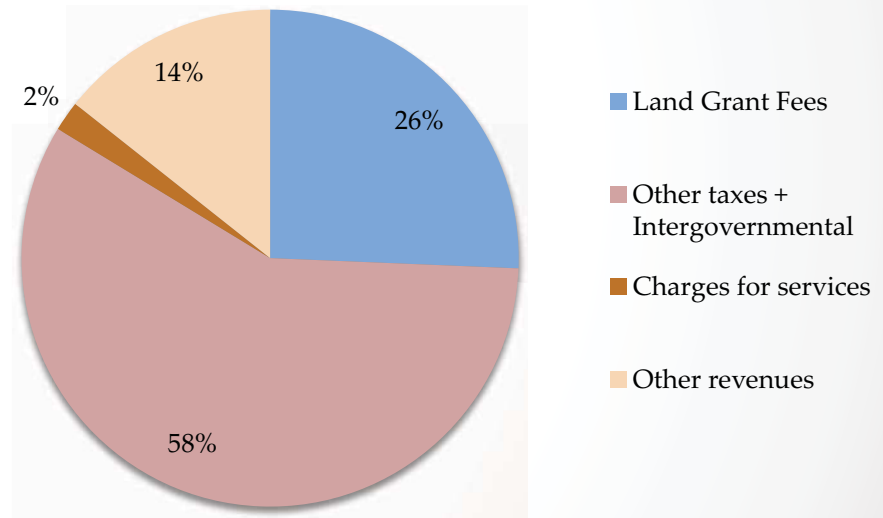
Source: *China Statistics Yearbook, 2012; China Land and Resources Statistics Yearbook, 2012*

# Municipal Budget: NYC vs. Beijing

## New York City Revenues 2011



## Beijing Revenues 2011



Source: New York City CAFY 2011; Beijing Budget Report 2012; Both figures only reflect the operating budget.

# Difference?

- Property tax: land rent for that year;
- Land grant fees: land rent for 70 years!

# Origin of Land Finance

- A conversation between a communist prime minister (left) and a capitalist developer (right) in 1981
  - Prime Minister Zhao Ziyang (赵紫阳): “we lack capital for city developments.”
  - Dr. Huo Yingdong (Henry Fok, 霍英东) the capitalist in Hong Kong: “how come you lack capital if you have land?”
  - Prime Minister Zhao Ziyang: “We can’t charge people for using land. That’s capitalism.”
  - Dr. Huo Yingdong: “Well, even capitalism has got some merits.”

# A Compromise Solution: The Land Transfer System

- 1988 - Amendment to the *Constitution*
  - Reiterating the state's absolute ownership of all city land, the amendment made the use rights of land transferable;
- 1988 (later) – Revision to the *Law of Land Administration*
- 1990 - *Interim Regulations of the People's Republic of China Concerning the Assignment and Transfer of the Right to the Use of the State-owned Land in the Urban Areas*

# Urban/Rural Dichotomy of Land Property Rights

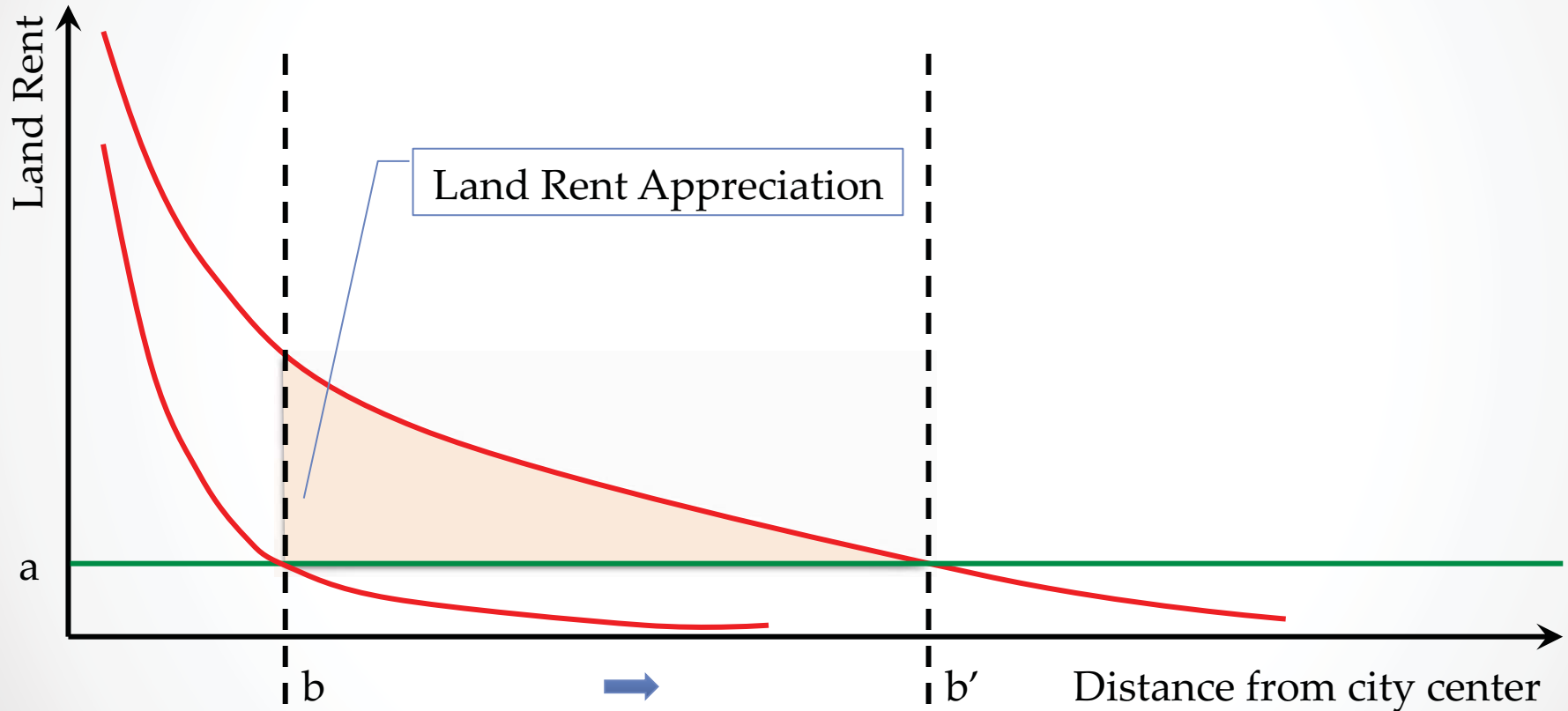
	Rural Land	Urban Land
Ownership	Rural collectives	The State
Use Rights	Households with rural Hukou	Anyone <ul style="list-style-type: none"> <li>• Individuals (city residents, villagers, migrant workers, foreigners, etc.)</li> <li>• Firms</li> </ul>
Use Rights Transferability	Transferable for agricultural use ONLY	Transferable (usage subject to zoning regulations)
Developability	User cannot develop on the land, unless <ul style="list-style-type: none"> <li>• For own household use (need approval by the villager's committee);</li> <li>OR,</li> <li>• It's transferred as urban land (via local governments)</li> </ul>	User can develop on the land

# Differential Financial Obligations

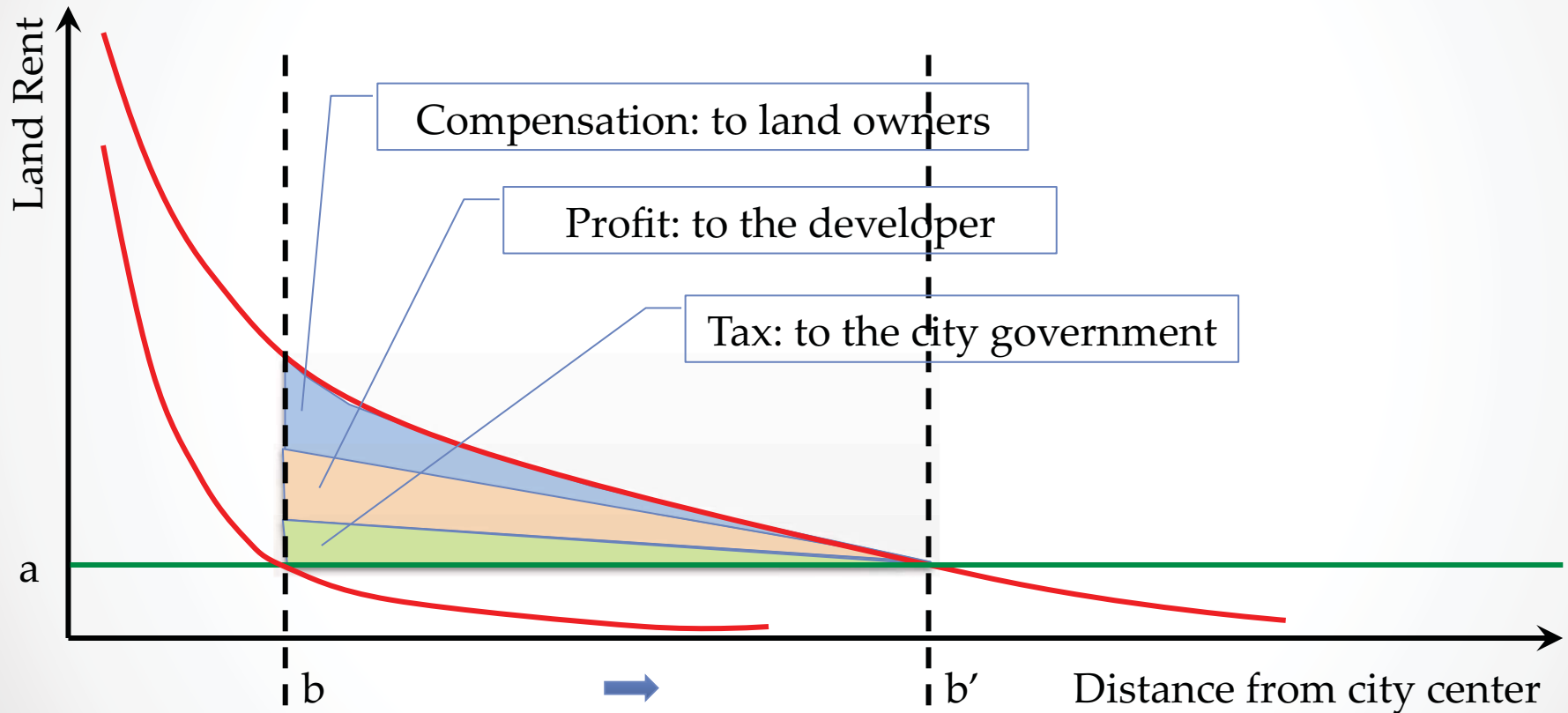
	Rural land	Existing urban developments	New urban developments/ urban redevelopments
Property tax	No	No	No  (except for commercial developments, which are subject to an one-time tax; and for a few recent experiments in Shanghai and Chongqing)
Land transfer fee	No	No	Yes  (except for some State-run developments)



# How is Land Finance Possible?

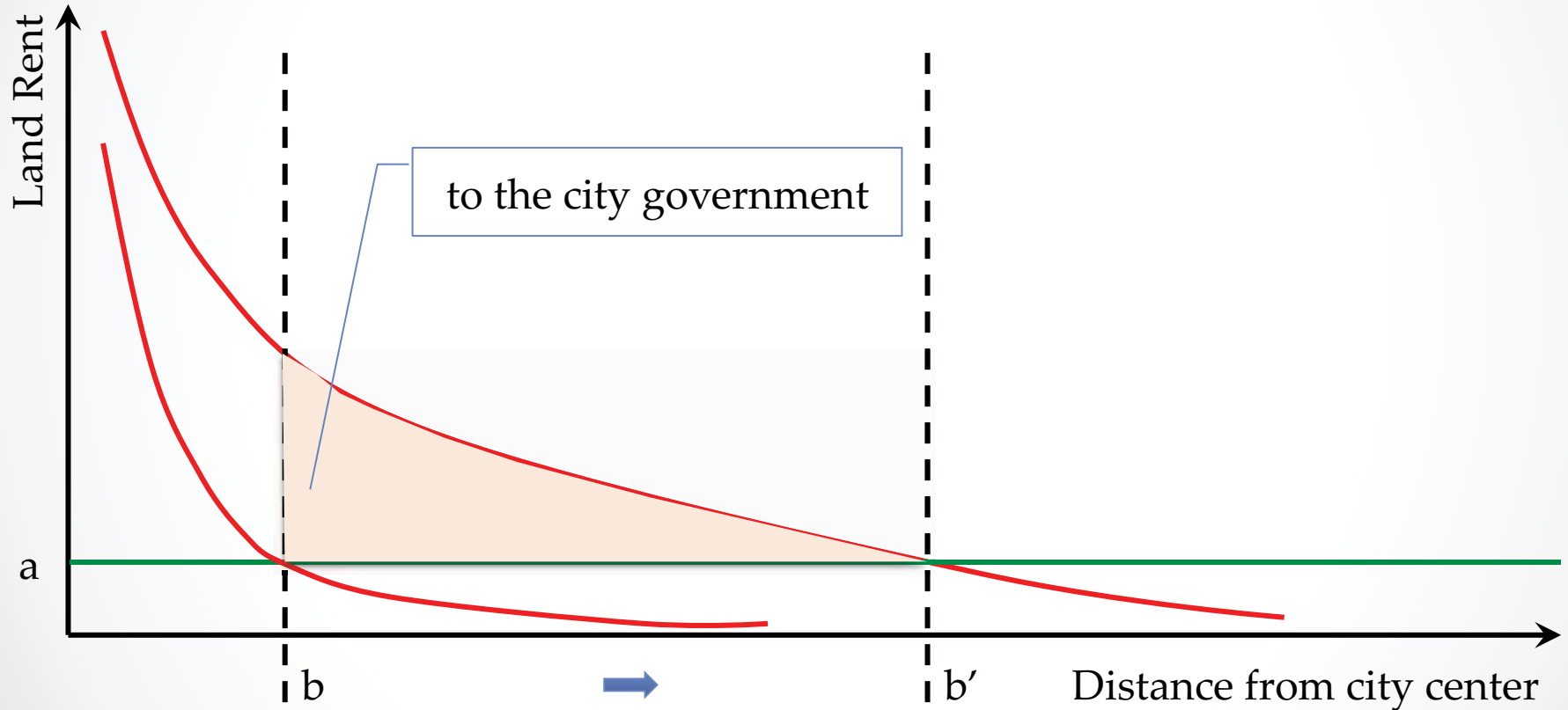


# Splitting the Cake: Free Market with Government



# Splitting the Cake: City Government's Ideal Scenario

- City government's ideal: take it all



# City's Government's Strategy

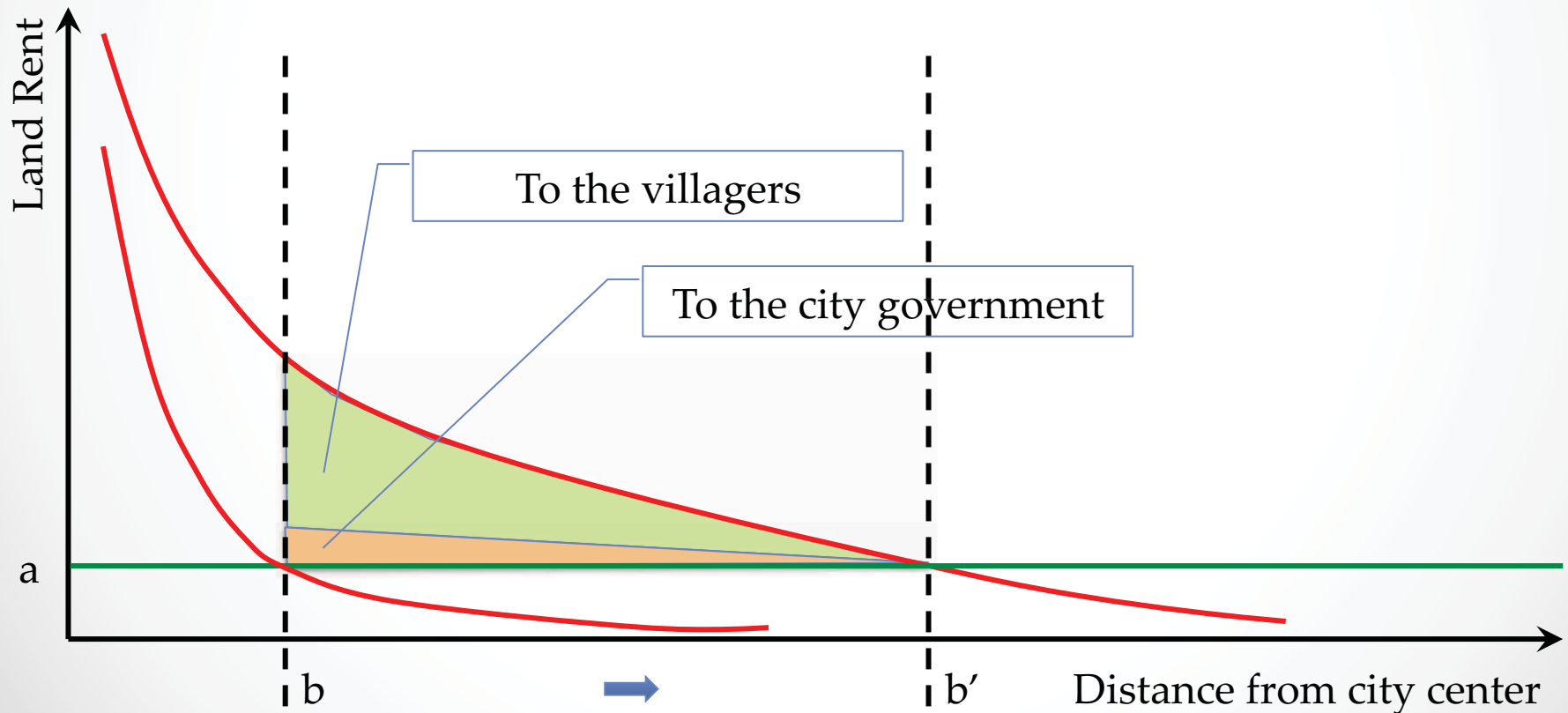
- The golden rule: buy low sell high
- The procedure
  - Buy land from villages; compensate them at the agriculture rent level
  - Build infrastructures
  - Sell the ready-to-develop land to real estate developers

Done! Enjoy!

- Not really selling – 70/50/40 year-leases

# Splitting the Cake: the Shenzhen Variation

- Reality: other stakeholders; need negotiation
- The Shenzhen context: strong village collectives vs. weak government

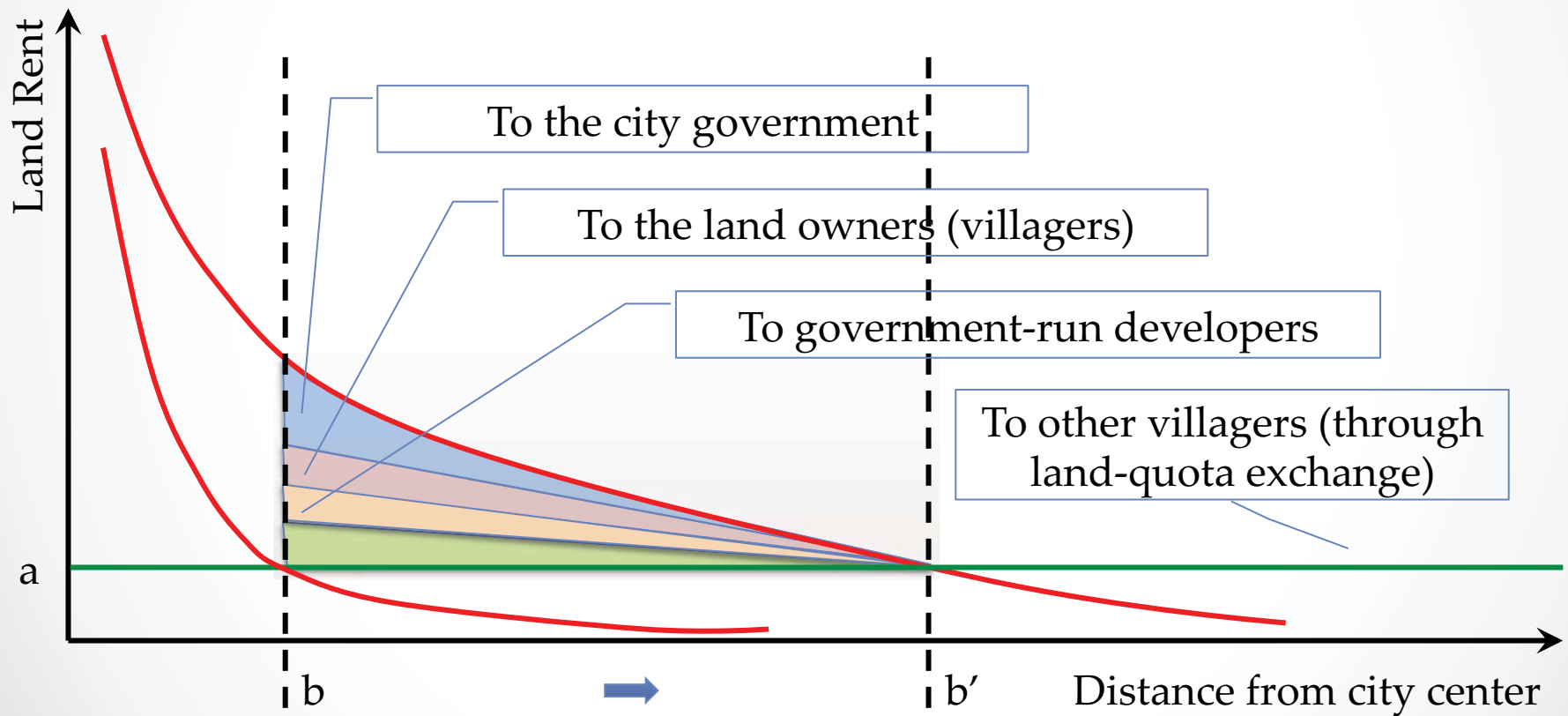


# The Shenzhen Variation

- Urban villages as bulk of housing supply
  - Laissez-fair. Landlords (villagers) get all.
  - Village Collectives as infrastructure investment companies

# Splitting the Cake: the Chongqing Variation

- Institutional Innovation: Land-quota exchange



# The Chongqing Experiment

- Measures
  - Urban Construction Land Quota Exchange
  - Share of appreciation value between the government, the land owners, and other farmers living in remote areas
  - Land as assets of government-run infrastructure investment companies
- Assumptions
  - Enough government land reserve (~30 years)
  - Sustainable land appreciation
  - Efficient government; no corruption



# Summary

- Situations vary across cities; actual distribution of rent depends on the relative power of the players.
- However, in most cases, the local governments get the largest part, thus the land finance is possible.

# Dialogue

- Agenda
  - Role playing game
  - Debates on the land finance system

# Role Playing

- Stakeholders
  - Suburban farmers (*de facto* original land owners)
  - Village collectives (via the villager's committee; *de jury* original land owners)
  - City residents
  - Migrant workers
  - Other farmers (living in remote, “real” rural areas)
  - City government
  - Real estate developers
  - Central government

# Debate

- The land finance system: merits and disadvantages
  - The moral dimension
  - The practical dimension
- Overarching issues
  - Government-lead vs. market oriented
  - Efficiency vs. equity
  - Short run vs. long run

# Concluding Remarks

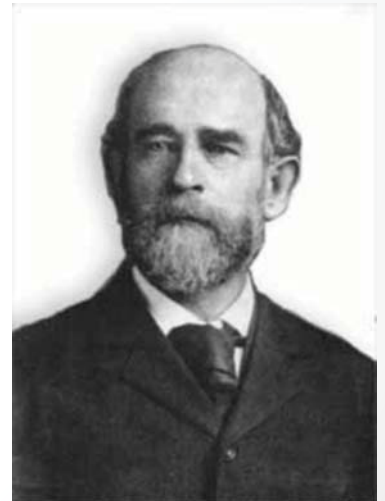
# Debates – the moral dimension

- Georgism

- People own what they create, but that things found in nature, most importantly land, belong equally to all.
- Single tax on land

- Supporters and critics

- Pro: Joe Stiglitz; Winston Churchill; Martin Luther King, Jr.  
Frank Lloyd Wright, Leo Tolstoy; Sun Yat-sen
- Con: Karl Marx; most neoliberal economists

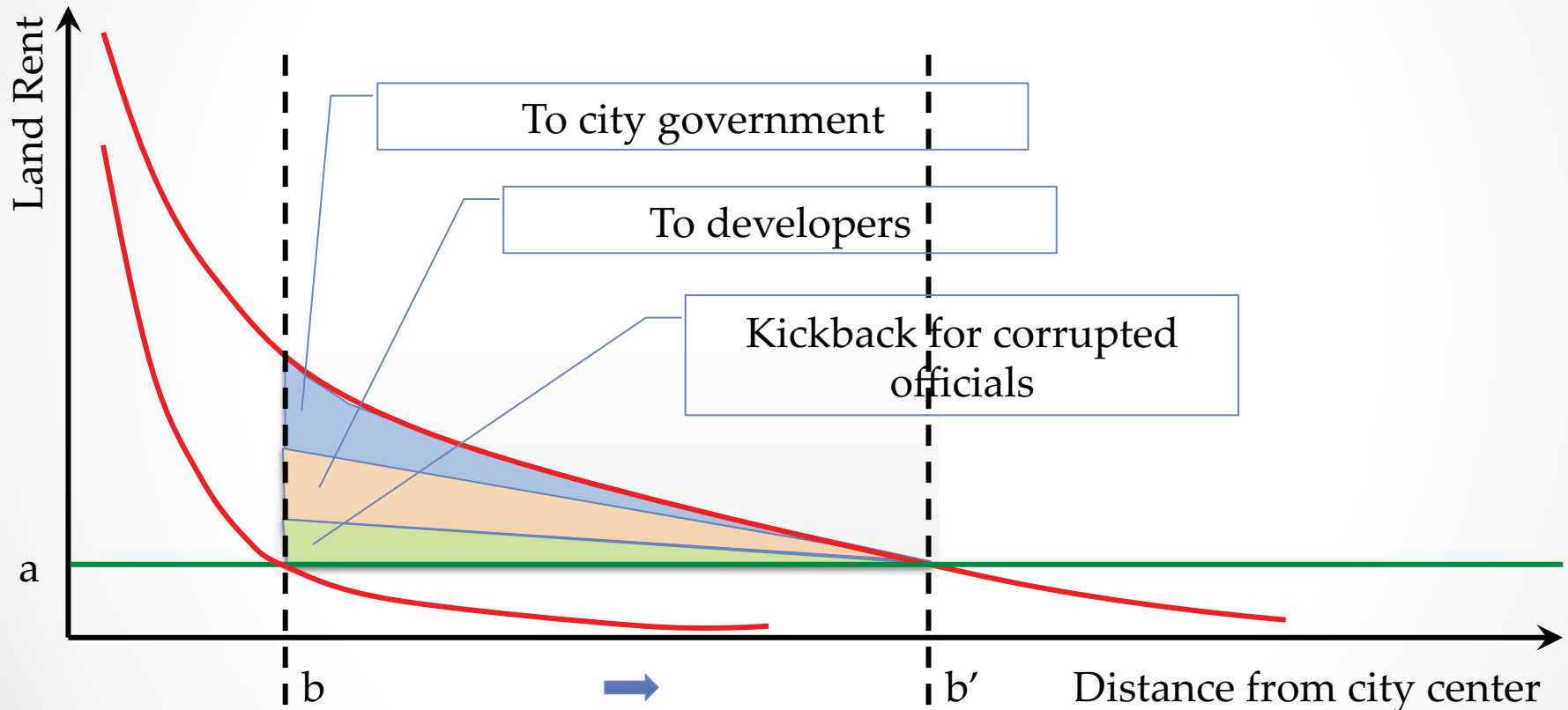


This image is in the public domain.

**Henry George**  
American Economist (1839-1897)

# Debates – the practical dimension

- Corruption: room for rent-search



# Example: the Wanliu Project

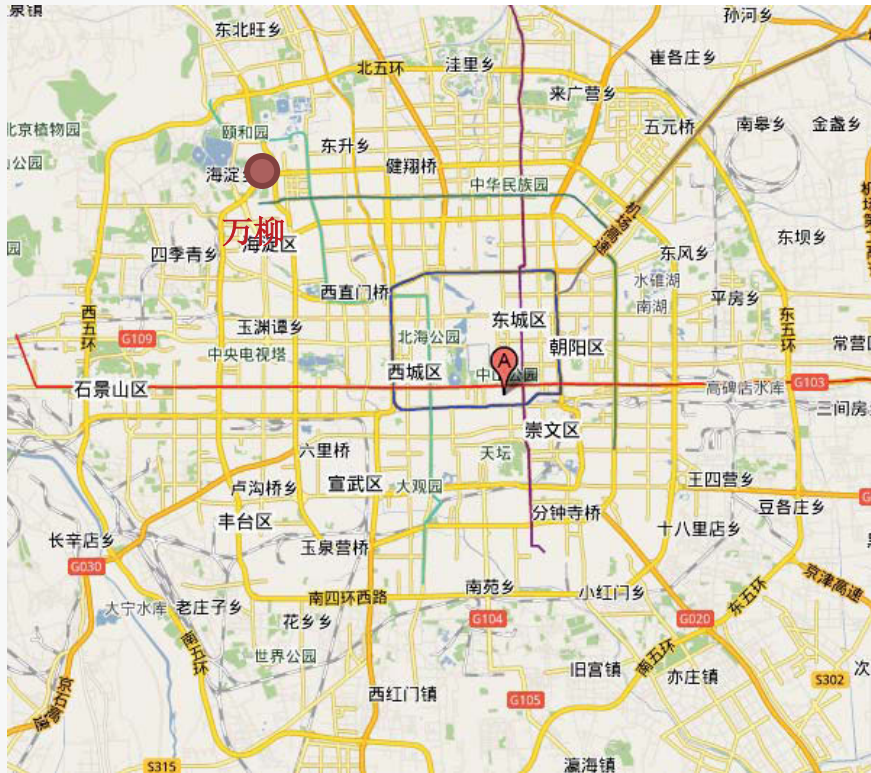


Image of the project site removed due to copyright restrictions.

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Satellite images of the Wanliu site in 2001, 2002, 2003, and 2005 removed due to copyright restrictions.

Zhou Liangluo, then-mayor, arrested for land-related corruption in the Wanliu Project in 2006.

# Debates – the practical dimension

- Sustainability through growing
  - Demands for construction land have been high
  - Land value appreciation appears forever
  - So far so good
- However, in the long term...
  - Cities cannot expand forever
  - Incremental land development will eventually diminish
  - What next?

# What Next?

- Ongoing experiments
  - Municipal debt
    - Ubiquitous
    - Financial risks
  - Property tax
    - Limited cities (Shanghai, Chongqing)
    - Political risks
- Other proposals?

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