

Regionally Decentralized Authoritarian Regulatory Regime of China

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FINDING THE RIGHT BALANCE OF REGULATION
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Regulation and Political System

- Regulation is a sub set of law enforcement
- Efficacy of law enforcement depends on the political system
 - Separation of powers
 - Judicial independence
 - The political system determines either a regulatory regime follows rule of law, or it rules by law, or it is a rule of person
- Cross country evidence: stable and effective regulation follows rule of law
 - Affects stability/sustainability of long run growth

The Chinese Political System

- I characterize the Chinese political system as regionally decentralized authoritarianism (RDA)
 - Highly centralized politics controls all top positions via the monopolistic ruling party
 - No separation of powers; no judicial independence
 - Unchallenged monopolistic ruling party
 - Highly decentralized administrative implementation and resource allocation
 - Different from other authoritarian regimes
- The party defines sub-national jurisdictions
- All subnational levels' legislatures/courts are controlled by the party at that level

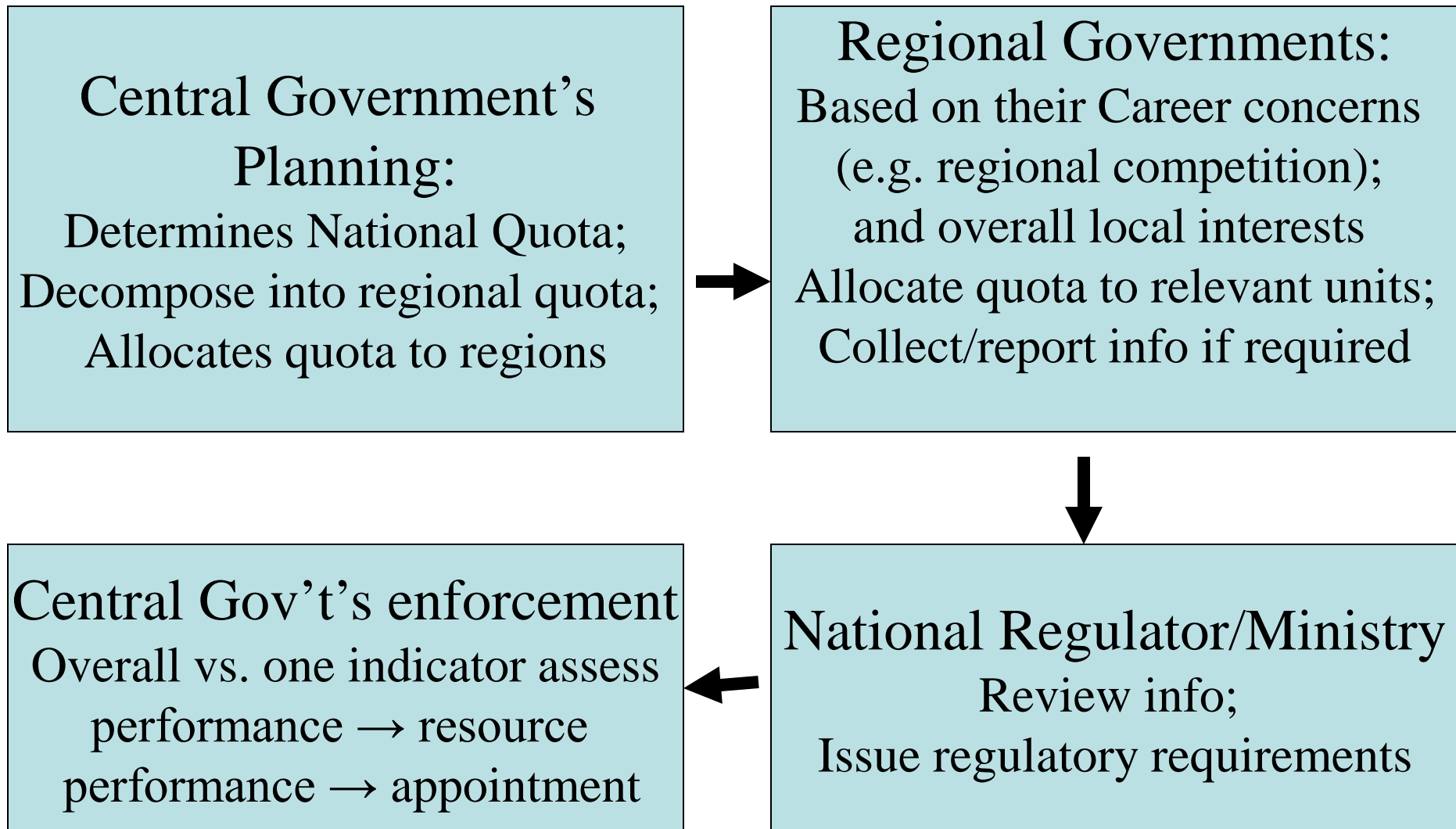
China's regionally decentralized regulatory regime

- Under the RDA regime every subnational party-government controls over all legal-economic matters within its jurisdiction
- Local courts are not independent from local governments
 - Judicial system malfunction because of this
- Thus, a law based regulatory regime would not operate
- Any thing can operate must be administrative
- The regulatory regime has to be based on subnational governments' admin capacity

Quota System in Decentralized regulatory regime

- The regulatory regime involves local government deeply
- Quota is a device between central and local governments
 - As a device for planning, assessment, and incentives
- Examples: quota based regulatory regime
 - Land conversion quota: regulate land use through regions
 - Credit quota: regulate money supply through regions
 - Quota of equity shares: regulate securities market through regional governments
 - Designed to control the size of financial markets and to keep balance among regions
 - Pollutant emission quota: regulate environmental pollution
 - Other examples:
 - Bankruptcy quota
 - Work place safety quota, e.g. how many is allowed to die
 - Import/export quota

Stylized operation of quota system



Quota system operates together with regional competition

- Under the RDA regime regional competition was the driving mechanism for reform/growth
 - Subnational governments compete for growth
 - Regional competition resolves incentive problems
 - Also determine the direction of regional experiments
- Quota system is part of the regional competition
 - Decentralized regulatory responsibility and information collection
- Promotion and resources needed for competition are linked to fulfillment of quota based regulation
- As a transitional regime the quota system never worked well
 - Although administratively it might implement a decree fast

Why this kind of admin based regulatory system may not always function

- Take Land quota, credit quota, pollutant emission quota and food-and-drug regulation as example
- Sub-national governments' interests are in conflict with the subjects of those to be regulated
 - Local governments care more about growth
 - For promotion; for fiscal revenue; for opportunities of rent-seeking and corruption
 - Local governments can easily manipulate the information
- The resources to be regulated are directly controlled by local governments
 - Other than promotion, the central government has no leverage in incentives

When regional competition fails to work

- When the economy is relatively developed, regional governments' competing for GDP becomes a problem
 - The transition from central planning to market is over
 - The transition from very poor to moderately poor is over
 - Regional competition/experiment do not work beyond these transitions
- But there is no way to design a comprehensive indicator for regional competition
 - The old problem faced by central planning
- No better solution for incentives than regional competition in the RDA regime
- Incentives of subnational governments are further distorted => regulatory failure becomes more severe

RDA regime is the source of problem

- Appointed bureaucrats are not responsible to the citizens
 - The local governments are only accountable to the bosses
 - There is no way to design an incentive scheme
- No checks and balances, no separation of powers
 - Unstoppable power abuse, rent seeking, corruption
- Regulation becomes tools of keeping monopoly, rent-seeking
- Corrupted regulatory regime destabilizes the socio-economy
 - Chinese government's huge/growing expenditure on “maintaining social stability(维稳)” indicates the seriousness of the problems
 - 2011 social stability budget 624 billion RMB (95 billion USD) vs. defense budget 600 billion RMB
 - 2012 social stability budget doubles that of the defense budget

Conclusion

- The Chinese regionally decentralized regulatory regime was a transitional solution when the legal institution is very weak
- It is admin based and its function was associated with regional competition
- When regional competition fails to work and the judicial independence is absent this admin based regulatory regime further degenerates
 - Due to seriously distorted incentives of regulators
- There is no alternative than building a law-based regulatory system
- Requires judicial independence

Thank you!