

## Government-enterprise integration and centralization in the third areas

CHEN Guoquan, MAO Yimin

*School of Public Administration, Zhejiang University, Hangzhou 310058, China*

**Abstract** Different from the administration of urban and rural areas, administration of development zones, new cities, new districts and functional zones forms a unique administrative mode of third areas. The key feature of such administration is government recentralization in the form of government-enterprise integration. Such institutional arrangement has not only gone beyond the bound of laws and policies, but also contradicted reform proposal of political decentralization and separation of government and business functions established at the beginning of China's reform and opening-up. Development and construction of third areas is a collective action of large-scale public goods production, and its attribute as a task determines institutional evolvement logic of government centralization. Centralization is conducive to optimizing policy-making and coordination, ensuring constant injection of development funds and overcoming collective action problem so as to maximize production efficiency. Such administrative mode has largely expanded governments' capabilities of capital, organization and human resources management; however, it has demonstrated obvious relativity in the administrative outcome, reflected in three aspects including regional economic development, government institutional reform and social order maintenance. In a word, rationality of local government recentralization and government-enterprise integration is constrained by development phase of regions and areas of public administration, and its evolvement direction depends on change of national governance system.

**Keywords** recentralization, government-enterprise integration, the third areas, public goods

---

Translated by LIU Yingyi and edited by LI Xing.

Supported by: National Social Science Foundation of China (14ZDA016).

The third areas refer to administrative areas including development zones, new cities, new districts and functional zones, where special administrative modes are adopted. In terms of administrative environment, most of the third areas administration started from suburban or rural areas with insufficient infrastructure. Its main administrative objectives are to develop land and other resources, to attract foreign and domestic investments and to promote local industries and economy. In terms of administrative mode, administrative committees are established as government agencies for overall administration of the areas, with development and investment companies as assistance. As a result, rapid transformation from a rural society to an urban one has been achieved and new urban space has been created for local economic and social development. Therefore these areas are categorized as the third areas given the remarkable difference in governance pattern compared to that of traditional urban or rural areas.

As pioneers of China's reform, the third areas have provided favorable industry environment through connecting domestic market and overseas market. It has also attracted investment and technology, and become the main engine driving China's economic development and urbanization with remarkable economic achievements. Meanwhile, administration of these areas is centralized. The Party working committees and administration committees, as agencies sent respectively by the higher Party committees and the higher governments, generally work in joint offices, forming an administration committee that integrates the Party and government. Development and investment companies are also combined into the system. They together are usually referred to as "the same team with two or multiple entities." Such practice centralizes power to the leading body at the higher level, and centralizes power such as enterprise management right to the top leaders in the Party and government.

Such institutional arrangement has undoubtedly contradicted reform proposal of political decentralization and separation of government and business functions established at the beginning of China's reform and opening-up. The report *On the Reform of the System of Party and State Leadership* submitted by Deng Xiaoping in 1980 is the guiding document for China's political system reform. The report emphasized

decentralization to avoid patriarchal problems as one of the focus in the reform of the system of Party and state leadership. In addition, the central government has issued a number of statements stressing separation of government functions from those of enterprises so as to forbid government officials holding positions in enterprises and to restrain governmental interference in the market. However, in the practice of local governments, such centralized mode remains to be the top administrative option for the third areas like new development zones, new cities, new districts and functional zones, even with deepening market-oriented reform today. It has become the practice for local governments to send administrative committees and to register investment companies.

In this study, we will conceptualize the administration mode of administrative committees<sup>①</sup> and investment companies as government-enterprise integration (or integration), which is, in essence, a government organization that combines enterprise management and operation. How to view the logic behind recentralization in the third areas development? And why such integration favored by local governments?

## 1 The third areas: carrier for rapid capital accumulation

Since the opening-up and reform, local governments have played a vital role in China's economic and social development. Large amount of researches and analyses, such as integration of central and local governments, local governments being manufacturers, and village and town governments being companies, have underlined local governments' ability to manage local enterprises.<sup>②</sup> In recent years, with deepening of market reform, there has been a shift in local government's strategy from enterprise operation to area management.<sup>③</sup>

The key in area management is to set up all types of the third areas,

---

<sup>①</sup> Party committees of higher level send Party working committees, and governments of higher level send administrative committees to the third areas, with the two working in joint offices. For the purpose of this essay, the two are combined and addressed as administrative committee.

<sup>②</sup> Qiu, H. & Xu, J. *Sociological Studies* (社会学研究), (4) (2004).

<sup>③</sup> Cao, Z. & Shi, J. *Sociological Studies* (社会学研究), (4) (2009). Zhou, L. *Local Governments in Transition: Official Incentive and Administration* (转型中的地方政府: 官员激励与治理). Gezhi Press, (2008).

such as development zones, new cities, new districts and functional zones. The objective is to improve physical infrastructures and institutional conditions in a short time and build a capital investment and industry development environment that meets modern market economy requirements through space concentration of government power and administrative resources. It will consequently attract domestic and overseas investment and promote local economy. To be specific, this is achieved through three channels. (1) Attracting and fixing global capital flow to propel local industry concentration and achieve rapid capital accumulation. (2) Raising land leasing prices. Land value depends on multiple factors including functional positioning of its location, infrastructure environment, supporting municipal facilities and the degree of industry development. Concentrated development and construction of the third areas could boost land value by several or even dozens of times. (3) Large-scale government investment on the third areas, which is a process of capital accumulation itself. The above capital accumulation will eventually be converted into components of local economic development, and in turn, competitive edge for local government officials in their promotion competition.

Therefore the third areas are essentially carriers for local governments to realize rapid local capital accumulation. Relying upon their monopoly on regional production factors and using the third areas as carriers, local governments control and manage regional economy as a whole, forming a unique “double-level management structure.”

Two types of administrative bodies exist within China’s economy on two corresponding levels. One is the management level where the local governments act as the main administrative body. At this level, the local governments plan, develop and manage the areas as a whole to enhance local economy growth rate and fiscal revenue as much as possible. The other is private (including foreign) enterprises act as main administrative bodies, conducting businesses utilizing the land, infrastructure, investment environment provided by local governments, and pay land rent

and taxes to the latter.<sup>①</sup>

As carriers for capital accumulation, the third areas are featured by the following three aspects. (1) Space selection. Space allocation for institutions and policies by local governments within their administrative areas is imbalanced, which reflects their efforts to create local competitiveness by concentrating constrained resources and capabilities. Such efforts are illustrated not only by all types of preferential policies, subsidies and high configuration of administrative levels towards the third areas, but also by forcing monopoly on the third areas space construction and development. For example, when the economic development zone was set up in SX County in Zhejiang Province, the following regulation was imposed: “from now on, any construction projects (collective or individual) that conflict with major infrastructure or key engineering projects within the planned zone must be called off, regardless of whether application has been made and approved. Individual construction approval is suspended to explore new ways of individual construction within the area, except consented by Household Demolition and Placement Management Office. Those already approved should stop implementation.”<sup>②</sup> (2) Oriented tasks. The construction of third areas has clear development objectives, so all resources and work within the area should be aggregated based on the objective, while those conflicting objectives should be ignored or separated. Both development zones and new cities have specific development and construction and investment attraction aims set by local governments every year as their performance indicators. Meanwhile, in order to fulfill the tasks, local governments even deliver all social comprehensive affairs of the third areas to the original governing authorities so as to maintain efficiency and specialization. For example, when promoting the development and construction of Qianjiang New City, Hangzhou Municipal Government made the following regulation: “in line with the development and construction of Qianjiang

---

<sup>①</sup> Cao, Z. & Shi, J. *Sociological Studies* (社会学研究), (4) (2009).

<sup>②</sup> Data sourced from surveys on some urban and county development zones and new cities construction conducted by the authors.

New City, Jianggan District and Shangcheng District shall be responsible for land acquisition, household demolition and placement, and urban management within the development zone of Qianjiang New City Administrative Committee, with the expenses undertaken by the latter.”<sup>①</sup>

(3) Partial market. Building “local climate” that suits modern market requirements within local scope is in fact a kind of incremental reform by local governments when traditional planning system is yet to unravel completely. It is to establish market system on small scale in areas far away from city centers to connect such areas international markets. Within the third areas, microsystems of modern enterprises are introduced, and private (including foreign) enterprises become independent managing bodies of market economy. Meanwhile local governments endeavor to provide the most possibly efficient and complete administrative services such as make administrative approval processes simple, to improve production efficiency of resident enterprises.

In summary, with “double-level management structure” coming into existence, it has become a vital target of local governments to promote construction and development of the third areas in a more efficient way. To achieve such a target is no easy task for sure, and depends on local governments’ capability of human and financial resource management. Therefore it becomes necessary for them to seek a new strategy and organization to enhance their resource management ability.

## **2 Recentralization and development efficiency of the third areas**

With deepening market reform and growing civil society, overall control is disappearing in traditional urban and rural areas while decentralization, participation and coordination become mainstream as grassroots administration grows more diversified and technological.<sup>②</sup> The third areas

---

<sup>①</sup> Hangzhou Municipal Government. *Suggestions on Further Acceleration of Qianjiang New City Construction and Development by CPC Hangzhou Municipal Party Committee and Municipal Government* (中共杭州市委杭州市人民政府关于进一步加快钱江新城建设和发展的若干意见), (6) (2006).

<sup>②</sup> Qu, S., Zhou, F. & Ying, X. *Social Sciences in China* (中国社会科学), (6) (2009).

used to be parts of traditional urban or rural areas geographically, but the former differ entirely from the latter in terms of administrative mode: within the third areas, decision-making and resources are centralized upward towards higher local governments and their administrative committees, which contradicts decentralization reform of government administration.

This phenomenon is linked to the underlying logic behind the efficiency orientation of the third areas development and construction. Development and construction of the third areas is largely the process of building new urban space in suburban and rural areas by city governments in the form of massive land resources development, infrastructure planning and construction, and public services supply. Therefore it is essentially a large-scale collective action of public goods supply with three characteristics: production of public goods, scale of public goods production, and collective action of large-scale public goods production. These characteristics, together with attributes of the third areas development and construction, have led to centralization in the third areas.

Firstly, recentralization of local governments contributes to improvement in decision making and coordination efficiency in the third areas development and construction, which is a process of public goods production. Chen Guoquan and Yu Yang divide public goods supply into production and distribution, and further point out different administrative logics behind them.<sup>①</sup> According to Chen and Yu, efficiency is the key to public goods production, and input and output are the basic examination variants. As scientific administration, scientific decision-making of governments is essential for high efficiency in public goods production, consequently, decision-making power tends to be centralized towards the few top management elites. The key to public goods distribution is fairness and equity, and the democratization of power operation is the examination variable. Fair and equal goods distribution is achieved through thorough

---

<sup>①</sup> Chen, G. & Yu, Y. *Journal of Zhejiang University (Humanities and Social Sciences)* (浙江大学学报(人文社会科学版)), (4) (2014).

democratic decentralization and procedures to guarantee rights of the majority as much as possible. Based upon the above analysis, they further point out that business centralization of local governments could help improve their efficiency in decision-making and coordination in public goods production and management, and then realize overall efficiency in public goods production. As efficiency is the fundamental objective pursued by the main bodies in the third areas development and construction, government centralization in the process of public goods production is strengthened.

Secondly, as the third areas development and construction is a large-scale investment process, recentralization of local governments helps to ensure constant injection of development fund. The third areas development and construction is special since it involves major projects such as land development and infrastructure construction. Miao Kai summarizes the features of such investment as follows: involvement of upstream production sectors in social production process; large and inseparable investment scale; comparatively long lasting production flow and the resultant low capital mobility; low capital productivity; and forward-facing construction requirements.<sup>①</sup> Those features determine that such large scale investment cannot maintain with government input only. Strong external problems and the risk of excessive political intervention make external investors reluctant to invest unless there is institutionalized interest guarantee. Recentralization of local governments is the strategic response to such dilemma. Through concentration of decision-making power over land resources, local governments strengthen their ability to utilize the resources. With government authority as credit and land as pledge, external investments are attracted to provide steady injection of funding for the development and construction of third areas.

Lastly, as the third areas development and construction is a collective action process, recentralization of local government could help to overcome the “collective action problem.” In actual operation of grassroots governments, authority fragmentation is increasing, reflected in

---

<sup>①</sup> Miu, K. doctoral thesis, Nanjing University, 2001.



disagreement or symbolic compliance with higher authorities in value, and, from the perspective of institution, selective execution of higher authority deployment based on individual needs among different sectors and levels of governments.<sup>①</sup> Collective actions are severely impeded by such haggling among governments, leading to efficiency loss. To complete collective actions in development and construction, effective organizational arrangements and incentive design are necessary. Mancur Lloyd Olson, Jr. proposes selective incentives, an important mechanism to overcome collective action problem. It is, however, worth noting that it could only be adopted by organizations that meet the following requirements: with the authority and capability of mandatory execution, or be able to provide positive incentives to potential individuals within the organization.<sup>②</sup> In other words, monopoly on authority or abundant incentive resources are the base on which an organization can conquer collective action problem. Centralization strategy of the third areas has to some degree responded Olson's statement by monopolizing authority and acquisition of sufficient incentive resources via market operation. This could make selective incentive possible and collective actions reachable.

As shown in the analysis above, recentralization of local governments is closely linked to development and construction objectives. The attributes of the third areas development and construction, as a process of collective and massive public goods production, determine the rationality of local governments' recentralization. It is conducive to improvement in efficiency and coordination, continuing funding injunction and conquering collective action problem, consequently, it will finally maximize the construction efficiency. Recentralization strategy of local governments must reply upon systematization in certain forms for sustainable administration of the third areas, with the government-enterprise integration being the core institutional design.

---

<sup>①</sup> Zhao, S. *China Development Observation* (中国发展观察), (11) (2006).

<sup>②</sup> Olson, M. *Logic of Collective Action*. Chen, Y. (trans) Gezhi Press & Shanghai People's Publishing House, (1995).

### 3 Government-enterprise integration and systematization of the third areas

In contemporary China, the increasingly refined and extended bureaucratic organization ability constitutes national governance foundation.<sup>①</sup> The systematization of third areas, namely government-enterprise integration, is based on reform and expansion of existing bureaucratic institutions. It has integrated government bureaucratic power and enterprise management mechanism to break free from constraints of current national judicial system. Consequently, it mobilizes multiple resources and enhances government administration ability.

As an institutional arrangement, government-enterprise integration of the two functions is essentially a government organization with management and operation mechanism of an enterprise. In practice, such integration often appears in the form of “administrative committee plus investment company,” under which major leaders and staff have overlapping positions, and is usually referred to as “the same team with two (multiple) entities.” Administrative committees, as agencies sent by local governments,<sup>②</sup> exercise authority on behalf of the latter and act as authority bodies within the development areas. As a type of matrix organization operating under traditional bureaucratic systems, they result from vertical delegation across different levels and horizontal integration across different sectors. With flexible institution structuring and strict performance management, administrative committees have become important carriers of local governments’ will. Investment companies are state-owned enterprises set up and owned wholly or partially by local governments and report directly to administrative committees. They could be substantive entities or nominal ones, and could contain single or

---

<sup>①</sup> Zhou X. & Lian H. *Social Sciences in China* (中国社会科学), (5) (2011).

<sup>②</sup> According to Organization Law of Local People’s Congress and Local People’s Governments at Various Levels, development zone administrative committees are not included in administrative organization sequences. They are neither first-level governments, nor agencies sent by local people’s governments or agencies of government functional departments. Although called by local governments as “agencies sent by governments,” their legal status has always been disputable among academia.

multiple entities. As enterprises, investment companies enjoy all power granted by the state and hence broaden behavioral areas government organizations could reach. In official discourse, government-enterprise integration is worded as “government-guided, enterprises as main bodies, and market operation.” Based on market operation, administrative committees and investment companies support and complement each other, generating huge governance capacity. As an administrative organization for new urban spaces, the integration creates stronger construction and development capacity for urban spaces compared to traditional bureaucratic government bodies.

Firstly, through integration, constraints on government financing from legal and policy systems are bypassed and channels of large-scale financing are provided for local governments, which significantly enhance their capital management abilities. With the large power imbalance between authority and finance and under the immense pressure of local competition and GDP assessment, land development inevitably becomes a rational option for local governments. However, according to Article 28 of China’s Budget Law (1994), “The local budgets at various levels shall be compiled according to the principles of keeping expenditures within the limits of revenues and maintaining a balance between revenues and expenditures, and shall not contain deficit. The local governments may not issue local government bonds, except as otherwise prescribed by laws or the State Council.” Article 8 of Guaranty Law of the People’s Republic of China further stresses that state organs should not act as sureties. Therefore, legally, local governments themselves could not operate on debts. Through setting up urban investment companies and borrowing on behalf of them, these two rules are bypassed and local governments could run with debts.<sup>①</sup> Statistics show that by the end of 2010, there were over

---

<sup>①</sup> In fact, the establishment of urban investment companies would have been impossible without permission and drive by the central government. As early as 1998, the central government delegated National Development Bank for a pioneer project at Wuhu, Anhui Province, to combine utility and infrastructure as “package loans” through investment companies. In 2004, the State Council issued Decision on Investment Institution Reform to promote local investment and financing companies to a larger scale. In 2006, the central government banned them out of concerns that large amount of loans would turn into banks’ bad debts, but started further promotion of these companies in 2008.

10,000 local government financing platforms nationwide, among which 70% were on county level.<sup>①</sup> When financing with banks, urban investment companies are guaranteed by public rights and credit of local governments. Despite no formal legal contracts were formed, a kind of relational contracts serve as stabilizing bonds among governments, companies and banks.<sup>②</sup> More often than not, the companies enjoy high credit rating and easy access to bank finance, as their borrowings are pledged by local finance and land, with major projects guaranteed by political commitment from the Local People's Congresses.<sup>③</sup> Funds raised through investment companies are managed outside budget and regulated less tightly, thus the local governments have greater flexibility in the operation.

Secondly, consolidation of enterprise management method and principle into traditional bureaucratic institutions brought by integration not only lifts the restriction of staffing, but also reshapes staff incentive mechanism and strength, offering support to the "small and concise" administrative committees from "big and strong" companies. Administrative committees allow limited headcount as agencies and faced with "small team with big tasks" dilemma under the continuing expansion of the third areas, while the integration helps raise staffing level significantly. Under government-enterprise integration, staff could be categorized into four types in terms of their status: administrative, governmental, enterprise and contractors; but only three in terms of labor division: administrative, enterprise and mixed. The mixed type refers to administrative committee leaders who are also top management members of one or more investment companies. Due to the combination of political authority and enterprise resources on these leaders, internal operation of investment companies is indeed extension of government administration; staff status and labor division, nonetheless, are not related by absolute terms but rather adjusted flexibly according to policy requirements. For

---

<sup>①</sup> People's Bank of China. 2010 China Regional Finance Report. 1 June 2011.

<sup>②</sup> Liu, S. *Sociological Studies* (社会学研究), (4) (1999); Zhou, X. *Sociological Studies* (社会学研究), (2) (2005).

<sup>③</sup> Zhe, X. *Social Sciences in China* (中国社会科学), (1) (2014).

example, with repeated requests on separate administration from management by the central government, staff assumes the roles of heads in investment company, only nominally, as the real decision-making power is still with administrative committee leaders. In other words, staff of various statuses could hold mixed positions and company employees are often dispatched to handle administrative affairs. Such overlapping staffing provides convenient human resource allocation and use for leaders. In regard to staff incentive, market-oriented payroll design is adopted to link payroll with regional economic growth performance, and assessment encouragement is used as strong incentive drive for employees in core departments. Through establishment of one or more companies, both organization and staff are remarkably expanded.

It is clear that government-enterprise integration is essentially organizational reflection of local governments' recentralization strategy under existing legal system. Integration of agencies and enterprises makes the two entities most efficient, while their limitations are eliminated through mutual support. By virtue of its unique organization form, it bypasses national legal system, promotes governments' control over capital, organization and human resources, and thus it is generally adopted by local governments to realize the third areas systematization.

#### **4 Relative performance of government-enterprise integration in the third areas**

As an organization mode under the third areas centralization, what are the outcomes of this integration? Surveys have revealed apparent relative performance, on which dialectical analysis could be performed from aspects of regional economic development, government institutional reform and social order maintenance. An understanding of relative performance of the integration is not only reflection upon history, but also outlook for future reform orientation.

##### **4.1 Efficiency of government-enterprise integration in the third areas**

First of all, under the government-enterprise integration, concentration of power and capital led by local governments has brought rapid economic

growth to the third areas, which becomes growth pole in China's economic development. The number of national economic and technological development zones rose from 54 in 2009 to 90 in 2010, 131 in 2011 and 171 in 2012. As a result, their share of GDP in the entire nation increased significantly from 5.29% in 2009 to 10.38% in 2012, while the growth of their share of GDP rose from 9% in 2009 to 19.4% in 2012.<sup>①</sup> In other words, almost 1/5 of total national GDP growth came from national economic and technological development zones. The above statistics applied only to national zones. In fact, a multitude of provincial economic and technological zones have been approved and set up. If they both were taken into account, the combined contribution would be even greater. For example, in 2012, 65 economic and technological zones (including national and provincial) in Zhejiang Province utilized foreign capital of USD 6.48 billion, accounting for 49.6% of that of the entire province; total volume of foreign trade was about USD 146.7 billion, accounting for 47% of the provincial level; total industrial output value of industries above a designated scale was CNY 2919.8 billion, accounting for 50% of the provincial value; fiscal revenue was CNY 181.88 billion, accounting for 28.4% of that of the entire province; and fixed investment was CNY 569.32 billion, accounting for 33.3% of that of the entire province.<sup>②</sup> It is evident that these economic and technological development zones are undoubtedly the driving engine behind economic development of Zhejiang Province in terms of these major economic indicators.

Secondly, under the integration, administrative committees, with entrepreneurship, have resolved to some degree institutional conflicts caused by isomorphic responsibility via consolidating resources of different levels and sectors. Isomorphic responsibility refers to "high unity and similarity of governmental functions, responsibilities, and set-ups at different levels of government in China."<sup>③</sup> Under isomorphic

---

<sup>①</sup> Based on calculation on historical issues of China Business Yearbook by the authors.

<sup>②</sup> Data sourced from 2012 Economic Development Report on Development Zones in Zhejiang Province.

<sup>③</sup> Zhu, G. & Zhang Z. *Journal of Peking University (Philosophy and Social Sciences)* (北京大学学报 (哲学社会科学版)), (1) (2005).

responsibility, government functions could not be transformed while contradictory structures continue to exist. This issue is, to a great extent, responded by the integration. With such integration, entrepreneurship is introduced into government administration, and performance-oriented reforms, such as super-ministry reform and one-stop service, are practiced well in the third areas. The objective of the integration in the third areas is to achieve “small government, big society,” structured with super-ministry system for coordination among departments, and operated with one-stop service for efficiency. In addition, under the integration, various administrative tasks are packaged into public projects such as comprehensive treatment projects. From the perspective of histology, projects are essentially a temporary cross-organization configuration. They are lasting and temporary, controlled and innovative. They could coordinate relationship among bodies with diversified interests more effectively and promote local governments’ abilities in dealing with unique tasks.<sup>①</sup>

And last, under the integration, labor division and cooperation between administrative committees and their investment companies, and grassroots governments at village, town and sub-district levels, are conducive to the balance between development and stability of the third areas. While the administrative committees take charge of planning, construction and management, the latter are responsible for comprehensive social governance such as specific work of land acquisition and household demolition. Scaled construction of the third areas is not only space development but also social reconfiguration. As land acquisition and household demolition has become the focus of current social conflicts in China,<sup>②</sup> maintenance of social order is a necessity in the third areas administration. Members of administrative committees, mostly from functional government sectors of higher or same levels, have expertise in regional planning, construction and management, while

---

<sup>①</sup> Winch, G.M. “Three Domains of Project Organizing,” *International Journal of Project Management*, (32): (5) (2014).

<sup>②</sup> Yu, J. *The World of Survey and Research* (调研世界), (3) (2005).

investment companies are composed of specialists in capital operation. However, both of them lack experience and authority on land acquisition; therefore, household demolition and order maintenance must rely upon governments at village, town and sub-district levels. Under the integration, administrative committees tend to entrust them with such work through administrative outsourcing, and set strong performance incentives as encouragement. Under such institutional arrangement, governments at village, town and sub-district levels serve as bridges and buffers between administrative committees and society, and facilitate smooth development and construction of the third areas.

#### **4.2 Limitation of the government-enterprise integration in the third areas**

Firstly, under the integration, chaotic debt financing and selective law enforcement by local governments have severely impacted market order and impeded sustainable development of local economy. Chaotic debt financing could lead to financial and fiscal risks. While the integration offers local government easy access to debt financing, it also increases debt risks. With current system of control over cadres and competition pressure, incumbent government officials' behaviors are short-term based, that is "borrowing without worrying about repaying" when it comes to debt financing. According to reports from National Audit Office of PRC, by the end of June 2013, local governments had CNY 10.88 trillion outstanding debts, CNY 2.66 trillion guaranteed debts, with another CNY 4.34 trillion bearing partial compensation obligation.<sup>①</sup> Such large amount of government debt may trigger financial and fiscal risks, and, when the two are combined, sustainable development of local economy would be ultimately effected.

Selective law enforcement is another inevitable result from the integration and could lead to non-institutionalized market competition and further to network spread of corruptive exchange. The integration enabled local governments to become super managers in the capital

---

<sup>①</sup> National Audit Office. Audit Results on National Government Debts (No. 32 Issuance of 2013)



market, and their investment companies a strong tool for local market manipulation. As Zhou Xueguang mentions, “Today government roles are no longer limited to planning, coordination and corporate organizations managing, or protecting and promoting local industrial and commercial activities. Rather they are independent economic bodies and direct competitors with other corporate organizations for resources and opportunities.”<sup>①</sup> Local governments select policies out of their own interest demand. Such action would inevitably undermined market order, resulting in upsurge of non-institutionalized competition and illegalized government-business relationships. Under the integration, corruptive exchange has become conspiracy strategy between governments and enterprises, and finally led to network spread of corruption.<sup>②</sup>

Secondly, under the integration, many conflicts arise between administrative committee system and traditional government system, and they gave restrict the administrative effect of such mode. The third areas are outcomes of selective development of space by local governments, and it sets up special administrative committees on the separated economic development and construction power of certain districts and breaks the traditional administrative district-based dependency system. Administrative committees’ power expansion resulted from concentrated administrative resource investment has led to resources aggression to neighboring villages and towns, and severely imbalanced space development.<sup>③</sup> Over recent years, trusteeship of neighboring towns and villages has become a common practice. However, the lack of administrative authority and motivation of administrative committees has resulted in severe gaps in public service in those villages and towns.<sup>④</sup>

Separations of the Party from government and government from businesses have always been basic objective of institutional reform; the three, however, are highly integrated in the third areas. The common

---

<sup>①</sup> Zhou, X. *Open Times* (开放时代), (3) (2013).

<sup>②</sup> Chen, G. & Mao, Y. *Journal of Zhejiang University (Humanities and Social Sciences)* (浙江大学学报), (2) (2013).

<sup>③</sup> Lin, T. & Liu, J. *Economic Geography* (经济地理), (2) (2002).

<sup>④</sup> Nan, Y., Li, F. & Bai, Z. *China Economic Weekly* (中国经济周刊), (44) (2012)

combination of secretary of the Party committee, director of administrative committee and president of the board in investment companies on one top leader has obviously deviated from the reform objective. Vertically, power concentrates towards superior leaders caused by administrative committees, and horizontally power concentrates towards top leaders caused by the integration. Therefore, administration follows rule of men rather than rule of laws. While the third areas are “special zones” in regional jurisdiction, government-enterprise integration has provided top leaders with privileges, creating grounds for corruption.

And lastly, under the integration, dual leadership upon governments at village, town and sub-district levels from administrative committees and traditional superior governments could give rise to severe logical and behavioral distortion, which increases with the rapid expansion of the third areas. Administrative committee system is not entire restructure of traditional government system, but rather partial transformation of it. The third areas are specialized operation of development and construction and the economic development which is separated from other government functions. In these areas, administrative committees rely on governments at village, town and sub-district levels for efficient completion of land acquisition and household demolition involved in space development; while traditional superior governments still expect them to handle large amount of comprehensive social affairs such as healthcare and education. With limited resources, effort allocation is vital for these governments and will have significant impacts on behaviors of government officials.<sup>①</sup> From the perspective of reality, tremendous pressure and strong incentive related to performance assessment from administrative committees, and fiscal benefits from land appreciation, have made land acquisition and household demolition the absolute focus of officials in these governments. Accordingly, other tasks are ignored or weakened, restraining overall development of the society at basic level. Rapid expansion of the third areas will create additional difficulty for land acquisition and household demolition to governments at village, town and sub-district levels, draw

---

<sup>①</sup> Zhou, X. & Zhao, W. *Sociological Studies* (社会学研究), (3) (2009).

even more attention from them, and lead to more distorted behaviors and increasing group conflicts in the process.

## **5 Conclusion and reflection**

Since the reform and opening-up, government administration theory and practice have been increasingly themed by marketization, democratization and decentralization. Meanwhile, highly centralized government-enterprise integration, however, is now generally adopted in the third areas, including development zones, new cities and new districts. Researches have shown that as far as the third areas development and construction is concerned, recentralization of local governments optimizes decision-making and coordination, guarantees sustained capital input and resolve collective action problem. As an organization design under centralization strategy, this integration has vigorously promoted urban development and economic construction under the circumstances of short public goods and insufficient local government funding. Nevertheless, subsequent problems, including debt risks, disordered market, power corruption, administration institutional conflicts, social instability and so forth, also significantly restrict sustainable development of the third areas. Rationality of recentralization strategy, constrained by development stage and administrative area, will gradually lose its ground for existence with completion of the third areas construction.

In practice, with gradual achievement in development and construction objectives, some development zones have started to transform towards traditional government system by ceasing administrative committee systems and establishing local governments. The more common practice, however, is that local governments continue to expand development spaces for government-enterprise integration. Development zone expansion in recent years demonstrates local governments' preference towards and dependence upon integration. Through development zone expansion and by means of entrusted management and delegated development, neighboring villages and towns are merged and more land resources are combined within development zone planning so as to ensure legal development rights of administrative committees. Since the second

half of 2008, 67 development zones (parks) in Zhejiang Province started integrating and upgrading work in three batches, consolidating various industry function zones nearby or far away. Those zones were authorized by local governments to expand their administration. As a result, average area of development zones promoted after integrating and upgrading reached 105.87 square kilometers, compared to the original average of 8.38 square kilometers approved by the state, and total areas which were facilitated by the integration reached 6,000 square kilometers, accounting for 30% of total land suitable for construction in Zhejiang Province.

Therefore, the reflection upon factors that influence existence and evolvement of the integration is necessary. Such reflection should go beyond the third areas themselves and be focus on institutional environment of the Chinese economic society changes during transformation. The following institutional factors offer key support for the integration.

First, the tension between central government jurisdiction and local government administration has provided institutional space for the formation and expansion of the government-enterprise integration. Central government jurisdiction focuses on power with resources concentrated upwards; and therefore weakens local governments' problem-solving abilities. While local government administration tends to act on their own, deviates from and threatens the core of the authority system. Tension and incompatibility between the two demonstrates conflicts between power system and effective administration. Three basic responding systems are formed to mitigate such conflicts, maintaining dynamic relationship between uniform decision-making and flexible implementation, formalization of political indoctrination and dynamic administration.<sup>①</sup> In addition, Cao Zhenghan holds that the vertical restraint system of "separated functions between superior and lower levels" has been developed within China's power system. Namely the central government is responsible for management of government officials, including selection, supervision, rewards and punishments; while

---

<sup>①</sup> Zhou, X. *Open Times* (开放时代), (3) (2013).

local governments enjoy flexibility in handling local affairs in line with fundamental principles of the central government.<sup>①</sup> Therefore institutional space is left between authority control and effective administration for reform and innovation by local governments. As the integration of the third areas is ambiguous to some degree and has varied forms, even though the central government attempted to regulate such integration, the local governments continue to adopt such integration by transforming it into other forms.

Secondly, public ownership of land transferred into the governments, which has provided material basis for formation and expansion of the integration. The public ownership of land in China has actually represents a public area with ambiguous ownership, where “power” replaces “rights” to become the main principle in effect.<sup>②</sup> Academics like Liu Shouying and Zhou Feizhou summarized the characteristics of China’s land ownership as: dual rights, government monopoly, non-market configuration and integration of management and operation. Dual rights refers to the following: rural lands are collective property of farmers, who own the rights to use and transfer land, and usufruct when the lands are used for agricultural purposes; when the lands are turned for non-agricultural purposes, farmers lose these rights after receiving compensation equaling multiple of benefits from their original use. Urban lands are owned by the state, while local governments have the rights of disposal, transfer and usufruct of construction land. Government monopoly refers to the following: local governments, acquiring lands from farmers and transferring construction lands under their names exclusively, become the sole legal channel for conversion from agricultural lands to construction lands. Non-market configuration refers to governments’ strong interference and control over transfer and pricing of profit-oriented land.

---

<sup>①</sup> Cao, Z. *Sociological Studies* (社会学研究), (1) (2011).

<sup>②</sup> For discussion on the ambiguity of China’s land ownership institution, please refer to: Ho, P. *Institutions in Transition: Land Ownership, Property Rights and Social Conflict in China*. Social Science Academic Press, (2008). For discussion on public areas in property rights analysis, please referred to: Barzel, Y. *Economic Analysis of Property Rights*. Fei, F. & Duan, Y. (trans) Shanghai People’s Publishing House, (1997).

Under the agricultural land use approval system and local governments' quota control on constructions lands, government assignment and agreement selling remain a significant part of total construction land transfer. Integration of management and operation refers to local governments being both managers and operators of land.<sup>①</sup> Analysis above demonstrates that local governments, being both actual owners and handlers, are the strong power in land ownership area, which provides material basis for the formation and expansion of the integration.

Lastly, dual pressure from local fiscal demand and inter-governmental competition offers constant drive for the formation and expansion of the integration. Subsequent to the reform of tax distribution system, imbalanced fiscal strengths and authority between the central and local governments have placed large amount of financial pressure upon local governments. Meanwhile increasing inter-governmental competition forces local governments to make the most effort for economic growth and gain competitive edges in government performance assessment. Despite growing calls for "de-GDP assessment," the core importance of GDP in government performance assessment has never been diminished substantively. Under the pressure of local competition and official promotion and to ensure local GDP growth, government investments, especially infrastructure investments, are the key leverage local governments could exert effective control over, which further aggravates local government fiscal stress. Under the integration, land resources are used not only to gain fiscal returns, but also as leverage of financial capital to accelerate development and construction of the third areas. With the trinity mode of "land-public finance-banking,"<sup>②</sup> the integration plays a vital role in guaranteeing capital flow. Therefore the dual pressure of fiscal demand and performance assessment competition has made the integration a rational option for local governments.

It could be concluded from the analysis above that centralization

---

<sup>①</sup> Liu, S., Zhou, F. & Shao, T. *Land Institution Reform and Transition of Development Ways* (土地制度改革与转变发展方式). China Development Press, (2012).

<sup>②</sup> Zhou, F. *Fiscal Relationship and Local Government Behavior* (以利为利——财政关系与地方政府行为). SDX Joint Publishing Company, (2012).

strategy and the integration of the third areas are historical results of China's governance system transformation. The improvement and replacement of such administration mode depends on the process of governance system transformation, including inter-governmental and central-local power system, land expropriation system, public finance system, and government performance assessment system. In the future, research and analyses shall be conducted on the evolvement of and interaction among these systems so as to deepen academic theoretical understanding of the third areas.