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Social Security under Decentralized Authoritarianism: Politics of The Public Pension Program in China

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ABSTRACT

Welfare provisions are commonly regarded as an intrinsic product of democracy. Why do authoritarian rulers provide welfare programs to the people? How do authoritarian rulers promote welfare development under decentralized authoritarianism? This dissertation investigates these theoretical puzzles through a detailed study of the urban pension program for enterprise employees in authoritarian China. The decentralized fiscal and administrative structure in China makes the operation of the pension program a particularly challenging one. What are the redistributive incentives of the Chinese rulers? How does the central government differ from local governments in their redistributive calculation? How do these two levels of governments interact to ensure implementation of an expensive pension program? These are the questions this dissertation is set to address. This dissertation argues that while the Chinese central government more resembles long-sighted rulers and emphasizes welfare development, subnational governments are more short-sighted, being more motivated to promote short-term economic growth. The conflict of interests between these two actors leads to the classic principal-agent problem. This dissertation argues that the center uses fiscal subsidies as a leash to lead and restrain subnational governments, particularly those from regions with strategic importance to the center, to ensure proper implementation of the desired pension program. As the center's fiscal subsidies reduce the costs of welfare programs, subnational governments with center fiscal support are more incentivized to promote welfare development. Therefore, the center's subsidy program creates an uneven base of redistributive incentives for its subnational rulers. In addition to the availability of center fiscal support, this dissertation contends that the level of economic openness in a locality also shapes subnational governments' redistributive incentives. Being

afraid of capital flight, subnational governments in localities with a higher level of economic openness oftentimes discount welfare responsibility for investors with mobile assets. In localities where state-owned investments account for a larger share of the economy, the governments can impose higher taxes for welfare development. By combining these two factors – the availability of center fiscal support, and the level of economic openness – this study proposes five types of fiscal structure of the pension program at the subnational level.

This dissertation's contribution is threefold. First, it promises to enrich the existing literature on comparative welfare states, by filling the void in the redistributive incentives of authoritarian rulers. Second, instead of treating authoritarian rulers as a unitary actor, this study highlights the role of subnational governments in welfare politics, and details the center-local interplays in redistribution under the Chinese decentralized political system. This dissertation finds that the center uses fiscal subsidy programs to regulate its subnational governments. In so doing, this study also sheds new light on center-local relations in Chinese politics. Third, instead of attributing the Chinese regime's authoritarian resilience to formal institutions, this dissertation contends that welfare programs, like the urban pension program, are employed by Chinese rulers to pre-empt and resolve public oppositions and thus to increase the regime's resilience.

Social Security under Decentralized Authoritarianism

Politics of The Public Pension Program in China

by

Jing Lin

B.A. Political Economy, Renmin University of China 2009

Dissertation Submitted in partial fulfillment of the requirements for degree of
Doctor of Philosophy in Political Science

Syracuse University

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Abbreviations

ACFTU: All-China Federation of Trade Union

CPI: Consumer Price Index

GDP: gross domestic product

FDI: foreign direct investment

LGDP: local gross domestic product

MOF: Ministry of Finance

MOL: Ministry of Labor

MLSS: Ministry of Labor and Social Security

MHRSS: Ministry of Human Resources and Social Security

NSSF: National Social Security Fund

PAYG: pay-as-you-go

SOE: state-owned enterprise

Chapter 1 Introduction

1.1 Introduction

China is aging. A more striking fact is that China grows old faster than it gets rich. In today's China, more than 15 percent of the population, namely over a quarter billion people, is aged sixty or above. Worldwide almost one in every four persons aged sixty years or above lived in China in 2015 (World Bank, 2015). China will be experiencing a substantial demographic shift in the next three decades – from a country benefiting from a large base of workforce to a country with an enormous aging population. Two major factors explaining this fast-changing aging trend: (1) China's baby boom generation begins to reach their 60s in the 2020s; and (2) the working-age population comes to consist of one person per family, thanks to the so-called “One Child Policy”, implemented for more than three decades in China. The demographic aging trend is certainly not unique in China; however, China is the oldest country in the developing world. As a country whose GDP per capita just stepped into the upper middle-income country category, China is pressed to address the population aging problem prematurely. Table 1-1 compares projected aging trends in economies at all income levels. It clearly demonstrates that by all measurements of population aging indicated in the table China's aging level will surpass those of all income groups, including high-income countries. An equally challenging job for the Chinese government in the years to come is to further propel economic development under this fast-paced population aging trend in order to be fiscally prepared to tackle the aging issue along with many high-income countries.

Table 1-1 Putting China's aging issue into perspective

	Percentage aged 60 or over		Median age (years)		Age dependency ratio, old (% of working-age population)		GDP per capita (current US\$)
	2030	2050	2030	2050	2030	2050	2015
China*	25.3	36.5	43.2	49.6	25.3	46.7	7,924.7
High-income countries	27.7	31.9	42.9	44.7	36.9	46.4	39,576.9
Middle-income countries	15.4	21.9	33.2	37.1	16.1	25.3	4,667.6
<i>Upper-middle-income countries</i>	21.2	30.5	39.7	44.1	22.1	37.6	7,737.4
<i>Lower-middle-income countries</i>	11.2	16.5	28.8	33.4	11.5	17.8	1,988.2
Low-income countries	5.8	8.3	18.5	20.7	6.4	8.6	615.6

*Data for China do not include Hong Kong, Macau or Taiwan.

Source: World Bank (2015), and World Bank online database.

Moreover, China has a relatively early retirement age: The mean retirement age for the urban working population in total was estimated to be only 53, and the life expectancy in China reached 73.8 years old in 2010 (Han & Guo, 2012). As a result, the payment burden of the Chinese pension program is particularly heavy, as in average the program provides 20-year post-retirement benefits to the participants. As the ratio of working-age population to retirees will be quickly shrinking in the next decades, who pays for this enormous amount of retirement benefits is an unthinkable yet realistic question.

Is China's old-age social security program ready to meet this grand challenge? In today's China, there are two major pension programs – one for urban employees, including public and private employees, and the other for rural residents. The pension program for enterprise employees was created in 1951, among the first welfare programs the government established, and underwent a series of reforms during the economic transition period. Public employees used to enjoy a more privileged pension program than enterprise employees with no individual contributions yet much higher retirement benefit payments. The Chinese government announced

in 2015 an end to this dual-track pension system (*shuang gui zhi*), and merger of public employees' pension program to the program for urban enterprise employees; however, this merger leaves the two programs operated independently with separate pension fund pools, which means that in practice they still represent two pension programs. The development of the pension program for rural residents is still at its early stage – only started very minimum benefit payments in 2009. This study focuses on the pension program for urban enterprise employees, as the program for enterprise employees (hereafter, the pension program) represents the Chinese government's most consistent and comprehensive old-age security policy attempt.

The public pension program for urban enterprise employees was transformed from a socialist-style state funded program into a social insurance program during the economic transition period. SOE (state-owned enterprise) reforms during the economic transition period led to significant growth in the numbers of early retirees (*nei tui*) and laid-off workers (*xia gang*). Reductions in pension amounts, delays in payments, and even outright non-payments of pensions began in the mid-1980s, leading to vocal protests which became widespread in the 1990s (West, 1999). In the face of mounting pressure arising from economic transitions and widespread social grievances regarding pension non-payments, in 1997 the State Council issued Circular No. 26 which (1) broadened the pension coverage to cover all urban enterprise employees; and (2) established a nationwide pension scheme for all participants. The 1997 pension reform plan laid the groundwork for the current pension model for employees in urban enterprises, which is said to be based on three pillars: (1) public pensions, contribution from employers at the rate of 20 percent of the company's wage bill; (2) compulsory individual accounts, contribution from employees at the rate of 8 percent of payrolls; and (3) voluntary supplementary annuities. The Chinese central government pledged to create a nationally unified pension program for enterprise

employees, aiming at “four unifications” (*sige tongchou*) – a unified employers’ contribution rate, a unified employees’ contribution rate, a unified benefit provision formula, and unified administrative standards in pension fund management.

Almost twenty years have passed, even though the center repeatedly urged to create a nationally unified pension program, the latter three unification goals the center proposed were very much achieved nationwide, but the employers’ contribution rate continues to be highly diverse at the subnational level. Since all provincial governments have set up intra-province pension adjustment fund (*tiaoji jin*), it makes the pension program functioning very much like pooling at the provincial level. As the center’s requirement of 8 percent contribution rate from employees is well enforced nationwide, the observed variations in the total contribution rate in fact come from the difference in employers’ contribution rates across subnational units (BJN0402121; Yuan, 2016).

Table 1-2 presents the *de facto* total pension contribution rates¹ aggregated to the provincial level from 2007 to 2011. The *employers’ pension contribution rate* – the share of pension premium payments remitted to social security agencies by the enterprise on behalf of their employees – is synonymous with the “pension burdens” felt by employers. Given the fact that employers’ pension contributions are levied by the government very much as taxes are, variation in contribution rates suggests different redistributive scenarios at the sub-national level.

¹ Because of restriction from the central government, the data on *de facto* employers’ contribution rate at the provincial level are not allowed to be publicized. This study was only allowed to cite the information on the total contribution rate.

Table 1-2 *De facto* total pension contribution rates by province, 2007-2011

Province	2007	2008	2009	2010	2011	Average
Anhui	23.9	22.9	19.9	18	19.3	20.80
Beijing	19.8	19.2	18.5	17.3	17.7	18.50
Chongqing	24.7	24.6	29.8	18.6	21.5	23.84
Fujian	18	16.4	15.5	13.3	13.5	15.34
Gansu	30.6	27.9	27.3	28.5	34.5	29.76
Guangdong	11.6	11.5	10.5	10.1	9.3	10.60
Guangxi	24.8	25.9	24.3	25.5	20.5	24.20
Guizhou	24.1	24.3	22.9	21	21.1	22.68
Hainan	21.3	19.2	16.9	15.9	16	17.86
Hebei	27	25.6	23.6	23.3	22.4	24.38
Heilongjiang	21.1	21.1	20.3	24.3	23.7	22.10
Henan	19.3	17.3	16.5	17.6	17.3	17.60
Hubei	17.7	19.8	19.5	18.7	21.9	19.52
Hunan	19.7	18.8	17.2	17.4	17.7	18.16
Jiangsu	19.9	19.5	18.1	16.9	16.9	18.26
Jiangxi	16.2	14.6	14.3	14.2	14	14.66
Jilin	18.9	20	20	19.6	21.6	20.02
Liaoning	20.1	20.5	18.8	18.3	19.4	19.42
Neimenggu	20.7	21.7	20.8	20.6	24.6	21.68
Ningxia	25	25.8	24	25.1	20.9	24.16
Qinghai	22.4	24.8	24.8	24.6	28.2	24.96
Shaanxi	24.5	23.7	21.4	25.5	20.5	23.12
Shandong	26.2	21.3	23.4	22.2	21.1	22.84
Shanghai	25.9	24.9	25.1	25.2	21.2	24.46
Shanxi	26.1	24.4	23.5	25.4	24.4	24.76
Sichuan	27.3	28.1	30.9	27.3	26.3	27.98
Tianjin	29.6	26.8	22.5	21.3	20.9	24.22
Tibet	23.6	24	24.7	24.5	24.6	24.28
Xinjiang*	24.6	24.5	-	23.5	23.9	24.12
Yunnan	22.7	25.4	25	25.8	30.3	25.84
Zhejiang	15.1	13.4	11.7	10.9	12.1	12.64
National average	22.34	21.87	21.06	20.66	20.88	21.36

*: Data on Xinjiang do not include Xinjiang Production and Construction Army Corps.

Source: Zheng et al. (2013), p. 101.

Motivated to explain these sub-national variations, this study sets to answer the following questions:

- First, *what are the redistributive incentives of the Chinese rulers? How do central rulers differ from subnational rulers in their redistributive calculation?*
- Second, *what does the fiscal structure of the pension program look like at the subnational level?*
- Lastly, *what does the study of workers' pension tell us about China's center-local relations?*

1.2. Definitional clarifications

This study adopts a minimum definition of *authoritarian regimes* – regimes in which rulers acquire power by means other than competitive elections (Gandhi, 2008), and seeks to understand the redistributive incentives of authoritarian rulers. The characteristic of lacking competitive elections in authoritarian regimes is highlighted in the definition. Without free and fair elections, the connection between political elites and the people is not transparent in authoritarian regimes. Unlike political leaders in democracies, dictators are not subject to electoral pressure. As such, authoritarian rulers may not be motivated to provide welfare benefits in exchange for votes to secure power. Meanwhile, people's demands are not formally channeled to top political elites, and thus are not expected to be properly reflected in government policies. Therefore, it is both theoretically and empirically intriguing that authoritarian rulers decide to create and maintain expensive social programs that benefit the general masses, rather than distributing the resources within their small political coalition groups to ensure their loyalty and extend regime survival.

This study defines *redistribution* as a political decision that distributes scarce resources and materials away from the haves to the have-nots and across time. There are three layers of redistribution discussed in this dissertation. First, the rulers extract from those rich in economic resources and distribute the extraction to those who have lost in the market. In the case of a public pension program, the government collects mandatory contributions from employer and employees based on their payrolls like taxes are – with a set contribution rate, those who earn more profits in the economy are responsible for a higher social security contribution – and the government uses the fund collected to provide basic old-age retirement benefits for all participants. Second, even though the Chinese three-pillar pension design was intended to separate the public pension pillar from the individual account pillar, in practice subnational governments with no exception all dip into the money in individual accounts to pay for retirement benefits of current retirees. In other words, individual accounts are emptied and the current pension system works as a pay-as-you-go (PAYG) pension system.² In a PAYG system, in addition to the redistribution between economic groups, the pension system also redistributes across generations – active employees pay for retirement benefits of current retirees. Moreover, in a fiscally decentralized country without a national unified pension pool, as the public pension program is set up in China, the central government is responsible for redistributing resources across sub-national units to promote inter-regional welfare equality, which constitutes the third layer of redistribution.

² In practice, individual accounts are emptied (*kong zhang*) by local governments to pay for retirement benefits of current retirees. The World Bank categorizes the Chinese pension system as a notional individual account system, instead of the three-pillar scheme the Bank had advocated (see Dorfman, et al., ‘China’s Pension System’, World Bank working report, 2013). However, many scholars still call the Chinese model a three-pillar model, as it arguably does have three pillars -- public pensions, individual accounts, and supplementary insurance programs; and the government requires compulsory contributions to the first two.

The concept of *welfare* discussed here goes beyond its narrow definition of mean-tested relief-giving programs, but includes all government social programs that intend to protect citizens from market insecurities and economic risks and promote the general well-being of the public. These policies together constitute the foundation of a welfare state. Public pension program is thus considered one important component of a welfare state. In addition to discussing the appearance of social-amelioration welfare policies, this study is more interested in how these policies are arrived at politically, and what impacts these policies have on social, economic, and political structures in the long run.

1.2 Conventional wisdom on authoritarian welfare politics

Repression has become the hallmark of authoritarianism (Frantz & Kendall-Taylor, 2014). The common wisdom of authoritarian politics is that modernizing authoritarian rulers often rely heavily, or sometimes exclusively, on systematic repression to rule the society (Linz, 2000; Svobik, 2012). Repression is typically defined as the use of force of the government to increase the likelihood of containing opposition and extending power tenure. Unlike in democracies, in authoritarian regimes electoral accountability is largely absent. The institutionalized limit to the use of repression is minimal. According to these studies, as authoritarian rulers constantly face threats from both inner-circle rivalry groups and the contentious masses, suppressing dissent is a more convenient instrument than justifying legitimacy and building loyalty. By repression, it does not only include the actual application of repressive apparatus to eliminate the discontent, but more broadly, it poses a threat to latent troublemakers and increases the cost to overturn the regime. Studies show that repression does increase the likelihood of dictator's survival (Escribà-Folch, 2013).

Do autocrats prefer repression over redistribution? The empirical data this study collected do not support this conventional view. Empirically, we can use government’s spending on defense and public order and safety as a proxy for the rulers’ reliance on repression.³ Similarly, we can use the spending on the two most extensive redistributive programs – social security and healthcare – as a proxy for the rulers’ reliance on redistribution as a tool to maintain social order. Table 1-3 demonstrates that in over 80% of the cases the differences in authoritarian rulers’ spending on repression and redistribution are within 5% of their gross domestic product (GDP). More interestingly, in about 30% of the observations, the rulers spend more on redistribution than repression. Moreover, the emphasis on redistribution would only become even more impressive if we include government spending on other social programs in measuring a government’s redistribution efforts, or only include government’s spending on police force and leave out the spending on military to measure a country’s repressive expenses.

Table 1-3 Authoritarian Rulers’ spending on repression and redistribution, country-year* from 1970-2009 (unit: # of observations)

% of GDP	More on repression than redistribution	More on redistribution than repression	Total
0 to 1	203	89	292
1 to 3	118	76	194
3 to 5	121	20	141
5 to 10	72	32	104
10 to 50	10	8	18
above 50	5	0	5
Total # of cases	529	225	754

*Note: The selection of authoritarian regimes is based on Freedom House’s scores on political rights. Political rights ratings are based on an evaluation of three subcategories: electoral process, political pluralism and participation, and functioning of government. Countries are scored by 1 to 7, with 1-3 indicating “free”, 3.5-5 “partly free”, and 5.5-7 “not free”. This study takes countries that receive 3.5 or higher as authoritarian. There are 754 valid country-year observations in total.

³ It is worth noting that the spending on military is supposed to be used for defense against external invaders, and not to be used for repressive purposes toward the population. However, there is a possibility that authoritarian rulers send military for domestic suppression, such as what we observed in the 1989 Tiananmen Event.

Source: IMF Government Financial Statistics (1970-2012), Freedom House Reports (1970-2009).

This study notes that regardless the nature of political rule, the employment of repressive apparatus is economically and politically expensive for a ruler, and she is likely to find that the use of repression is usually counter-effective on maintaining daily social order (Goldstone & Tilly, 2001; Svobik, 2012; Tyler, 2006).

In addition, if authoritarian rulers are indeed all repressive, how can we explain various welfare programs that exist in the authoritarian world today? In fact, Mares and Canes (2009) find that an overwhelming number of social insurance programs, including disability, old age, and work sickness insurances, originated in authoritarian regimes and were later adopted by democratic countries. A recent development in the study of welfare politics is the publication of a few high-impact scholarly works that recognize that authoritarian rulers employ both sticks and carrots to encourage loyalty and extend the tenure of power (Gallagher & Hanson, 2009; Gandhi & Przeworski, 2007; Magaloni, 2006). Scholars argue that institutionalized one-party authoritarian regimes are more prone to redistribute than other types of authoritarianism, as one-party regimes are more vulnerable to shocks outside the ruling group. As such, one-party regimes require to establish a broader base of support via a patronage system, such as creating a welfare state (Gandhi, 2008; Kim & Gandhi, 2010). Hence, we should expect that rulers from an institutionalized one-party authoritarian regime, like the Chinese one, would in general prefer redistribution over repression. These scholarly works have marked a new territory in the field of comparative welfare politics, and more importantly call for greater attention to further our knowledge of welfare politics in dictatorship.

However, our understanding of redistributive incentives of authoritarian rulers is still nascent. Welfare is still overwhelmingly regarded as an intrinsic product of democracy. The

dominant theories in the field of welfare politics are Euro-centric and democracy-centric. The impacts of factors such as partisanship of a government (e.g. Esping-Andersen, 1990), institutional design (Immergut, 1992; Iversen & Soskice, 2006), and the role of labor unions and industrial relations (Swenson, 1991) on contouring the shape of a welfare state are emphasized and investigated. However, as mentioned, the lack of direct representation of people at the government's policymaking table in authoritarian states has decided that these factors are not directly applicable to explain what happens on welfare development in authoritarian regimes.

Beyond the unbalanced focus of current welfare politics literature on democracies, a glaring weakness in the current welfare politics literature in general is the focus of politics at the national level, simply assuming the state as a unitary actor. This top-down approach assigns a passive role to local governments, machine-like implementing policies designed by the center. As a result, the role of local governments in policymaking process is often undermined in current discussion (Frazier, 2010; Pierson, 2005). This approach is all the more problematic in dealing with large welfare states that are embedded in a decentralized political structure, as is the case with China. Systematic research on center-local relations in welfare politics holds a broad and important potential.

Welfare development in a decentralized authoritarian regime is far more challenging than in a highly centralized one. In a decentralized setting, interests of the center and subnational governments may not always coincide, yet the center lacks the power and rights to forcefully impose its will on its subnational agents. As such, the classic principal-agent problem arises. This delicate political arrangement is particularly prominent in welfare politics, as oftentimes welfare programs require substantial commitments from the government over a long period of time. Which level of the government is fiscally responsible to build a universal welfare program?

How does the central government ensure its subnational governments work faithfully toward a national welfare program that benefits beyond local administrative boundaries? Without a close examination of subnational governments' redistributive incentives and their interactions with the central government, any attempts to understand welfare politics in decentralized authoritarianism is incomplete.

The present study represents a step toward redressing this imbalance. This dissertation selects the public pension program in China that has a decentralized fiscal and administrative structure as a case to investigate welfare politics in decentralized authoritarianism. This study highlights the role of provincial governments and details the interaction between two levels of governments, the center and its provincial governments. The significance of this study is threefold. First, it promises to enrich the existing literature on comparative welfare states, by filling the void in the redistributive incentives of authoritarian rulers. Second, instead of treating authoritarian rulers as a unitary actor, this study looks into the center-local interplays in redistribution in the Chinese decentralized political system. In so doing, this study also sheds new light on center-local relations in Chinese politics. Third, instead of attributing to formal institutions, this study contends that welfare programs, like the urban pension program, are employed by Chinese rulers to pre-empt and resolve public opposition and thus to increase the regime's resilience.

1.3 Why studying public urban pension program in China?

Studying old-age social security programs in a country that will be faced with a population aging crisis unprecedented in human history by 2050 (United Nations, 2015) is self-evidently an important research topic. According to the United Nations new statistics estimate the median age of the Chinese population will more than double in a 75-year time frame, from

20.6 years in 1975 to 43.8 years in 2050 (United Nations, 2015). As the Chinese baby-boom generations hit retirement age by 2020, the impacts of the population aging on social development, economic prosperity, and political stability will start to show yet all at once. With more population exiting the workforce than entering it, the Chinese public PAYG pension program will face an enormous amount of payouts in near terms. Is the current public pension program ready to absorb this dramatic demographic shift? Understanding the Chinese government's incentives in funding the current pension program is a meaningful first step in addressing this pressing aging crisis.

In addition to the demographic decline that has set the country to a time bomb, unpaid transition costs from the reform of the urban pension program for enterprise employees during the economic transition puts additional pressure on the current public pension program. Between 1993 and 2006, more than 60 million jobs were lost in SOEs and urban collective sector enterprises in China (Hurst, 2009). As the number of early retirees and laid-off workers dramatically increased, the old socialist pension program started to crumble in the early 1990s with reductions in retirement benefit amounts, delays in payments, and even outright non-payment. Large-scale protests and demonstrations on the pension issue broke out throughout the nation (Hurst & O'Brien, 2002; West, 1999). To resolve the problem, the government decided to separate welfare provision responsibility from enterprise operation, and to change the pension program from a Soviet-type state-funded public program only for state-owned enterprise employees to a pension insurance scheme that covers all urban employees and requires contributions to the pension fund from both employers and employees. As mentioned, in practice, it was a transition from a socialist public pension program to a *de facto* PAYG program. The government thus sought to absorb and internalize transition costs in the pension reform, by 1)

creating a broader base of contributors by including non-SOE employees, and 2) asking current employers and employees to pay for the equivalent of two generations' retirement benefits. By transition costs is meant legacy pensions for a market pension reform departing from the old socialist program. In other words, transition costs are retirement benefit payments to current retirees and those were about to retire at the time of the pension reform, since these pensioners and workers had not made any pension contributions and yet were entitled to receive retirement benefits after retirement, under the old contract with the state. This reform idea requires a delicate balance between 1) collecting sufficient contributions from employers and employees for timely pension benefit payments, and 2) incentivizing labor participation and facilitating economic transitions.

Regardless of any good intentions behind a policy, how the policy is actually implemented has a direct impact on final policy outcomes. Unfortunately, the decentralized administrative and fiscal structures⁴ in the Chinese system only make the idea of internalizing the transition costs more challenging. In this decentralized system, every pension administrative unit is responsible for making ends meet – collecting contributions and using their pension fund to pay benefits. In other words, the idea of internalizing the transition costs in the new pension program shifted the pension liability to subnational governments. Yet Chinese sub-national governments in general lack genuine incentives to promote welfare development, while they are more motivated to boost short-term economic performance and to create high-profile merit projects (Tsui & Wang, 2004). They have no obvious motive to operate an expensive old-age pension program and bear the transition costs on their own. As subnational governments'

⁴ Administrative decentralization here means that the national government delegates authority to sub-national governments to make certain policy decisions, subject to review and possible veto from above; fiscal decentralization implies that the national government permits sub-national governments to retain a significant share of nationwide fiscal revenues.

decisions on the pension program directly determine the budgeting and staffing for related central government agencies, a conflict of interest between the center and subnational governments is a serious concern of the center. This dissertation joins other scholars to offer an assessment of the center's capability to monitor local governments and sanction their behavior (Hurst, 2009). Therefore, investigating the interaction between the center and subnational governments in building an expensive welfare program in a decentralized structural context has both theoretical and practical importance.

Perhaps not surprisingly, the resulting new pension program is highly decentralized, from policy design to program administration. As Table 1-2 shows, there is considerable variation in employers' pension contribution rates to the public pension pools across provinces. What factors help explain these subnational variations? As provincial governments set up intra-provincial pension fund adjustment mechanisms, the pension program works like being pooled at the provincial level to a certain extent. As such, we may expect that conventional factors such as a province's demographic composition, pension fund sustainability, and fiscal capacity would directly affect how the pension contribution rate is set by the government (Agarwala, 1997; Holzmann, 2009). We employ the official old-age dependency ratio from *China Statistical Yearbooks*, which measures the ratio of the people aged 65 and above and those aged between 14 and 64, to measure the demographic structure at the subnational level. Other things being equal, we may expect that governments in regions with higher dependency ratios would be faced with greater challenges to provide retirement benefits. The change in pension fund balance in a year shows the difference between pension fund contribution collected and pension benefit payments in the end of a year, which reflects vividly sustainability of a pension fund. Regions with sufficient pension fund reserves may relax their contribution policies, and vice versa. Also, we

may use GDP per retiree in a province to measure one province's economic development level in relation to the pension benefit provision burden. We also include GDP per capita in a province as an alternative measure of the level of economic development at the individual level. The impact of economic development on pension development in a region may be two-sided. First, governments with a financially sound economic base may not be immediately pressed to extract resources from the society to run their pension program. Second, to the contrary, a province with a higher level of economic development may find demands from the enlarging working class in important economic sectors no longer dismissible, and thus raise contribution rates in order to provide more generous welfare benefits.

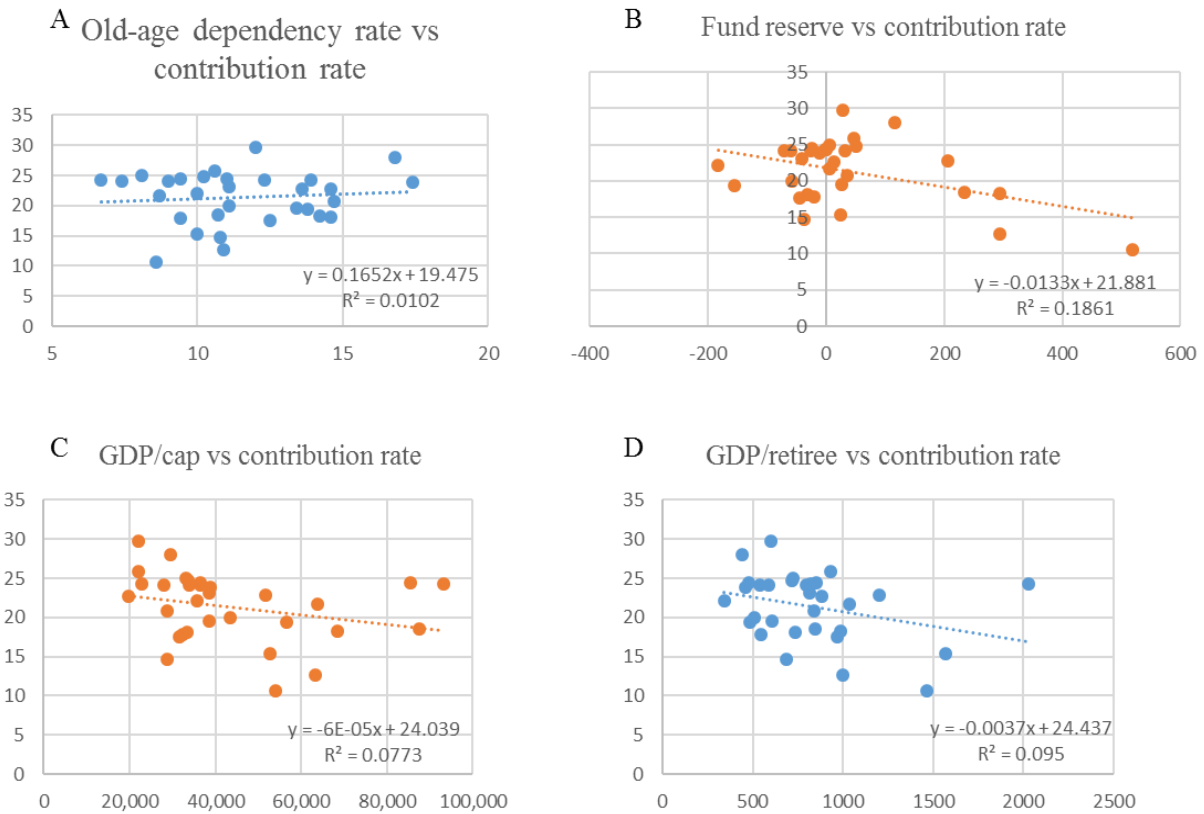
Table 1-4 Key conventional factors that may shape old-age pension contribution rates in provinces

Province	Ave. pension contribution rate (%, 2007-2011)	Old-age dependency ratio (%, 2011)	System dependency ratio (%, 2011)	Change in pension fund balance (0.1 billion yuan, 2011)	GDP/cap (yuan, 2012)	GDP/retiree (thousand yuan, 2012)
Anhui	20.8	14.7	35.6	36.24	28,792	838.16
Beijing	18.5	10.7	22.7	233.92	87,475	848.66
Chongqing	23.84	17.4	51.5	-10.82	38,914	461.98
Fujian	15.34	10	20.5	24.23	52,763	1,570.18
Gansu	29.76	12	47.8	27.46	21,978	602.71
Guangdong	10.6	8.6	10.9	518.58	54,095	1,462.35
Guangxi	24.2	13.9	45.6	-26.95	27,952	796.85
Guizhou	22.68	13.6	33.8	12.63	19,710	881.80
Hainan	17.86	9.4	31.4	-19.72	32,377	543.60
Hebei	24.38	11	36.8	-1.62	36,584	850.96
Heilongjiang	22.1	10	63.2	-182.83	35,711	340.89
Henan	17.6	12.5	32.7	-44.81	31,499	967.17
Hubei	19.52	13.4	44.3	27.02	38,572	605.79
Hunan	18.16	14.6	39.1	-32.44	33,480	737.59
Jiangsu	18.26	14.2	27.8	293.32	68,347	988.31
Jiangxi	14.66	10.8	34.8	-36.74	28,800	684.70
Jilin	20.02	11.1	55.8	-56.93	43,415	508.94
Liaoning	19.42	13.8	45.5	-155.98	56,649	486.81
Neimenggu	21.68	8.7	43.3	5.82	63,886	1,038.22
Ningxia	24.16	7.4	42.8	31.62	36,394	587.27
Qinghai	24.96	8.1	44.7	5.55	33,181	723.77
Shaanxi	23.12	11.1	45.6	-40.91	38,564	816.00
Shandong	22.84	14.6	24.3	205.73	51,768	1,201.28
Shanghai	24.46	9.4	41.6	-25.08	85,373	476.18
Shanxi	24.76	10.2	34.2	51.2	33,628	717.27
Sichuan	27.98	16.8	49.6	116.36	29,608	440.73
Tianjin	24.22	12.3	48	-71.6	93,173	821.77
Tibet	24.28	6.7	40	0.95	22,936	2,031.03
Xinjiang	24.12	9	36	-60.08	33,796	540.01
Yunnan	25.84	10.6	43.7	47.5	22,195	931.22
Zhejiang	12.64	10.9	15.2	294.11	63,374	996.71
National avg.	21.36	11.53	38.35	37.60	43386.74	822.55

Source: *China Statistical Yearbook* (2013), and Zheng et al. (2013), pp. 101, 103, and 129.

Figures below present the scatter plots showing the relationships, with the contribution rate on the x-axis and structural factors on the y-axis respectively. These figures indicate that none of these structural factors, old-age dependency ratio, pension fund reserve, or local economic capacity, provides satisfactory explanations to the puzzle.

Figure 1-1 Scatter plots of the contribution rate and conventional explanatory factors



One may question the validity of employing the general old-age dependency ratio to explain contribution rate of a pension program, as the contribution rate should be set according to the demographic structure of pension participants, namely the ratio of pension contributors and recipients. This study here also uses each province’s old-age dependency ratio in the pension system, or the ratio of numbers of recipients to contributors in the PAYG system, which may be called the “system dependency ratio.” The system dependency ratio reflects the pressure pension

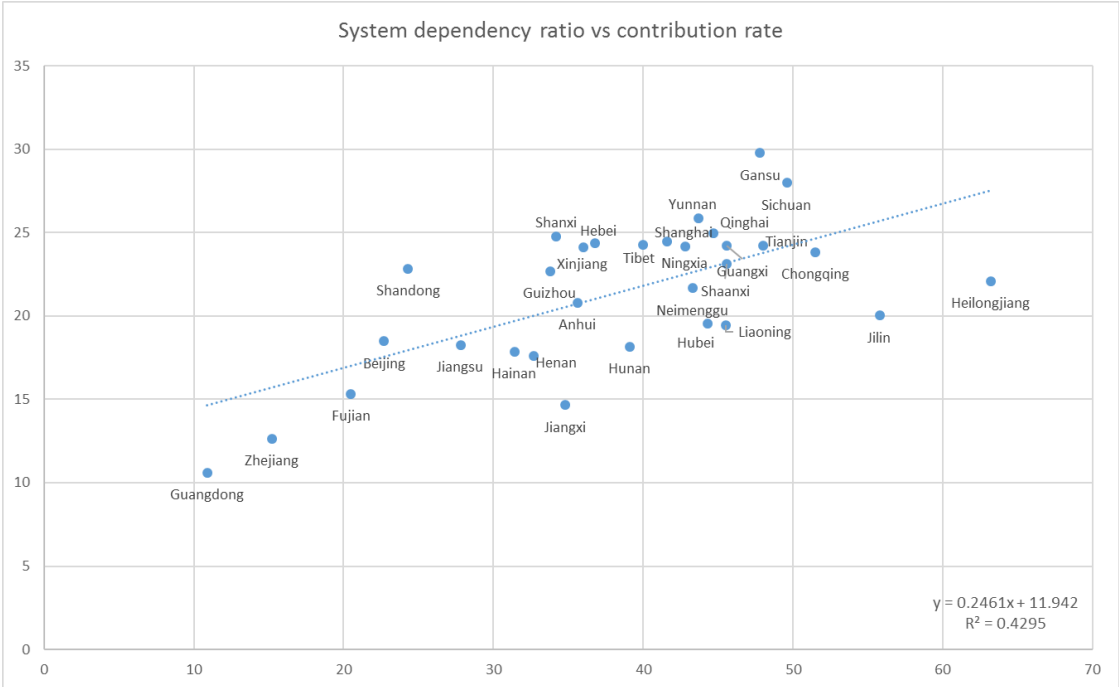
recipients put on contributors who are economically active employees. Figure 1-2 shows that system dependency ratio seems to show a general trend that localities with higher system dependency ratios are more likely to set a higher pension contribution rate.

However, strictly speaking, the system dependency ratio is more than a simple structural endowment. The old-age dependency ratio, shown in Figure 1-1's A Figure, is an indicator of a natural demographic distribution, while the system dependency ratio is an outcome of the pension policies implemented by subnational governments, which means system dependency ratio is affected by the contribution rate itself. This dissertation will demonstrate that a low pension contribution rate will attract more investments to come and thus produce more employment opportunities. However, due to the pension program's limited portability problem, a large number of pension contributors, mostly migrant workers, are not retirement benefit recipients, which deflates the system dependency ratio. And a low system dependency ratio gives local governments more flexibility to lower the contribution rate, which in fact creates a virtuous circle that reinforces the collinearity of these two factors. Therefore, economically more developed regions are likely to be associated with a lower system dependency ratio.

Bearing this in mind, we here take a closer look at the relationship between the system dependency ratio and the pension contribution rate. Figure 1-2 provides province names as data labels. The best-fitting line divides the provinces to two groups: Provinces fall below and above the line. It is clear that provinces falling below the regression line are almost exclusively economically more developed regions, and all data points, except Shandong and Shanghai, falling above the line are economically more backward regions located in remote landlocked areas. This means that taking the imbalanced recipients-contributors ratio in mind, while economically more developed regions set lower pension contribution rates than their pension

systems permit, economically less developed provinces set higher pension contribution rates than needed. How do regions that set lower contribution rates operate their pension programs? In addition, if we consider the center’s fiscal support to provincial governments for the pension program, the relative positions of these 31 provinces presented in this figure is more puzzling. How does the center’s fiscal subsidy affect the pension designs at the subnational level? And why do governments in provinces like Tibet, Xinjiang, Liaoning, and Jilin that have all been heavily subsidized by the center, react systematically differently – Liaoning and Jilin falling far below the line while Tibet and Xinjiang fall on the opposite side of the division line. This discussion reveals that while the system dependency ratio may be a factor that contributes to variations in the pension contribution rate, in fact this relationship raises more questions than answers. This study is set to address these questions.

Figure 1-2 A closer look at the relationship between system dependency ratio and pension contribution rate



In addition, compared with other welfare programs, old-age pensions provide us an ideal angle to investigate the power dynamics within the Chinese welfare states for four reasons. First, old-age pensions are typically the most expensive entitlement program in welfare states, which requires a substantial commitment from the government. Second, old-age pensions establish a long-term relationship between the state and its people. The government needs to make a credible long-term commitment to participants of the public pension program that their contributions will be paid off at retirement, and the pension benefits will likely be higher than the payouts from saving the same contributions in individual savings accounts. As such, via this public old-age pension program, the government increases the cost of the exit option for the people, and hence creates a long-term binding relationship with its citizens. Third, since funding an old-age pension program requires a substantial amount of resources over a long period of time, the advantage of a public pension program over a private one mainly lies in the ability of the government to pool the assets across the country to secure long-term sustainability of the program. However, contrary to this norm, the highly decentralized Chinese pension program offers an interesting case to investigate, as this pension program is operated at the subnational level in an authoritarian regime with a decentralized administrative and fiscal structure. Fourth, based on a series of interviews with pensioners and layoffs, Hurst and O'Brien (2002) find that, compared with other social welfare programs, such as healthcare and unemployment insurance, public pensions "appear to be considered a truly sacred right in the eyes of both workers and the state" (p.360). Hence, how this symbolic pension program that workers hold dear is transitioned and conducted has profound implications for the stability of the regime more than for other welfare programs.

1.4 Main arguments

This dissertation argues that autocrats are more likely to prefer welfare programs over repressive tools, when 1) they are faced with strong potential of political unrest, and 2) they are far-sighted political rulers that value long-term regime stability and prosperity. Repressive force is undoubtedly the most fundamental defender of a dictator's power. Surely, one dictator may develop what Olson (1993) calls a "robbery model", where the dictator may grab whatever is left and run. However, in the long run of regime operation, employing repressive tools for daily management of the state is often counter-effective. This study highlights specifically three ways in which repression may incur enormous costs for the rulers. First, it takes major resources to train and maintain a repressive apparatus with a credible threat, punishing violations and rewarding desirable behavior. Second, adopting repression simply ameliorates the dictator's dilemma. Without electoral channels, the dictator is challenged by an information asymmetry problem when it comes to understanding the public demands and keep an upper hand over the ruled, and excessive use of armed forces would only intensify the problem to the rulers' disadvantage. Third, political conflicts disrupt economic development, which imposes tremendous costs on regime profitability and legitimacy. The first two costs are applicable to all authoritarian regimes, and the third one is particularly prominent in regimes whose economies are greatly dependent on labor force participation.

This dissertation contends that welfare programs offer an important tool to enhance authoritarian resilience. Specifically, this dissertation notes that the effects of welfare programs are twofold. First, welfare programs promote economic productivity, which is particularly important for regimes that rely their legitimacy on economic performance. In addition, increased economic productivity generates more long-term rents for the ruler, which may be distributed

toward political supporters to reassure their loyalty. Second, welfare programs show rulers' benevolence, and directly buy off loyalty and cooperation from the public. In order for the people to take on high-risk political actions to overturn the regime, they need to be convinced that the price they pay for a rebellion would be paid off after a new regime is established. As such, directly distributing economic fruits to the public through welfare programs increases the benefits of staying obedient to the current regime, and thus makes the exit option more costly. A public pension program creates such a long-term binding effect between the ruler and the ruled, and thus the design of a pension program bears prominent implications for regime stability.

Furthermore, among different types of authoritarian regimes, one-party regimes are particularly more prone to welfare redistribution than military and personalist regimes. Two reasons that explain one-party regimes' pro-welfare incentives. First, compared with military and personalist regimes, one-party regimes are more vulnerable to exogenous shocks. Therefore, one-party regimes need to establish a broader institutional support base. A reward/punishment system is a crucial component to manipulate the support base, provided that the system distributes privileges to the people who show loyalty to the regime, and punishes those who rebel, by withdrawing the privileges (Lust-Okar, 2005; Magaloni, 2006). Second, institutionalized one-party regimes extend rulers' time horizons so that one-party rulers are more willing to invest for future benefits. The political party system and the pseudo-democratic legislature provide institutionalized power sharing mechanisms, which help balance various political interests, facilitate political coalitions, and reduce the likelihood of intra-elite splits. With a stable prospect of political development, one-party rulers are more likely to engage in longer-term investment and development.

With its almost seventy-year history so far, the Chinese one-party regime is particularly resilient (Magaloni, 2008). This dissertation seeks to demonstrate that welfare programs play an indispensable role in promoting its resilience. Before the economic transition, not surprisingly, the state-funded welfare package was an integral part of the socialist regime; during and after the transition, the Chinese government deems welfare development (*min sheng*) as a matter of life or death for the regime, as welfare programs are employed by the government to facilitate the economic transition and help pacify potential oppositions to its ruling. Over the past three decades, the Chinese government has devoted a substantial amount of fiscal resources to developing nationwide welfare programs, including the pension program examined here, public health insurance, maternity insurance, work injury insurance, unemployment insurance, and the housing provident fund (often referred to as “five insurances and one fund”). Among these welfare programs, the public urban pension program is the most developed, and accounted for around 70 percent of the Chinese government’s expenditure on the five insurance programs in 2009 (iFeng Finance, 2009).

However, the decentralized administrative and fiscal structure in China today makes welfare development particularly challenging. With the center only proposing policy development guidelines, subnational rulers become *de facto* welfare policymakers in China. Compared with the center, subnational rulers are oftentimes more short-sighted and economy-oriented. Provincial governments are the highest-level government at the subnational level, in charge of policymaking and approving policies implemented at the sub-provincial level. Being motivated to climb the political career ladder, provincial government officials’ policy preferences are shaped by the career evaluation scheme. As the current career evaluation scheme for government officials in China is still heavily dominated by economy-related terms (Li &

Zhou, 2005), subnational governments at all levels are motivated to promote short-term economic growth by inviting profitable private and foreign investments to come, yet not being incentivized to spare economic resources to increase the well-being of the people.

However, despite their reluctance, a welfare program being a nationwide mandatory program, subnational governments are obligated to obey the center's order, yet have the power to adjust the center's guideline to local conditions. To provide welfare benefits, subnational governments must extract resources from the society to fund welfare programs, which increases production costs and reduces economic efficiency. In the current global capital market, the mobility of capital enables investors to locate their businesses in localities that offer most favorable policies and inviting business environments. This dissertation finds that to minimally reduce the costs of welfare provisions imposed on the economy, subnational governments are more likely to extract less from investors with mobile assets, and impose higher contribution rates on SOEs. In line with the exiting research on tax rate and evasion (Allingham & Sandmo, 1972; Clotfelter, 1983), this study argues that the government needs to strategically tax contributors that are bounded in certain ways. SOEs, compared with private and foreign investments, are less able to avoid contribution responsibility, since the activities of SOEs are often confined within the physical boundaries of political administrative units. It is more convenient for the governments to enforce SOEs' contributions, so they may choose to tax SOEs more heavily. In contrast, mobility of foreign and private investment means investors can seek the best fit to locate their businesses. Therefore, rulers often grant more favorable policies to these mobile-asset investors to attract them to come, including offering discounts on welfare contributions.

As the center and subnational governments have a direct conflict of interest in welfare provision, the center needs to incentivize subnational governments to carry out the welfare programs the center desires. This dissertation finds that to ensure proper implementation of welfare programs at the subnational level, the center has to prioritize and heavily subsidize regions with strategic importance through fiscal subsidies, namely those with potential economic and political instabilities. As a result, the center's subsidy program to subnational governments in fact creates an uneven base of redistributive incentives for its subnational governments. First, here we utilize the concept of *cost externalization*, under which some actor other than the decision maker absorbs some or all of the costs associated with a decision (in this case, to develop the pension program). When political actors can externalize the costs of a project that substantially benefits their geographically-defined constituents, such actors will tend to maximize local interests at the expense of the general national budget. As such, the center's fiscal subsidies to a region reduce the cost of running a welfare program in that locality. Regions that are able to externalize the costs have the luxury to reduce extraction from the society if needed at the cost of the national resources. Second, regions that do not receive the center's fiscal support strive to make ends meet by either collecting sufficient contributions via setting a high contribution rate, or utilizing their local budget to fill in any potential welfare fund deficits. The difference between these two options lies in who bears the final costs – employers or the government. As mentioned, governments tend to offer favorable terms to investors with mobile assets. For regions where private and foreign investments account for a large share in the economy, local governments can hardly increase the contribution rate, so they must utilize their fiscal budget to subsidize the welfare program.

This dissertation uses the public urban pension program for enterprise employees in China as a case to investigate the Chinese central and subnational rulers' redistributive incentives. This study shows that the supposedly nationally unified pension reform is messy and highly uneven across subnational regions, and the variations are explained by political economy of each region. By combining the two factors discussed above – the availability of center fiscal funding, and the level of local economic openness – this study proposes a typology of five funding structures of the pension program in subnational China. This dissertation further argues that China has a *welfare federalism* – with the central government proposing welfare policy guidelines and subnational government adjusting the center's proposal according to local conditions and needs. As subnational governments are responsible for designing and implementing welfare policies and pooling risks and contributions at the provincial level, each province acts very much like an independent welfare state within the Chinese welfare state umbrella. In addition, this is an *asymmetrical* welfare federal system, with certain subnational regions enjoying more favorable treatments from the center.

While regions that enjoy the center's fiscal transfers have more financial flexibility, regions that do not rely on the center's fiscal support have more autonomy in general. This study contends that the Chinese central government utilizes fiscal subsidies as a leash to lead and restrain the provinces. Although the center deemed welfare development to be a major "strategic priority" in the country's approach to development, it has to count on provincial governments to carry out that grand vision. To counter provincial governments' predictable disinclination to operate an expensive welfare program faithfully, the center often must rely on special fiscal subsidy programs to incentivize its provinces to comply with the center's directions, and to facilitate their compliance. Hence, regions that do not rely on the center's fiscal subsidies have

more autonomy and flexibility in adapting the center's policies to local conditions. This study also shows that regions that enjoy complete fiscal independence from the center may even oppose the center's policy proposals, and wield a potential veto power in China's welfare politics.

1.5 Research method

This study adopts a sub-national comparative research method (Snyder, 2001). As Hurst (2009) notes, even though the central state controls basic parameters, subnational variation is often objectively more important and theoretically interesting. Holding the environment (the country) constant, sub-national comparisons can largely eliminate potential explanatory variables, which helps conduct a controlled comparison. In the pension case in China, as the Chinese central government issues reform guidelines and subnational governments have the flexibility to adjust the center's proposal to local conditions, which offers an ideal scenario to directly investigate subnational governments' policymaking rationales and the different interaction patterns between the center and its various subnational agents. Keeping national policy constant, in-depth case studies on different subnational units enable this study to generate more accurate causal stories of sub-national rulers' redistributive incentives. In addition, in a country like China with a vast geographic range, aggregating data to the national level often contributes to the so-called "whole-nation bias" (Rokkan, 2009). Sub-national comparisons offer a chance to unveil the spatially uneven development patterns across the country, and develop a more comprehensive description of complex political processes.

This research focuses on province-level governments in China. There are 31 province-level political units at the provincial level for all (twenty-two provinces, five autonomous regions,

and four municipalities directly under the center)⁵. In China, most pension pools are administered by municipal/county-level governments. Provincial governments spell out the center's policy plans and give these lower governments general guidelines, and sub-provincial governments then make specific policies for the provincial governments to review. This approach applies to the pension policy design discussed here. By the end of 2009 all provincial governments set up intra-provincial pension fund adjustment mechanisms, which to a certain extent make the pension program works like pooling at the provincial level (Wang, 2016b). Moreover, the author was unable to collect information of all these pension administration units, and thus provincial data were used. Indeed, such data may not exist. To be sure, there are sometimes considerable within-province variations. As provincial governments were granted power to make policy decisions on the pension program and are directly accountable to the central government, using province-level units as the unit of analysis would seem to be an appropriate option as well as the best practical course.

This study employs a mixed-method approach – in-depth case studies to understand how political actors make policy decisions, and tests of the generalizability of the cases by statistical analyses. This study compares five cases – Liaoning, Tibet, Hunan/Hubei, Gansu, and Guangdong. These five cases represent respectively the five main stories of pension funding structures in subnational China. Moreover, the five cases cover all four primary geographic regions in China – northeast, midland, and coastal regions. In doing so, this study expands the current research focus of Chinese welfare studies from the northeast and coastal regions (Frazier, 2010; Lu, 2008) to other important yet less-studied regions of the country. The author carried out

⁵ Xinjiang Production and Construction Army Corps (XPCC) is excluded from this study. Created in 1954 by the central government, the XPCC enjoyed special political treatment as a unique economic and semi-military organization. Although from 2005 the XPCC coordinated its retirement benefit increase plans with the government of Xinjiang Uygur autonomous region, its special political identity makes it inappropriate for the kind of inter-regional comparisons conducted in this study.

multiple month-long field research trips in Beijing, Hubei, Hunan, Gansu, Guangdong, Fujian, and Liaoning, in the summers of 2012, 2013, and 2016. Given the multiple difficulties of conducting a field research in Tibet, the author collected information on Tibet's pension program via interviews with officials of other provinces, central government officials, and scholars, and also conducted a thorough literature review on various written sources related to pension development in Tibet.

The author used focused interviews with provincial-level policymakers, central-level government officials, and scholars familiar with the pension program, and conducted 48 interviews in total. All interviews took approximately one hour, and were conducted in one-to-one office settings, without utilizing a recorder during the conversation. For government officials, the author targeted three government departments – the old-age pension division, and social security fund administration division in the Ministry/Provincial Bureau of Human Resources and Social Security, and the social security division in the Ministry/Provincial Bureau of Finance, as these three government departments are active participants in policymaking processes of the pension program in both levels. Thanks to the reference letter from the Political Science Department of Tsinghua University, the author was able to approach individuals in the midst of their daily activities in offices and ask for interviews. The author found the “snowball” sampling method to select interviewees, namely introducing the investigator to the next interviewees through initial contacts, to be ineffective. Two interviews with provincial government officials were conducted through direct references by the author's contact persons and the meetings were set up before the interviews. Mainly due to the nature of mutual introduction by a third person, interviewees responded to questions less naturally, and information collected from those interviews is more or less a simple repetition of the center's policy papers. In addition, instead of

following the same questionnaire in every interview, the author allowed interviewees to discuss issues and ideas that concerned them most, and asked follow-up questions. Five frequent themes in interviews included: 1) their comments on the 1997 pension reform, 2) difficulties their province faced in handling the pension program, 3) any discount in the program to attract investors, 4) their comments on the program's limited portability problem across provincial-units, and 5) their response to the center's proposal on centralizing the pension program.

This study combines this rich, qualitative data with an original quantitative data set. Thanks to the generosity of Dr. Zheng and Dr. Yang, who kindly permitted this study to use the data they collected directly from inside sources at the central government, including rarely found data on the center's pension subsidies to provincial governments and employers' actual pension contribution rates aggregated at the provincial level. Other data analyzed in this study, including the unemployment rate, percentage of ethnic population in the overall population, economic openness data (FDI investments) are either directly from *China Statistical Yearbooks*, or calculated using the raw data from the *Yearbooks*.

1.6 Plan of this dissertation

The next theoretical chapter first starts with incentives of authoritarian leaders to repress versus redistribute. It points out material and political costs of employing repression toward the masses, and also explains the advantages of employing redistributive programs in maintaining the ruler's power tenure. It further argues that one-party authoritarian regimes are more prone to welfare provision than military and personalist regimes. As a particularly resilient one-party regime, China provides an important case to study. The decentralized political structure in China complicates welfare development throughout the country, but enables us to investigate both central and subnational Chinese rulers' redistributive incentives. This dissertation differentiates

the redistributive incentives of central and provincial rulers, and argues that the central government acts as a principal facing the classic principal-agent problem to make sure its agents, sub-national governments, follow its policy recommendations. This study argues that while the center is more far-sighted and all-encompassing and thus is more prone to welfare development, subnational governments, being incentivized by the cadre evaluation system, focus more on boosting short-term economic growth than on promoting welfare development. To rescue this conflict of interests, the central government often uses fiscal subsidies to subnational governments to limit the latter's policy options. Yet the center's fiscal support for subnational units shapes the latter's redistributive incentives. Chapter Two develops a micro-level theoretical framework that explains redistributive incentives of the center and provincial governments, and the way center-province interactions affect the making of local pension policies. This chapter generates hypotheses to be tested in the succeeding chapters.

Chapter Three presents a thick historical overview of the Chinese urban pension program for enterprise employees. In order to better understand how the current pension program came about, this chapter traces politics behind the series of pension reforms in the 1990s. This chapter shows that the current decentralized nature of the pension administration is a heritage of the highly decentralized Chinese administrative and fiscal structure.

Chapters Four to Six use empirical data to test the hypotheses presented in the theory chapter. Chapter Four focuses on the Chinese central government, and investigates factors that shape the center's decisions of distributing limited financial resources across subnational regions. As the center's fiscal subsidies for the pension program come from the center's fiscal budget, the distribution of pension subsidies across subnational units involves deliberate political consideration. Using a mixed-method approach, this chapter finds that the center often prioritizes

regions challenged by economic and political instability, namely regions with high unemployment rates during the economic transition period, and a large share of ethnic minorities in local population. The center's special attention to these regions is often channeled through substantial fiscal transfers and creation of favorable benefit programs targeting these regions and the population.

Following Chapter Four's discussion of the distribution of fiscal resources from the center to local governments, Chapter Five examines how provincial governments react to the center's redistribution decisions and adjust the center's pension policies to local conditions accordingly. A typology of five local pension fiscal structures is developed throughout the discussion in Chapter Five. Drawing heavily from the author's field research, this chapter utilizes five in-depth case studies to examine political consideration behind the variations in the pension program we observe today. It demonstrates that two factors at the subnational level – 1) economic openness of the local economy, and 2) availability of the center's fiscal support – have major impacts on shaping provincial governments' redistributive incentives.

Chapter Six discusses how the center and provincial governments interact on the pension issue, using three in-depth case studies to process trace the back-and-forth negotiation between the two levels of governments. It shows that in addition to pension inequality across subnational regions, more importantly provincial governments were equipped with varying levels of political power when bargaining with the center. Regions with fiscal independence from the center have more autonomy than regions that have to rely on the center's fiscal support. Meanwhile, the center selectively strengthens its control over politically strategic regions, and relaxes its influences over those fiscally independent regions to further promote economic growth.

Chapter Seven concludes with a summary of major findings, and offers some implications for future research.

Chapter 2 A micro-level theory of redistribution in decentralized authoritarianism

2.1 Introduction

This dissertation seeks to understand authoritarian Chinese rulers' redistributive incentives. This chapter develops a micro-level theory to analyze Chinese central and subnational rulers' preferences on redistribution, and applies the theory to the pension case. This chapter breaks the conventional nexus between welfare development and democracy, and argues that welfare programs offer a valuable tool for authoritarian rulers to extend power tenure. In particular, mainly due to their vulnerability to exogenous shocks, one-party authoritarian regimes are oftentimes more pro-redistribution to secure a broad support base. Among various welfare programs, a public pension program is especially valuable for the ruler, as it promotes long-time bonding between the ruler and the ruled, helps register citizenship, and encourages multi-dimensional redistribution in the society.

However, the decentralized nature of the Chinese fiscal and administrative structure poses a great challenge to welfare development. How do central rulers differ from local rulers in their redistributive calculation? How does the Chinese central government ensure its subnational governments' compliance on welfare development? What factors contribute to the variations in the redistributive design of the pension program across subnational units? This dissertation notes that under the current political arrangement in China, subnational governments become *de facto* policymakers. This chapter differentiates redistributive incentives of central and subnational governments, arguing that the center is often more prone to welfare development than are subnational governments. By contrast, provincial governments are in general motivated to boost local economic growth through attracting and retaining investment, yet are more reluctant to

spare resources for welfare development. This chapter posits that the center employs fiscal subsidies to alleviate the principal-agent problem in welfare development. This chapter argues that the Chinese central government is more likely to concentrate its resources in regions 1) that suffer from economic instability, and 2) where ethnic minorities are concentrated. Furthermore, this chapter points out two factors that shape subnational governments' redistributive incentives: 1) the availability of the center's fiscal subsidies for welfare development, and 2) the level of economic openness in a locality. Based on these two factors, this study develops a two-by-two typology of provincial governments' redistributive incentives, and explains China's pension fiscal structure at the provincial level.

The rest of the chapter is organized as follows. Part Two discusses the redistributive incentives of authoritarian rulers, with a particular focus on rulers in institutionalized one-party authoritarian regimes, and on the political significance of a public pension program to the rulers. Part Three differentiates redistributive incentives for the central government and sub-national governments in the context of a decentralized fiscal and policymaking institution. Part Four develops a micro-level theory to analyze the Chinese central and subnational governments' redistributive decisions, and generates a typology of the pension program's fiscal structure at the subnational level. Following upon that, Part Four defines the Chinese center-local relation in welfare politics, and proposes a concept to be called *dynamic asymmetrical welfare federalism*. Lastly, Part Five concludes.

2.2 Redistributive incentives of authoritarian rulers

No society can work satisfactorily without political order (Huntington, 2006). The ultimate goal of authoritarian rulers of all types is to extend power tenure. However, the vulnerability of authoritarian rulers comes essentially from the fact that they do not exactly know

what the people think of the ruling regime unless some social unrest breaks out. To maintain power, under the condition of incomplete information about the society, the dictator has two principal options: repression or redistribution⁶ (Dahl, 1971). As Kirkpatrick (1982) famously puts, the rulers could hardly manage to control the masses through ideological and socioeconomic sanctions *if the constraints of coercion is removed* (emphasis in original, p. 123; also cited in Wintrobe (1998)). Therefore, armed forces become the most fundamental repressive tool. However, brutality comes at a price, both political and economic. This dissertation argues that while heavy reliance on repression is a double-edged sword and is oftentimes counter-effective to solicit public cooperation, redistribution offers authoritarian rulers a clear path to build up a reservoir of the public's long-term loyalty to the regime, and enhance economic productivity in a society, thus generating more rents for the rulers in the long run.

2.2.1 The costs of repression

Repression in fact can be a costly option for the ruler (Tyler, 2006). This study highlights three specific ways in which repression may incur enormous costs for the rulers: 1) costs of training and maintaining a repressive apparatus, 2) political dangers of expanding repression, and 3) costs from disrupting economic development. The first two costs are applicable to all authoritarian regimes, and the third is particularly prominent in regimes with economies that depend greatly on labor force participation.

First, in order to create a credible threat to foreign invasion, to monitor the domestic public, and to be ready to repress rebellious masses, the rulers need to be equipped with well-

⁶ There are various versions of the rulers' "two options". Wintrobe (1998) contends that the rulers have two instruments: political repression and the accumulation of loyalty from supporters. A problem with the second instrument, accumulating loyalty, is that oftentimes rulers are not clear who their supporters really are, since people who are currently indifferent might be potential supporters for the rulers. Thus, it is far from enough for the rulers to maintain power if they only target certain groups of apparent supports. In addition, Svoblik (2012) argues that dictators have two options to alleviate the problem in authoritarian control over the masses—repression and co-optation. According to Svoblik, co-optation is most effective when it works through party system. However, co-optation seems to co-opt social elites into the political system, instead of the general masses.

trained policing and military systems. Training and maintaining an effective repressive system is highly expensive. For instance, the Chinese government spent nearly 130 billion US dollars in 2014, ranked the second highest around the globe behind the United States whose spending level reached 580 billion US dollars (Cabaniss, 2015). However, despite the high costs of maintaining the repressive apparatus, the effectiveness of the armed forces in defending against political opponents and challengers is far from guaranteed. As Mann (1984, p. 200) points out the repressive state power becomes ineffective when faced with everyday individual-level behaviors, such as protests and petitions happening on a daily basis across the country. According to Mann, authoritarian rulers' power may be compensated by the employment of infrastructural power, namely setting up infrastructures and social institutions to penetrate into the civil society and obtain effective control of the society and economy.

Secondly, heavy reliance on repression causes not only budgetary but political problems (Svolik, 2012). Free from electoral pressure, in fact, authoritarian rulers are more sensitive to public resistance than their democratic counterparts are. However, excessive reliance on repression toward the masses would easily make authoritarian rulers blind to public demands. Without electoral channels, the dictator is already challenged by the information asymmetry problem when it comes to understanding the society, and an excessive use of armed forces would only intensify the problem at the rulers' disadvantage. In fact, instead of simply repressing the public, the rulers sometimes intentionally create certain safety valves to release public grievance, and also to obtain the information they need from the public (King, Pan, & Roberts, 2013). Second, a reliance on force is likely to arouse and escalate public resentment (Goldstone & Tilly, 2001). The escalation of public resentment may help rebels overcome the collective action problem and form cross-class coalitions, which poses greater threats to regime survival. In

addition, the employment of repression may turn non-violent activities into violence when confronted with violent repression (Lichbach, 1987). Thus, even though using the armed force may seem to be a convenient option for the rulers, it in fact may arouse unnecessary social and political conflicts.

Moreover, although repressive tools are set up as sticks against the disloyal masses, the sticks may potentially become a strong-armed instrument employed by opposition elites against the ruling group. This is the famous guardianship dilemma (Svolik, 2012). Professionalization of the military has led the armed forces to be a relatively isolated entity from civilian elites and the society. Studies have well established that maintaining loyalty of the military is at least as important and as challenging as creating a repressive apparatus (Belkin & Schofer, 2003; Skocpol, 1979). However, buying the military's loyalty by excessive power sharing is never wise. Studies find a strong correlation between the rulers' reliance on repression and the likelihood that the military elites would demand political powers over policymaking and intervene in domestic politics (Holmes, Maravall, & Przeworski, 2003; Svolik, 2012). Vulnerability of the rulers actually increases spontaneously as investment in the repressive agents expands. As such, rather than expanding state's repressive capability, an authoritarian ruler may in fact deliberately contain the power of his repressive agents.

Lastly, suppressing labor's demands has tremendously negative effects on economic development, which directly leads to a reduction in the rulers' revenues. To be sure, for dictators whose economies are luckily endowed with an abundance of natural resources to generate a healthy amount of revenues, they would not need to be much concerned about pleasing the labor force (Ross, 1999, 2001; Wantchekon, 2002). However, for most authoritarian rulers whose economies depend mainly on labor force participation, repressing workers simply means

disrupting the supply of the most important means of production. Also, an unstable social and political environment may deter economic growth, because for investors a stable business environment helps minimize investment risk and increase predictability of business performance (Alesina & Perotti, 1996). In addition, as Valenzuela (2001) notes, rapid development of technology and free market economy in today's world provides workers with many opportunities to disrupt economic production, and thus it makes simple repression less effective in eliminating labor movements as in decades ago, and the result of repression would only be counterproductive. Furthermore, for an economy that aims to transition from a labor-intensive economy to a skilled-labor and capital-intensive economy, like the Chinese one, the state needs to take on even more initiative to protect labor and nurture human capital. Therefore, instead of repressing labor, it would be in the rulers' best interests to accommodate workers' demands and motivate them to engage in productive activities.

To summarize the discussion above, merely relying on the armed force to maintain regime stability is unwise and even counterproductive. As a result, while maintaining a basic level of repressive capability is crucial for the rulers to claim authority, violent repression is often the last resort for a ruler. Thus, it is not surprising to find that authoritarian rulers often tie their hands. For example, in 1998 the Chinese central government issued an act regulating the use of violence in dealing with social resistance. The government distinguished between 1) political demands that challenge the authority of the party and government, and 2) non-political social grievances, as the government claimed as "contradictions among the people". The use of violence toward non-political demands is strictly prohibited by the act (Cai, 2008).⁷

⁷ For more details on this act, see Long, Xianlei (2001) "Jianchi 'yifazhiguo' fanglue tuoshan chuzhi quntixing shijian" ["Insisting ruling by law and appropriately handling instances of collective actions"], *Gongan yanjiu* [Research on Public Security], No. 12, pp. 50–53.

2.2.2 Redistribution: Towards long-term prosperity and stability

Redistribution is commonly used by authoritarian rulers in modern societies: from the universal entitlement program established in Iran under the Shah, to the expansion of social security program in Brazil under military rule during 1960s and 1980s, and to extensive social programs developed in one-party Singapore. Regardless types of authoritarianism, autocrats often adopt welfare programs to serve their ultimate goal of regime survival. This dissertation argues that the essence of employing redistributive programs is to increase the benefits of the status quo to the public while raising the costs of anti-regime behavior. More specifically, redistributive programs help authoritarian rulers 1) generate more economic gains for the rulers in the long run, and build up internal legitimacy, and 2) register the masses and create a reservoir of public support for the rulers.

First, welfare programs promote economic gains for the rulers in the long run. Wintrobe (1990) assumes that authoritarian ruler is a short-sighted power holder who seeks to maximize personal gain by minimizing redistribution. Rulers are more likely to grab whatever immediate benefits seem available in the society. Olson (1993) further differentiates far-sighted and short-sighted rulers. He argues that far-sighted authoritarian rulers would extract and redistribute, which could bring them larger future returns. In fact, the same self-interest that leads an autocrat to maximize his extraction from the society also gives him an interest in the productivity of his society (McGuire & Olson, 1996, p. 76). As a result, instead of extracting from the society without limit, far-sighted rulers are likely to create social programs, such as public education, healthcare, social security, and social assistance program, for long-term economic security, as these programs help develop human capital and thus promote economic performance in the long run (Heckman, 2000). However, one problem exists in this discussion – as Olson implies, the

time horizon of the rulers varies by institutional setting, but how institutions and the ruler's time horizon interact remains unclear. Wintrobe (1998) points out that rulers may not be concerned about promoting economic development, especially those generated from long-term investment, if they do not know the duration of their power; instead, immediate survival-related incentives are stronger. However, when their survival is secured, the rulers may learn to transform themselves from being political leaders to being propertied economic elites (Gershenson & Grossman, 2001). In other words, a secured political prospect extends the rulers' time horizon. We will come back to the discussion of the interaction between political institutions and the rulers' time horizon later in this chapter.

Moreover, a sustained economy does not only generate more long-term rents for the rulers, but also indirectly boosts public support for the regime. Muller (1985) notes that public discontent is not generated by inequality *per se* but rather is triggered by the gap between an individual's expected and achieved well-being. The prospect of economic development gives the public an expectation that their lives will be better tomorrow. It is often called vertical economic improvement. Evidence from survey data shows that vertical economic improvement has immediate and significant effects of enhancing the public's support and trust toward the government (Lin & Meng, 2016; Wang, 2005). In addition, for authoritarian regimes whose legitimacy is largely built upon the governments' economic achievement, most notably capitalist developmental states in East Asia (Evans, 1995; Wade, 1990), economic sustainability is crucial to regime survival. As studies point out, intra-elite splits and democratic transition are more likely to happen when the economy stumbles (Haggard & Kaufman, 1995). Therefore, government's spending on social programs indirectly contributes to order maintenance via promoting healthy and continuous economic growth.

Second, more directly, redistributive programs show benevolence of the rulers, buy off loyalty from the public, register citizenship and cultivate dependency, and thus increase the legitimacy of the regime. Welfare programs are important building blocks of authoritarian state building (Rimlinger, 1971). As Weatherford (1992) nicely puts it, legitimacy provides a “reservoir of support” to the institutions and regime. The purpose of setting up redistributive programs is to accumulate such support, with the payouts usually in the long run. Social programs require the rulers to reinvest the extracted resources on needed issue areas or regions, and thus involve an important aspect of redistributing rulers’ resources. The function of these social programs is not only to provide assistance to the needed or disadvantaged in the market economy, but politically more importantly to register citizens and cultivate dependence (Slater & Fenner, 2011). Scholars also view the state’s gesture of welfare provisions as nurturing a clientelistic relationship, and see welfare programs as “social contracts” between the state and the people (Haggard & Kaufman, 2008). To put it from the program recipients’ perspective, these social programs create a long-term bonding relation between them and the state, and thus raise the costs of anti-regime mobilizations (Doner, Ritchie, & Slater, 2005). In particular, when public grievance arises around specific social issues or concentrates in certain geographic regions, redistributive programs offer an option that could directly target the affected regions and population and could resolve the problem more effectively for the rulers. This option is particularly effective to address social discontent around labor related issues, since demanding more generous redistributive programs is oftentimes the goal of labor protests and strikes regardless in authoritarian or democratic societies (Sabel, 1982; Swenson, 1991).

In addition, we should also bear in mind that people tend to legitimate the status quo, even where it is in their disadvantage (Major, 1994, p. 309). This means that unless the

individuals are professional protesters (Lee & Zhang, 2013), ordinary people can self-process a certain level of political and economic disadvantages, and still remain obedient to the current regime. For the masses to take on high-risk political actions and to overcome the collective action problem, they need to be convinced that the price they pay for a rebellion would be paid off after a new regime is established. As people oftentimes discount future benefits, this motivation is usually weak among the public. The bonding relation created by social programs helps reinforce this mindset of the public by increasing benefits of the status quo and thus raising the tolerance level of the public to potential mistakes of the regime.

2.2.3 Welfare development in one-party authoritarian resilience

Among different types of authoritarianism, one-party authoritarian regimes are shown to be the most likely to employ redistribution. Here we adopt the widely-used division and definitions of three authoritarian regime types. One-party authoritarian regimes are those that are dominated and ruled by one political party. In military regimes, the armed forces control the government. Personalist regimes are ruled by one powerful individual who often is or claims to be the leader of a royal family, a clan, a tribe, or a kinship group (Geddes, 1999). There are two main reasons why one-party authoritarian rulers, compared with the other two types, are more prone to welfare redistribution.

First, given its vulnerability to exogenous opposition, one-party authoritarian rulers need to establish a reward/punishment system to justify their legitimacy. One-party rulers do not have the natural synergy with military leaders as in military regimes, neither do they have the charismatic leadership as personalist regimes do. Thus, one-party regimes are particularly vulnerable to opposition from outside the ruling group, namely the society and political rivalries (Geddes, 1999; Haggard & Kaufman, 2012). To justify their legitimacy, one-party regimes need

to create a broader institutional base than military and personalist regimes (Gandhi, 2008). To rally and manipulate this institutional base, as one-party regimes do not have the luxury to tap into the credibility of kinship ties or military backing, they therefore need to build a patronage and punishment regime. The patronage system distributes privileges to the people who show loyalty to the regime, and gives them a vested interest in the current system. In turn, the punishment regime punishes those who rebel by withdrawing the privileges (Lust-Okar, 2005; Magaloni, 2006). Studies also show that the punishment regime works particularly effectively to secure support from those who are financially dependent on state transfers, which in fact constitutes a majority of the masses in most cases (Lin & Meng, 2016; Zhong & Chen, 2002). Welfare programs are an important ingredient in this state privilege/punishment regime. Yet, the sustainability of this reward/punishment regime lies in the rulers' resource availability. The state-owned sector offers the rulers a convenient and reliable access to resources to fund these transfer programs. Therefore, scholars find that privatizing SOEs often leads to the collapse of one-party authoritarian regimes (Greene, 2007). For one-party regimes that underwent economic transitions, who controlled access to SOE resources and how the resources collected from economic privatization were distributed became critical questions that would directly affect regime stability.

Second, institutionalized one-party authoritarian regimes extend individuals' time horizons, and thus political elites in these regimes are more likely to redistribute for future benefits. Studies have reached a consensus that, thanks to the institutionalized political structure, one-party regimes are more stable and enduring than the other two types, whereas military regimes are more subject to internal disintegration, and personalist regimes are too dependent on individual leadership and thus hardly enjoy long-term stability (Gandhi & Przeworski, 2007; Geddes, 1999; Haggard & Kaufman, 1995). The key to the relative longevity of one-party

regimes is having a credible power-sharing mechanism in place, which could create lock-in effects between potential political rivalries and the rulers and substantially increase the costs of overturning the regime. Two institutions are key components of this power-sharing mechanism – the legislature, and the party organization. Granting legislative seats to potential opponents is a cooptation strategy to make rivals feel empowered and invested in the current regime. In addition, the legislature provides political actors a routine venue where negotiation, concession, and political coalition are realized. Constant negotiation and coalition-forming helps reduce dictators' predatory behaviors (Gandhi, 2008; Kim & Gandhi, 2010). Magaloni (2008) notes that using the legislature is insufficient in securing loyalty from opponents, yet an institutionalized party organization that can offer the prospect of progressive career advancement better motivates long-term loyalty. Geddes (1999) also finds that party organization helps unite different fractions to create a unified party elite group, and thus is more immune to intra-party elite splits. Equipped with the pseudo-democracy legislature and the party organization, one-party leaders are more patient and long-sighted, yet military and personalist leaders more resemble short-sighted rulers in Olson's model. As discussed, the prospect of losing power is more likely to induce rulers to engage in opportunistic behaviors to maximize short-term gains, whereas institutionalized power security supposedly induces rulers to redistribute for future benefits.

Despite the longevity of one-party authoritarian regimes, studies find that the probability of one-party regime survival dramatically falls after 40 years (Magaloni, 2008, p. 22). Given its over 60-year history, China is a particularly enduring one-party authoritarian regime with remarkable economic achievements. Since the Tiananmen Incident in 1989, the world scholar community has been debating when and how a democratic transition will happen in China (Fewsmith, 2001; Nathan, 2013; Pei, 1998, 2007; White, 1994). Others want to find the secret

formula that helps promote resilience of the Chinese regime. Nathan (2003) famously concludes that there are four main formal institutions that contribute to the Chinese regime's resilience: 1) the increasingly institutionalized succession norms and procedures, 2) the increase in meritocratic considerations, rather than fractional politics, in the promotion of political elites, 3) increasing functional specialization of government institutions after several rounds of institutional reforms; and 4) the creation of input institutions to increase political participation from the people. Shambaugh (2008) adds that the Chinese Communist Party itself is highly adaptive to the changing politics and society. Several "advance with the times" (*yu shi ju jin*) institutional reforms expanded the Party's support base, and enhanced its capability to retain its grip on power. Sheng (2009) calls our attention to the importance of territorial dimension of the regime's measures to enhance resilience. He argues that the central government strategically co-opts economically more resourceful but potentially more politically restive subnational regions to ensure its access to resources and thus prolong survival.

While most discussion of Chinese authoritarian resilience focuses on formal institutions, only a few studies explore the impacts of welfare programs on promoting legitimacy of the Chinese regime. Using the compulsory education program implemented in China, Lu (2014) finds that the program enhanced the public's trust toward the central government, and thus helped contribute to the regime legitimacy. Huang (2015) shows that Chinese local governments design and implement the healthcare program in ways that help maintain social stability in a locality. Building on these studies, this dissertation seeks to show how the Chinese government uses welfare schemes to construct its legitimacy, rationalize center-local relations, and further to lengthen its power tenure. As we noted above, one-party rulers' access to economic resources to fund social programs is crucial to the survival of the regime (Greene, 2007). Thus, the welfare

funding problem during economic marketization reforms becomes a matter of life and death for the regime leaders. How the Chinese government funded and operated its welfare programs amid market economic transition in the 1990s offers an empirically and theoretically intriguing question.

2.2.4 The significance of a public pension program

The public pension system is an important tool of redistribution, among sub-national regions, social groups, and demographic generations. A public old-age pension program that requires current employers to contribute to the program and fund the current retirees' pension benefits is often called a "pay-as-you-go" (PAYG) system, which is the focus of this study. Among various social programs, a public pension program is particularly important in an authoritarian ruler's redistributive toolbox for two reasons: 1) the associated long-time state-society bonding effect, and 2) three dimensional redistributions – inter-generational, inter-social groups, and inter-regional. To borrow a vivid metaphor of a PAYG pension program from one of my informants to demonstrate the time frame of public pension development: You start to cook a big pot of porridge when you are young, continuously add some rice to the pot throughout your working years, and have the porridge ready to eat when you retire (BJN0604131). This metaphor indicates two key features about a public pension program. First, it requires long-term continuous contributions to the program. Second, as it takes years for a pension account to mature, how much one pension participant contributes to the program in early years does not significantly affect the thickness of the porridge at retirement, or the wealth of the pension account.

Given these features of a public pension program, the role of a government becomes essential. First, the government needs to make a credible long-term commitment to participants

of the public pension program that their contributions will grow and be returned at retirement, and the paid-off benefits will likely be higher than the payouts of saving the contributions in individual savings accounts. Individuals may make myopic decisions and undertake insufficient retirement saving (Holzmann, 2009). A public pension program forces participants to save for retirement, yet do not take responsibility of investing the money against inflation. Doing so increases the rate of saving in a society, and also offers the government patient and stable capital for its long-term strategic investments, such as infrastructural development (Estevez-Abe, 2004; Manow, 2001). For participants of the public pension program, the cost of the “exit option”, namely overturning the regime, becomes higher as they continue to invest in the program. As mentioned, this is particularly relevant in one-party authoritarian regime, as citizens will only support the ruling party if they expect the regime will continue to distribute social goods (Kricheli, 2008) Thus, the long-term bonding relation between state and society generated by the public pension program is particularly valuable for one-party authoritarian rulers.

Second, a PAYG public pension program requires the government to redistribute economic resources in three dimensions: inter-generational, inter-social groups, and inter-regional redistributions, and favor those disadvantaged in the market economy. This three-dimensional redistribution involves high risks, in particular with respect to longevity risks, namely how long one person can expect to live following retirement, for the government to run the public pension program. As such, to manage the risks, it is usually done through pooling (Barr, 2002). A key advantage of a public pension program over a private plan is that it has the capacity to set up a pool large enough to spread risks and benefits across all participants. A national-level system that allows pooling of risk across sub-national borders would be ideal for a government to operate a public pension program. However, this function of redistribution

demands strong state capacity to extract economic resources from the society, and implement the redistributive policy down to the street level. Institutionalized one-party authoritarian regimes are often regarded as more capable of maintaining regime solidarity and steering national grand development strategies (Gandhi, 2008; Geddes, 1999). However, as we shall see below, it is a more complicated scenario where a one-party authoritarian regime also has decentralized policymaking and implementation institutions.

2.3 Welfare provisions in a decentralized political system

For a public welfare state to aim at universalistic and egalitarian ends, territorial centralization is essential, as centralization offers a primary means to assure equal provision regardless of location (Sellers & Lidström, 2007). Particularly, as stated, one obvious advantage of public welfare programs as against private ones is public programs' ability to pool risks across social groups and subnational regions. As such, nationalized welfare policymaking is often preferred. That to a certain extent explains the current welfare politics literature's biased focus on national politics, typically treating the state as a unitary actor (Esping-Andersen, 1990). This top-down approach assumes a passive role for sub-national governments, mechanically implementing policies designed by the center. As a result, the roles played by sub-national governments in the policymaking process are often understated in current discussions (Frazier, 2010). This approach is all the more problematic in dealing with large welfare states that are comprised of diverse sub-national units across a vast landscape, as is the case with China.

On the other hand, public policy scholars and policy advocates argue that to ensure effective implementation of a welfare program, empowering subnational governments is essential. In his famous *Fiscal Federalism*, Oates (1972) puts forward that if there are no economies of scale associated with centralized provisions, a decentralized pattern of public

outputs reflecting different local conditions will be welfare enhancing as compared to a centralized outcome. Empowering subnational governments and decentralizing public services to the local level were encouraged by scholars and international organizations (most notably, the World Bank, and the International Monetary Fund) as a remedy for underdevelopment in the developing world in the 1980s and 1990s (Ostrom, 1990; Putnam, Leonardi, & Nanetti, 1994). Local governments are believed to be more acquainted with local needs and thus be more capable of carrying out welfare programs that suit local conditions. Certainly, this decentralized approach assumes that either interests of the center and its subnational agents are in total agreement, or strong penetration of the central government to the local level to supervise proper implementation of the center's policy guidelines.

How the national government, as many have wondered, supervises subnational governments to make sure they faithfully carry out the welfare vision it desires, while granting local governments sufficient flexibility to tailor the policies to best serve local conditions? Chinese welfare development offers an ideal case to investigate this question. After a series of decentralization reforms in the 1970s and 1980s, the Chinese political system transitioned from a highly-centralized to a decentralized fiscal and administrative structure. Chinese provincial governments become supposedly self-sufficient fiscal units, with direct fiscal transfers between provincial units prohibited. While the central government proposes development guidelines, subnational governments are responsible for making specific policies regarding local social and economic development. Welfare provisions fall under subnational governments' responsibility. The classic principal-agent problem arises when the center and subnational governments have interests which do not coincide (Moe, 1984). The principal-agent problem looms large when it

comes to developing an expensive welfare program like a universal public pension that benefits constituents beyond local administrative boundaries.

Therefore, taking the above discussion into account, as welfare development constitutes one important strategy for the one-party Chinese regime to extend power tenure, how the Chinese national rulers coordinates with their subnational agents to deliver a public pension program to urban workers amid the market economic transition presents an intriguing question with both empirical and theoretical significance. As stated before, the public pension program shifted from a state-funded program to a PAYG system that requires contributions from both employers and employees in the 1990s to facilitate the market economic transition. In the beginning of the reform, the center granted subnational governments the right to adjust the center's reform proposal to local conditions until 1997 when the center sought to gradually centralize the policymaking power and create a nationally unified pension scheme. As two decades have passed, we still observe considerable variation in the redistributive design of the pension program across subnational units. This dramatic reform context offers an ideal historic background to investigate the interplay between the center and subnational governments on welfare provisions in a decentralized political structure.

2.3.1 Differentiating redistributive incentives of Chinese central and sub-national rulers

The present study argues that redistributive incentives differ between the Chinese center and local rulers, even though they are both authoritarian in nature – *while local governments in China more resemble short-sighted rulers, the central elites look more like the far-sighted type.* There are two factors that explain their different redistributive incentives – 1) ruler's time horizon, shaped by political institutions, and 2) the availability of other funding sources for redistributive programs.

First, recall the previous discussion on short-sighted vis-à-vis long-sighted authoritarian rulers (McGuire & Olson, 1996, p. 76; Olson, 1971; Wintrobe, 1998). As mentioned, if a ruler has stable interests in the domain over which his power is exercised, he may have more positive expectations toward the future and thus a longer time horizon. In other words, a ruler's time horizon is a function of how institutionalized a political system is – a system with a high level of institutionalization is likely to produce stable interests and thus longer time horizon of the ruler. In China, senior local officials are often assigned positions by the center, and personnel transfers from one region to another are common (Landry, 2008). That means that local rulers' time horizons are limited by the cadre appointment system for sub-national government officials. Especially during the economic transition period, promoting local economic growth was weighted heavily in officials' evaluation schemes (Li & Zhou, 2005).⁸ This economic-oriented cadre evaluation system still remains mostly the same today (Zuo, 2015). Sparring resources for welfare development is in conflict with local rulers' short-term interests in economic growth. In addition, Lü (2014) notes that in fact the central government collects the most credit for successful social programs, like free compulsory education. However, the public often blame local governments if the program fails, even though the failure may mainly result from insufficient fiscal support from the center. As a result, compared with the center, local government officials are more reluctant to devote resources for welfare development.

Second, an important difference between the center and local rulers is the availability of external grants and subsidies for welfare development. Qian and Weingast and their co-authors

⁸ The career progression scheme for government officials is not publicly transparent. Tsui and Wang (2004) argue that as of the mid-1990s, the system assigned 60 out of 100 points to targets related to economic performance. To conceptualize promotion, Shih et al. (2012) use the admission to the Central People's Congress as an indicator, and Svobik (2012) measures within-Party promotion in the *nomenklatura* system. Given the dual-track bureaucracy (*shuanggui zhi*) in China, this study defines career promotion in the system as any promotion that would increase the ranking within the Party and bureaucracies.

(Jin, Qian, & Weingast, 2005; Montinola, Qian, & Weingast, 1995; Qian & Weingast, 1997) introduce the concept of Chinese-style “market-preserving federalism” (MPF). Among the three key characteristics of MPF, hard budget constraints faced by both the center and local rulers are highlighted. The center indeed has a hard budget constraint, as it has to make its ends meet by reasonably allocating its limited fiscal resources. However, as Goldstein (1995) and Tsai (2004) note that while the center has hard budget constraints, local governments can soften the constraint by turning to the center for fiscal assistance when needed. Despite the center’s efforts to institutionalize the subsidy and grant fiscal system since the 2000s, special subsidy programs are common. The decentralized fiscal system in China has in fact led to market-thwarting behaviors, such as local protectionism and increasing fiscal responsibility of the center. Building on the existing discussion, the present study argues that *not all localities face hard budget constraints, and the center strategically relaxes fiscal constraints on certain localities*. The particularistic contracting system observed by Shirk (1993) in China during the 1980s still marks the flexibility of the Chinese center-local fiscal relations today. One of the effects of the flexible fiscal system is that costs of redistributive programs vary by locality. For regions that receive special subsidies for welfare development from the center, redistributive programs become less costly than their counterparts.

To be sure, by far-sightedness, this study does not imply that the Chinese central government always makes long-term leap-forward plans. The central government often makes decisions through “learning by doing”. In the setting of imperfect information, in practice, political actors take baby steps, muddling through the policymaking process (Lindblom, 1959). As Deng proposed, “crossing the river by feeling the stones underneath”, the center used experimentation for a variety of policies to address major social and economic problems, like

land reforms in the 1950s, the open-door policy in the 1980s and 1990s, and relaxation of the one-child policy in the 2000s. However, both bounded by limited rationality, as compared with local rulers, central rulers have more stable interests over the jurisdiction, and have a forward-looking vision of the overall development outlook for the country. Therefore, the center is more willing to sacrifice short-term benefits for longer-term interests.

2.4 A micro-level theory of pension politics in China

This section develops a micro-level theory of pension politics in China, detailing the redistributive incentives of Chinese central and subnational rulers in China and their interaction. Based on the discussion, this section generates hypotheses that help us better explain pension policy variations across subnational units in China as presented in Chapter One. The section includes two parts. The first part focuses on the central government, investigating 1) How does the center ensure subnational governments' compliance with the center's welfare development vision? and 2) How does the center allocate its limited fiscal resources across subnational units? The second part analyzes factors that shape subnational governments' redistributive incentives, and develops a typology of the pension program's funding structures in subnational China.

2.4.2 The center

As a principle, national leaders whose jurisdiction covers the whole country have more encompassing interests than local rulers do. The greater power and longer time horizon of the center suggest any power overturn would be prohibitively costly for them. As mentioned, the center values welfare development as an important strategy to extend power tenure, yet the high costs to develop welfare may turn subnational governments to evade the full welfare responsibility. As such, the center may use fiscal transfer as a tool to incentivize and regulate its subnational governments to deliver its development plan (Shih, Zhang, & Liu, 2010). Since

fiscal resources of the center for inter-regional redistribution are typically limited (with a hard budget constraint), any inter-regional redistribution necessarily involves an explicit calculation by the central government. Imagine local governments as kids in a family and the center as the family head (*jia zhang*). Being the family head of a household with 31 kids with diverse personalities and endowments, the central government in China must deal with one of the most complex fiscal systems. As regime survival is its ultimate priority, the center is likely to subsidize pension development in regions with political significance through fiscal transfers to ensure proper implementation of the pension program. However, the definition of political significance is too abstract to be helpful. What does the map of the center's fiscal transfer look like? And what specific factors shape the center redistribution decisions?

As order maintenance is the center's ultimate priority, this study contends that regions with a high likelihood of arousing political unrest are attached with highest political significance to the center. Two types of political unrest of the center's particular concerns are identified: 1) economy-induced unrest, and 2) politics-induced unrest. Economy-induced political unrest was of great relevance in the economic transition period. Before economic reforms, the planned economy had achieved almost full employment in urban localities. However, SOE reforms resulted in a wave of massive layoffs that significantly increased the urban unemployment rate. A sudden increase in numbers of laid-off workers in a short time window added additional pressure on the pension fund to support the aging population. Interrupting retirement benefit provisions aroused public anger, and threatened regime legitimacy. In addition, compared with long-term unemployed workers, laid-off workers are of particular concern for the government, as they would have previously formed interaction networks at their work place, which helps alleviate potential collection action problems when organizing large-scale protests. The increase

in layoffs becomes a triggering factor that sparks grievance of the unemployed. As a result, the unemployed, including laid-off workers, form a social group with a clear political identity and demands. As seen in the second half of the 1990s, large-scale violent pension protests certainly became a political issue in some regions (Hurst & O'Brien, 2002; West, 1999). The center's fiscal support for these regions to support pension development could directly target the discontented groups and alleviate social tension. Thus, we may suspect that the center is more likely to concentrate fiscal resources on regions that are suffering from high unemployment rates.

H1-1: The center is more likely to redistribute via transferring fiscal resources to regions with high unemployment rates.

The second type of political unrest, politics-induced unrest, focuses on ethnic conflicts. Ethnic clash is a common factor that triggers civil wars in a country with multiple ethnic groups (Collier & Hoeffler, 2004), and ethnic cleavages deepen as social and economic inequality increases along ethnic lines, which shapes the intensity of ethnic conflicts (Esteban & Ray, 2011). Almost all governments challenged by ethnic conflicts spare no efforts on ethnic relations, and the Chinese government is no exception. The Chinese government granted autonomous region status to five provinces with high percentages of particular minority ethnic populations, and these local governments enjoy more legislative rights than ordinary provincial governments. The central government, which is overwhelmingly dominated by Han Chinese, often seeks to preempt violent inter-group confrontations and the escalation of ethnic tension into potentially large-scale political crises. The Chinese central government has granted a series of preferential policies to ethnic minority regions, ranging from family planning, hiring and promotion, financing and taxation of businesses, and regional infrastructural support (Sautman, 1998). As mentioned, redistributive programs provide a convenient co-optation tool for the center.

Distributing more fiscal resources to ethnic minority regions involves two advantages for the center: 1) economically, it narrows the gap of inter-group inequality, a key factor that sometimes ignites ethnic tension; and 2) politically, it not only helps (re)gain local population's political loyalty, but also signals the center's greater political emphasis on those areas with high ethnic concentration. In all, we have a basis to predict that:

***H1-2:** The center is more likely to transfer fiscal resources to regions with high concentrations of ethnic minorities.*

Moreover, these two factors that potentially trigger political unrest may have cross effects. Table 2-1 lays out four possibilities that result from interaction between the two factors, unemployment and ethnic concentration. Category (A) indicates a situation where a high unemployment rate is coupled with a high ethnic concentration rate, and there are good reasons as discussed above to expect that regions falling into this category are likely to receive the most fiscal transfers from the center. Category (B) and (C) represent cases that have lower scores in either one of the two factors, but one factor that can potentially trigger instability is sufficient to arouse the center's attention. Lastly, Category (D) represents cases with neither a high unemployment rate nor high concentration of ethnic minorities, and these cases, not sensitive in either way, are least likely to receive fiscal transfers from the center. These four scenarios are all hypothetical, which means that there may not be any case to fit in each of the category. For instance, no strong evidence has been found as yet to match Category (A).

Table 2-1 The center’s hypothetical redistribution patterns

		Unemployment rate	
		High	Low
Ethnic concentration	High	(A) A highest redistribution rate	(B) A higher redistribution rate
	Low	(C) A higher redistribution rate	(D) A lower redistribution rate

2.4.3 Local rulers

As we discussed earlier, short-sighted local rulers often have little incentive to redistribute unless they face social unrest; they are instead being motivated to promote local economic growth. Thus, local rulers’ opportunistic decision of evading full welfare responsibility in exchange for immediate economic benefits may be in direct conflict with the center’s concerns over keeping order. However, this does not imply that local rulers do not care about political order in their localities. On the contrary, major social unrest in a locality could directly halt an official’s career advancement (*yi piao foujue*). Instead, what this study suggests is simply that, when it comes to redistribution programs, motivated by their economic-oriented mindset, local rulers will have an inclination to create a less expensive welfare system than the center seeks. To put it differently, local rulers are likely to create redistributive programs upon the center’s request, but they may relax the center’s requirements for their own short-term interest. When directly challenged by social unrest, instead of distributing public goods to the general public to pacify social grievances, local rulers may choose to target individual opposition leaders to regain short-term control (Lee & Zhang, 2013).⁹

As subnational governments seek ways to reduce the costs of funding this compulsory pension program, two immediate questions for subnational governments are 1) from whom to

⁹ This point was also confirmed by an informant from Guangdong (GDP0421151).

extract pension revenues, and 2) how much to extract. The more they extract, the more resources will be available for the government to allocate to the targeted population. Given the fact that extraction works like taxation, contributing to the pension program may incur higher immediate costs and thus reduce economic efficiency of economic entities that pay the contributions. Therefore, high tax rates significantly increase individuals' incentives to evade contribution (Allingham & Sandmo, 1972; Clotfelter, 1983). In order to promote an efficient collection of taxation, the government may levy taxes primarily on commodities that are inelastic in demand or supply. More generally, that means that the rulers need to strategically choose tax-payers that are bounded in certain ways to tax. In a similar vein, SOEs, compared with private and foreign investments, are less able to avoid contribution responsibility, since the activities of SOEs are often confined within physical boundaries of political administrative units. It is more convenient for the government to enforce SOEs' contributions, so subnational governments may tax SOEs more heavily. From SOEs' perspectives, higher pension contributions and the resulting higher retirement benefits after retirement are often regarded as a bonus of SOE employment, which is used to attract and retain young talent (Huang, 2015). In contrast, as studies on inter-jurisdiction competition suggest that the profitability and mobility of foreign and private investments means investors can seek the best fit to locate their business. In order to invite mobile investments to come, rulers – authoritarian ones in particular – are willing to grant favorable terms to them, including lower contribution to the public system, which is also commonly called “race to the bottom” (Garrett & Mitchell, 2001; Revesz, 1992). As a result, these subnational governments need to fund the pension program from other sources.

The center's fiscal support is one source of funding, yet the level of fiscal support subnational governments receive varies by locality. As discussed in the prior section, the center

seeks to incentivize its local agents via direct fiscal transfers to make sure they deliver the welfare programs that the center desires, especially in localities that are vital to the center's strategic interests. Even though every local ruler is eager to gain more funding from the center, when it comes to dividing the center's fiscal cake, local governments most of the time are passive grant recipients, and room for negotiation with the center is very limited. Local rulers do not generally know how the center calculates the amount of transfers. They do know that the amount they get this year will be used as a base line for next year's calculation. Local governments from different localities do not generally communicate how much subsidy they receive from the center, as both the center and local rulers deem the information highly sensitive. As a result, some provinces get a larger piece than the others, and the inequality endures and even increases over time (BJC0614131, FJN0630131, and HBP0708132). Of course, there are other informal ways in which local rulers could compete for greater subsidies from the center. First, local rulers may "run ministries for more subsidies" (*pao bu qian jin*). The most well-known channel is perhaps through each province's (even cities' and counties') Beijing office (*zhu jing ban*). However, the room for negotiation is quite limited. Second, being policy experimental bases (*zhengce shiyan jidi*) brings subnational governments direct fiscal transfers and also other counterpart funds (*peitao zijin*). Yet it is highly competitive to be selected as an experimental base.

The center's subsidy program reduces the costs of redistributive programs felt by local rulers. In other words, for those who receive more subsidies from the center, redistributive programs become less expensive for them. Here this dissertation utilizes the concept of *cost externalization*, under which some actor other than the decision maker absorbs some or all of the costs associated with a decision (in this case, to promote pension development). Weingast et al.

(1981) point out that when a project is funded through national generalized taxation and yet has identifiable geographically targeted beneficiaries, there will be political decisions that systematically bias outcomes toward inefficiently large local "pork barrel" projects. In other words, when political actors can externalize the costs of a project that substantially benefits their geographically-defined constituents, such actors will tend to maximize local interests at the expense of the general national budget. Subnational governments that receive the center's special grants on welfare development are more incentivized to develop local welfare. However, without a rigorous supervision mechanism that closely monitors how the subsidies are used at the local level, the agent's moral hazard problem emerges – local rulers may vary the degree of flexibility of using the supposed welfare funding, and divert the funding for other purposes.

Therefore, according to the level of fiscal support received from the center, this dissertation classifies the sub-national units into two categories: 1) localities with, and 2) localities without major and sufficient fiscal support from the center. Since the amount of pension fund debt varies by locality, it makes sense to measure the fiscal support a locality receives from the center by the percentage of local pension spending that comes from the center's fiscal transfer for the pension program.

First start with regions that receive major fiscal support from the center. As stated before, there are two major reasons that the center grants substantial fiscal transfers to a locality – 1) economy-induced or 2) politics-induced political instability. Local rulers of these two types react differently toward the center's funding (see Figure 2-1).

First, for regions that suffer from economy-induced political instability, reviving economic productivity and maintaining political stability are two priorities. Under depression a promising economic outlook often helps rulers quickly regain political confidence and stabilize

social conditions (Haggard & Kaufman, 1995). A healthy economic system also generates more employment opportunities, which consolidates the pension fund and alleviates the immediate pension deficit crisis. Attracting more business by increasing economic openness is often chosen by government as a solution to revive the economy. Furthermore, creating a non-SOE economic pillar is the guiding policy from both the center and local governments during the transition period. In contrast, raising employer's contribution rate is less preferred, since increasing labor costs does not help business recover nor attract new business during an economic downturn. Therefore, local rulers are likely to see the center's pension subsidy as leeway to promote economic growth by reducing the pension contribution rate. In turn, the responsibility of filling pension deficits is pushed to the next local rulers who are appointed to take the position. As a result, with the center's fiscal support, these regions may still have a high level of pension fund deficits due to the lower contribution rate requested.

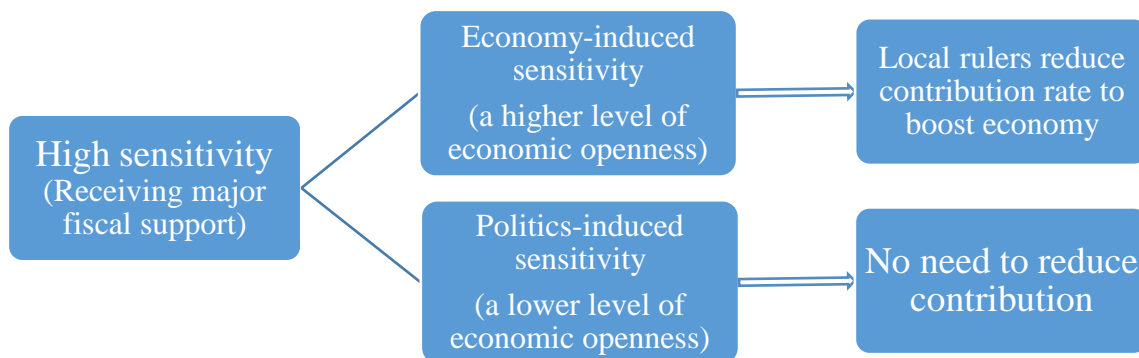
H2-1: Local rulers challenged by economy-induced political unrest may use the center's pension subsidy to reduce employers' contribution rates in order to revive the economy.

Second, instead of promoting economic growth in general as regions with economy-induced unrest do, regions with politics-induced unrest have a well-targeted population, ethnic minorities, to reach. Rulers in these regions need to make sure that economic gains equally benefit all groups, if not even better for the specific group of people that may potentially ignite unrest. Thus, to effectively pre-empt political unrest, rulers are likely to use fiscal transfers from the center in the form of government subsidies to the targeted group. In addition, economic development is not as urgent a task as it is in other parts of the country, because the governments, both central and local, are cautious of undertaking any aggressive approach to assimilating these

minority regions. As a result, economic opening up in these regions has been at relatively slower pace compared with the rest of the country. We may reasonably expect that:

H2-2: Regions with politics-induced unrest are likely to have a higher contribution rate than regions with economy-induced unrest, and special pension-related subsidy programs implemented for ethnic minority groups.

Figure 2-1 Categorizing sub-national regions (Part 1: regions receiving major fiscal support from the center)



As mentioned, the center’s fiscal resources are unevenly distributed among sub-national regions. That means that some regions do not have the fiscal luxury the regions in Category One enjoy. There are two possibilities with the regions that do not receive much fiscal support from the center. First, regions that suffer from the lack of financial support from the center have to find ways to fill the pension deficits. These local rulers have two options to overcome the funding problem of the pension program: 1) to fund the program by setting a higher employers’ contribution rate, and 2) to employ local fiscal budget to fill in the gaps from shortfalls in the central government support. Second, some regions are fortunate enough to have sufficient pension fund surpluses, and do not count on the center’s fiscal transfer (see Figure 2-2).

First, start with the regions that do not gain much support from the center yet have a constant struggle financially to run the pension program. Rulers in these regions may apply for more fiscal support from the center; however, as stated before, the center's fiscal distribution decision allows very limited room for local rulers to negotiate. As such, subnational governments oftentimes have to live with the resources at hand. As discussed before, local rulers have two options to choose from – 1) to subsidize the pension program by using local fiscal resources, and 2) to extract more from employers to fill the deficits. What are the differences between the two options? And under what circumstances rulers are likely to prefer one option over the other? Compared with option 1, option 2 directly transfers the pension funding problem caused by the lack of the center support to employers in the locality, by asking them to contribute more to fill the funding gap. Recall the discussion of rulers' pro-economic growth strategies in the previous section – increasing the pension burden of employers may lead to capital flight in an open economy, especially when the investment is mobile in nature, mainly foreign investment (Oi, 1992), and inward flows of foreign direct investment (FDI) is a key measurement of local government officials' performance (Whiting, 2004). Therefore, in open economies, where local economic development is largely dependent on attracting foreign investments, the government has to pay from its own pocket to keep the contribution rate low and ensure proper operation of the pension program.

H2-3: Regions that are economically dependent on mobile investment are likely to subsidize the pension program with local fiscal resources to keep the contribution rate low.

H2-4: Regions where the level of economic openness is lower, meaning that state investment is a high proportion of all investment in the economy, are likely to increase the contribution rate for employers to fill pension deficits.

Second, while some regions are suffering from the lack of the center financial support, other provinces will have accumulated a fair amount of pension fund surpluses mainly due to limited mobility of pension accounts across regions. Thanks to the center's marketization reforms first implemented in these areas in the late 1970s and early 1980s, these regions feature the most vibrant market-economy business environments in the country today. Like a gold rush, migrant workers fluxed into the regions seeking their life fortunes. They (their employers on their behalf) contribute to the local pension pool, but due to the high mobility associated with their jobs, they often relocate to pursue higher paychecks before they become eligible for retirement payment in one locality. Due to the limited portability of pension programs across sub-national administrative borders, these migrant-receiving localities have accumulated a considerable amount of pension fund surpluses (Lin, 2015). These governments' fiscal affluence earned these eight provinces a nickname, "fiscal G-8", among the Chinese academic community (BJN1115121). Pension fund surpluses give governments of migrant-receiving regions a high level of flexibility to reduce employers' pension burden to further propel economic growth, which creates a powerful virtuous circle that attracts both investment and cheap labor to come and secures these regions' economic advantage.

H2-5: Regions with pension fund surpluses, thus enjoying complete fiscal independence from the center, afford to reduce the contribution rate to attract more investment.

Figure 2-2 Categorizing sub-national regions (Part 2: regions NOT receiving much fiscal support from the center)

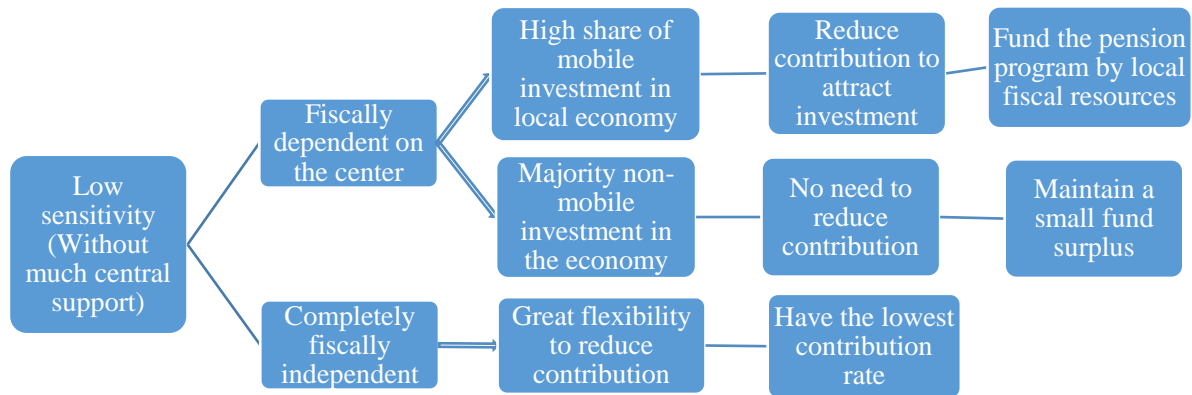


Table 2-2 below summarizes local rulers’ reactions in response to 1) local economic structural conditions (economic openness), and 2) fiscal resources granted by the center. The interaction pattern depicted here between the center and local officials tells us five different stories on how local pension programs are funded and operated.

Table 2-2 A typology of fiscal structures of local pension programs

		Economic openness	
		High	Low
Political instability → level of center fiscal support	High	Scenario I. Economy-induced unstable regions	Scenario II. Politics-induced unstable regions
		Local rulers receive major fiscal transfers from the center, but use the funding to run the pension program and keep contribution rates low to revive economic growth (e.g. Liaoning Province)	Local rulers receive major fiscal transfers from the center, and use the funding for subsidy programs to pacify targeted groups in order to maintain political order. Employers' pension contribution rate remains unaffected (e.g. Tibet)
	Low	Scenario III. Open development zones	Scenario IV. Inland agricultural center
		Without sufficient support from the center, rulers have to use local fiscal budget to keep the contribution rate low to attract new investment (e.g. Hunan)	Scenario V. *Rulers with full fiscal independence from the center have the flexibility to keep the contribution rate low (e.g. Guangdong)
			Given insufficient support from the center and the dominance of state investment in the economy, rulers need to set a high contribution rate to fund the program (e.g. Gansu)

Note: * indicates that regions with fiscal independence from the center are a sub-category of the group of open development zones.

2.4.4 Dynamic asymmetrical welfare federalism in China

The pension case offers a great venue to investigate Chinese center-local relations in welfare politics in a decentralized political context. The debate on decentralization simply assumes a top-down streamlined implementation of a universal welfare program or a bottom-up local-oriented welfare design that suits local needs (Oates, 1972; Ostrom, 1990; Sellers &

Lidström, 2007). This study depicts a more dynamic interactive relation between the center and subnational governments. It argues that once the welfare policymaking power is delegated to subnational governments, it is very difficult to centralize the power as subnational governments have developed interests in the current welfare arrangement, particularly those who have benefited from the current system design. In the decentralized structure, the Chinese central government must use fiscal transfers as a leash to lead and restrain its subnational governments. Yet subnational governments often find leeway to adjust the center's policies to best serve local conditions. In particular, subnational regions that do not count on center fiscal support seem to have more policy autonomy than those that rely on center support. The Chinese pension case explains much frustration of the central government in steering the development of the pension program under the current decentralized administrative structure, and the resulting uneven welfare development across sub-national regions.

Previous studies have noted that local governments have become the gatekeeper to the realization of the center's welfare goals due to the decentralized fiscal and administrative structure in China (Huang, 1999). While the Chinese central government only proposes policy guidelines, Chinese sub-national governments, mostly provincial governments, become *de facto* policymakers in welfare affairs. In a comparative perspective, China is also one of the most fiscally decentralized countries in the world (Xu, 2011). One result of this high level of decentralization is that welfare development outcomes may be greatly diverted from what the center originally seeks. For example, Solinger and Hu (2012) note that in the implementation of the urban social assistance (*di bao*) program, local governments implement the policy based on their interpretation of the center's policy guidelines, and they interpret in ways that matches local officials' best interests in political career promotion. As a result of this localized randomization

of policy implementation, studies find that fiscal decentralization may greatly enhance local government officials' chances of promotion, yet negatively affect provision of public services and long-term well-being of local residents (Qiao, Fan, & Feng, 2005; Wang, Zheng, & Zhao, 2012).

Instead of coming to a sweeping conclusion on the erosion of the Chinese central government's control over subnational governments, this dissertation argues for a more nuanced understanding of China's welfare federalism. This study contends that two distinct scenarios of center-local relations exist in the case of pension politics in China, categorized by the availability of the center's fiscal subsidies to local governments – 1) regions fiscally dependent upon the center, and 2) regions with complete fiscal independence. Localities with deficits depend financially on the center, and always look for chances to expand the portion of the center's fiscal resources they receive. However, fiscal subsidy programs offer the center a great opportunity to contain subnational agents. The center can vary the level of subsidy to advance its own goals. When the center detects localities' improper use of subsidies, it may reduce the subsidy level or mandate a rectification. Prior studies also draw a similar conclusion that the center maintain grassroots officials' obedience through fiscal transfers (Shih, Zhang, & Liu, 2010). As a result, these fiscally-dependent localities are likely to work to their best to deliver what the center desires, especially when the center's goals coincide with local governments'. In sharp contrast to these regions, fiscally independent regions are expected to have more autonomy in policy-making processes, and can sometimes even act counter to the center's decisions. Therefore, governments in these fiscally independent regions have more bargaining power with the center in this center-local "negotiatory relationship" as Zhao (1992) puts it. We will expect to see greater policy departure from the center's commands in these localities.

H3-1: The center is likely to use its fiscal power as a leash to restrain rulers in regions that are fiscally dependent on the center.

H3-2: Regions that are fiscally independent of the center have more policy autonomy than the regions dependent on the center's subsidies.

This dynamic center-local relation tells that the center selectively concentrates its resources and power over politically strategic regions, and fiscal subsidy may offer an effective way for the center to manipulate its subnational agents. The relaxation of the center's control over fiscally independent regions may be explained by two equally important mechanisms. First, these subnational regions indeed have more economic and political resources to demand more political autonomy from the center. Second, the center may intentionally turn a blind eye toward these regions to grant more autonomy and motivation to local agents and to help promote economic growth (Montinola et al., 1995). In the end, these regions are the economic engine of China, and their economic success speaks to the regime's legitimacy at the national level. Yet this asymmetrical welfare federalism has determined that the Chinese central government may compromise welfare development to meet economic demands particularly in those affluent regions. This dissertation seeks to present a big picture of reciprocal relations between the center-local political system and urban pension program. This interactive relationship creates an institutionalized feedback loop that reinforces the existing political and welfare inequality across sub-national regions in China (Frazier, 2010; Pierson, 2005).

2.5 Conclusion

This chapter starts with an assumption that authoritarian rulers have a strong desire to extend their power tenure, and the rulers mainly have two principal options to achieve that goal – repression and redistribution. This chapter argues that authoritarian rulers cannot rely solely on

repressive tools to secure their ruling because it is both economically and politically expensive. In particular, long-sighted authoritarian rulers employ welfare programs to buy off the public and promote long-term economic development. However, in this globalized world, capital mobility gives investors with mobile assets more bargaining power with governments to obtain more favorable investment terms. Therefore, rulers often relax taxation policies to reduce these investors' operating costs, including discounting investors' welfare responsibility. Moreover, welfare development becomes a more challenging task in a decentralized political setting. This dissertation argues that while the central elites more resemble long-sighted authoritarian rulers with more over-compassing interests, subnational governments are more short-sighted, being more motivated to promote local short-term economic growth. This chapter develops a micro-level theoretical framework to explain redistributive incentives of the center and subnational governments, and examine the interaction between these two levels of political actors in welfare politics.

This study applies this framework to explain pension politics in the one-party authoritarian Chinese regime with a decentralized administrative and fiscal structure. Specifically, this study seeks to differentiate redistributive incentives of Chinese central and subnational rulers, and how these incentives shape the formation of pension policies at the subnational level. This dissertation argues that the center's redistributive incentives are shaped by their concerns over political instability (measured by economic volatility and geographic concentration of ethnic minorities) in specific regions in China. This chapter posits that the center is more likely to channel fiscal resources to regions suffering from political instability. Local governments' redistributive incentives are shaped by the availability of center fiscal support and the mobility of investment assets in their administrative units.

Based on these arguments, this chapter develops several hypotheses to test in the following chapters. First, the central government is more likely to subsidize localities with high unemployment rates and geographic concentration of minorities—two factors that signal high risk of political unrest. Second, localities which rely on mobile capital are more likely to set lower employer pension contribution rates than other localities from the fear of capital flight. Combining these two sets of predictions, there are four scenarios of the funding structures of local pension programs. First, localities with major fiscal subsidies from the center and a high percentage of mobile investments in local economy are likely to see the subsidies as way to lower the contribution rate. Second, localities with major center fiscal subsidies and a less mobile economic profile are likely to set a higher contribution rate. Third, localities that are without much fiscal support from the center and economically dependent on mobile investments are likely to subsidize the pension program from local fiscal resources to keep the contribution rate low. Fourth, localities without much fiscal support from the center and economically with less mobile capital can afford to raise the contribution rate to compensate local pension funds for the lack of center fiscal subsidies. Lastly, this chapter hypothesizes that regions that are fiscally independent from the center enjoy more autonomy than regions that count on center fiscal support.

Chapter 3 The development of the pension program

3.1 Introduction

This chapter discusses how the fragmented and decentralized pension program came about in China – how it transitioned from a key component of a socialist-style welfare package to a three-pillar pension design, why the center allowed subnational governments to adjust its policies according to local conditions, and how the pension program’s past experience shaped its current development path. This chapter seeks to demonstrate that regardless of the policy design of the pension program, it has always been an organic part of the overall political and economic development strategy. The evolution of the pension program was politically driven. Therefore, this chapter builds a foundation for the subsequent discussion in this dissertation.

Created in 1951, the urban pension program for enterprise employees has evolved dramatically over the sixty-year course of its development. Under the planned economy, the socialist-style pension program was a key component of the state-funded welfare system that took care of SOE employees’ wellbeing from employment to post-retirement life. This “cradle to grave” welfare system was interrupted during the Cultural Revolution period. As the national pension pool dissolved, the pension program essentially turned into an enterprise-based insurance program in practice, with individual enterprises bearing all the risks and responsibilities of funding and managing their own pension programs. This enterprise-level pension insurance program became a serious handicap to further SOE reforms and economic transitions. Entering the 1990s, to facilitate economic transitions, the Chinese central government carried out a series of reforms to convert the old socialist enterprise-based pension programs to a multi-pillar public program that covers urban employees regardless of the nature of enterprise ownership. Via these reforms, the center attempted to re-create a nationally unified pension

system that accommodated the needs of a new market economy. This chapter situates the Chinese urban pension program in the context of social and economic development, which helps us better understand how the current pension program came about.

The remainder of the chapter unfolds chronologically and pauses at critical junctures of the pension development. The second section discusses the socialist-style pension scheme under the planned economy, and its collapse during the Cultural Revolution. The third section examines the need to transform the pension program entering the reform era of the late 1970s and 1980s. Following upon that, the fourth section introduces pension reform trials at the national level in the early 1990s, which put the pension system on a path toward decentralization and fragmentation. Section Five discusses the 1997 landmark pension reform and the center's ambition to create a nationally unified pension scheme. The sixth section comments on the center's proposal to consolidate individual pension accounts in the 2000s and its failure. The seventh section reviews the center's recent efforts to reform the program to correct its development path, and their mixed results. The eighth section summarizes the evolution of the pension program and discusses challenges arising from the resulting localized pension program.

3.2 Socialist-style centralized pension scheme

In 1951, soon after the founding of the People's Republic of China, the State Council issued Labor Insurance (*lao bao*) Regulation, which marked the creation of the first insurance system including old-age pensions, healthcare, maternity insurance, and work-related injury protection. That system was modeled on the Soviet-type socialist welfare state, so-called "cradle to grave" protection. The pension program included in the welfare package was a strict PAYG system. It required employers to submit 3% of payroll, where 30% of the 3% contribution was submitted to All-China Federation of Trade Unions (ACFTU) to create a national social security

reserve, which had the function of inter-regional redistribution. The remaining 70% was managed by local-level trade unions. The local pension funds were used to pay for retirees' benefits, with central funding to adjust inter-regional fund sustainability. In other words, the pension program was a national insurance program, pooled at the national level. No separate budget for the pension program at both the central and local levels, as governments used general fiscal revenue to support pension provisions.

This 1951 pension program started with very narrow coverage – only enterprises (including SOEs, joint state-private enterprises, and collectively-owned enterprises) with more than 100 employees, and enterprises in railroad, shipping, and post and telecommunication sectors were allowed to participate in the program. It needs to be noted that ownership of enterprises bore no weight in this initial qualification criterion. In 1955, the State Council amended the Regulation, and lifted the 100-employee qualification minimum. With restoration of economic development, in 1956 program coverage expanded to enterprises in commercial, foreign trade, financial, petroleum, geological, fishery, farming, and forestation industries. After the expansion, by the end of 1956 the pension program covered 94% of employees in all participating industries. The replacement rate of the program was between 50 and 70 percent -- retirement payment for those who had served 15 years or more was 70% of pre-retirement salary, and those with less than 15 years but more than 5 years would receive 50% (Song, 2001). However, after the Socialist Transformation Reform (*shehui zhuyi gaizao*) in the 1960s, enterprises with private and individual backgrounds were all regarded as “capitalist tails” being cut off. Thus, SOEs and COEs became the only economic entities in the economy and thus the only participants in this pension program.

During the Cultural Revolution in the 1960s to 1970s, the labor insurance program was criticized as a product of revisionism and capitalism, thus being terminated. In 1968 the national pooling system collapsed, and each enterprise created and managed its own pension program. In 1969 the MOF issued *Reform Suggestion on SOEs' Financial Transactions*, categorizing welfare spending as enterprises' non-operating outlay. Therefore, the pension program essentially became an "enterprise-based insurance" program. In this enterprise-based pension system, risks and financial responsibility were pooled within each enterprise. Thus, the profitability of an enterprise directly affected the generosity of its pension program. While some enterprises struggled financially to pay retirement benefits in a timely manner, others provided benefits with a near 100% replacement rate in relation to pre-retirement income (Zheng, 1994, p.122).

In 1978, after the ten-year period of turmoil, the State Council issued a *Temporary Provision on Enterprise Retirement* to restore the pension insurance program. The Provision stated that men at 60 years old, and women at 55 years old who had at least worked for consecutive ten years were eligible for retirement benefits. In addition, the Provision set high replacement rates for retirement income. Workers with more than twenty years of service would receive 75% of pre-retirement wage level as post-retirement income, those with more than fifteen years and less than twenty years of employment would be 70%, and fewer than fifteen years would be 60%. The efforts to facilitate restoration of the program was reemphasized by the State Council in its *1981 Notice on Strictly Enforcing Enterprise Retirement*. In addition, this Provision included a substitute policy, which also promised to offer a job position per retiree to their immediate family members. In other words, it urged employees in SOEs who were approaching retirement ages to leave positions for the younger generation. It was a policy designed to resolve the employment problem of millions of the educated urban youth who had

been sent to rural areas during the Cultural Revolution. According to official statistics, 16.5 million young people were sent to rural areas between 1967 and 1979, and by 1979 a total of about 15 million had returned to cities (Wang, 2008). A direct result of this substitute policy was a sudden increase in the number of SOE retirees. In 1978 there were only 2.84 million retirees nationwide, and by 1986 the number reached 13 million. This policy-directed retirement wave led to a skyrocketing fiscal spending on retirement benefit provisions. The amount of total retirement income payments increased significantly from 1.6 billion *yuan* to 13 billion *yuan* during the same period (Jiang, 1987). Enterprise contributions made up a major source of the payments, with the center bailing out the deficits (Xu & Wan, 2009). As the fiscal boundary between SOEs and the government was not clearly defined, SOEs were still able and willing to shoulder the heavy pension responsibility.

3.3 Pension program amid initial political and economic reforms

Stepping into the economic reform era since the late 1970s, the center initiated a series of political and social reforms to facilitate the economic transition. To depart from the original highly-centralized planned economy and transition into a market economy, the government knew it should first withdraw itself from the economy, and return the economic control to market mechanisms. The center implemented fiscal and administrative decentralization reforms, to grant substantial powers and rights to subnational governments. A market-oriented management system was introduced to SOEs, and non-SOEs started to mushroom. During this reform period, wherein basic political and economic structures were undergoing profound changes, deep-seated social problems, such as enterprise-based welfare provision, were surfacing. These social problems were obstacles to further economic reforms, and posed direct threats to the legitimacy of the socialist regime. It was in this context that pension reforms were launched.

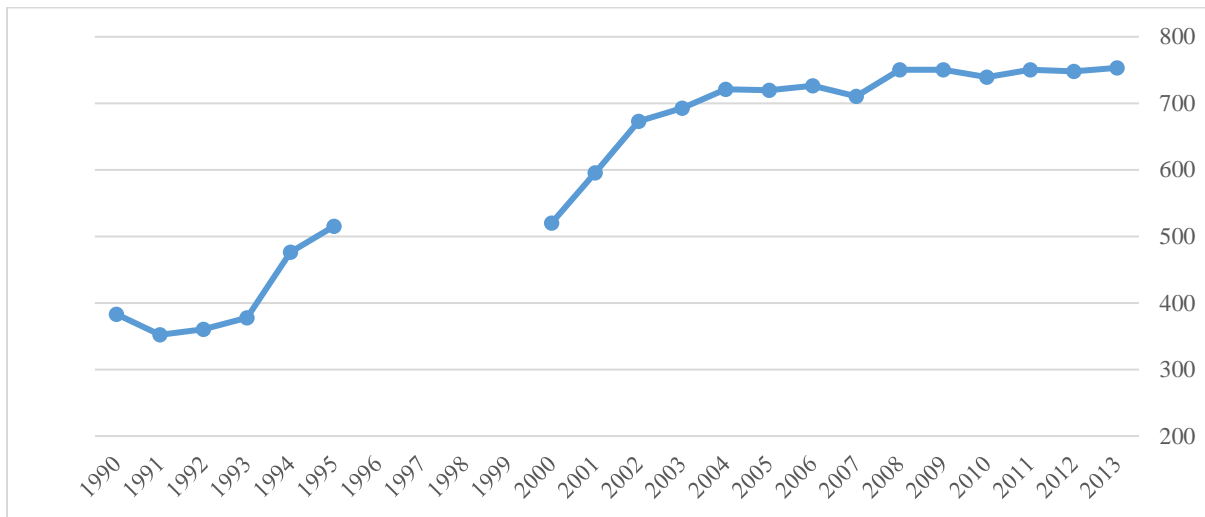
As the economic reform was initiated, the original highly centralized political system no longer served the purpose of running the economy. A series of administrative and fiscal decentralization reforms were carried out by the center in the mid-1980s in response to the burgeoning of industrial and commercial firms, initially in rural areas (Cai & Treisman, 2006; Naughton, 1996). The fiscal reforms formalized a revenue-sharing method called a “fiscal contracting system” (*caizheng chengbao zhi*). This fiscal system created sub-national fiscal units, and required that provinces, as autonomous fiscal entities, be financially self-sufficient – meaning that each budgetary unit be responsible for the balance of its expenditures and revenues – and that they be separate, with no transfer of fiscal resources across sub-national boundaries. However, the fiscal responsibility between the center and provincial governments varied by province. In 1994, the center launched another round of fiscal reform, seeking to institutionalize a nationally unified revenue sharing system with its provincial governments, and also to strengthen the central government’s ability to use tax and expenditure policy instruments (Ma & Norregaard, 1998). Along with the fiscal reform, the center granted provincial governments authority to make social and economy-related policies according to local conditions, following the center’s general guidelines. These policies are subject to the center’s review and approval. Welfare policy, including the pension program, is one of the areas for which provinces were granted discretion to make policy decisions. Thus, the decentralized structure created an arrangement with two *de facto* policy makers in certain areas – the center and the province.

On the economic front, the old SOE-dominant economic system, including social functions derived from the economic system, was overhauled by the government. In 1986, the Standing Committee of the National People’s Congress passed the *Enterprise Bankruptcy Law (pilot)*. The passage of this pilot law marked that the SOE reforms had entered a crucial stage.

SOEs were to change from state-run giant corporations to self-sufficient market economic entities. A contractual employment system was introduced by the government, breaking the “iron rice bowl” (*tie fan wan*). A modern enterprise management system was introduced to replace the old state-sponsored (*guojia baoban de*) enterprise management system. Being independent economic entities, SOEs started to face budget constraints. Like a flower incubated in a greenhouse, being long immune to direct market competition, in some localities, more than 40% of SOEs ceased operation wholly or partially in the first five-year period after the reform was launched (The National Commission on Economic Reforms, 1991, p. 378). To further the progress of reform, the government introduced labor force reduction measures in the early 1990s, including laying off redundant workers and allowing employees to retire before the required retirement age. A direct result of these labor market reforms was a significant growth in the number of early retirees (*nei tui*) and laid-off workers (*xia gang*) (Naughton, 1996).

Figure 3-1 presents official statistics on the registered unemployed population in China from 1990 to 2013. The numbers include only those who self-claimed unemployment and registered at the government’s reemployment centers, which covered only a portion of the informally employed, laid off, and early retirees. Therefore, they do not represent the real unemployment situation in China, yet give us a rough sense of the economic and social space the government faced. Based on the interpretation of the undoubtedly underreported data, the number of the registered unemployed in China more than doubled from the 1990s to the early 2000s, rising from 3 million to 7.5 million. Studies estimate that the real unemployment rate in China during that time period was over 10% (Giles, Albert, & Zhang, 2005; Zhou, 2011).

Figure 3-1 Registered unemployed persons in China, 1990-2013 (unit: 10,000 persons)



Source: *China Statistical Yearbooks* (various years). Data for the years 1996, 1997, and 1998 are missing.

With the soaring increase of early retirees and layoffs, the SOE-based pension program started to crumble with reductions in retirement benefit amounts, delays in payment, and even outright non-payment of pensions from the early 1990s. A substantial number of SOEs were financially unable to continue paying pension contributions and providing pension benefits on a timely basis. Under the old enterprise-based system, once the employed status ceased, early retirees and layoffs stopped contributing to the enterprise pension program, yet the company was responsible for their future retirement benefits. Upon stepping down from their positions, early retirees started to receive retirement benefit payments, yet in a smaller amount than that of regular retirees, since they were not officially retired and thus not entitled for full retirement benefits. Laid-off workers only received an immediate one-time compensation. The amount of compensation varied according to profitability of the enterprise. When those laid off reached full retirement age, according to the old pension arrangement, their employers would still provide retirement benefits to their prior employees. Many laid off workers were close to retirement age, which means that SOEs would deliver their pension benefits very soon. Therefore, even though

massive labor reduction would improve SOEs' production efficiency, the suddenly increase in welfare responsibility overwhelmed these already fragile companies. Thus, as SOE reforms progressed to this stage, pension reforms became a hurdle for the economic transition.

Moreover, delay in pension payments and non-payments posed a direct threat to the legitimacy of the socialist regime. As the only source of income after retirement, a pension was regarded as the most valuable right for workers under the socialist regime, and as a contract between the working class and the state. Any changes to the existing pension arrangement was viewed as violating the contract (BJC0614131). Aggressive economic reforms not only brought about a sudden decrease of individual income and welfare benefits, but also a substantial increase in food prices and expenditures on household services that had originally been subsidized by the government, such as medical treatments and education (Meng, Gregory & Wang, 2005). The combination of price inflation and loss of guaranteed pension provisions drove those affected retirees, early retirees, and layoffs to desperation. They became losers in the market economic reform, and had legitimate grievance against the government – the proletariat who used to be the master of the country had become new marginals in the society and the economy.

Pensioners' protests became a nationwide phenomenon as the SOE reforms picked up more momentum from the early 1990s (Hurst & O'Brien, 2002; West, 1999). The protesters gathered in front of city halls, blocked railway tracks, and occupied main streets, requesting their contractual social benefits, mainly pensions. The protests sometimes turned highly contentious when local rulers refused to respond with any promise to take care of the protestors' concerns. Take a mass gathering in Shenyang for example, the capital city of an old industrial base in Liaoning Province. Around 400 pensioners protested concerning pension payment delayed over

eight months. A hundred or so policemen came to prevent passers-by from stopping and move rioters apart (Kernen, 2005). These protesters had established extensive networks at workplaces, which helped in organizing large-scale opposition. In addition, as mentioned, Chinese people working in enterprises retire at a very early age (50 for women, and 60 for men)¹⁰. It is commonly argued that elderly people are less politically active, and one major reason is that they are often physically too weak to be politically active (Campbell, 2003). The relatively early retirement ages thus have profound implications on the Chinese old-age pension politics – 1) these “younger” retirees are presumably more physically capable for political involvement, and 2) their longer post-retirement life requires more resources for their pension benefit provision in the old system.

In addition to declining SOE capability, the expanding non-SOE sector also challenged the SOE-based welfare arrangement. Table 3-1 reports percentage of employment in the economy at the national level by registered enterprise ownership. It shows that after the launch of SOE reforms, with the downsizing of SOE, the share of non-SOE employees increased only gradually until the late 1990s. It means that the massive reduction of labor force employed in the state sector was only partially compensated by the employment growth in the non-SOE sector in the early 1990s. However, as new economic entities, non-SOEs attracted a mainly young labor force, and plus they did not have the historic burden of welfare provisions to retirees. Non-SOEs’ growth quickly forced SOEs into defense. Moreover, under the current welfare system, non-SOE employees were not entitled for welfare benefits, which would not be a sustainable development strategy for these companies nor for the economy. Under such social and economic conditions,

¹⁰ The actual average retirement age for both men and women is 54. The government now is considering postponing the retirement ages for both men and women to solve the aging problem. However, a public poll carried out by the largest online media company in China, Sina, showed that over 90% of the people who participated in the pool were against this policy idea (He & Chen, 2013).

increasing pension burden of SOEs, and concurrent rapid expansion of the non-SOE sector raised an acute question regarding how to honor pension commitments to the urban population.

Table 3-1 Percentage of employment by registered enterprise ownership, 1978-2010 (unit: %)

	1978	1985	1990	1995	1998	2000	2005	2010
SOEs	78.32	70.19	60.71	59.14	41.9	35	22.85	18.43
COEs	21.53	25.95	20.83	16.53	9.08	6.47	2.85	1.59
Cooperative	0	0	0	0	0.63	0.67	0.66	0.40
Joint-venture	0	0.30	0.56	0.28	0.22	0.18	0.16	0.11
Share-holding LLC	0	0	0	1.66	1.90	1.97	2.46	3.35
Other LLC	0	0	0	0	2.24	2.97	6.16	10.21
Hong Kong, Macau and Taiwan invested corporation	0	0	0.02	1.43	1.36	1.34	1.96	2.61
Foreign investment company	0	0.05	0.36	1.27	1.36	1.43	2.42	3.36
Individual	0.16	3.51	3.60	8.19	10.45	9.23	9.79	15.21
Others	0	0	13.59	8.95	26.36	35.26	38.51	24.36

Source: People.com.cn (2014).

As the first step to address the welfare provision problem, the center requested subnational governments to conduct experimental reforms on separating welfare responsibility from enterprises, and creating a welfare system covering all types of economic entities. A few municipal/county-level governments in Guangdong, Jiangsu, Sichuan and Liaoning carried out pilot reforms on socializing pension pool management (*shehui hua guanli*) in 1984 to replace the old enterprise-administered welfare system, and achieved noticeably positive effects. The need to create a cross-enterprise pension pool at the municipal/county level was acknowledged in the center's Seventh Five-Year Plan proposed in March 1986. Following this grand proposal, the State Council issued Circular No. 77 in 1986, officially mandating elevation of enterprise-level pooling to the municipal/county level. The Circular also suggested creating Social Insurance Agencies (SIA) at the municipal/county level to administer pension funds and be responsible for

collecting pension contributions and providing retirement benefits. By March 1987 there were already 27 province-level units, nearly 400 municipalities or counties, elevated pension pooling to the municipal/county level (Jiang, 1987). In addition, the Circular also recommended that both employers and contracted employees should contribute to the pension pool. The contribution rate for employers was recommended to be around 15% of payroll, and employees were suggested to pay no more than 3% of salary to the pension fund. The temporary enterprise-level pooling pension during the Cultural Revolution was thus ended. In other words, after this round of reforms, the responsibility to collect pension contributions and pay retirement benefits was shifted from enterprises to municipal/county level governments.

The intention of municipal/county level pooling was to promote cross-enterprise risk sharing in a locality. However, the planned economy produced large-scale SOE towns. In these cases, municipal-level pooling did not solve the problem, since the locality was still challenged by providing pensions to a large number of retirees from bankrupt SOEs. As a result, these localities had to impose much higher pension contribution rates than new economic development zones with fewer SOEs and more non-SOEs. A survey of 13 provinces and 12 municipalities carried out by the World Bank showed that employers' pension contribution rates varied greatly in the end of the 1980s, ranging from 3% in Shenzhen to 40% in Shanghai (World Bank, 1997). The World Bank report also noted that although the pension fund was expected to be pooled at the municipal level, municipal governments were not equipped with the capacity to administer the fund. As a result, powerful enterprises still exerted much control over their pension money, and many municipal pension funds suffered from large-scale embezzlements across the country (World Bank, 1997). Moreover, there was widespread evasion of the pension contributions. Many new private enterprises were reluctant to contribute toward the common pool, and they

often underreported wages to evade a large pension bill. Municipalities often lacked the capacity to enforce conformance (Keran & Cheng, 2002; Williamson & Deitelbaum, 2005).

As a crucial component in the labor insurance scheme, the old pension program had gone hand in hand with the centrally planned economic system. Breaking the promise of employment tenure and state-funded welfare provision was being viewed by the public simply as the state breaking the contract with its people. Regime legitimacy was hanging on by a thread. Nationwide major pension reforms were brewing under this delicate situation.

3.4 Reform trials at the national level: 1991 – 1995

To facilitate the economic transition and address widespread social grievances, the government needed to formalize a mandatory public pension system that accommodated the new demands of the economy. In Circular No. 33 (*A Resolution on Pension Reform for Enterprise Employees*) in 1991, the center proposed a tentative three-pillar pension plan, including a basic public pension plan, a supplementary corporate-based annuity provided by profitable enterprises, and optional individual savings. The document stated that the pension provision responsibility for enterprise retirees should be shared among the state, employers, and employees. The Resolution marked the first time that the government had recommended funding sources other than state budget, and had highlighted individuals' responsibility to fund their post-retirement life. It required individual employees to contribute to the pension program, in addition to employers' contribution, and a portion of the total contributions could be diverted to individual savings accounts in preparation for retirement. The intended replacement rate targeted a range of 60% to 75% of prior salary, depending on types of employment and profitability of work units (Hu, 2006). The Circular permitted municipal/county-level governments to propose specific reform plans based on the reform guideline set forth by the center, and provincial governments

were granted the power to approve lower level governments' reform proposals. In other words, the center only provided some rough reform guidelines in the 1991 plan, and left ample room for sub-national governments to tailor their pension programs to local conditions. In addition, some powerful SOE-derived ministries, such as the Ministry of Railways, the Ministry of Coal Industry, the Ministry of Metallurgical Industry, were not to be regulated by the 1991 reform plan. At the time of the 1991 reform, they still provided separate pension programs for their employees and pooled the program within the industry at the national level.

In 1994 the State Council invited 12 ministries and departments, such as Commission for Economic Restructuring, Ministry of Labor (MOL), Ministry of Finance (MOF), and Ministry of Civil Affairs, to join a focus group discussion on the possibility of transforming the current PAYG pension system to a fully funded system. The participants first denied the sustainability of the current PAYG system, as it would require at least a 40% total contribution rate in order to get prepared for the rapid aging trend. On the other hand, the experts estimated that if the government implemented a fully funded pension system from the mid-1990s, it would require contributions from both employees and employers of at least 37% of payroll until 2030. It was obvious to the group that no enterprise could afford such a high contribution rate, and neither would the high contribution rate help facilitate healthy economic development. Therefore, the group proposed innovating a new pension system that combined advantages of PAYG and funded systems (Song, 2001).

To implement the suggestion reached at the meeting, in 1995 the State Council for the first time mentioned the concept of "individual pension accounts" in an official document, Circular No. 6, *A Notice on Deepening the Reform of Enterprise Retirement System*. However, the document offered two reform options as incremental reform trials. Option one proposed to

create a pension program with large individual accounts (*da zhanghu, xiao tongchou*).

Employees would contribute no less than 3% of their wages to individual accounts, and the contribution would increase by 1% every other year till it reached 5%. Meanwhile, employers needed to contribute 11% of payroll to employees' individual accounts. Both employees' and employers' contributions, 16% of payroll in total, would be deposited in individual accounts.

Option one required employees to contribute for at least fifteen years to be entitled to claim retirement benefits. The monthly retirement benefit level would be determined by the amount left in individual pension accounts at time of retirement divided by 120. Option two would create a system with a larger public pool and smaller individual accounts (*da tongchou, xiao zhan hu*). By smaller individual accounts was meant that contributions from employees and employers would be shared between individual accounts and a public pool. Local governments could decide how to divide the 16% contribution. Option two required individuals to participate in this program for at least ten years to qualify for retirement payments. The public pension part targeted 20 to 25 percent replacement rate of last year's average wage in a locality for retirement benefit payments. Since money in individual accounts were owned by employees, so they could choose to have a one-time withdrawal of the money (reform plan 2-A) or monthly payouts throughout retirement years (reform plan 2-B). These two reform proposals represented reform ideas, or more accurately speaking political interests, of MOF and MOL respectively (BJN0402121). As the center did not reach an agreement regarding the reform plan, sub-national governments were allowed to choose from these two reform options to best serve local situations. Table 3-2 below summarizes reform plans each province adopted.

Table 3-2 Reform plans adopted by provincial governments in the 1995 reform

Province	Policy	Reform plan	Employees' contribution (% of payroll)	Individual account (% of payroll)	Implementation areas
Anhui	Wan Gov't No.39 (1995)	2-B	3	10	Whole province
Beijing	Jing Gov't No.1 (1996)	2-A	5	5	Whole municipality
Fujian	Min Gov't No.13 (1996)	2-B	4	8	Whole province
Gansu	Gan Gov't No. 46 (1996)	2-B	3	12	Whole region
Guangdong	Yue Gov't No. 54 (1995)	2-A		3	Whole province
Guangxi	N.A.				
Guizhou	Qian Gov't No.43 (1995)	Allow to vary	3	Allow to vary	Whole province
Hainan	Qiong PPC ¹ No. 7(1993)	2	3	0	Whole province
Hebei	Ji Gov't No.7 (1996)	2-B	3	11	Whole province except Handan
Heilongjiang	Hei Gov't No.9 (1995)	1	3	16	Jixi, Jiamusi, Mudanjiang, and Qiqihaer
Henan	Yu Gov't No. 11 (1995)	2-B	3	12	Luoyang, Xinxiang, Anyang, and Kaifeng
Hubei	E Gov't No.111 (1995)	2-B	3	12	Xiangfan, Qianjiang
Hunan	Xiang Gov't No.18 (1995)	2-A	3	12	Whole province
Jiangsu	Su Gov't No.69 (1996)	2-B	4	12	Whole province
Jiangxi	Gan Gov't No.50 (1995)	1	3	17	Whole province
Jilin	Ji Gov't No.18 (1995)	1	2	16	Whole province
Liaoning	Liao Gov't No.1 (1996)	2-B	3	12	Whole province
Neimenggu	Nei Gov't No.143 (1995)	2-B	3	12	Whole region
Ningxia	Ning Gov't No.113 (1995)	2-B	3	12	Whole region
Qinghai	Qing Gov't No.4 (1996)	1	3	16	Whole province
Shaanxi	Shaan Gov't No.113 (1995)	2-B	2	11	Baoji
Shandong	Lu Gov't No.98 (1995)	2-B	2	11	Whole province except Qingdao
Shanghai	Hu Gov't No. 63 (1994)	1	3	16	Whole municipality
Shanxi	Jin LIP ² No. 233 (1995)	2-B		4	Whole province
Sichuan	Chuan Gov't No.178 (1995)	2-B	3	11	Whole province

Tianjin	Jin LIP ² No.415 (1995)	2-A	4	4	Whole municipality
Tibet	N.A.				
Xinjiang	Xin Gov't No.85 (1995)	2-B	3	14	Urumuqi, Jichang, Hami, Boertala
Yunnan	Gov't No.25 (1995)	1	3	16	Whole province
Zhejiang	Zhe LIP ² No.173 (1995)	2-A	4	4	Whole province

Source: Author's collection.

Note: N.A.: not available; 1: Provincial People's Congress; 2: Labor Insurance Policy.

Table 3-2 reveals three important points. First, offering two reform options to sub-national governments resulted in a very fragmented system at the national level. The majority of provinces adopted reform Option 2, while a few others chose Option 1. Most provinces whose economies were dominated by SOEs chose Option 1, whereas new economic zones preferred Option 2. This difference in preferences demonstrates the reluctance of provincial governments with large pension liabilities to shoulder the pension provision responsibility, and that they would rather establish large individual pension savings accounts to push the retirement benefit payment responsibility from the government to individuals. Provincial governments set specific requirements for individual employees' contribution rates, yet left employers' contribution rates to lower-level governments' discretion. Different redistributive designs in fact led to very diverse retirement benefit payment schemes across sub-national regions. Clearly, this patchwork of province-level pension programs would hinder the formation of a national market in the long run and could only serve temporary purposes.

3.5 A landmark reform to create a nationally unified pension scheme: 1997 to 1999

Whether to create a nationally-pooled and centrally-administered pension system or adopt a decentralized pension administrative structure had been a major debate since the inception of the pension reform, and was a focal point in the 1997 reform policy discussion. Local

governments opposed the idea of creating a centralized pension system as proposed by the MOL, arguing that there would be irreconcilable conflicts between the decentralized fiscal and administrative system and a centralized pension system. In fear of arousing opposition from its local governments amidst market economic reforms, the center decided to postpone the discussion, leaving the pension administrative power to subnational governments, and allowing local governments to administer their pension programs and make adjustments according to local conditions (Gao, 2006). Scholars contend that in fact from the 1991 reform when the center had proposed to work toward creating a nationally unified pension system, provincial and municipal governments intentionally enacted pension policies distinct from plans implemented in other areas to ensure their control over the local pension program, and reduce the likelihood of centralization (Wang, 1998).

Yet the center was determined to unify the pension reform plan across subnational units to help facilitate labor mobility. The center reached an agreement internally to formalize reform option 2 at the national level, which was proposed by the MOL with a large public pension pool and small individual accounts, and was also adopted by most of the provinces after the 1995 reform. In 1997 the central government released Circular No. 26, attempting to establish a nationwide unified pension scheme. In this reform, the government proposed “four unifications” – a unified system, a unified standard, a unified management, and unified pension fund usage. In addition, the Circular also extended pension coverage to all urban employees, regardless of enterprise ownership. The 1997 document offered a concrete pension reform plan, which laid the ground for the current three-pillar pension model for employees in urban enterprises: 1) public pension, 2) individual account, and 3) supplementary annuity (voluntary). Pillar 1 was to be financed entirely by enterprise contributions which equaled 13% of payroll, and would provide

20% replacement of the previous year's mean wage at a locality. The qualification for a full basic retirement payment set by the regulation was 15-year employment, and this 15-year contribution requirement is still valid today. Pillar 2 would be financed by individual contribution equivalent to 8% of salary plus 7% of payroll from enterprise contributions. Retirees would receive monthly payments from Pillar 2, which would be calculated by dividing the remaining balance in the individual account by 120 upon retirement. Pillar 2 was proposed to give a 38% rated replacement of work salary. In addition, Circular No. 26 explicitly stated that only regions with difficulties in funding current retirees would be allowed to set a higher enterprises' contribution rate, but lowering the contribution rate was not mentioned as an option in the policy. Combining benefit payments from Pillars 1 and 2, the overall target benefit replacement rate of the pension program was set at 58.5% (see State Council's Suggestion No. 27634, and also Song, 2001, p.58).

Among the three pillars, Pillar 3 has been the least well developed. Pillar 3 was designed to promote the development of an enterprise annuity and commercial retirement insurance market. As the government noted when designing the current three-pillar pension scheme, the public pension would only support the basic livelihood of the people, and the government encouraged urban employees to save for their post-retirement life. To alleviate the pressure of population aging put on the public pension program, the government pledged to create a multi-level social security net for the people, and highlighted this proposal at the Party's Third Plenum of the Eighteenth Party Congress in 2012. In December 2013, the government issued a preferential tax exemption and deferral policy for contributions going into the supplementary old-age insurance programs in several experimental cities. However, in the past two decades, Pillar 3 has not yet seen much progress. Statistics show that the number of participants in the

third pillar was only 23 million by 2016, less than one tenth of total pension participants. The growth rate of third-pillar participation was less than 1% in 2016 (Zheng, 2017). Given the third pillar's underdevelopment, this study focuses only on the first two pillars.

Attempting to make a smooth transition, the 1997 reform plan divided pension participants into three groups – current retirees (also called “old men”), current workers (“middle men”), and new workers who would enroll in the new pension program when entering the job market (“new men”). According to the 1997 reform plan, those old men would continue receiving original retirement benefits, even though they had not contributed to the pension fund while employed. The benefit payment of middle men who enrolled in the pension system before 1997 would be calculated using the same formula as for new men. However, since middle men had not contributed to individual accounts before 1997, they would receive monthly transitional pension benefits upon retirement. To calculate the transitional benefits, the government used an accrual rate, ranging from 1-1.4% per year of the years covered before the 1997 reform.

An immediate question is who should be responsible to pay for the transition costs (also called implicit pension debt), namely old men's retirement benefits and middle men's covered yet noncontributing years. Experts estimated in the mid-1990s that the transition costs would range from more than 1 trillion *yuan* to 3 trillion *yuan* (Gao, 2006, p. 197). When designing the pension program, policymakers proposed three options to address the transition costs – 1) bail out by center's fiscal resources, 2) sell off some SOEs in payment for the costs, and 3) digest the costs gradually by the pension program itself. The first two options had been widely adopted by transitional economies in East European countries (Müller, 1999). However, the center decided that, as the government did not have sufficient fiscal resources to bail out the costs, nor did it have a readily available proposal to sell off SOEs, the third option seemed to be the best

available option (Gao, 2006). The center decided to postpone the payment to the pension transition costs in hope that the new program design would settle the issue itself. However, although option three was a convenient plan, it had serious drawbacks. First of all, it is theoretically unfair for new men to pay for these transitional costs. Second, to achieve that goal, the government must set a higher pension contribution rate, which might reduce economic efficiency and increase the likelihood of contribution evasion. Third, new men's contribution was simply far from sufficient to fill the gap, not to mention a portion of the contributions is supposed to create funded individual accounts in preparation for their own retirement benefits under the new pension system. As a result, in practice local governments have had to dip into the supposedly consolidated individual accounts to pay for current retirees' pension provisions, and individual accounts are emptied and become notional in practice. Thus, in practice the first two pillars of the Chinese pension program are still operated as a PAYG system.

The compulsory public pension program was first resisted by non-SOEs, as the high contribution rates greatly increased their production costs. To ensure the pension program's compulsory nature, in 1999 the State Council issued *Interim Regulations on the Collection of Social Insurance Premiums* to urge sub-national governments to strictly enforce the non-SOE sector's pension participation. By 1997, 93.9% employees in SOEs participated in the pension program, accounting for a super majority of the program's participants. However, the participation rate in the non-SOE sector was less satisfactory. Only 53.8% of employees in urban collective enterprises, and 32% of employees in other non-SOEs, participated in the program (MLSS, 1999, pp. 2 and 92). As we shall see in the discussion below, partly as a result of this 1999 regulation, the coverage ratio of the pension program picked up quickly in the early 2000s.

The difficulty of the reform was made worse by the arrival of the 1997 Asian Financial Crisis. The transitioning Chinese economy stumbled in this unexpected economic recession. Timely pension benefit payments became an even more challenging task. The central government issued two policies to aid local pension development. First, the center requested provincial governments to report the amount of pension fund deficits by 1997 and promised to bail out the reported amount as a one-time special fiscal transfer. However, the effect of this policy was far from satisfactory. Subnational government officials, not only provincial officials, were afraid of reporting the real deficit amount, as it would reveal their incompetence. Thus, the numbers the center received were greatly underreported (BJC0614131). Second, in 1998, the State Council issued *A Notice on the Elevating the Enterprise Pension System's Pooling System to the Provincial Level and Transferring Industry-based Pools to Local Governments*. With the implementation of this Notice, industry-based pension schemes were terminated, and merged with the general urban enterprise pension system. This move was a product of the center's 1998 Super Ministry Reform (*da bu wei gaige*). It signaled the center's determination to break through powerful blocks to create a nationally unified pension system and put an end to fragmentation. In addition, the center decentralized the administrative power of those industry-based pension programs to subnational governments, which provided subnational governments a lucrative source of pension fund revenues. However, the center's decision to further decentralize the pension administration to subnational governments intensified the tendency of pension localization and strengthened the power of local pension administration, which further complicates future centralization reforms. In 1998, the center granted the MOL the power to administer the urban enterprise pension system at the national level, and replaced the old Ministry of Labor with the Ministry of Labor and Social Security (MLSS).

3.6 Consolidating individual account reform: 2000 – 2008

As mentioned, the very purpose of inventing a multi-pillar pension program was to take advantage of both a PAYG program and funded individual accounts. To keep subnational governments from using the pension funds in individual accounts to pay for current retirees' pension benefits, in 2000 the State Council issued a follow-up regulation, Circular No. 42, to reconfigure the allocation of the contribution. The new regulation, *A Pilot Program for Improving Urban Social Security System*, required that enterprises' 20% contribution should go to the public pension pool entirely, and individual accounts should be financed solely by the 8% individual employees' contribution. This document also required local governments to separate the management of individual accounts from the public pension fund, and strictly prohibited subnational governments from using individual account funds to subsidize the public pool. This pilot reform plan was also called a "consolidating individual account reform", or "consolidation reform" for short. Based on the guiding principles in this Circular, the center selected Liaoning for a pilot reform in 2001 and granted healthy fiscal subsidies. This reform plan was expanded to the other two northeast provinces, Jilin and Heilongjiang, in 2004 and 2005 respectively. However, the size of consolidated individual accounts shrank from 8% of wages in Liaoning to 5% in the other two provinces. By 2006, another eight provinces were included in this consolidation reform: Henan, Hubei, Hunan, Shandong, Shanghai, Shanxi, Tianjin and Xinjiang. The center warned local governments not to aim too high, and urged them to push forward the consolidation reform slowly yet steadily. The center suggested downsizing of individual accounts and fully consolidating these accounts (*zuo xiao zuo shi*), so it further reduced the size of consolidated accounts to 3% of wages in this round of reform expansion. Most reform-participating provinces received center fiscal support, yet in varying degrees. Meanwhile, the center recommended other

provinces to carry out the consolidation reform with local fiscal resources. No province responded to that call.

The consolidation reform was deemed a failure. Despite substantial fiscal investments from both center and subnational governments, after seven years of consolidation reform efforts, subnational governments still struggled to make ends meet in their pension programs. The center had to allow the Liaoning government to borrow up to three eighths of the reserve in consolidated individual accounts to ensure timely retirement benefit payments to current retirees in 2008. This decision declared the consolidation reform a failure (Li & Jiang 2012). By 2010, only 203.9 billion *yuan* were consolidated in all individual accounts across the country, rather than the 1.96 trillion *yuan* the center had estimated before the reform was carried out. Ironically, most of those funded accounts were achieved by regions suffering from pension fund deficits, such as Liaoning (BJN0828121). We will return to a more detailed discussion of center-local interactions on this consolidation reform in Chapter Six, where center-local interactions in the pension program will be discussed.

3.7 Recent reform attempts

The pension program has lately become a major battlefield of reform proposals. Over the past few years, although the main structure of the pension program remains intact, the center undertook major reform efforts on the pension program, including 1) facilitating inter-regional pension transfers; 2) transferring SOEs' assets to the center's pension reserve; 3) ending the dual-track pension system, and merging public employees' pension with the urban enterprise pension program; and 4) allowing pension funds in certain localities to be invested in the stock market. These reform attempts in general are steering development of the pension program in a

positive direction, yet some reforms are deemed less than satisfactory, and the others' results remain to be evaluated.

First, the center failed to promote inter-regional pension transferability. As noted above, the pension program has become highly localized, which greatly discourages labor mobility. Migrant workers, given that they often engage in seasonal jobs and constantly move from one locality to another, suffer the most from the current highly decentralized pension administrative arrangement. To overcome this problem, the State Council issued a tentative inter-regional pension-account transfer plan in 2008. However, thus far the plan has not been effectively implemented. The main reason behind this policy failure was resistance of migrant-receiving provinces, who have vested interests in the current localized pension administration. Migrant workers contribute to the pension program, but often relocate before they become eligible to collect pension benefits. These migrant workers thus become pure contributors to the pension program. The center's inter-regional transfer reform would interrupt these migrant-receiving provinces' vested interests, so that these provinces set up additional hurdles for inter-regional transfer applications to go through. The Ministry of Human Resources and Social Security (MHRSS) reported that even though more than 1.1 million pension participants filed requests for inter-regional pension transfers in 2011 and 2012, only 20% of the applications went through in 2011 and 25% in 2012 (Zheng et al., 2013). We will return to a more detailed discussion of the limited portability problem in Chapter Six.

Second, after the 1997 reform scholars and policymakers submitted multiple feasibility studies and petitions to urge the center to transfer part of SOEs' assets to create a national pension reserve fund in preparation for rapid aging (see He, 1995; Liu, 1994; Zhou & Wang, 1994). In 2000, the center set up the National Social Security Fund (NSSF) and decided to

allocate a certain amount from the center's annual budget to go into this strategic reserve (*zhanlue chubei*) from the year onward. As an independent entity, the NSSF reports directly to the State Council. The NSSF is the only entity that is responsible for investing and managing the fund. In June 2001, the State Council mandated that all state-owned companies must contribute 10% of their initial public offering proceeds to NSSF at the time of their public offerings. In October 2001, only four months after this policy was issued, the center called an urgent end to the plan, as the asset transfer plan aroused significant pushback from both SOE managers and the stock market (China Insurance Regulatory Commission, 2006). The discussion of the possibility of transferring SOE assets gained another momentum since 2011, as the baby-boomer generation will reach their retirement age in less than a decade. The importance of using SOE assets to aid the public pension program was again mentioned in the government's 2016 Central Government Work Report. The center planned to realize the transfer by the end of the Thirteenth Five-Year Plan (Wang, 2016). However, no detailed reform plan has been revealed.

Third, the center pledged to end the dual-track (*shuang gui zhi*) pension system under which public employees had long enjoyed significantly higher benefit levels than enterprise employees without having to make any contribution to their pension fund (Luo & Zhao, 2014). According to the *China Labor Statistical Yearbook*, in 1990 the average retirement benefit for civil servants was 1.2 times as high as that for enterprise retirees; by 2005 the ratio had grown to 2.1 times (Sun, 2016). This system aroused significant social discontent and distrust of the government. In 2002 the government began conducting online surveys in preparation for the "Two Conferences" (*liang hui*) to determine the issues the public most wanted addressed. From the beginning, social security has always been ranked among the top ten concerns; and the dual-track pension system was ranked first among all social security topics from 2009 to 2014. The

public had strongly urged the government to tackle the pension benefit gap issue, arguing “no fairness, no harmony”, and “return the fairness and justice to the people” (Chang & Huang, 2016). In December 2014, the center announced its intention to merge the two pension programs. However, the real effects of this reform would be far from what the word “merge” implies, as after the reform there will still be two separate pension funds for public and private employees, and the benefit calculation formula for the two groups is expected to be different (BJC0413151, and GSP0410152). In addition, no subnational governments had revealed a specified reform plan by the time the present study was completed.

Fourth, in the 1997 reform policy the center had only allowed subnational governments to save pension contributions in national bonds and bank savings accounts to guarantee the proper use of the pension fund. However, in the past two decades, the average investment return rate of the pension fund was only 2%, lower than the inflation rate. In other words, the pension fund depreciates in real terms as it only sits in banks (BJN0715121). While most localities are still challenged by large pension fund deficits, some provinces have accumulated a substantial amount of pension fund surpluses, mainly thanks to the program’s limited portability. These provincial governments with fund surpluses have been very tempted to increase the value of their pension reserve. In 2012, the center allowed the Guangdong government to take 100 billion *yuan* from their local pension fund reserve to invest in NSSF, which constituted the first step forward to make better use of the pension money. The average investment return rate was reported to be around 8.4% from 2012 to 2015 (Li, Xu & Xi, 2016). However, since then, the investment expansion has had very heavy going. Only Shandong was allowed to invest 50 billion *yuan* into NSSF in 2015. The discussion of further expanding the involvement of the pension money in the capital market again became a focal point in 2016. However, it is clear that the center has been

very conservative in expanding the investment scale, as fund stability is always the first priority for the center.

3.8 An overview of the pension reforms

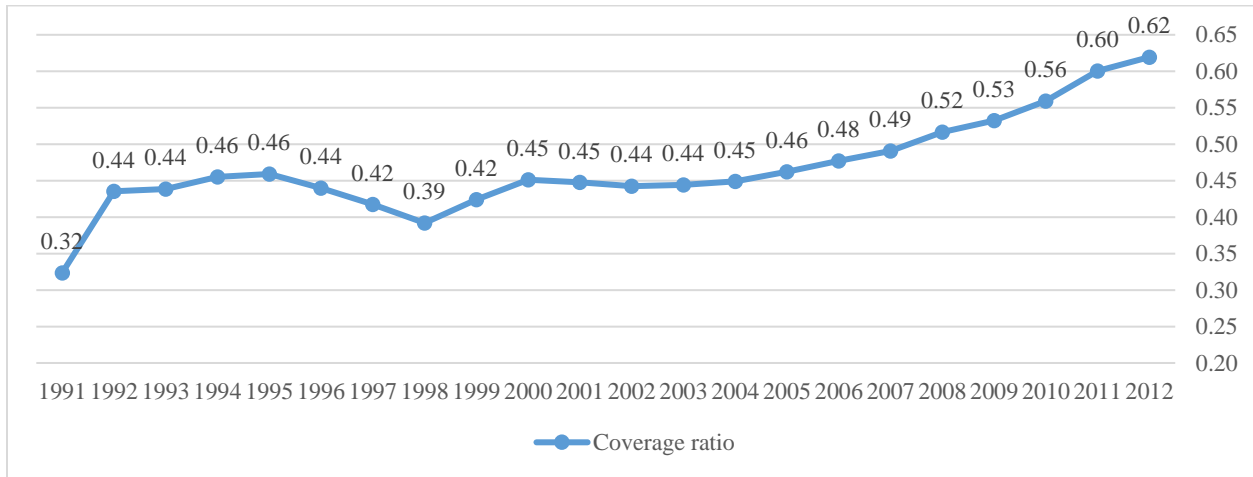
Major reform plans discussed above constructed a new pension scheme departing from the original 1951 socialist pension plan. Three major milestones along the reform process. After a decade-long policy trials at the subnational level, the center first issued a national-level reform plan in 1991 to mandate pension contributions from employees and elevate the pension pooling level from enterprises to the city/county-level. Subnational governments were allowed to experiment with different reform plans to search for the best suited strategy. The 1997 landmark reform aimed to end subnational variation in pension design and to create a nationally unified three-pillar pension program, specifying contribution rates for employees and employers and the benefit calculation formula. The center left substantial pension administrative rights to subnational governments, yet repeatedly urged them to work toward creating a centralized pension program. Realizing the unsustainability of emptied individual accounts, in 2000 the center conducted several “consolidating individual accounts” trials. The purpose was to separate the public pension pillar from the individual account pillar, and to realize the hybrid pension design. However, the effects of the reform were quite limited. Yet since 2000, employers’ pension contributions all remain in the public pension pool, and employees’ contributions are supposed to fund their individual pension accounts. Table 3-3 summarizes key features of these pension policies from 1951 to 2000.

Table 3-3 Major Pension Policies in China after 1949

	1951	Circular No. 33 (1991)	Circular No. 26 (1997)	Circular No. 42 (2000) (Liaoning pilot)
Public Pension (Social pooling)	Employers contributed 3% of payroll, 30% of which was pooled at the national level	Employers contribution rate varied by region; Employees contributed 3%; Benefit not clarified	Employers contributed 17% from payroll; Benefit: 20% replacement rate + additional benefit for participating 15 years or above	Employers contributed 20% of payroll; Benefit remains the same
Individual Accounts	None	Voluntary	Employees contributed 8% + 3% from employers; Benefit 1/120 monthly annuity	Employees contributed 8% of wages; Benefit remains the same
Supplementary pension	None	Voluntary	Voluntary	Voluntary, with the limit of 4% of pre-tax wage bills
Recommended pooling level	National-level	City/county-level	Province-level; Working toward national-level pooling	Province-level; Working toward national-level pooling

Figure 3-2 below demonstrates the increasing population coverage ratio of the pension program since 1991. We may calculate the coverage ratio by dividing the number of contributors in the pension system by that of urban employees in the same year (including employees in government agencies and public institutes). We observe that the coverage ratio almost doubled in twenty years since the center announced the first national pension reform plan in 1991, from 0.32 in 1991 to 0.62 in 2012. However, by 2012 there were still about 40% of urban employees not covered by this plan, most of whom were migrant workers and employees in small private enterprises and the informal labor market.

Figure 3-2 Coverage ratio of the urban enterprise pension system

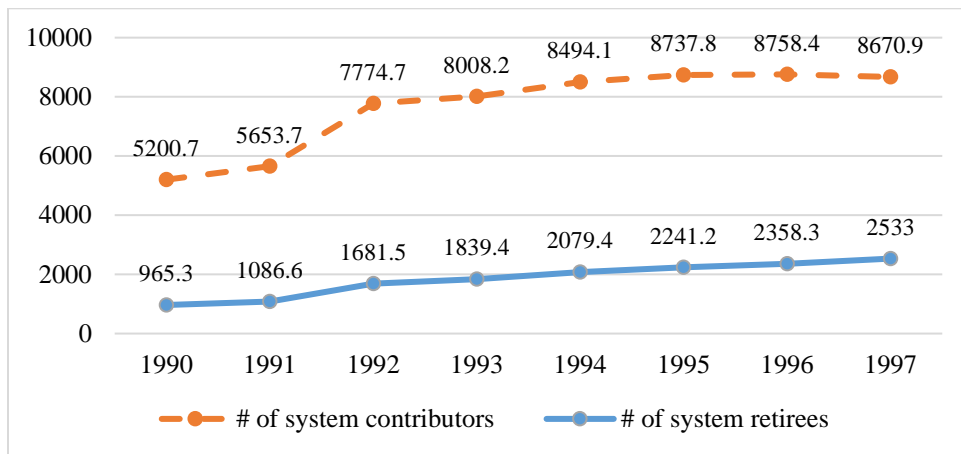


Source: *China Statistical Yearbooks* (various years).

To further examine the development of the program, Figures 3-3 and 3-4 below divide the reform period into two segments: from 1989 to 1997, and from 1998 to 2012. As discussed, the main purpose of the pension reforms in the 1990s was to separate welfare responsibility from SOEs, and expand pension coverage to include employees in the non-SOE sector. The coverage expansion should recruit more contributors to the pension program, and thus reduce pension fund burden. Figure 3-3 shows that the number of system participants skyrocketed in 1992, the year following the implementation of the 1991 reform plan, and the pension program went into a steady growth period. However, in spite of the increase in system contributors after 1991, the reform did not seem to outpace the increase in the number of retirees. The system dependency ratio in fact rose from 18.6% in 1990, to 21.6% in 1992, and to 29.2% in 1997. These numbers suggest that as retirees accounted for an increasingly larger percentage of pension participants, the pension program’s funding responsibility imposed on current retirees increased across time under the PAYG pension design. In 1989 on average 5.4 employees paid pension benefits to one retiree, but in 1997 3.4 employees needed to take the financial responsibility to fund one retiree’s retirement benefit provision. In other words, while the number of contributors increased 1.8

times from 1989 to 1997, the number of system retirees grew 2.8 times during the same period. This counter-expectation result was mainly due to the massive increase of early retirees and layoffs starting from the early 1990s, which simultaneously increased the number of retirees and decreased the number of pension contributors.

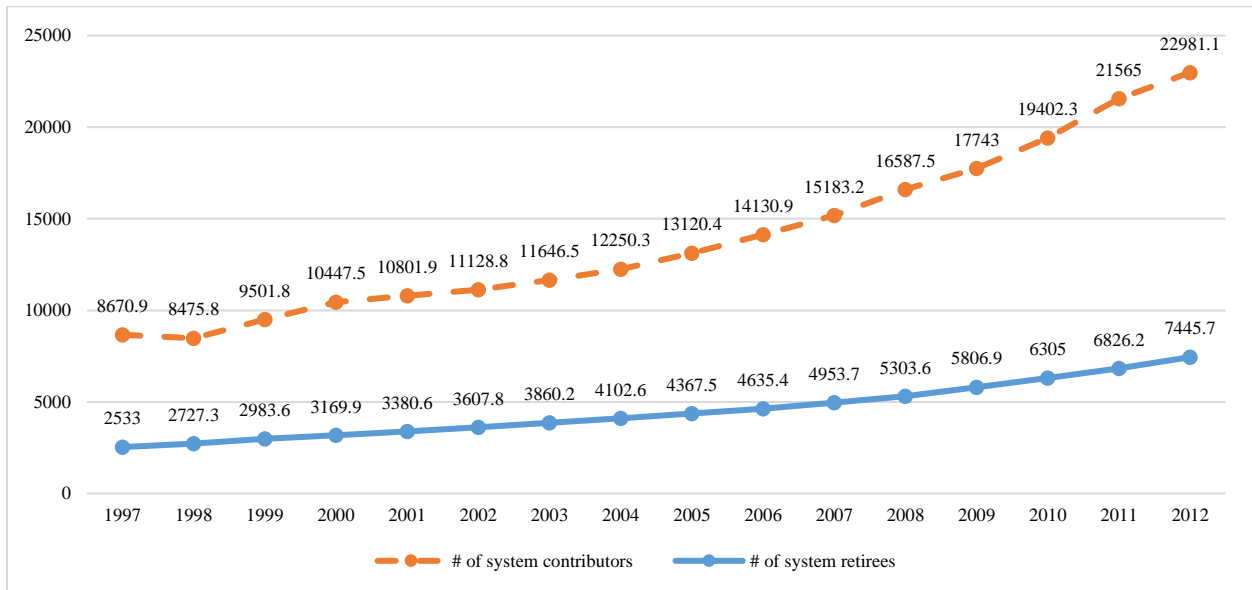
Figure 3-3 Numbers of system contributors and retirees in the urban enterprise pension system, 1989-1997 (unit: 10,000 persons)



Source: *China Statistical Yearbooks* (1990 to 1998).

The 1997 landmark reform gave the pension program a full-fledged push. Figure 3-4 indicates that between 1997 and 2012 both the numbers of pension participants, and retirement benefit recipients from the program almost tripled. The number of pension contributors by the end of 2012 reached 86 million, and the number of benefit recipients was more than 25 million. The pension system dependency ratio that had worsened in the early 1990s was held in control after 1997. During this period, the dependency ratio increased around 3%, from 29.2% in 1997 to 32.4% in 2012. That meant that the growth of retirees still outpaced that of contributors in this period. However, considering the rapidly aging demographic structure, the only slightly increased dependency ratio could be recognized as one major achievement of the pension reforms.

Figure 3-4 Numbers of system contributors and retirees in the urban enterprise pension system, 1997-2012 (unit: 10,000 persons)



Source: *China Statistical Yearbooks* (1998 to 2013).

3.8.1 The resulting localized urban pension system

Although one main purpose of the center’s 1997 reform was to create a “unified” pension scheme for urban employees at the national level, the resulting program is highly fragmented. There are currently estimated to be 2000-plus pension pools throughout China. This estimate is based on the number of cities and counties at the subnational level (BJN0828121). Some other estimates exist, such as 1180 pools (Hu, 2004). No matter exactly how many pension pools are in place, what these numbers suggest is how fragmented the pension system is at the sub-national level. Not only is the pension program pooled at a very subnational level, but subnational governments have been allowed to adjust the center’s policy to best advance local interests. Subnational governments became the real policy makers of the pension program. Three problems derived from this highly-decentralized pension administrative structure.

First, the pension program has distinct redistributive designs across subnational units, as manifested in the variations in pension contribution rate. The *de facto* average pension

contribution rate at the provincial level ranged from 10% in Guangdong to almost 30% in Gansu between 2007 and 2011 (see Table 1-1 in Chapter One). Pension contribution rates have profound impacts on the economy besides determining the sustainability of local pension programs. How much government extracts from the society directly affects the efficiency of economic production, and thus the development outlook of local economies. As discussed in Chapter One, structural factors can hardly provide satisfactory explanations for the variations. The following chapters will develop a micro-level theory to explain redistributive incentives of subnational rulers in China.

Second, related to the prior point, another challenge derived from the fragmented pension system is its very limited portability. By 2009 most provinces created intra-province pension fund adjustment mechanisms to mobilize pension resources at the provincial level so that the pension program could work more or less as if pooled at the provincial level. Before then, transferring pension participation from one city to another was a long haul. After 2009 provinces became the major boundary for pension transfers. As mentioned, even though the center attempted to resolve the issue through a top-down policy revision in 2008, the real effect of this policy was shown to be very limited. In this current economic market with high labor mobility, this localized pension administrative structure has been constantly challenged by new demands from the labor market.

Third, as the pension program is pooled at a very local level, the risk bearing capability of the program is highly contingent on local conditions. Pension programs in regions with more system retirees thus have a less favorable system old-age dependency ratio, and are more challenged fiscally to provide timely retirement benefit payments. Thus, the center inevitably has to aid pension development in certain localities to ensure proper implementation of its pension

policies. How does the center distribute its resources across subnational regions? What factors shape the center's redistributive incentives? The next chapter will investigate these questions.

3.9 Conclusion

The historical overview of the pension program in this chapter shows that the evolution of the pension program has always been imbedded in the broad political and economic context. The pension program departed from a state-funded socialist-style centralized pension system to a multi-pillar decentralized system, as the economy transitioned from a centrally planned type to a decentralized mixed-market economy. The different designs of the pension program for enterprise employees throughout the investigated periods reflect the Chinese central government's changing political priorities across time, including manifesting the government's socialist ideology, facilitating market economic reforms, and pacifying losers during the economic transition. Once the new pension program was enacted in the 1990s, the center has employed gradualist strategies to make minor revisions to the program, although major structural problems exist. The pension program produces new politics itself, and the new politics interact with the political environment together to shape actors' interests and preferences. The following chapters will demonstrate in more detail this boomerang relationship between politics and the pension program.

Chapter 4 The center's redistributive rationales

-- *Stay vigilant in peacetime* (居安思危)

4.1 Introduction

In light of the discussion in the theory chapter, this chapter investigates the Chinese central government's redistributive behaviors. This chapter focuses on two questions: 1) why the center distributes resources to subnational units, and 2) how the center allocates its limited fiscal resources among subnational units. As noted in the prior theory chapter, current research on welfare politics often focuses on politics at the national level. Yet the implementation of welfare programs relies mainly on subnational governments. How the center interacts with subnational units to ensure that they behave faithfully is under-researched. This potential principal-agent problem between the center and subnational governments looms large in a decentralized political institution like the government of China. As the theory chapter argues, the center may use fiscal subsidies as a leash to lead and constrain subnational rulers and ensure proper implementation of its desired welfare programs at the subnational level, particularly those ruling strategically important regions. This chapter uses both qualitative and quantitative empirical evidence to demonstrate that the center prioritizes its fiscal resources in regions that suffer from either economy-induced political instability or politics-induced political instability. Through this redistribution mechanism, the center offers direct fiscal alleviation to these regions to develop welfare programs, in order to help pre-empt or settle down unrest caused by economic difficulties and political conflicts.

In China, even though its government has been accused of being predominately economy-oriented, as economic inequality has been on the rise over the past three decades, the central government started to worry that the economic profile and the increasing number of mass

incidents would undermine the legitimacy of the socialist Party regime. Particularly over the past two decades, the center shifted slightly its emphasis on economic development to start to promote social welfare development (*min sheng*). The *2013 Central Government Work Report* devoted more than two thousand words to the importance of social welfare development in the government's strategic development plan (China News net, 2013), signaling a pledge by the center to expand social welfare provision and to create a safety net for the population. In the *2015 Central Government Work Report*, Premier Li Keqiang mentioned "old-age pension" fourteen times, which was interpreted as showing the center's determination to tackle the population aging crisis by improving the old-age social security net (Qiao, 2015). Since the Hu-Wen government, the center has used rational appeals such as "creating a people-centered and service-centered government", "building a harmonious society", and realizing the "China dream" to actively manage the society, which also reflects the center's growing concern over the under-developed social safety net in China (Fewsmith, 2012). However, as noted in the theory chapter, compared with the center, which has more long-term encompassing interests, subnational governments are oftentimes more short-sighted. Among all social welfare programs, the public old-age pension is particularly challenging, as it 1) involves a long-term commitment from the government, and 2) is particularly expensive in a rapidly aging society with a large population as in China. Therefore, the questions of which level of governments should shoulder the responsibility to fund this costly old-age pension program, and how the central government should incentivize subnational governments to promote pension development, are more about politics than they are simply fiscal issues.

This chapter first briefly reviews China's decentralized welfare governance structure, and how this structure came about. Second, given the decentralized administrative structure and the

imbalanced center-local relations regarding retained revenue and actual expenditure, this chapter discusses the center's fiscal subsidies to subnational units. Lastly, this chapter uses both qualitative and quantitative methods to test the rationale behind the center's decisions on subsidizing certain subnational localities but not others.

4.2 The decentralized fiscal and administrative structure

There are five levels of governments in China: 1) central, 2) provincial, 3) prefecture, 4) county, and 5) township governments. Below the township level, the village is an informal level of government. China adopted a one-level down administrative structure – a government is accountable to the government one level above it. This study focuses on the relationship between the center and provincial governments. As the highest authorities at the sub-national level, provincial governments are directly responsible for reviewing and approving social and economic policies implemented at the sub-national level. Yet largely due to its limited accessibility, Chinese provincial governments are understudied, as are their interactions with the center. This dissertation helps fill in this gap, and this chapter focuses on the center's fiscal relations with provincial governments.

The administrative and fiscal structure in China experienced substantial changes in the 1980s and 1990s, from a highly-centralized system to a decentralized one. Before the 1980 and 1990 reforms, under the planned economy, China had a fiscal system of "unified revenue collection and unified spending" (*tongshou tongzhi*), or what is known as "eating from one big pot" (*chi daguofan*). Under this old fiscal arrangement, subnational governments submitted all revenues collected to the center, and in turn all subnational expenditures came from the center's distribution. In the command economy, this fiscal arrangement worked as a nationwide redistribution mechanism, yet subnational governments' incentives to increase revenue were

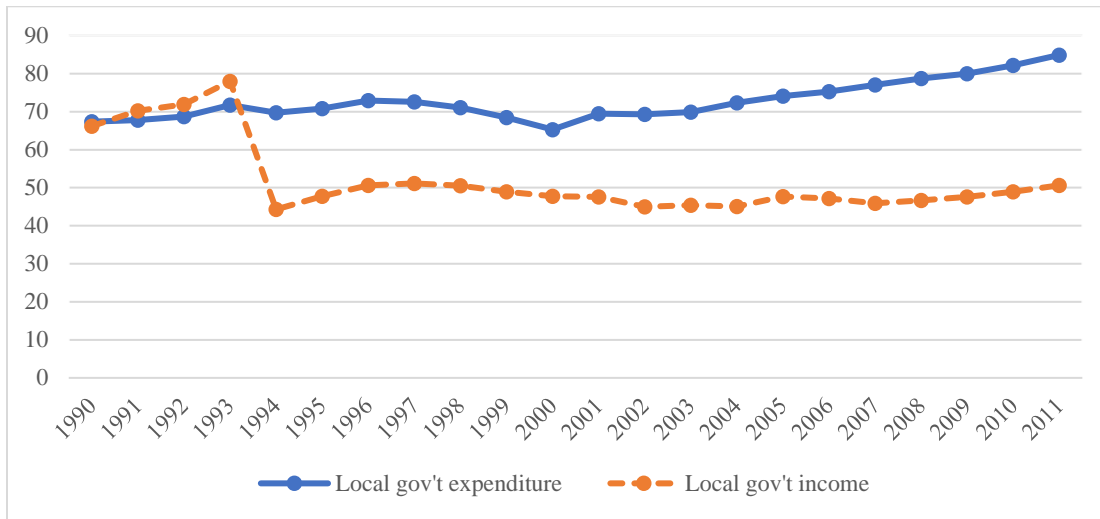
very minimal. As the economic transition of the late 1970s and 1980s proceeded, the old highly centralized political system no longer served the purpose of running the economy. Therefore, the government initiated a series of administrative and fiscal decentralization reforms¹¹ in the 1980s (Cai & Treisman, 2006). The fiscal reforms formalized a revenue-sharing system called “fiscal contracting system” (*caizheng chengbao zhi*), which is also popularly known as “eating in separate kitchens” (*fenzao chifan*). The subnational governments were required to remit a small portion of their revenues to the center, and the center-local divide of revenues was negotiated on a case-by-case basis. This fiscal system required that local governments, as autonomous fiscal entities, be economically self-sufficient – meaning that each budgetary unit would be responsible for its expenditures and revenue collection – and be separate fiscal entities, with no transfer of fiscal resources across sub-national regions. In some cases, sub-national governments, however, were able to turn to governments at higher levels for fiscal subsidies to achieve balance between expenditures and revenues. Meanwhile, local governments were granted the power to make social and economic-related policies, subject to the center’s review and approval. Pension policy is one of the areas for which local governments have discretion to make policy decisions. This series of decentralization reforms is often regarded as a crucial institutional innovation to incentivize local governments to pursue rapid economic marketization and generate revenue income (Naughton, 1996). After the reforms, local governments gained unprecedented substantial rights and an increased budgetary share in the country’s overall revenues (Kumar, 1994; Oi, 1995; Tsai, 2004).

¹¹ Administrative decentralization here means that the national government grants to sub-national governments authority to make certain policy decisions, subject to review and possible veto from above; fiscal decentralization means that the national government permits sub-national governments to retain a larger share of nationwide fiscal revenues.

Overcorrection is usually short-lived. As the share of the center's fiscal resources dramatically declined due to the prior decentralization reforms, in 1994 the center decided to institutionalize the revenue sharing system with its provincial governments and sought to strengthen the central government's ability to use tax and expenditure policy instruments (Ma & Norregaard, 1998). However, after this round of fiscal structure reform, with more revenue retained by the center, local governments were still expected to fund and administer welfare programs, including public pensions. This new arrangement created an unbalanced center-local relationship in administrative and fiscal powers (*shi quan yu cai quan*) (Wedeman, 1999). The data shown in Figure 4-1 confirm that the share of local governments' income in total government revenue dropped significantly in 1994 and that the share has stayed stable since then, whereas their spending increased gradually across time. In 2011 local governments were responsible for more than 84.9 percent of public spending, with only a 50.6 percent share of total government revenue. Because of that imbalance, the center necessarily has to transfer fiscal resources to local governments. Regions that are unable to make ends meet may turn to the center for subsidies upon negotiation (Frazier 2012, p. 24).

It is worth noting that in only a few countries, such as Switzerland and the United States, is local government spending more than 40 percent of total government spending. On average, the figure is 34 percent for industrialized countries and 22 percent for developing countries (World Bank, 1996). Therefore, by this measure of decentralization alone, the fiscal system in China is extremely decentralized as compared with other countries.

Figure 4-1 Local government income and expenditure as shares of national totals, 1990 to 2011 (unit: %)



Source: National Bureau of Statistics, <http://data.stats.gov.cn/workspace/index?m=hgnd>.

Note: From 2000 onward, fiscal expenditures included interest payments on domestic and foreign debts.

As the public pension program experienced substantial reforms in the 1990s, in order to not delay the reform process, the center decided to transplant pension administration to the existing administrative and fiscal structure. As noted in Chapter Three on the development of the pension program, the center’s decision on this institutional transplantation was meant to overcome opposition from subnational governments, mainly those from economically more developed regions, and to avoid any complication amid already painful pension reforms (Gao, 2006). Therefore, instead of having a centralized pension pool, the pension program inherited this highly decentralized, almost fragmented, fiscal and administrative structure. There are estimated to be over 2,000 separate pension funds at the sub-national level in today’s China.¹²

4.3 An overview of the center’s fiscal subsidies

This fragmented pension administrative structure only intensifies the potential center-local conflict in policy preferences. To enable local governments to implement particular policies

¹² Only four provinces have centralized pension funds at the provincial level so far; fourteen provinces have centralized administration of pension funds; and pension funds in the remaining thirteen provinces are still pooled at city or county level (BJN0402121).

designed by the center, the center created “earmarked subsidies” (*zhuanxiang butie*), as they are called by the MOF. These grants are allocated for specific purposes. As the center’s new policy initiatives mushroomed from the late 1990s, the number of these grants has multiplied quickly (Shah & Shen, 2006). As mentioned, a public pension program often requires substantial financial support from the government over a long time span. As such, the center’s fiscal commitment on the pension program is critical to the pension development, especially in such an unbalanced fiscal-administrative structure as in China. From 1997 to 2010 the center’s subsidies to pension programs increased from .03% to .57% of annual GDP (*China Statistical Yearbook, 2010*), in spite of rapid economic development in the prior two decades. The center’s subsidies increased gradually over the course of pension reforms. The accumulative amount of the center’s fiscal subsidies for the urban pension program reached one trillion *yuan* by 2010, and in 2011 alone the amount was 1.3 trillion *yuan* (Guo, 2013).

Table 4-1 Fiscal transfers to the pension system from the center and local governments, 1999-2004 (unit: 0.1 billion *yuan*)

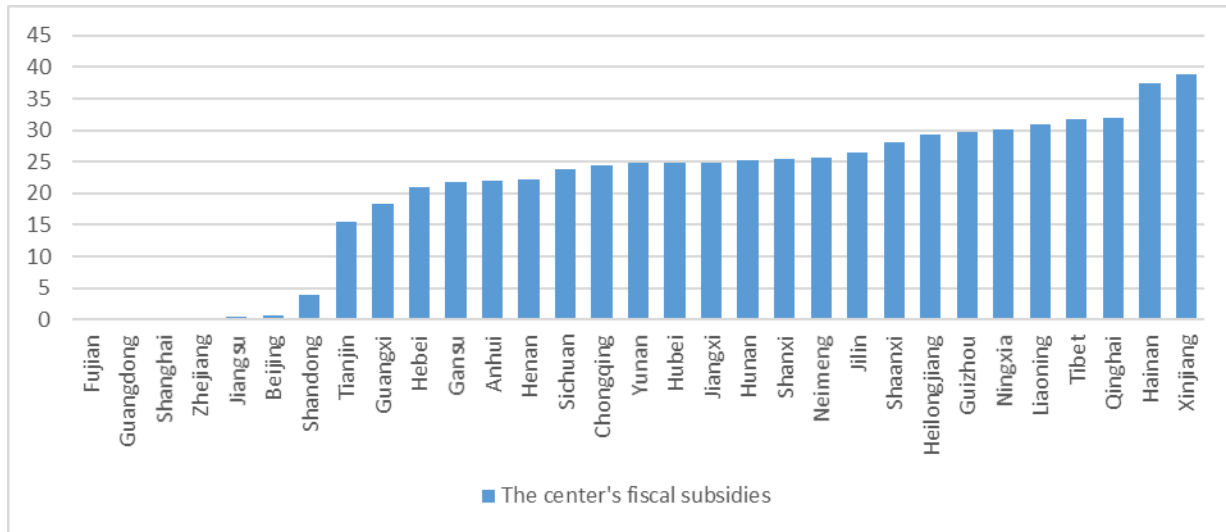
	1999	2000	2001	2002	2003	2004	Sum	Percentage
Center	174.7	338.3	349.3	408.2	474.3	521.9	1768.8	89.7%
Local	18.5	27.7	53.5	46.6	51.7	71.5	203.3	10.3%

Source: Yang (2006), p. 175.

Table 4-1 shows the latest available data on the amount of transfer payments to the pension system from the center and local governments respectively from 1999 to 2004. It shows that the transfers came mainly from the center, with only 10% of the transfers coming from local revenue. How to allocate this massive number of fiscal subsidies across subnational units is nothing more than a strategic decision for the center. In addition, where the 10% local fiscal

contribution came from, namely which subnational units paid for the pension program from their fiscal budgets, also is not shown in this table.

Figure 4-2 The center's fiscal subsidies as the average percentage of each province's local pension spending, mean values from 1999 to 2004 (unit: %)



Source: Yang (2006), pp. 181-2.¹³

Figure 4-2 reveals the breakdown of the central government's pension transfers at the provincial level. Since the amount of pension deficits/surpluses varies greatly across provinces, it makes more sense to compare the percentage of each province's expenditure on the pension program that came from the center's subsidies.¹⁴ Figure 4-2 shows significant variation among provinces – while some coastal provinces were completely self-reliant, provinces like Hainan and Xinjiang had more than 35% of the pension spending coming from the center.

¹³ Data on 1998 are reported in Yang (2006). All entries for 1998 are small numbers. Since 1998 was the second year after the 1997 reform plan was announced, the data on the center fiscal transfers may not immediately reflect in the center's fiscal budget. Therefore, I decided to drop the data for 1998.

¹⁴ There are mainly three income sources to fund the local pension program. They are 1) pension contribution from employers and employees, 2) fiscal transfers from the center, and 3) fiscal transfer from local governments.

Figure 4-3 Map of the center's fiscal subsidies

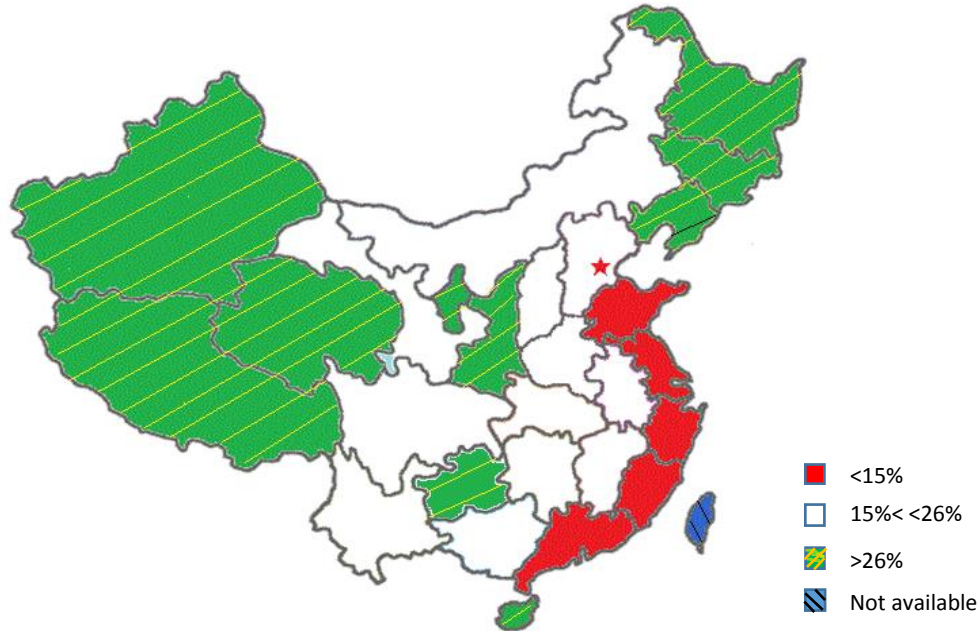


Figure 4-3 visualizes the regional allocation of the center's fiscal resources on a map. The map shows that as a sharp contrast with fiscally self-independent coastal provinces, northeastern regions, and western border regions were more heavily subsidized by the center. A high majority of mid-land regions' subsidy situations were in between these two groups. What factors contribute to the center's redistributive decisions?

4.4 The contentious economic transition

Like many other post-Communist countries, China experienced economic stratification and social grievances during economic transitions (Cook, 2007). How to maintain political solidarity while pushing forward economic reforms was of great importance for the regime's survival. Premier Zhu Rongji was the main political entrepreneur at the central level who strongly pushed forward economic marketization. He advocated changes to 1) introduce the market mechanism both to SOEs and government departments, and 2) substantially downsize

humongous state-run entities developed under the planned economy, to improve their economic efficiency. The slogan he proposed – “Encourage mergers, standardize bankruptcy, lay off workers, and implement a re-employment policy” – boldly signaled his reform ambition.

Certainly, he understood potential social problems that might be brought about by this wave of reforms. Thus, to couple with these reforms, he urged local governments to ensure basic livelihood for the people, and to provide old-age pension benefit payments in a timely manner for current retirees and new early retirees and even some laid off workers (Zhu, 1998).

Unexpected, the 1997 Asian financial crisis swept through China and made the already difficult economic transition even more challenging. Many SOEs went bankrupt, and many others were on the edge of bankruptcy. During the five-year period from 1995 to 2000, there were more than 14 million registered unemployed urban residents in total, which includes only those who self-claimed unemployed and registered at the government’s reemployment centers. In the year 1999 alone, the official number of the registered unemployed, including layoffs and those retain the position without pay and allowance, was 2.2 million. These numbers did not include rural migrant workers who could not find jobs in urban areas or lost jobs during the period (Cai et al., 2001). Studies estimate that the overall number of layoffs reached 45 million from 1995 to 2002 (Giles et al., 2005), and the actual unemployment rate in China between 1978 and 2006 was around 12%, much higher than the number announced by the government (Zhou, 2011).

Delays in or non-payments of retirement benefit were rampant across the country in the late 1990s and early 2000s (Pan, 2005). By 1997 only five political administrative units in the country – Beijing, Tibet, Xiamen city from Fujian Province, Qingdao city from Shandong Province, and Shenzhen city from Guangdong Province – had not encountered any problem in paying retirement benefits on time and in full (Gao, 2006). Table 4-2 reveals regions and

industries that suffered particularly severely from delays in pension payments, with the amount of delayed payments exceeding 100 million *yuan* in 1997.

Table 4-2 Regions and industries with delayed pension payments by over 100 million *yuan*, 1997

Regions and industries	Number of people affected (in 10,000)	Delayed amount (in 100 million <i>yuan</i>)
Heilongjiang	35.5	13.13
Jilin	16.1	3.45
Liaoning	20.6	2.14
Sichuan	16.5	1.9
The coal industry	20.7	1.86
Jiangsu	11.4	1.5
Hunan	22.9	1.08

Source: Gao (2006), p. 137.

There were three main reasons that caused the nationwide delays in or nonpayment of pensions. First, the pension program was not officially pooled at the municipal level until the mid-1990s. Non-SOEs' involvement in the pension program was minimal, so SOEs were still the dominant providers of retirement benefits. However, the tough economic situation of SOEs did not allow them to continue taking on this expensive responsibility. Second, many SOEs stopped paying pension premiums for their employees with the beginning of SOE reforms in the early 1990s. As these employees retired, the non-contribution problem surfaced. Third, as a result of SOE reforms and the financial crisis, the number of layoffs and early retirements skyrocketed in the late 1990s, which dramatically reduced the number of pension contributors while greatly increased the number of pension benefit recipients. These effects of reform together crushed the old pension arrangement. Among the 31 provinces, the number of provinces whose annual

retirement benefit payment amount exceeded its pension contribution income increased from 16 in 1997, to 21 in 1998, and to 25 in 1999 (Gao, 2006, p. 137).

As a result, pensioners, including early retirees and layoffs, took to the street to demand their sacred rights of retirement benefit payments, their only source of income for living (Hurst & O'Brien, 2002). The multiplication of workers' protests occurred simultaneously with speeding up of SOE reforms. The protesters often gathered in front of city halls, blaming the managing authorities of their enterprises for not providing the contractual social benefits, mainly retirement benefits. The protests sometimes got really contentious when local officials refused to respond with any meaningful resolution to address their concerns. Take a mass gathering in Shenyang city for example, the capital city of an old industrial base in Liaoning Province. Around four hundred pensioners protested for an over eight-month delay in making retirement benefit payments. A hundred or so policemen came to prevent passers-by from joining the protest and moved rioters apart (Kernen, 2005). Protests like this were common during the transitional period, especially in old industrial bases where SOE towns were located (Hurst & O'Brien, 2002) (BJN0402121, BJC0614131, HBP0705131, and LNP1213131).

The immediate cause that led to the center's decision on large-scale fiscal transfers to assist local pension programs was a protest in Shenyang city in July 1997. Premier Zhu paid a visit to Liaoning to inspect SOE reform progress from July 18 to 24 in 1997. Upon the arrival of Zhu, hundreds of retirees and layoffs sat on small benches in the middle of a main road in Shenyang to request the government to give a reasonable explanation to the pension nonpayment issue. Instead of trying to pacify the protestors, Zhu decided to make a detour to avoid direct contact with them (BJC0614131). Soon after the visit, Zhu announced a decision to "open the granary and distribute the grain to the public" (*kai cang fang liang*), to put in his own words,

which began the center's heavy fiscal subsidies to subnational governments for welfare development. Meanwhile, he proposed two specific social policies to support the SOE reform: "two guarantees" (*liangge quebao*) policy, and "three support lines" (*santiao baozhang xian*) policy. The "two guarantees" policy was to guarantee 1) subsistence allowances for laid-off workers from SOEs would be provided, and 2) basic pension benefit payments for retirees would be paid on time and in full. And "three support lines" policy noted that layoffs from SOEs may receive no more than three years of basic subsistence allowances from the newly created Re-Employment Service Center; if no re-employment occurred within the three-year period, workers would receive unemployment insurance benefits for up to two years; and if they were still unemployed after the two-year period, they could apply for minimum living allowances for urban residence (*di bao*) from their local county government. To ensure smooth implementation of these subsidy programs, the center promised to provide financial support to subnational governments if needed.

In addition, to ensure local rulers had sufficient financial resources to carry out the pension reform and provide retirement benefits, the center decided to bail out all historic pension deficits local governments had at that time, using the central fiscal budget as a one-time special fiscal subsidy in 1998.¹⁵ However, as subnational governments sugarcoated their pension situation and underreported the deficit amount, the real effects of this bailout program did not meet the center's expectation (BJC0614131). In addition, the center decided in 1998 to break down the industry-based pension programs for powerful center-owned industries, such as the ones for workers in coal, mining, railroad, and gas industries, and merged these outstanding programs for the general public pension programs. That meant that subnational governments

¹⁵ The information on the amount of this one-time fiscal transfer each province received was not available. The data on the center fiscal transfers used in this study do not include this special transfer.

were granted the right to manage pension contributions and benefit payment provisions for these SOE employees. This decentralization reform of industry-based pension programs brought subnational governments a healthy amount of fiscal revenue and pension contribution income. As local governments started gaining more financial resources and began to revitalize the pension program, the acute pension crisis was temporarily relieved. As such, sub-national governments were brought on board to carry out the center's 1997 pension reform.

4.5 Consolidating the great unity of all ethnic groups

China is a very diverse and multi-ethnic state, and many ethnic groups are especially found in the border regions. Ethnic and territorial integrity has always been a priority for Beijing. Upon the founding of New China, the center set up five autonomous regions in areas where a single ethnic group accounted for a large majority of the local population; and these five province-level governments were granted more discretion and powers than other provincial governments. These five autonomous regions are Tibet, Xinjiang, Ningxia, Guangxi, and Inner Mongolia. The center has launched various preferential policies in these minority regions including trading, finance and the monetary sector, and welfare programs for ethnic minorities. In the *Twelfth Five-Year Plan on the Development of Ethnic Minorities 2012* (General Office of the State Council Notice No. 38), the center reiterated that:

“The overall development of ethnic minorities, is a matter of well-being of all ethnic groups, of socialist modernization, of national unity and long-term stability, and of great practical significance and far-reaching historical significance.”

The center takes ethnic issues as a matter of regime survival. To accomplish its grand vision, the center requested that all sub-national governments support its preferential policies

toward ethnic minority groups, by all means, unconditionally. On the ethnic minority issue, all sub-national governments should “stress Party spirits and dedication, but not negotiate the terms or price (with the center)” (*jiang dangxing, jiang fengxian, bu jiang tiaojian, bu jiang jiaqian*) (Li, 2005). This section presents a general overview of preferential policies ethnic minority regions enjoy, and discusses the favorable fiscal and welfare programs these regions receive.

Ethnic minority regions were created with more privileges from the center than their counterparts. In addition to giving ethnic minority governments more autonomy on fiscal policymaking, the center also granted them subsidies for economic production, and health and social assistance programs, as well as providing them interest-free loans, among other benefits. These policies were vitally important in aiding these regions in recovering economic production, maintain social stability, and most importantly building political solidarity. In the 1980s when the center carried out “eating in separate pots” fiscal reforms, the central government still provided fixed-amount subsidies annually to eight ethnic regions, including the five autonomous regions and other three other regions with a high percentage of ethnic population, namely Qinghai, Yunan, and Guizhou. In addition to general and regular fiscal transfers, the center created a “development fund for supporting less developed regions”, a “border development subsidy program”, a “special subsidy and investment program for borderland construction”, and so forth, targeting exclusively these regions. These supporting grants remain intact today.

As the fiscal capacity of the center increased dramatically after the 1994 tax-sharing reform, the center’s subsidies for these minority regions multiplied. In the single year alone, the center granted policy-oriented fiscal subsidies of 2.9 billion *yuan* to ethnic minority regions, accounting for 48 percent of the center’s transfer payments nationwide that year (Wang, 2001, p 190). According to statistics published by the State Council, between 1978 and 2008, the center’s

fiscal transfer payments to minority regions reached 2.1 trillion *yuan*, with an annual increase rate of 15.6 percent (State Council Information Office, 2009). Table 4-3 summarizes major preferential fiscal subsidy policies the center has provided to ethnic minority regions.

Table 4-3 The center’s major preferential fiscal policies to ethnic minority regions.

Policies	Implementation period
General subsidies to ethnic minority regions	1955 until now
A tactical fund for ethnic minorities	1964 until now
A higher proportion of local fiscal reserve in minority regions	1964 until now
A border development subsidy program	1977 until now
A special subsidy and investment program for borderland construction	1977 until now
A development fund for less developed regions	1980 until now
A 10% increase rate for the center’s fiscal subsidies to minority regions	1980 to 1988

Source: Wen (1998).

Fiscal transfer is one major strategy adopted by the center to ease ethnic tension. The amount of the center’s subsidies to ethnic minority regions is correlated well with the level of social and political unrest in these regions. For instance, the 1987-1989 turmoil against Chinese rule in Lhasa, the capital city of Tibet, led to a bloody clash with the Chinese security force. After the event, the center proposed a sixteen-word guiding principle for any ethnic minority related government work – taking the initiative to address issues, consolidate, and seek both temporary and permanent solutions with a focus on the latter (*zhudong zhili, qiangji guben, biaoben jianzhi, zhong zai zhiben*). The center’s fiscal subsidies to Tibet increased by 20 percent that year, which doubled the original routine 10 percent increase each year, and in the following year, the center allocated an additional 84 percent of annual funding to Tibet for infrastructure

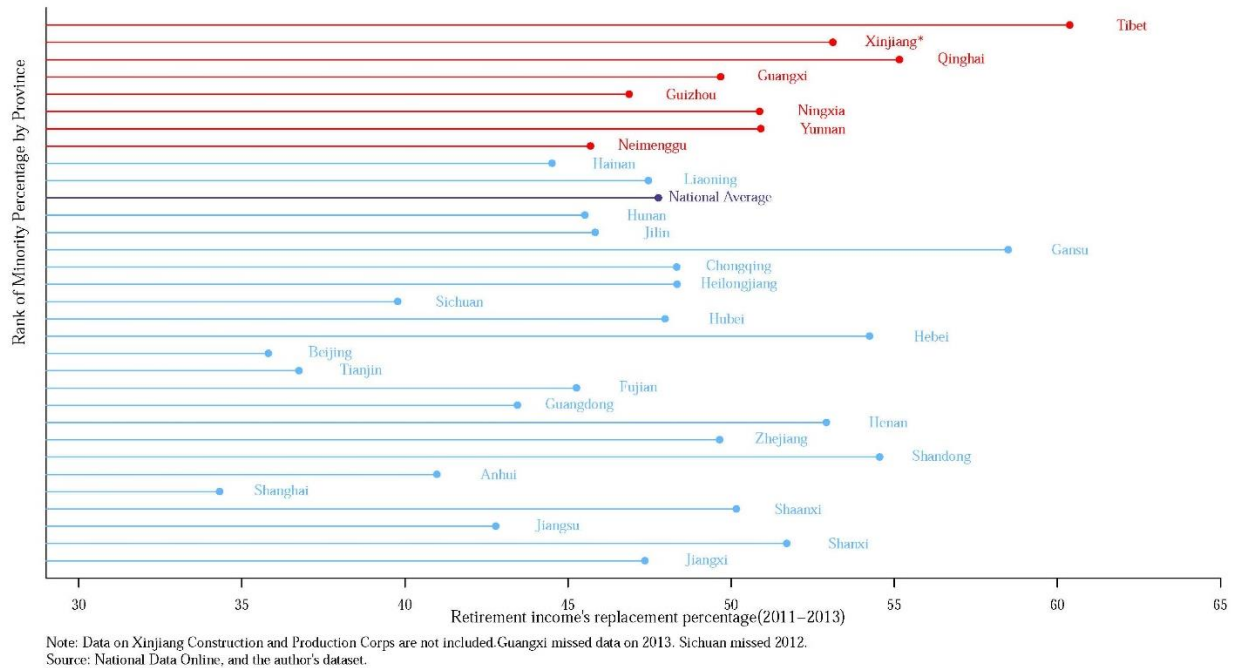
construction (Tibet Autonomous Region Party Committee Office of Policy Research, 1994, p. 30). The same strategy was employed in the large-scale riot attacking Han Chinese in Urumqi on July 5, 2009. In 2010 the center convened a special Xinjiang Work Conference to discuss preferential policies to support the Xinjiang provincial government. In addition, the center requested 19 other provinces and cities to participate in a “large-scale coordinated partner assistantship program with Xinjiang” (*da guimo yuanjiang gongzuo*). A series of special fiscal subsidy programs to Xinjiang were introduced following the conference (Xinhuanet, 2010).

In addition to more favorable fiscal policies toward ethnic minority regions, the center utilizes welfare programs to build and consolidate its support base in the regions, including the urban pension program studied in this dissertation. As Zheng Gongcheng (2000) puts it, social welfare programs are programs that address social programs via economic means. The center prioritizes welfare development in minority regions by elevating the level of welfare protection and benefit provision to achieve its political goal of securing regime stability. The center initiated a program called “ethnic minority old-age social security project” (*shaoshu minzu yanglao gongcheng*) to advance social security development in ethnic minority regions specifically. Urban enterprise retirees in Tibet, Xinjiang, Qinghai, and Ningxia, the four ethnic minority-concentrated provinces, received additional retirement payments, including payments from subsidy programs for ethnic minority regions, for living on highlands, and for living in outlying mountain areas. These subsidies are paid directly from the center’s fiscal budget, not costing subnational governments a penny (*Southern Daily*, 2014). Moreover, the center included Tibetan lamas in the urban residence pension system in 2012, even though the plan was supposed to only cover urban residents who are not enrolled in the public pension program for enterprise employees. Lamas only need to pay 112 *yuan* per person per year, and they will receive 120

yuan per month after they reach the age of 60 years. Any pension fund deficit incurred due to this pension coverage expansion would be bailed out by the center's fiscal budget (Bai, 2012).

Largely due to the factors discussed above, the average retirement benefit level in regions with geographic concentrations of ethnic minorities is much higher than the rest of the country. The pension benefit replacement rate, which is the ratio of retirement income to pre-retirement earnings, measures the value of retirement income in relation to local economic conditions. As an indicator of the replacement rate, this study uses the average income per employee working in urban enterprises as a proxy for pre-retirement income. This dissertation divides mean retirement income by pre-retirement income for the same year to represent the replacement rate. Figure 4-4 presents a simple comparison of retirement income's replacement rate between the major ethnic minority regions and the other provinces. Regions with ethnic minority population accounting for over 20% of the overall population are marked in red, whereas the remaining provinces are shown in blue. The y-axis present provinces by rank of their ethnic minority populations percentage, with Tibet ranked the first and Jiangxi ranked the last, and the x-axis shows the average retirement benefit replacement rate between 2011 and 2013. It is obvious that in general these ethnic minority regions consistently had higher replacement rates than their peer provinces. As we discussed earlier, the center's fiscal support has been an evident contributor to the development of the urban public pension program in ethnic minority regions in China. We will continue to discuss inter-regional welfare inequality in Chapter Six.

Figure 4-4 Retirement income's replacement rate against ethnic percentage, by province (2011-2013)



In addition to the urban pension program, the center's emphasis on promoting welfare development in ethnic minority regions is also manifested in its endeavors in other social policy areas. For example, ethnic minority regions also received preferential treatments from the center to build the new rural pension program, initiated by the center in 2009. According to official statistics reported, the coverage ratio of the new rural pension program in Tibet reached 100 percent, 66 percent in Xinjiang, and 63 percent in Ningxia in 2010, while the unweighted national mean coverage ratio was only 24 percent during the same reported period (Yang, 2010). Since 1990 the center granted a 200-million-*yuan* budget annually to set up a subsidiary education fund for education programs in ethnic minority regions. In 2014, the center created a Poverty Relief Fund, and allocated 18.5 billion *yuan* specifically for the eight ethnic minority regions, which accounted for over 42.7% of the total funding the center provided that year for the program. In addition, by the end of 2014 the central government had granted the eight ethnic

minority regions 1) 9.94 billion *yuan* accumulatively for the urban social assistantship program (*dibao*), accounting for 19.2 percent of the total spending on the program from all levels of governments nationwide; 2) 19.4 billion *yuan* for the rural social assistantship program, which was 33.3 percent of the total spending at the national level; 3) 3.8 billion *yuan* for developing basic urban healthcare insurance, which comprised 27.1% of the national total; and 4) temporary assistance subsidies of 820 million *yuan*, taking up 25.6 percent of the national sum (Zhang & An, 2014). In 2014, the population in the eight ethnic minority regions only accounted for 14% of the national population.

The discussion in this section demonstrates that the center's fiscal assistance to the ethnic minority regions is an enduring and expanding endeavor. The Chinese central government always places "opposing ethnic separatism, and safeguarding national unity" as the highest and most fundamental interest of the nation. The fiscal subsidy program for the urban public pension program is one important component of the center's master scheme of promoting national unity and prosperity.

4.6 Data and measurement

This section uses quantitative data to test the hypotheses on the center's redistributive incentives as stated in the theory chapter. This dissertation hypothesizes that the center is more likely to redistribute to regions with a potential for instability, measured by economic volatility and concentration of ethnic minorities. An original dataset was compiled for all 31 provinces¹⁶, which for each province consists of: 1) the level of fiscal subsidies from the center, 2) the unemployment rate, 3) the percentage of ethnic minorities in the population, 4) a measure of

¹⁶ Xinjiang Production and Construction Army Corps (XPCC) is excluded from this study and is not calculated in any of the data for Xinjiang Province. Created in 1954 by the central government, the XPCC enjoyed special political treatment as a unique economic and semi-military organization.

local economic capacity, 5) the old-age dependency ratio, and 6) a measure of *guanxi* (personal connection).

4.6.1 Measurement of key variables

Dependent variable: The dependent variable for this section's analysis is the support level of the center's fiscal transfer to the pension program to each province ("**transfer**"). As discussed, given that these provinces have a very distinct demographic structures, pension policy designs, and fiscal capacities, instead of using the actual transfer amount, it makes sense to use the center fiscal transfer as of a percentage of annual local pension spending to measure the relative adequacy of center fiscal support to provincial governments. Dr. Yang Fangfang (2006) collected data on the center's fiscal subsidies for the urban pension program to provinces from 1999 to 2004 (see footnote 13 for more details). More recent data would have been ideal. However, given the sensitivity of the information (BJN0619141), Yang's data are the best available. Since the base of the center's fiscal transfer remain quite stable across time (BJC0614131), this data source, in spite of its limited time coverage, provides useful insights into the relative importance of subnational regions in the center's fiscal transfer plans.

Independent variables: There are two sets of independent variables that are of interest – the unemployment rate, and an ethnic minority's geographic concentration in a locality. To match the availability of the dependent variable, the data for all independent variables and control variables are from 1999 to 2004.

*Measurement of unemployment rate ("**unemploy**"):* An unemployment rate may be used as a proxy to measure economic volatility during transitions. Before economic reforms, the urban employment rate was near one hundred percent under the command economy. That means that those unemployed in the 1990s were mainly those who lost jobs during the reform period.

However, measuring the unemployment rate in China is notoriously difficult (Zhang, 2003). Official statistics count only those individuals who register for unemployment benefits with local governments as unemployed. These figures overlook millions of workers who were laid off with no expectation of reemployment, namely those who lost jobs yet did not register with local governments, and also who involuntarily retired early, among others (Solinger, 2001). Estimates of the overall unemployment rate in certain localities based on survey data are available (Giles et al., 2005). However, to ensure cross-regional comparability, this study used data released in *China Statistical Yearbooks*, and calculated an estimated total unemployment rate. This study will use official statistics for the number of the registered unemployed, the number of layoffs, and the number of total urban employees to estimate the unemployment rate.

$$\mathbf{unemploy} = \frac{\# \text{ of registered unemployed} + \# \text{ of layoffs}}{\# \text{ of urban employees}}$$

Measurement of ethnic concentration: *China Statistical Yearbooks* have data on the ethnic composition of urban population in each province. To measure ethnic concentration, there are two possibilities – 1) the proportion of all ethnic minorities in urban population, and 2) the proportion of one dominant ethnic group in urban population. Two variables “**ethny**”, and “**oneeth**”, were used to represent these two measurements respectively.

Control variables: Several controls were included for factors that might be expected to affect the center’s fiscal resource allocation. To capture the economic capacity of a locality, I used gross local product per capita (“**gdppercap**”). It is expected that the center is more likely to redistribute to localities with a lower level of economic capacity to balance inter-regional development. Local GDP per capital is commonly thought to be badly skewed, so log-transformed **gdppercap** (“**lgdppercap**”) was used. To capture the existing demographic structure of a locality, the urban old-age dependency ratio, calculated as the proportion of 60 year-old and

older in the urban population (“age”) was used. The information is available in *China Statistical Yearbooks*. A society with a high old-age dependency ratio is more likely to be burdened with old-age pension provisions. Thus, the center is more likely to provide fiscal subsidies to localities with a higher old-age dependency ratio. Lastly, a variable called “**guanxi**” was also included to measure personal connections (*guanxi*) in center-local relations. It is commonly believed that if top government officials from a locality have personal connections with officials at the central level, especially in the Ministries, the locality is likely to receive more favorable fiscal treatment from the center. The dataset collected by Qingjie Zeng, Professor of Political Science at Fudan University in China, was used. The dataset traces career development paths of members of each province’s provincial standing committees, and records whether these members had work experience at the center, and when. If an official had work experience at the central level, s/he is coded as “1” and “0” otherwise. A “**guanxi**” variable was constructed by counting how many members serving in the Provincial Standing Committee in a year that had previously worked at the central level.

To overcome the limitation of traditional ordinary least square models for the estimation of time-series cross-section data (Beck & Katz, 1995), a Prais-Winsten regression with Cochrane-Orcutt transformation and autocorrelation of residuals is conducted to test the hypotheses (Keele & Kelly, 2006). Using the Cochrane-Orcutt transformation will drop the first observations, which reduces the final number of observations in this estimation from 185 to 155.

An econometric model is specified as follows:

$$Transfer_{it} = \beta_1 + \beta_2 unemploy_{it} + \beta_3 ethn_{it} + \beta_4 \log(gdppercap)_{it} + \beta_5 age_{it} + \beta_6 guanxi_{it} + \varepsilon_{it}$$

i=1, 2, ... 31;

t=1999, 2000, 2001, 2002, 2003, and 2004;

$$\varepsilon_{it} = \rho \varepsilon_{i(t-1)} + \eta_{it}$$

4.6.2 Analysis

4.6.2.1 Findings

Table 4-4 reports the results of the regression for the center's fiscal transfer decisions ("center's transfer", for short) from 1999 to 2004. Panel corrected standard errors are in parenthesis. *, **, and *** indicate significance on a 90%, 95% and 99% confidence level respectively. The analysis begins with the estimates that regress the center's transfer against the total unemployment rate ("unemploy") and the control variables mentioned above, and report the results in column (1). The coefficient of the unemployment rate is positive and significant at the .01 level, and the coefficient of local GDP per capita is negative and significant at the .01 level. Column (2) reports the estimates when the proportion of ethnic minority in population ("ethny") is included in the regression. In comparison with the regression estimates reported in column (1), this regression produces better results, because 1) the coefficients of "unemploy" and "lgdppercap" remain significant, 2) the coefficient of unemployment rate improves, and 3) the overall adjusted R^2 increases by .07. In addition, in Column (2), the coefficient of the "ethny" variable is positive and statistically significant at the .01 level. That means that adding the "ethny" variable increases the explanatory power of the model, and the "ethny" variable itself has a significant impact on shaping the center's fiscal transfer decisions.

Table 4-4 Center's redistributive incentives, 1999-2004, using Prais-Winsten regression with Cochrane-Orcutt transformation and autocorrelation of residuals.

Dependent Variable: the center fiscal transfer as a percentage of local pension spending						
	(1)	(2)	(3)	(4)	(5)	(6)
unemploy	.61*** (.22)	.83*** (.21)	.79*** (.21)	.95*** (.22)	.83*** (.20)	1.23
ethny		.31*** (.08)		.33*** (.08)		1.36
oneeth			.30*** (.09)			
lgdppercap	-.13*** (.02)	-.11*** (.02)	-.11*** (.02)	-.10*** (.02)	-.11*** (.02)	1.90
age	-.74 (.49)	-.39 (.48)	-.42 (.48)	-.28 (.47)	-.18 (.47)	2.18
guanxi	-.005 (.007)	-.005 (.007)	.005 (.006)	.003 (.006)	-.004 (.007)	1.08
lethny					.034*** (.008)	
Constant	1.45*** (.20)	1.19*** (.19)	1.26*** (.19)	1.08*** (.19)	1.34*** (.17)	
# of observation	155	155	155	155	155	
R ²	.35	.42	.40	.45	.44	

*p < 0.1; **p < 0.05; ***p < 0.01

Source: Author's dataset.

However, as stated, we may measure ethnic concentration in a locality by the proportion of one dominant ethnic group in the population. Column (3) reports regression results when “ethny” is substituted by “oneeth”. Comparing columns (2) and (3), these two regressions yield similar results, which means the effects of “ethny” and “oneeth” are very similar. However, in

regression (2) “ethny” has a higher coefficient than “oneeth” does in regression (3), and the overall performance of model (2) is slightly better (measured by a two percentage points higher R^2). Therefore, regression (2) is preferred over regressions (1) and (3).

On the basis of the regression results presented in column (2), the effects of the independent variables, and then the control variables are interpreted. The coefficients of both independent variables are positive and statistically significant at the .01 level. The positive coefficient of “unemploy” means that more fiscal resources from the center are allocated to regions experiencing high unemployment rates, or economic volatility, as predicted in Hypothesis 1-1. A calculation of marginal effects shows that a one percent increase in the unemployment rate is associated with an average .83 percent increase in the center’s fiscal transfer to total local pension spending (for simplicity, the center’s transfer). The positive coefficient of “ethny” means that the center distributes more fiscal resources to localities with more ethnic minorities. A one percent increase in the proportion of ethnic groups in population is associated with an average .31 percent increase in the center’s transfer, consistent with Hypothesis 1-2.

Among all the three controls, only local economic capacity has statistically significant coefficients at the 0.01 level. Local GDP per capita has a negative coefficient, which indicates that the center distributes more fiscal resources to regions that are economically backward. This finding is not surprising as the very purpose of redistribution is to transfer resources from the rich to aid the less developed. The coefficient of “lgdppercap” implies that a one-thousand *yuan* decrease in local GDP per capita is associated with a 1.1 percent increase in the center’s transfer. Surprisingly, demographic structure does not have significant impact on the center’s redistributive decisions, which means that the center grants more fiscal subsidies to regions with

a younger demographic structure. The insignificant impact of the “age” variable lends support to the argument that the center’s redistributive decisions in the pension case is nothing more than political, rather than simply aiding regions suffering from unfavorable demographic structure. Provincial officials’ personal connections with central level government officials as measured by the *guanxi* variable do not seem to have much impact on the center’s transfer decisions.

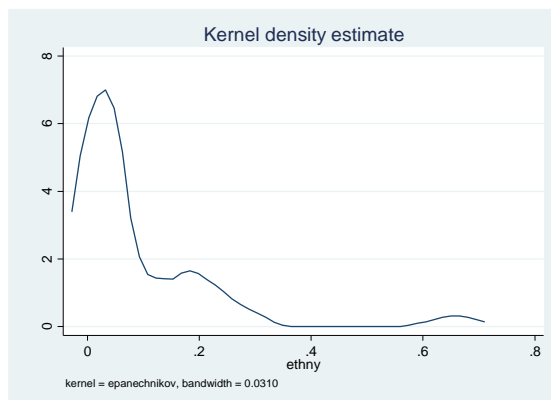
4.6.2.2 Robustness check

Three sensitivity tests were conducted to check that the major findings are robust to alternative specifications. First, previous analysis assumes that the center’s transfer decisions are shaped by factors from the same year. However, the center often makes budgetary decisions in the end of a prior year, and uses situations of the prior year to come to the decisions. Therefore, one-year-lagged independent and control variables are appropriate. Column (4) reports results of the same Prais-Winsten regression for variables from 1999 to 2004, with the *t-1* modification on independent and control variables. Results reported in column (4) show that signs and significance of all variables involved remain the same as in regression (2). The coefficient estimates for total unemployment rate and ethnic population increase, and the coefficient of local economic capacity decline slightly. The overall performance of the model increases by .03. However, a time-lagged regression model may overcomplicate the Prais-Winsten procedure, which may result in inaccurate estimation. Nevertheless, this robustness check confirms the conclusion drawn from regression (2) above.

Second, a Prais-Winsten regression assumes a normal distribution of variables. As for “gdppercap”, the data for ethnic groups in a population (“ethny”) are subject to a high possibility of a skewed distribution. To visualize the distribution of the variable, its histogram is included in Figure 4-5. The histogram shows an exponential form curve – long-tailed distributions skewed to

the right, of the data distribution of “ethny”. This means that one unit increase in the explanatory variables at the higher end results in a much larger change in the dependent variable than one unit change on the right. We may use log transformation to solve the problem. Column (5) in the table presents the regression results with the log-transformed “ethny” variable. Results reported in the table show that all variables keep their signs and significance. In addition, for the transformed “ethny” variable, the log transformation does not affect the values of the standardized coefficient estimate and its significance.

Figure 4-5 Histogram for “ethny”



Third, the explanatory variables included may not be mutually independent. The unemployment rate and economic development may be suspected to be highly correlated, and ethnic minority regions may be associated with economic backwardness too. Even though a violation of independence of variables will not affect the overall predictive power of the explanatory model, it will produce invalid coefficient estimates for the correlated variables. A *vif* test is included to diagnose whether the model has a collinearity problem. The results are presented in column (6) in the table. It is commonly held that a value of VIF greater than 5 indicates the presence of collinearity. The VIF values of the variables of interest in column (6) are lower than 2, and the VIF of the “age” control variable is at the 2.18 level. Thus, it is safe to conclude that the model does not suffer from a collinearity problem. Overall, the effects of

unemployment rate, ethnic concentration, and economic capacity remain robust after the three robustness checks.

4.7 Conclusion

This chapter has sought to examine factors that affect the Chinese central government's redistribution decisions. With a decentralized fiscal and administrative political structure, the Chinese central government has to rely on subnational governments to carry out its policies. However, the interests of the center and its subnational agents may not always be in line with each other. In such a situation, it is a well-known challenge for the center to incentivize subnational governments to behave according to the center's desires. Developing the public pension program is particularly challenging in this regard, as operating a public pension program requires a long-term and extensive financial commitment from the government. Since the 1994 tax reforms, the center has withheld a larger share of the national revenue, yet subnational governments are still obligated to fund and operate social programs such as public pensions. Meanwhile, the center placed increasing emphasis on welfare development to maintain regime stability during the volatile economic transition. For the center, these welfare programs were not simply measures to improve the wellbeing of the people, but more importantly a political strategy for a matter of life or death of the regime. This means that the center almost certainly needs to transfer fiscal resources to subnational governments to ensure smooth implementation of these programs, especially in localities with strategic importance to the center. Yet how the center distributes its limited resources across subnational regions is a political decision.

The center's fiscal subsidies of the pension program are distributed very unevenly across sub-national provinces. This chapter has examined the factors that contribute to the center's decisions regarding fiscal transfers for the pension program. Using both historic narratives and

statistical analyses, this study finds that two factors are crucial to help us understand the center's redistributive rationale – economic instability, and political instability. These two factors could ignite social grievances and arouse large-scale unrest at all times during the transition, which posed a great threat to the regime survivability. Maintaining political stability is the ultimate interest of the center. This chapter has shown that using pension subsidies as a redistributive strategy, the central government not only distributed more subsidies to regions with weak economic capacity, but more importantly to regions that faced high risks of instability, namely those with higher unemployment rates, and with higher percentages of ethnic minority population. Besides granting substantial fiscal aid to these regions, the center also provided preferential policies to governments suffering from economic and political instability to assist peacekeeping operations and further to economic and social development. Yet some usual suspects, such as demographic structure and personal connections between central and subnational rulers, do not seem to offer powerful explanations of the center's redistributive decisions in the public pension case. In addition, because of the uneven allocation of the center's fiscal resources at the provincial level, this chapter echoes the finding of Shirk (1993), who argued for a particularistic fiscal contracting system in China during the 1980s,¹⁷ which still marks the flexibility of Chinese center-local fiscal relations today.

The finding of this chapter sheds light on the fiscal relationship between the Chinese center and subnational governments. Consistent with the arguments of Goldstein (1995) and Tsai (2004), while the central government is faced with a hard budget constraint, subnational

¹⁷ Shirk argues that China has a particularistic fiscal contracting system, which was initiated during the 1980s and early 1990s. Instead of having a uniform fiscal system, the central government signed contracts with individual local governments on an *ad hoc* basis, which gave local governments added fiscal autonomy. Local governments may turn to the center to ask for more subsidies. Meanwhile, the center may build a political support base in a locality by rewarding its special reform programs with fiscal support. Shirk believes that understanding this system was crucial for explaining how the center incentivizes local governments to promote the market economy and economic growth.

governments may sometimes turn to the center for fiscal support. This study adds that the center may intentionally relax the budgetary constraint for regions that are of strategic importance to the center. In other words, the center uses fiscal transfers to regulate and motivate its subnational agents to carry out tasks the center desires. However, regions that do not have significant political significance are likely to face harder budget constraints, and resemble more the market-preserving federalism operation model famously advocated by Qian, Weingast and their co-authors (Jin et al., 2005; Montinola et al., 1995; Qian & Weingast, 1997). Therefore, instead of having one formula that explains Chinese center-local fiscal relations, this chapter uses empirical data to demonstrate that the two types of fiscal relations co-exist in today's China.

This chapter concludes with a new question – how do local governments react to the center's uneven distribution of fiscal subsidies? The center's pension subsidies created a situation wherein the costs of running the pension program vary greatly among local governments. In addition, local governments have very different local social and economic profiles, which may also affect their redistributive decisions. Lastly, how did the center's fiscal subsidies interact with local conditions to shape local governments' pension policy designs? The next chapter will address these questions.

Appendix Table 4-1 Retirement income replacement rates and ethnic percentages by province

Province	2011	2012	2013	Ethnic pct. (%)	Province	2011	2012	2013	Ethnic pct. (%)
<i>Major ethnic minority regions</i>									
Guangxi	48.83	50.52	N.A.	38.34	Qinghai	55.00	55.43	55.03	45.51
Guizhou	48.93	46.86	44.82	37.85	Xinjiang*	55.14	53.25	50.95	59.39
Neimenggu	47.34	44.59	45.12	20.76	Yunnan	50.68	51.38	50.66	33.41
Ningxia	50.39	50.42	51.80	34.53	Tibet	58.10	62.66	60.36	94.07
<i>Other provinces</i>									
Anhui	40.67	40.59	41.66	0.63	Liaoning	45.97	47.65	48.76	16.02
Beijing	36.06	35.59	35.78	4.26	Jiangsu	42.79	43.01	42.54	0.33
Chongqing	48.69	48.54	47.75	6.42	Jiangxi	47.65	47.17	47.24	0.27
Fujian	43.69	44.28	47.79	1.67	Jilin	45.63	45.71	46.14	9.03
Gansu	61.44	58.66	55.36	8.69	Shaanxi	51.00	49.63	49.83	0.49
Guangdong	44.07	42.60	43.66	1.42	Shandong	53.85	55.07	54.72	0.68
Hainan	43.37	45.83	44.32	17.29	Shanghai	32.67	35.48	34.80	0.60
Hebei	53.15	54.17	55.40	4.31	Shanxi	51.27	50.05	53.78	0.29
Heilongjiang	48.57	47.14	49.30	5.02	Sichuan	41.40	N.A.	38.15	4.98
Henan	52.27	51.20	55.27	1.22	Tianjin	36.65	36.67	36.92	2.64
Hubei	45.84	48.31	49.75	4.34	Zhejiang	49.71	49.99	49.23	0.85
Hunan	44.48	45.76	46.29	10.21					
National Average	47.59	47.94	47.77	15.02					

*: Data on Xinjiang Construction and Production Corps are not included.

N.A.: Not available

Data source: National Data Online, and the author's dataset.

Chapter 5 Provincial governments' counter plays against the center

-- Where there is a policy, there are countermeasures

(上有政策，下有对策)

5.1 Introduction

Building on the analysis of the center's redistributive decisions in the previous chapter, this chapter investigates provincial governments' rationales in designing their pension programs. As discussed earlier, provincial governments are the real policy makers of social and economic policies in China. The variations in the redistributive design of the public pension program we observed are direct policies produced by provincial governments. This chapter develops a typology to explain patterns of the fiscal structure of the pension program at the provincial level, which helps explain the variations in the pension contribution rates across subnational regions. I argue that two factors at the provincial level – the availability of center fiscal support, and the level of economic openness – largely define provincial governments' policy calculations in pension policymaking. The content of this chapter draws heavily upon the qualitative data from the author's fieldwork research in six provinces, Liaoning, Tibet, Hunan, Hubei, Gansu, and Guangdong. Through detailed case studies of these provinces, this chapter demonstrates five types of fiscal structure for pension programs at the provincial level.

As mentioned in the theory chapter, largely confined by the cadre evaluation system, subnational government officials are oftentimes short-sighted and administrative boundary-bounded. A recurring finding from the interviews was that provincial government officials are mainly concerned about political merits as measured by short-term economic development indicators during their terms in office, and often leave longer-term development goals, such as welfare development, to their successors (BJN0619141). When making policies, local government

officials often do an addition-subtraction calculation – they often take promoting economic growth as an addition, but see dedicating resources to welfare development as a subtraction (LNP1213131). Even though the center repeatedly emphasized the importance of social welfare development in measuring local government officials’ performance, economic indicators still weigh most heavily in the current cadre evaluation system. An official from Gansu frankly admitted that top provincial leaders were evaluated by the annual increase in the individual disposable income level, and the pressure of promoting economic growth was passed down to all levels of sub-provincial governments (GSP0409152). The rationality of sub-national government officials’ short-sightedness on welfare development may be best demonstrated via a story shared by a scholar. A government official from Yichang City, Hubei Province, responded to a scholar’s question on the sustainability of Yichang’s pension fund. He answered, the pension fund may collapse after ten years, but by then he would have been long retired, and it would be an issue out of his concern. He continued, the funding situation of Yichang’s pension fund was in the medium range of all counties nationwide. Therefore, before Yichang’s pension fund would encounter any serious problems, other cities and provinces would have cried out first. The center would find ways to resolve it before the problem hit Yichang (HBN0710131).

This chapter has nine sections. The next section categorizes the five types of funding structures for pension programs found at the provincial level. The subsequent five sections present six in-depth case studies respectively, Liaoning, Tibet, Hunan/Hubei, Guangdong, and Gansu. Section Eight discusses the effects of center-local interactions on pension generosity at the individual level. The last section concludes with implications of the findings.

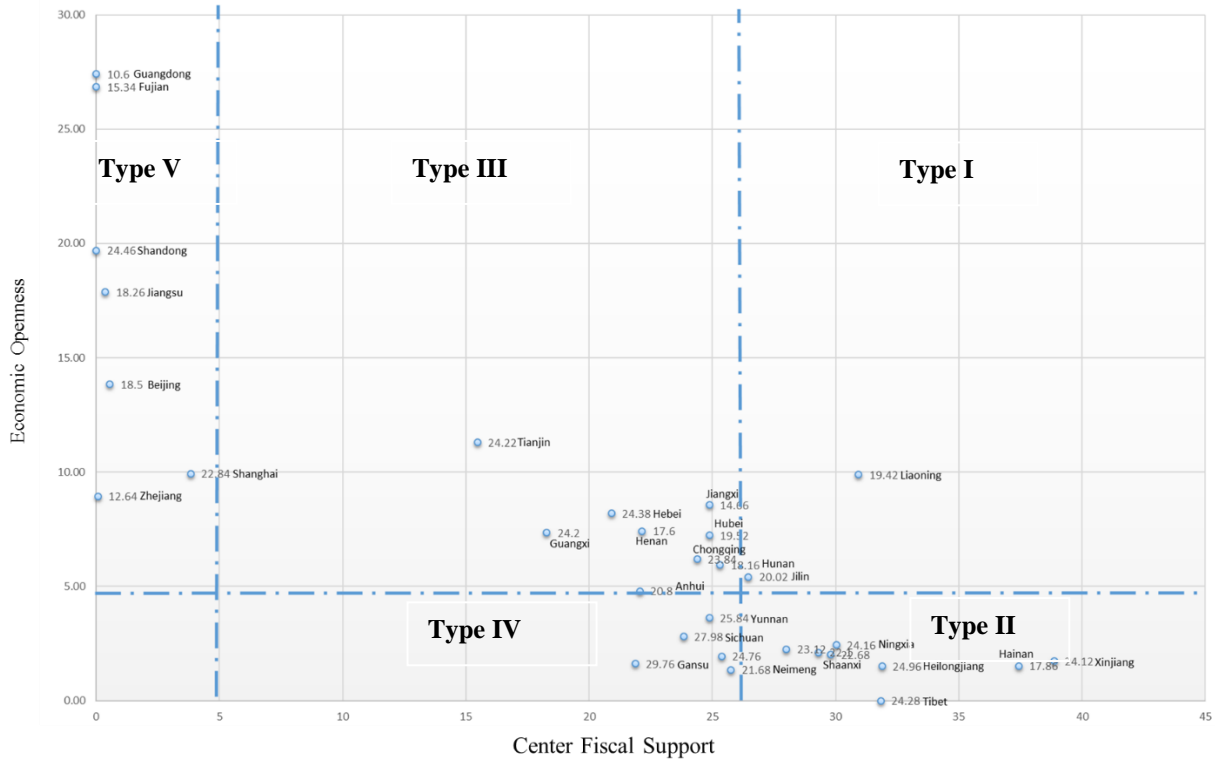
5.2 A typology of the fiscal structures of local pension programs

How provincial governments in China fund their expensive urban pension programs has never been systematically investigated. Lack of a centralized pension administrative system has led to a scenario wherein provincial governments become *de facto* policymakers to make specific pension policies based on local situations. This study calls for our attention to two factors at the sub-national level – 1) political sensitivity, and 2) capital mobility in the economy – that help us understand variations in the fiscal structures of local pension programs. First, as discussed in Chapter Four, localities challenged with economic volatility during the economic transition, or with a concentration of ethnic minorities, are regarded by the center to be politically sensitive regions, and these regions are more likely to receive center fiscal subsidies than regions not deemed to be politically sensitive. Second, fearing capital flight, government officials from regions that are economically dependent on private and foreign investments are likely to set lower employers' pension contribution rates, and compensate for this loss by drawing on other funding sources. This study finds that there are potentially three funding sources for local pension programs: 1) pension premiums collected, 2) fiscal subsidies from the central government, and 3) local fiscal resources. Here it is important to recall the typology of pension systems discussed in Chapter Two. Chapter Two explained how the causal theory put forth in this dissertation predicts five possible scenarios for pension funding structures at the subnational level (see Table 2-2). This chapter empirically tests whether subnational pension funds actually fall into those five scenarios or pension types predicted in Chapter Two.

Figure 5-1 displays the relationship of these 31 provinces as data points in a scatter plot chart, with the level of center fiscal support on the pension program displayed on the x (horizontal) axis, and the level of economic openness shown on the y (vertical) axis. Each data

point has two data labels: 1) province name, and 2) the average actual total pension contribution rate aggregated to the provincial level for 2007 through 2011. The dashed lines divide these data points into five groups. First, localities with major fiscal subsidies from the center and high percentages of mobile investments in the local economy are likely to see the subsidies as leeway to lower the contribution rate. Second, localities with major center fiscal subsidies and less mobile economic profiles are likely to set higher contribution rates. Third, localities that are without much fiscal support from the center and economically dependent on mobile investments are likely to subsidize the pension programs by using local fiscal resources to keep the contribution rate low. Fourth, the localities without much fiscal support from the center and with less mobile capital afford to raise the contribution rate to compensate local pension funds for the lack of center fiscal subsidies. Lastly, Type Five, a sub-category of Type Three, includes regions that enjoy complete fiscal independence from the center and the highest level of economic openness. These regions' vibrant economic environments attract talent from all over the country, including from migrant workers. However, with the pension program's limited portability problem, most migrant workers contribute only to pension program yet almost never receive any retirement benefits nor can they transfer their contributions when they relocate. The virtuous circle of economic vibrancy and a favorable pension-system old-age dependency ratio allows regions in Type Five to set the lowest employers' contribution rates among all sub-national regions. The distribution of these five types of subnational regions confirms the typology hypothesis in Table 2-2 in Chapter Two.

Figure 5-1 Five types of local fiscal structure of the pension program



Note: 1) Data for central fiscal support are average share of center fiscal support for the public urban pension program in annual local pension spending from 2000 to 2004; 2) economic openness is calculated by the percentage of foreign direct investment in total local fixed assets in 2004; 3) data labels are the average actual total pension contribution rate by province from 2007 to 2011, as presented in Chapter 1. Data source: National Data Online, and Zheng et al. (2013:101 and 103), and the author’s dataset.

Table 5-1 summarizes key economic and political features of the 31 provincial units, and includes information about their pension programs. The table is organized by the five types discussed above, to better demonstrate the differences between the groups. As discussed in Chapter Four, these five types carry different strategic weights to the center. Therefore, they receive varying amounts of center fiscal support to develop their pension programs, shown in column three in the table. Column four presents the share of foreign investment, including investment from Hong Kong, Macau, and Taiwan, in total local fixed asset investment, which may be used as an indicator of local economic openness and thus the level of capital mobility in

a locality. Column six presents the variable of our interest, total pension contribution rate at the provincial level.

Because the three provinces in Type I suffer from the largest scale of laid-off workers and early retirements, they have the highest system dependency ratios and the most problematic pension fund deficit situations in the country. However, as predicted, their mean total pension contribution rate is only third highest at 21.57% among the five groups. Type IV has the highest mean value of total pension contribution rate at 27.98% of payroll, even though most provinces in this category have positive pension fund reserves and are certainly not the fastest aging regions in the country. Even with major center fiscal support, Type II has the second highest contribution rate at 24.0%. Type V has the lowest pension contribution rate at 15.97% of payroll. Despite the fact that provinces in Type III are challenged by quite serious demographic aging and pension fund deficit problems, the mean contribution rate for Type III is 19.5%, which is the second lowest after Type V.

Table 5-1 A summary table of key features of 31 provinces, by five types of regions

	1	2	3	4	5	6	7
	Unemplm t rate, % (2003)	Ethnic pop., % (2003)	Center transfer , % (2003)	FDI, % (2003)	System depdcy ratio, % (2011)	Pension cntrbtion. rate, % (07-11 avg.)	Pension fund reserve, 0.1 bn yuan (2011)
<i>Type I</i>							
Heilongjiang	18.8	2.9	38.6	2.11	63.2	23.7	-182.8
Jilin	17.5	8.6	35.4	5.42	55.8	21.6	-56.93
Liaoning	14.1	8.3	35	9.89	45.5	19.4	-155.98
<i>Mean*</i>	13.7	6.15	36.33	5.81	54.83	21.57	-131.90
<i>Type II</i>							
Guizhou	9.2	18.5	30	2.01	33.8	21.1	12.63
Hainan	4.4	4.8	42.2	2.21	31.4	16	-19.72
Ningxia	7.0	19.3	25.7	2.44	42.8	29.9	31.62
Qinghai	7.4	21.3	34	1.51	44.7	28.2	5.55
Shaanxi	10.0	1.5	28.1	2.26	45.6	19.3	-40.91
Tibet	4.6	63.6	36.5	0.01	40	26.6	0.95
Xinjiang	4.1	27.0	31.2	1.73	36	26.9	24.83
<i>Mean*</i>	6.67	22.29	32.53	3.60	39.19	24.00	2.14
<i>Type III</i>							
Anhui	5.3	1.1	23.6	4.79	35.6	19.3	36.2
Chongqing	7.0	2.1	26.5	6.20	51.5	21.5	-10.82
Guangxi	4.2	26.0	20.3	7.36	45.6	20.5	-26.95
Hebei	9.1	3.5	24	8.20	36.8	22.4	-1.62
Henan	7.9	2.1	25.2	7.43	32.7	17.3	-44.81
Hubei	13.5	1.7	30.8	7.24	44.3	21.9	27.02
Hunan	9.0	3.8	29.2	5.95	39.1	17.7	-32.44
Jiangxi	12.7	0.3	30.8	8.56	34.8	14	-36.74
Tianjin	7.2	2.9	14.2	11.30	48	20.9	-71.6
<i>Mean*</i>	8.43	4.83	24.96	7.45	40.93	19.50	-17.97
<i>Type IV</i>							
Gansu	8.7	7.0	23.7	1.62	47.8	34.5	27.46
Neimenggu	5.7	15.0	26.9	1.36	43.3	24.6	-5.82
Shanxi	8.1	0.7	27.8	1.95	34.2	24.2	51.2
Sichuan	7.2	1.2	26.1	2.80	49.6	26.3	116.63
Yunnan	4.5	16.7	27	3.62	43.7	30.3	47.5
<i>Mean*</i>	6.84	12.9	26.3	2.27	43.72	27.98	47.394
<i>Type V</i>							

Beijing	1.0	4.2	0.5	13.84	22.7	17.7	233.9
Fujian	3.9	2.1	0	26.86	20.5	13.5	24.23
Guangdong	3.9	2.7	0	27.41	10.9	9.3	518.6
Jiangsu	4.4	0.7	0.4	17.87	27.8	16.9	293.3
Shandong	4.9	1.3	3.4	9.93	24.3	21.1	205.7
Shanghai	5.8	1.2	0	19.69	41.6	21.2	-25.1
Zhejiang	3.8	1.9	0.1	8.95	15.2	12.1	294.6
Mean*	3.96	2.01	0.63	17.79	23.29	15.97	220.75
National mean*	7.58	9.38	22.49	7.92	38.35	21.29	39.99

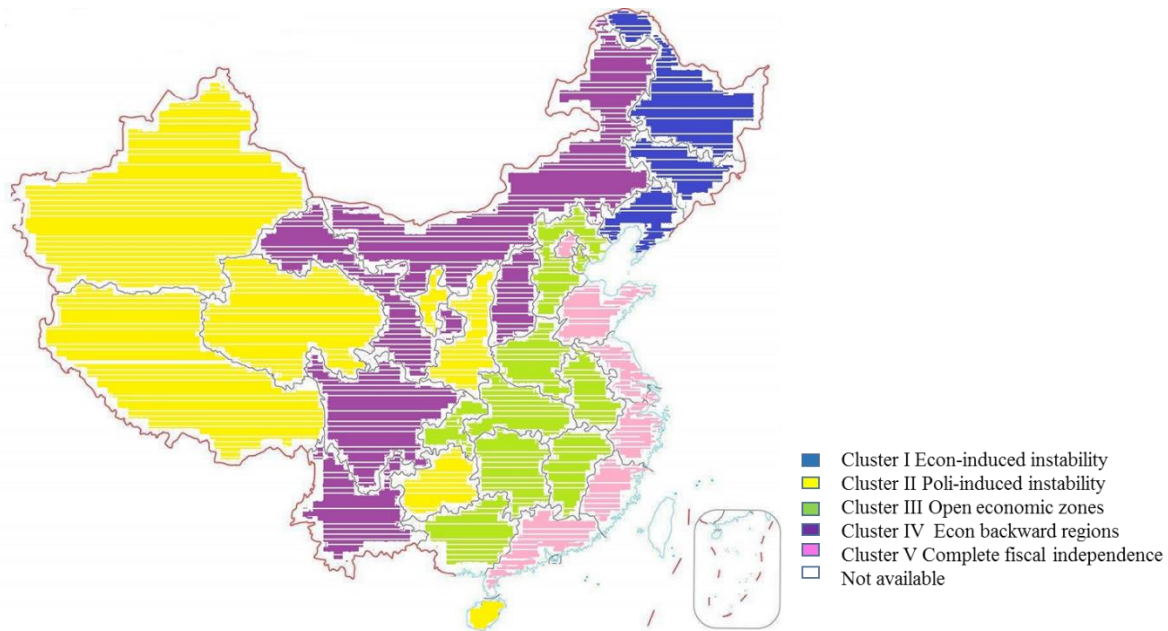
Data source: National Data Online, and Zheng et al. (2013, pp. 101 and 103), and the author's dataset.

* Simple (unweighted) provincial means.

Note: The data presented in this table are calculated in the following manner: 1) Unemployment rates calculated by percentages of layoffs and the registered unemployed in total urban population; 2) Ethnic population percentages as ethnic minorities in the population; 3) Percentages of the center fiscal support as provinces' spending on the pension program; 4) Share of foreign investment in annual total fixed-asset investment; 6) Percentage of the elderly population aged 60 years old and above in the population; 7) Average actual pension contribution rate aggregated at the provincial level from 2007 to 2011, calculated by Zheng et al. (2013); and 8) Year-end pension fund balances.

This categorization suggests geographic concentration of the five groups. Figure 5-2 presents the five types on the map to visualize the geographic locations of these five groups of regions. The figure shows that these types have clear territorial characteristics. Type I has three provinces in the northeast region, which are old industrial bases of the planned economy era. Type II includes mostly ethnic minority and border regions. Type III involves mid-land regions with more open economic structures, and the remaining mid-land regions with more domestic market-oriented economies fall in Type IV. Lastly, Type V comprises the seven most economically developed regions, located along the coastline.

Figure 5-2 The five types of provinces on the map



The remaining discussion in this chapter details five distinct stories of the funding structures of the pension programs at the provincial level. Based on the discussion in the theory chapter, six cases are chosen for investigation of local government officials' motives in these five groups of regions, namely Liaoning, Tibet, Hunan/Hubei, Gansu, and Guangdong. These six cases represent the extremes, to a certain extent, in the five groups – high economy-political sensitivity and high economic openness (Liaoning), high politics-political sensitivity and low economic openness (Tibet), and low political sensitivity and high economic openness (Hunan/Hubei and Guangdong), low in both sensitivity and openness (Gansu). Even though Guangdong and Hunan/Hubei share similar structural conditions in the two dimensions (political sensitivity and economic openness), Guangdong represents provinces which enjoy full fiscal independence from the center, and the government's redistributive mindset is vastly different from that of the Hunan/Hubei government. In addition, these five cases cover a great geographic range of Chinese sub-national governments: the northeast (Liaoning), the western borderland

(Tibet), the central south (Hunan/Hubei), the central north (Gansu), and coastal areas in the East (Guangdong). Pension programs in the northeast and the coastal regions are the most researched in previous studies (Frazier, 2010; Lu, 2010). By comparing these regions with diverse local conditions, this study seeks to present a uniquely complete picture of how the urban pension system is funded and operated in subnational China.

5.3 Liaoning – An economically unstable region

The northeast of China is often called “the eldest son of the Republic” (*gongheguo de zhangzi*), for two reasons: 1) The regions were the first in the country liberated by the People’s Liberation Army; and 2) the northeast region was concentrated with a large number of center-owned SOEs (*COEs, yang qi*), and these COEs played an indispensable role in the Chinese economy, particularly during the planned economy period. Among the northeast provinces, Liaoning has the largest legacy from the planned economy era. By 1978 Liaoning had more than 13,000 enterprises, and its net industrial output accounted for over 69% of total national revenue (Zhu, 1982). Thanks to the dominant development of state-owned industries on the Soviet model during the first decade of the founding of the People’s Republic of China, Liaoning was the first province in the country to experience accelerated large-scale industrialization and urbanization. This burst of industrialization quickly turned these COEs to super-sized inefficient enterprise empires, and the cities where these enterprises were located essentially became company towns. Fushun and Hegang were two great examples of those company towns (LNP1212131). During the command economy period, SOEs not only carried economic functionalities, but also responsibilities of cradle-to-grave welfare provisions. Therefore, the geographic concentration of these gigantic SOEs planted seeds of serious social and economic problems in the economic transition period.

The initiation of economic reforms brought a serious pension underfunding problem, particularly in old industrial bases like Liaoning. Economic reforms brought the market mechanisms to the originally highly centralized planned economy, which triggered a massive wave of layoffs. According to incomplete national statistics, Liaoning had the largest number of laid-off workers¹⁸ (*xiagang gongren*) nationwide, reaching 400,000 in 1998 alone and 1.1 million cumulatively in total in the 1990s (*China Labor Statistical Yearbook*, 2000). Besides laying off workers, asking employees who were near retirement age to retire early was another way to get rid of redundant employees and increase production efficiency. During the planned economy period, employees were entitled to receive pension benefits after retirement without making contributions to the pension fund while active at work. Early retirees were entitled to receive pension benefits immediately after they left their positions. These laid off received a one-time compensation from the enterprise, the compensation amount varying depending on the profitability of the business. As these laid off left their positions, their employers did not make further pension contributions for them in the new pension system. Upon reaching the retirement age, layoffs were still entitled to receive pension benefits, though in a smaller amounts than ordinary retirees because their employers ceased to make any pension contributions for laid-off workers. The abrupt increase in the number of layoffs and early retirees greatly challenged the old pension program in Liaoning. Delays in pension benefit payments, and even non-payment, were very common. Contentious pensioners took to the street in the northeast, in Liaoning in particular (Hurst & O'Brien, 2002; Kent, 2007). For one strike in Liaoyang, a major SOEs base in Liaoning, it gathered more than ten thousand pensioners and layoffs, and protests and lasted for 19 days, which drew media attention from home and abroad (*China Labor Bulletin*, 2002).

¹⁸ Only including registered laid-off workers.

Government officials interviewed in Liaoning seemed to be still unduly reticent on the subject of social grievances on the pension entitlement problem during the reform period.

The center has given substantially more attention to and support for Liaoning's pension program than to those of most other provinces, and has taken Liaoning as the most challenging case to gauge the progress of social and economic reforms. Premier Zhu Rongji visited Liaoning in 1997 to inspect the progress of economic reforms, but was welcomed by a sit-in protest staged by pensioners on a busy main road. After he returned to Beijing, he overcame bureaucratic politics and put forth a "two ensures" policy in 1998: 1) ensure that pension benefits were paid in time and in full to retirees; and 2) ensure those who were laid off received social assistance for basic living standards. He promised to employ the central fiscal budget to ensure proper implementation of this policy (BJC0614131). Top-ranking central government officials made several follow-up visits to Liaoning to gather firsthand information on the progress of economic and social reforms. When Minister of Labor Zhang Zuoji visited Liaoning, he conveyed the center's repeated emphasis on the "two ensures" policy to make sure that no further delay in pension payments should occur. After the Liaoning government reported its progress on market economic reforms in 2000, Vice Prime Minister Wu Bangguo commented that when economic progress was in conflict with the maintenance of order, economic reforms should give way to social stability. Wu promised that given Liaoning's particular difficulties, the center would grant necessary subsidies to the Liaoning government to help further implementation of the "two ensures" policy and of required economic reforms (Zhang, 2001). Local government officials confirmed that the center had given Liaoning "special treatment" (*teshu zhaogu*) toward annual fiscal support, yet the exact amount of this "favor" was unclear (LNP1213131).

In addition to more favorable annual fiscal support, the center handpicked Liaoning as the first province to carry out the center's reform plan for consolidating individual accounts. As stated in Chapter Three, the supposedly fully-funded individual accounts were emptied to pay for current retirees' pension benefits after the 1997 reform. Emptied individual accounts meant large future liability for the government, and thus had been on the center's reform agenda. In 2001 the center decided to choose Liaoning as an experimental province to carry out a "consolidation of individual accounts" reform (hereafter, simply consolidation reform). Being an experimental locality means more fiscal support and other complementary support (*pei tao zizhu*) (HBP0705133). The center promised to cover 75% of the costs of the consolidation reform in 2001 through fiscal transfers, and the Liaoning government was to pay the remaining amount (Lu, 2011). The center used 2001 as the baseline year to calculate fiscal transfer amounts to Liaoning in this reform, and the center's transfer amount would remain the same as the amount granted in 2001 as the reform progressed in the subsequent years. The amount the center granted to Liaoning was 1.89 billion *yuan* in 2001, and kept the same amount every subsequent year (LNP1211132). As the number of pension participants gradually increased and the average wage level rose over time, the fiscal responsibility of Liaoning for funding this consolidation reform in fact increased across time, beyond the initial 25%. The Liaoning government was at first discontented over the increasing fiscal spending on the reform plan proposed by the center, and saw the deal as "the center fishing money from Liaoning". However, the Liaoning government understood that with the center paying 75% of the reform costs, the room for further negotiation would be very limited (BJN0619141).

In 2008 the consolidation reform was deemed a failure. The consolidation reform required that the Liaoning government reserve the special subsidies from the center and the fund

from the local fiscal budget in a separate bank account exclusively for future benefit payments of individual pension accounts. In other words, the Liaoning government was prohibited from using the accumulated fund to pay for current retirees' pension benefits. However, as the Liaoning government's fiscal burden to carry out this reform increased across time, the Liaoning government filed a report with the center in 2008, stating that to continue this consolidation reform would compromise the "two ensures" policy. Starting in 2009 the center noted that the Liaoning government could borrow money from the individual account reserve to make current pension benefit payments, but Liaoning would need to pay back the borrowed amount plus interest. A government official from Liaoning commented that "even though the center only 'lent' us the money, it is really another matter when it comes to when to paying the money back." (LNP1211132).

Despite the difficulty of funding the pension program, the average contribution rate of employers and employees combined in Liaoning has never exceeded 28% since 2002. The main reason that explains Liaoning's below-target contribution rate is the pressure to revive the local economy. When asked why Liaoning did not set up a higher contribution rate to cover its pension fund deficits, Liaoning's provincial government official offered that:

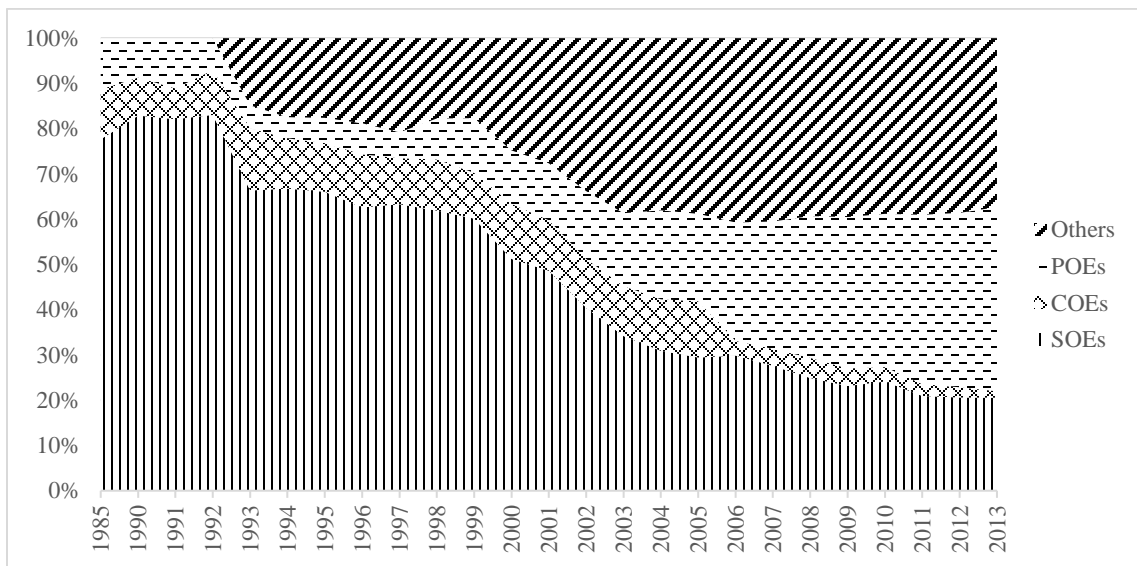
"Enterprises would not be able to afford to pay any higher pension contributions. Setting a higher contribution rate would produce exactly the opposite effects. We would be better off with a 20% contribution rate from employers – more enterprises would be willing to contribute, and more contributions would help our economy create more employment opportunities." (LNP1212131)

Enriching the pension reserve was apparently not the first priority of provincial officials during the economic transition period. Even though the center repeatedly emphasized building a

welfare safety net, promoting economic growth seemed to be a more urgent and convenient task for sub-national governments. As the “elderly son of the Republic”, Liaoning’s performance in the economic transition was under the spotlight. In 2003, the central government called for revitalization of the northeast old industrial base (*zhenxing dongbei lao gongye jidi*). However, as an old Chinese saying goes, a big ship cannot make a swift U-turn. Liaoning was challenged to increase productivity and efficiency of SOEs without arousing much social discontent.

Liaoning experienced substantial transition in its economic ownership, from an economy overwhelmingly dominated by state-owned investments to a true mixed economy. The composition of annual fixed asset investment by ownership type may be used as a proxy to measure shares of SOEs and non-SOEs in the economy. Figure 5-3 presents the composition of Liaoning’s fixed asset investments by registered ownership of business from 1985 to 2013. The figure shows that the share of SOEs in the economy shrank significantly in 1999, and the share of private companies increased considerably in 2005.

Figure 5-3 Composition of fixed-asset investments in Liaoning by ownership of business

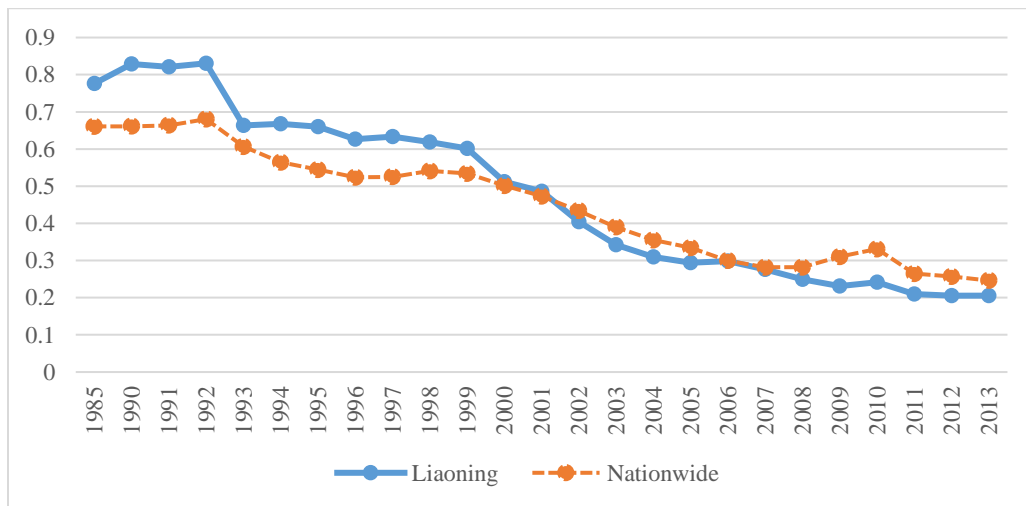


Notes: POEs: private-owned enterprises, COEs: collectively-owned enterprises, SOEs: state-owned enterprises, and others include internal-capital enterprises, cooperative enterprises, limited liability companies, enterprises with capital from Hong Kong, Macau and Taiwan, and foreign enterprises.

Source: *Liaoning Statistical Yearbook*, 2014.

Figure 5-4 compares the shares of SOEs' investment in the overall fixed-asset investments in Liaoning and at the national level. The figure demonstrates the great achievement of Liaoning in economic marketization. Before the economic reforms, about 80% of Liaoning's fixed-asset investment was from SOEs, higher than the national level by 10 percentage points. In 2013 SOE investments only accounted for 20% of the overall fixed-asset investment in Liaoning, lower than the figure aggregated at the national level. The turning point of this comparison was around the year 2000, which happened to be the most critical period of the pension reform.

Figure 5-4 Share of SOEs' investment in overall fixed-asset investment in Liaoning and at the national level, 1985-2013 (unit: %)



Source: *Liaoning Statistical Yearbooks*, and *China Statistical Yearbooks* (various years).

Obviously, a 60% reduction of the Liaoning economy's reliance on SOEs came with a hefty price tag. To realize this transition, sub-provincial governments had to suppress the pension contribution rate to attract foreign and private investment, even though the aging demographic structure begged for more contributions to solidify the pension program. As the transition progressed, the center emphasized the importance of increasing employment in Liaoning to

counteract the rising layoff rate. It noted that employment is the most fundamental protection for the people. For the government, boosting the employment rate could not only facilitate economic transitions, but it would also promote social stability (Zhang, 2001). A key to increasing the employment rate is to bring in non-SOE investments. However, with its dated administrative structure set that had been used to serve giant SOEs in the planned economy era, Liaoning found it difficult to compete with newly developed regions in inviting private and foreign investment to come under the new economic system. To increase their competitiveness, some municipal governments granted land to private and foreign investors for free in order to entice them to locate within their administrative boundaries. Some used reduction in pension contribution to attract investment (LNP1211132). To promote economic growth and social stability in the short run, the provincial government had to give a green light to sub-provincial governments to keep the pension contribution lower than necessary. Meanwhile, when the author was conducting interviews in Liaoning, government officials said that Liaoning was considering a province-wide pension contribution rate reduction for private companies to raise the province's competitive capacity (LNP1212131).

Fortunately, the subsidies granted by the center gave the Liaoning government some leeway to keep their pension contribution relatively low without using much of the province's own fiscal resources. For Liaoning, the center's fiscal subsidies not only alleviated its immediate under-funded pension problem, but also gave the government more leverage in negotiating with foreign and private investors by granting more relaxed tax and welfare policies. Every year when applying for center fiscal subsidies, the Liaoning government would urge the center to consider Liaoning's demographic burden and contributions to the economy as an old industrial base in the past. The center always replied that the amount granted had already taken that into consideration.

The Liaoning government confirmed that with the center's annual fiscal subsidies and the money accumulated in the individual accounts during the consolidation reform, it had not needed to divert much fiscal support from the local fiscal budget to fund the pension program. However, the government officials interviewed in Liaoning were uncertain whether they would be able to secure the center's continuous fiscal support in the long run (LNP1213131). Sometimes the center was irritated by the Liaoning government's playing the old-industrial-base card. When the Liaoning government requested more funding support, the center sometimes replied, "Does begging for more center fiscal subsidies increase economic productivity? You would be better off using the time here to think about how to improve pension premium collection" (LNP1213131).

During the transition period, the center emphasized the importance of keeping order by promoting steady economic development and timely welfare provisions in those regions hart-hit by economic reform. The center granted substantial fiscal support to those regions to ensure smooth transitions. However, the Liaoning case shows that the Liaoning government viewed the fiscal support received from the center as leeway for them to reduce the pension burdens of investors. The government sought to use this strategy to attract investment, and thus to revive the economy and rebuild legitimacy. As a result, nearly two decades after the 1997 reform, the pension deficit problem in the northeast region has only become more problematic even after all the resources the center has provided (BJN0403151).

5.4 Tibet – Sensitivity of ethnic minorities

The Tibet Autonomous Region is home to ethnic Tibetans, who constitute about 93% of the population in the region. Due to a combination of factors such as historical territorial disputes and religious differences, separatist campaigns challenging the center's rule happen from time to

time. Ensuring and enhancing Tibet's political stability is a long-standing priority at the top of Beijing's agenda (Xinhua, 2013). The center launched the Development of the West Regions Campaign in 2000, and initiated a special fiscal transfer program called "fiscal transfers to ethnic minority regions" to accompany this development strategy. In the first five years of the program, the center transferred cumulatively more than 500 billion *yuan* to ethnic minority regions in the West (*xi bu*), not including another 460-billion-yuan construction fund transferred from the center fiscal budget (Zhang, 2005). As we shall see in this section, despite the center's support, economic development in the five autonomous regions has shown to be intentionally more limited than in other regions included in the development plan. Both the center and these ethnic minority governments agreed to promote diversity and minimize assimilation of the minorities, and focus on stability maintenance. Not surprisingly, when asked to compare Tibet's pension program development with those in other regions, my interviewees, from central and provincial government officials to scholars and journalists, all noted that it would be like comparing apples and oranges (BJC0614131, BJN0413152, BJN0403151, HBP0705133, and HNP0724132). An interviewee informed that one of the center's regional categories was called "old, young, border, and poor" region (*lao shao bian qiong diqu*), and regions like Tibet that fit well with all the four criteria were attached with particular importance by the center (HNP0724132).

After Tibet and Beijing signed the *Seventeen Point Agreement* in 1951, the Chinese central government officially declared its rule over Tibet. In 1965, the central government named the Tibetan Autonomous Region, as one of the five ethnic autonomous regions in China. Due to its weak economic foundation and slow-paced economic reforms, Tibet has had the lowest economic output of any province-level units in China. Since the 1950s, the Chinese central government has exempted Tibet from all taxation. In addition, the operation of the government is

largely fiscally dependent on center fiscal support. Table 5-2 indicates that over 90 percent of Tibet’s fiscal revenue came from the center’s fiscal transfers, and the amount of center fiscal support almost tripled during the period investigated, 2006 to 2010. The center’s fiscal support accounted for an increasing share of Tibet’s fiscal revenue. The State Council’s report, *The Historical Choices in Tibet’s Development Path*, shows that from 1952 to 2013, the center’s cumulative fiscal transfers to Tibet reached 550 billion *yuan* (Zhang & Guo, 2015). With the center’s vigorous support, the administrative capacity of the Tibetan government gradually improved – Tibet’s total fiscal revenue as a percentage of local GDP increased from 0.6% in 1989 to 13.5% in 2014 (Wang & Liu, 2015).

Table 5-2 Tibet’s annual fiscal revenue and amount of center fiscal support, 2006 to 2010 (unit: 0.1 billion *yuan*)

	2006	2007	2008	2009	2010
Center fiscal support	185.02	256.22	355.43	440.19	531.00
Tibet’s fiscal revenue	202.29	279.36	383.86	470.56	561.50
The center’s support (%)	91.4	91.7	92.5	93.5	94.5

Source: *China Financial Yearbook* (2011).

The central government highly values welfare development in Tibet. The Minister of MHRSS, Mr. Yin Weimin, once remarked that aiding social welfare development in Tibet should be treated as a life-or-death political task, rather than a simple social welfare matter (Shi & Li, 2012). The Chinese central government noted in its *Eleventh Five-year Development Plan for Tibet* that improving workforce quality, stabilizing the employment situation, and perfecting the social welfare system are the very foundation of creating “a well-off Tibet, a peaceful Tibet,

and a harmonious Tibet”. It is specifically noted that the social welfare system has particularly indispensable effects in promoting stability in Tibet, and safeguarding the unity of the country (Chen, 2011).

Soon after the Chinese government announced its sovereignty over Tibet, the central government quickly replaced the original welfare programs provided by religious organization and local organizations in Tibet with the socialist-style welfare model (Luosang & Danzeng, 2011). Before the socialist welfare reform in the late 1950s, as a basic level of Tibetan monastic organizations, Khangtsens (Kang village) were responsible for welfare provisions to their associated members and families. As the Tibetan government implemented the socialist welfare programs and social reforms, the role and power of Khangtsens declined substantially. In addition to Khangtsens, Jidu was another important organization that had provided basic social assistance at the local level. Mainly organized by kinship and neighborhood, Jidu were often dominated by powerful local elites and social groups. The introduction of the socialist welfare programs in Tibet and the weakening of these religious and local organizations reinforced the viewpoint promoted by the central government – ensuring the people’s right as masters of the country.

Since its inception, Tibet’s pension program has received substantial support from the central government. Public old-age pensions and unemployment insurance were the first two welfare programs the Tibetan government created, followed by health insurance, work injury insurance, and maternity insurance. Tibet adopted the socialist-style public pension program in 1959. However, before this newly established socialist welfare program had been fully implemented in Tibet, it was put on hold during the Cultural Revolution. In 1987, the center issued a temporary regulation for the social pool pension program in Tibet, which marked the

official creation of Tibet's first public pension program. In 1991, to accompany the economic reforms, the Tibetan government revised the program to include both tenured and contract workers in SOEs, and required pension contributions from both employees and employers. In 2006, with the center's help, the Tibetan provincial government transformed the old socialist pension scheme to the three-pillar program, and included employees from the non-state-owned sector in the pension program. Tibet became the last provincial unit to adopt the new three-pillar pension scheme.

Even though Tibet adopted the same three-pillar pension development proposal from the center, its resulting pension program is quite different from those implemented in other regions. The compulsory retirement ages in Tibet are 55 for male workers and 45 for female workers, each five-year younger than the national requirements. Despite the early retirement ages and resulting longer-time pension benefit provision, with the center's fiscal support, pension benefit provisions in Tibet have never encountered any delay or non-payment since the introduction of the pension program (Yao, 2012). Full retirement benefit payments during the economic transition period was a remarkable achievement, which made Tibet one of the four provinces that achieved that goal, the other three being coastal economically more developed regions (BJN0402121). Besides basic pension benefit provisions, Tibet first introduced a concept called "altitude subsidy" in the pension system. After the introduction of this concept in Tibet, a few western provinces followed suit. This altitude subsidy program increased the retirement benefit level in Tibet by 5 to 15 percent, depending on profitability of the company and pre-retirement work experience (Luosang & Danzeng, 2011). In addition, since the center's pension benefit increase plan implemented in 2005, Tibet's average pension benefit level increased by more than 10 percent each year. And the center fully subsidized the pension benefit increase plan in a few

“politically important” regions, including Tibet (Lin & Tussing, 2016). In 2014 the mean retirement benefit per retiree in Tibet reached 3,300 *yuan* – the highest benefit provision level of the country, and 66 percent higher than the simple unweighted national mean (Tibet.cn, 2015). With the high benefit payment, Tibet’s pension program had the highest pension benefit replacement rate, ratio of retirement income to pre-retirement earning in the country. In 2012, Tibet’s pension benefit income replacement rate was 62.7%, making it the only provincial-unit that fulfilled the center’s goal of a 58% replacement rate¹⁹ (Lin & Tussing, 2016).

Table 5-3 GDP per capita, and public pension fund spending per pension program participant in Tibet and national averages, 2006-2013 (unit: *yuan*)

	GDP/capita		Pension fund spending/participant	
	Tibet	National avg.	Tibet	National avg.
2006	9,319.2	17,181.5	3,644.4	1,520.6
2007	10,943.3	20,642.4	4,919.1	1,852.2
2008	12,655.4	24,595.9	4,877.9	2,294.8
2009	14,146.1	26,956.5	6,075.5	2,762.2
2010	16,264.7	32,250.2	5,424.7	3,277.9
2011	19,417.6	38,478.2	7,573.0	3,964.2
2012	22,468.9	42,544.9	8,597.7	4,832.6
2013	25,886.8	46,489.7	9,634.3	5,735.6

Source: National Data Online, <http://data.stats.gov.cn/easyquery.htm?cn=E0103>.

Table 5-3 compares two sets of values: 1) local gross domestic/ product per capita in Tibet and at the national level, and 2) the mean values of annual public pension fund spending per pension program participant in Tibet and at the national level, both from 2006 to 2013. The annual public pension fund spending levels presented here are calculated by dividing the annual spending from the public urban enterprise pension fund by the year-end number of participants

¹⁹ The target rate was mentioned in *Suggestion No. 27634* issued by the State Council. However, the document was not released to the public.

of the program. To be sure, pension fund spending per participant is not equivalent to retirement benefit provision per retiree, as the pension fund spending figure includes administrative expenditures and other outlays. Instead, this variable indicates the financial situation of a pension fund, and the fund’s spending level per participant. According to the data on GDP per capita presented in the table, it is clear that Tibet’s economy is much less developed than that of the rest of the country. The economic development gap between Tibet and the national level did not seem to change across time. During the period covered, from 2006 to 2013, the national average GDP per capita was consistently around 1.8 to 2.0 times as high as the Tibetan level. However, the mean values of spending from Tibet’s public pension fund per participant were much higher than the national average. Meanwhile, the ratio of Tibet’s spending level per program participant to the national average gradually fell, from 2.4 times in 2006 to 1.7 in 2013. The data presented in the table clearly signal that although Tibet is economically less developed, Tibet’s pension program is much better funded than the national average, and the program’s spending level is substantially higher than the national level.

Figure 5-5 Pension fund situation in Tibet, 2006 to 2015 (unit: 1M yuan)



Source: *China Statistical Yearbooks* (various years).

Figure 5-5 presents Tibet's pension fund situation after Tibet adopted the three-pillar pension system in 2006. Its pension income, indicated by the solid blue line in the figure, includes both center pension subsidies and pension contributions collected. The figure shows that the increase of Tibet's pension revenue has been in lead of the pension expenditure increase, and the total accumulative pension fund reserve reached 5,000 million *yuan* in 2015. From the discussion above, it is safe to conclude that the center's fiscal support plays a major role in funding Tibet's generous urban pension program.

In addition to the urban enterprise pension, in 2011 the center created a basic pension program for urban Tibetan residents and workers (hereafter, residential pension program for short). The Tibetan program extended coverage of the residential program to include monks and nuns. Only monks and nuns from temples of Tibetan Buddhism in Tibetan autonomous prefectures, including a few prefectures located in neighboring provinces, could enjoy this welfare entitlement. The Tibet's program policy states that regardless of their registered residential locality, all urban residents currently living in Tibet aged at least 18 years old may enroll in the residential pension program. Participants may contribute to the pension program with a minimum of 100 *yuan* to a 3,000-*yuan* upper limit per year, and must contribute for more than 15 years before they become eligible for retirement payments as they reach retirement age. In addition to individual contributions to the pension program, the government subsidizes 30 to 85 *yuan* per participant per year, depending on the contribution level that the participant chooses. In 2012, the first year of the implementation of the policy, 1,897 monks and nuns in Tibet received basic pension benefit payments without prior pension contributions, marking the first time in Tibetan history that monks and nuns had received public pension payments (Zhao & Ji, 2012). According to the *2014 Tibet's Provincial Government Work Report*, the amount the

Tibetan government spent in 2013 on the monks' and nuns' pension program alone was 178 million *yuan*. This pension program was highly praised by Tibetan monks and nuns. A deputy director of the Tashilhunpo Monastery in Xigaze remarked that:

“The extension of the residential pension program (to monks and nuns) reflects the superiority of the socialist system. We will certainly bear in mind the tenth Panchan Lama's inculcation of 'love one's country and religion', and actively participate in the contest of patriotic and law-abiding model temples. We will make our best efforts for Tibet's harmony, stability and prosperity” (Ciren, 2011).

A study of over 2,000 survey participants conducted in 2009, shows that over 90% of urban elderly in the two major cities in Tibet, Lhasa and Xigaze, felt satisfied with their lives, much higher than comparable figures in other inland provinces in China (Yan, 2010). Among various factors contributing to this high level of life satisfaction, pension benefits provided by the government were most often cited (Yan, 2010). The center's report also lends support to the role of the pension programs in improving the well-being of the people and consolidating political support. According to government figures, the poverty rate fell from 34 percent to 18 percent over a three-year period from 2010 to 2013. This success was attributed to pension programs aimed at supplementing income (The Borgen Project, 2015)

Although the center aggressively assists welfare development in Tibet, the center's efforts in promoting Tibet's economic development and marketization have been quite conservative. After decades of development, Tibet's current pillar industries remain traditional, namely mining, traditional handicrafts, and Tibetan medicine and pharmacology. The effect of foreign investment in Tibet has been very minimal. According to data in the *China Statistical Yearbook*, by 2013 state-owned business accounted for more than 65% of Tibet's economy, and privately-owned business, including foreign investment and investment from Hong Kong, Macau

and Taiwan, accounted for only 11% of the province's total fixed asset investments in 2013. These numbers suggest that a high majority of participants of the urban pension program are SOE employees. The relatively isolated economic environment reduce the pressure on the Tibetan provincial government to reduce the pension contribution rate for the purpose of attracting investment as other provincial governments do. Tibet's pension contribution rate for employers is set at 20% of payroll, strictly following the center's recommendation. The actual pension contribution rate for employers in Tibet in 2010 was slightly higher than 20%, around 22% (Zheng et al., 2013, p. 150). Without worrying about capital mobility in the region or about inviting foreign investment, and with sufficient center fiscal support, the Tibet government is best situated to obey the center's commands and take advantage of SOEs' contributions to the pension fund.

As Wang (1995a) notes, the Chinese central government's emphasis on national unity seems to have had decisive effects on shaping the center's fiscal transfer decisions. Regions with more ethnic minorities often receive much more fiscal support per capita from the center than regions that are inhabited mainly by Han Chinese. As discussed in the theory chapter, promoting welfare programs is highly valued as it directly shapes individuals' perception of the government, and showcases generosity of the ruler. The philosophy of Tibet's public spending is "to ensure normal operation, to ensure people's livelihood, and to ensure stability" (*Tibet Provincial Bureau of Finance Work Report*, 2013). Unlike most slogans of Chinese governments at all levels, not a single word in this statement mentions economic development (*fa zhan*). Therefore, order maintenance in Tibet is the very purpose of the center's fiscal support, while boosting economic development is only a side issue for the center. As such, the development of the pension program

in Tibet seems to be closer to the ideal concept of a public social welfare program – paying from the public fiscal budget to promote the well-being of the public.

5.5 Hubei and Hunan – Midland provinces striving for rapid economic transformation

The Midland region (*zhong bu*) in China do not enjoy as much attention from the center as the old industrial zones and ethnic minority regions do, and their economic development can hardly compete with that of the coastal regions. It is because of this awkward political and economic situation that pension development in the Midland region has its particular challenges. In this section, Hunan is used as the primary case to demonstrate the fiscal structure of its pension fund; and examples were also drawn from Hubei, which as a neighboring province shares commonalities in many aspects with Hunan.

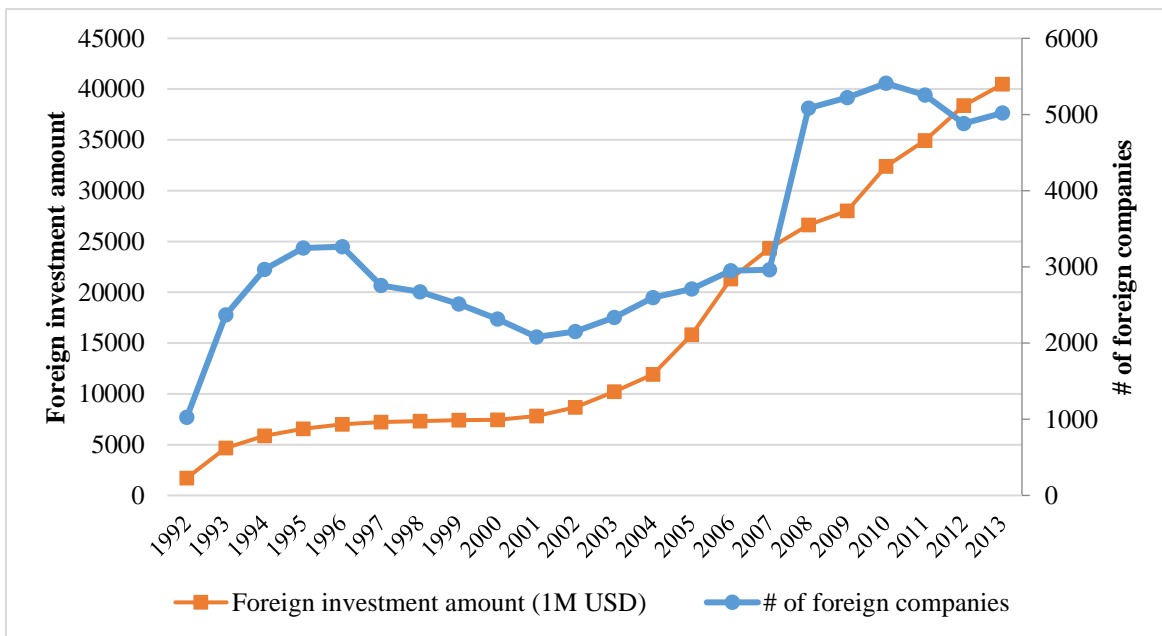
Industrialization of the Midland region did not start until the Chinese central government proposed a grand nationwide development strategy, called “The Third-Front Construction” (*san xian jianshe*) in 1964. Mainly out of consideration of national security, the central government invested heavily in infrastructure and military industries in remote areas of thirteen Midland provinces. As a result, state-owned investment became the main source of economic growth in most of these third-front areas, and local people were employed mostly in SOEs where social welfare benefits came automatically with SOE employment status. Compared with old industrial bases in the northeast, the size of these SOEs in the upper Changjiang region was smaller. Because of the heavy concentration of SOEs in some areas in the Midland region, SOE reforms shook the economic foundation of many Midland provinces. Workers laid off and early retirements were rampant in the Midland region. According to data from the fifth population

census, the Midland region had the second highest unemployment rate immediately after the old industrial zones in the northeast (Li, Liu, & Wang, 2007).

The economic transition in the Midland region was long in duration and short of center support. The Midland region became a central zone of sunken economic growth. “Allow some people and some regions to get rich first, and others will be brought along and through this process. The common prosperity of the entire nation will come”. This was Deng Xiaoping’s national development strategy at the inception of the market economic reforms of the late 1970s. Accompanying this development approach was increasing inter-regional economic inequality, we have seen. Under this grand development strategy, coastal provinces first opened up to foreign investors and introduced market reforms, and midland provinces like Hunan became late-comers to China’s economic boom. In 2000, over 87% of FDI received in China was located in coastal provinces, with only 8.9% in the Midland region and 3.3% in the West (Yang & Zhu, 2003). As the center initiated the Development of the West Regions Campaign in 2000 and provided substantial fiscal support, west regions quickly picked up development speed. Scholars compare midland provinces’ economic indicators, such as economic growth rates, fixed-asset investment growth rates, employment rates, and consumption growth rates, against those of coastal provinces and border regions, and noticed a phenomenon called “central sunken” (*zhongbu taxian*) in the early 2000s (Ma, 2001; Yang & Zhu, 2003). The growth of non-SOEs did not accelerate until the mid-2000s, when the center proposed a reform plan called “the rise of the center” (*zhongbu jueqi*) in 2006. Therefore, the Midland region experienced a prolonged period of development gap wherein a large number of SOEs went bankrupt while the growth of non-SOEs did not compensate the economic loss.

We may use the amount of foreign investment and the number of foreign companies investing in a locality as proxies to measure its level of market economic development. As indicated by both measurements in Figure 5-6, foreign investment picked up quickly in Hunan in the mid-2000s, as discussed earlier. The 1990s and early 2000s were a period when the development of non-SOEs did not fully compensate the slowdown in SOEs' production. As a result, studies find that during this period, many midland provinces experienced negative employment growth rate (Yang & Zhu, 2003). However, this period comprised the two decades in which the coastal region experienced the fastest economic transformation and achieved remarkable economic success. Because of this inequality in inter-regional economic development, the Midland region suffered from a large-scale labor outflow to the economically more developed coastal regions for an extended period of time.

Figure 5-6 Foreign investment in Hunan Province, 1992-2013



Source: National Data Online, <http://data.stats.gov.cn/easyquery.htm?cn=C01>.

The slowdown in the state-owned economy and the retarded development of the market economy in the region posed a challenge to these sub-national governments in relation to pension

contribution collections and benefit payments. Local governments sold bankrupt SOEs' properties to maintain pension provision for retirees of these SOEs; for those SOEs that did not have sufficiently valuable properties to sell for the payment of their pension responsibilities, their retirees had to bear delay of retirement benefit provision and non-payment. Delay in pension payment was still rampant in Hunan as late as 2006 (HNP0717131). How did these inland provinces strike to stimulate local economic development and keep the balance of their pension funds? Most existing studies of China's welfare programs focus on the coastal areas and the old industrial base in the northeast (Frazier, 2010; Lu, 2008), which has left welfare development in inland provinces an under-researched topic. This section and the section on Gansu help fill our knowledge gap in China's welfare development landscape.

In addition to the retarded economic takeoff, as mentioned, a result of inter-regional economic inequality was a large-scale labor movement across sub-national regions. Most inland provinces became labor-exporting provinces – losing labor force, and therefore losing pension contributors. As the household registration system (*hukou*) was gradually relaxed in the 1990s, people with rural residence registration were allowed to enter cities without applying for residence permits. A large group of young people left their inland home provinces for open economic zones in the coastal region to seek their life fortunes. Local people still remember how crowded were the trains leaving for the coastal region were back in the 1990s, and how many people were even crushed to death by the crowds in the massive population movement (HBP0705131). The impact of labor outflow from the local economy in these inland provinces was major, in particular during the economic boom period.

The effects of the labor outflow on these labor-exporting regions were twofold: first, the economically less vibrant localities lost manpower for economic production; and second, the

outflow of active labor force resulted in deterioration in local pension system dependency structures, and thus in increases in these localities' fiscal burdens for pension provision. Due to the limited portability problem of the pension program, migrant workers contribute to the pension fund at their work localities, and the contributions can rarely be transferred to their home governments when they return. Home governments induce these returnees who are already near retirement age to participate in local pension funds to fulfill their annual quota of pension participant recruitment. As such, these home governments shoulder the responsibility to provide retirement benefits to returning migrant workers upon reaching retirement age (HNP0717131). The benefit level depends on the type of pension program in which a returnee enrolls with their home government: it could be urban public pensions (with a higher benefit level) or rural pensions (with a much lower benefit level). Whichever it is, the home government bears the burden of providing benefits to retirees who do not make full pension contributions. We will return in Chapter Six to the discussion of the effects of labor movement and the limited portability problem of the pension system.

The combination of a reduction in the number of pension contributors and an increase that of pension recipients means a higher within-system dependency ratio, the ratio of the number of pension recipients to the number of pension contributors. Because the within-system dependency ratio is high in these provinces, these provinces might be expected to have a higher pension contribution rates. However, these localities required only a medium-low level contribution rate from employers, lower than the center's recommendation of 20% of payroll. Various government officials interviewed in Hunan and Hubei admitted that the center did not allow pension contribution reduction for non-SOEs (HBP0705131, HBP0708132, and

HNP0725131). However, they noted that employers really could not afford the welfare burden requested by the center. An official commented,

“Rather than consolidating the pension fund, setting a high pension contribution rate would only cause the opposite. It would lead to more social conflicts and disputes, particularly during economic recession periods. The government has the responsibility to help investors sustain healthy business growth and keep them from going bankrupt”

(HBP0708132).

The goal of collecting 20% of payroll from employers for pension contributions was deemed to be simply unrealistic, too high for enterprises to comply with. According to Hunan provincial government’s estimate, a 17% contribution rate should be sufficient to run their provincial pension fund (HNP0725131). However, this estimate was based on two questionable assumptions: 1) the government is able to enforce pension contributions in full and on time; and 2) the government does not need a pension program reserve in preparation for provision of future pension benefits for the rapidly aging demographic structure.

Furthermore, Hunan has a two-headed collection process for pension contribution, which offers more opportunity for evasion of pension contribution. After the 1997 reform, given the inability of many local social security bureaus to collect pension contributions, several provinces decided to grant local tax bureaus the power to collect pension contributions. Hunan’s Provincial Bureau of Local Taxes also requested authority to take over this power from the social security bureau. The head of the Provincial Bureau of Finance at that time had been the head of the Provincial Bureau of Local Taxes. He decided to create a unique dual-collection system, under which both the local tax bureau and the social security bureau collected pension contributions. The local tax bureau was made responsible for collecting pension contributions from private enterprises, and the remaining enterprises would submit their contributions to local bureau of

human resources and social security. This collection system remains intact today (HNP0725131). This dual pension collection system creates greater opportunity for corruption. The Hunan provincial government is also aware that some enterprises underreported the numbers of employees and their payrolls, but the Provincial Bureau of Human Resources and Social Security has the capacity to randomly check only about a hundred enterprises in a year to supervise their welfare contributions (HNP0724131).

In addition to government policies on contribution rate reduction and system loopholes in enforcing pension program participation and contributions, Hunan's pension fund became more problematic, as it has lately had to cope with investment relocation of labor-intensive production from coastal regions to inland provinces. Partly as a result of the litigation of *Labor Contract Law* in 2008 and *Social Security Law* in 2010, coastal provinces sought to transform and upgrade their industrial structure by inviting investment in high-tech and capital-intensive industries and discouraging the development of labor-intensive industries. Wave of relocation of these labor-intensive companies to inland provinces was observed. As indicated in Figure 5-6, Hunan's foreign investment soared quickly in 2008 soon after coastal provinces carried out the redevelopment reform. Business relocation to inland provinces might seem to be an exciting opportunity to revive economic development in the Midland region; but under the current market economy a mass inter-regional business relocation project was far beyond the government's capability to plan for.

Investors required inland governments to match (*pei tao*) the policies they received from coastal region as a precondition for relocating their business (HNP0725131). As occurred in the 1990s when these labor-intensive companies first settled in the coastal region, the relocation of these companies aroused infighting among local governments. In today's globalized world,

inland provinces not only compete against one another, but also against foreign countries with cheaper labor forces, such as Vietnam and Thailand. The incentive for local governments in inland provinces to boost local economic growth motivated them to race to the bottom, and grant favorable policies to attract more businesses to come. Even though it is the center's policy not to allow use pension contribution rate reduction to attract business, sometimes provincial governments reported that they could not resist strong policy demands from investors (HNP0725131). Starting 2013, the Hubei government issued new preferential policies to private and foreign high-tech companies, including favorable treatment for public pensions, healthcare, work injury, unemployment, and maternity insurances, and housing fund (the so-called "*wu xian yi jin*"). For example, Hubei allowed qualified foreign and private employers to pay pension contributions at a reduced 10% rate, and permitted a 1 percentage point reduction in work injury insurance. As the required contribution rate for work injury insurance had been only 1% of payroll, the reduction meant a total exemption from contribution for work injury insurance (HBP0705131). Hunan's favorable policies in 2014 were based on how many jobs an investment could bring to a locality – a 14% pension contribution rate for employers with investment that created more than 2,000 employment opportunities, a 12% rate for those producing at least 2,500 employment opportunities, but the rate would increase by 1% each year until it reached the required 20% (HNP0725131). When interviewed, these government officials were also eager to learn what preferential policies other inland provinces were implementing. They argued that if other provinces granted a contribution rate reduction and they did not, that would be deemed as an unfair competition (HNP0717132). Even though the Midland region took a beating during this wave of business relocation, the Midland region nevertheless lost some business to countries in Southeast Asia (HBP0705131).

Inland provinces' pension contribution reduction policies have aroused public anger. Thousands of workers petitioned the Bureau of Human Resources and Social Security each year – some workers were quite violent, threatening to drink poison or to jump out of the building (HBP0705131). Petitioners often brought their paystubs and requested their employers to make up for the pension contributions they were supposed to make. According to the policy, the government intervenes only if a petition reports a violation within a one-year period; but most petitions they received were for violations out of the one-year investigation range (HBP0705131). Like many other provinces, Hubei now requires the amount of pension contributions to be stated clearly in labor contracts and signed by both employers and employees. However, changes in individuals' welfare preferences over the life course increases the difficulty of enforcing governments' regulations –younger workers may not care about pension contributions and would rather cash in the amount for welfare contributions, but when they approach retirement age they would hope to have contributed more to their pension accounts (HBP0705132).

One may wonder how these midland provinces pay for their pension benefit provisions, if they grant discounts on employers' pension contributions while being challenged by a higher system old-age dependency ratio. It is learnt from interviews that these provincial governments have had to use their fiscal budgets to cover deficits in pension funds. At the end of every fiscal year, the Hunan government receives a quite limited amount of funding from the center, and in the beginning of the following year the government distributes that center funding to its sub-provincial governments. However, for some localities, mainly third-front areas, the funding from the center would sustain their pension funds for only about half a year. After that, these sub-provincial governments must often turn to the provincial government for fiscal support. The Hunan provincial government has to bail out part of the deficits using its own fiscal resources.

(HNP0724132). For the remaining deficits, these sub-provincial governments often 1) use local government reserves invested in national bonds, or 2) obtain loans from banks. In the latter case, they would need to repay the borrowed amount with interest from local fiscal budget, to guarantee timely pension benefit provisions. Borrowing money from banks happened quite often. Sometimes, these local governments would wait till the next fiscal year to pay back the loans. (HBP0708132). As a result of such pension contribution reductions and lack of center fiscal support, Hunan has become the province among the 31 provinces that is most fiscally burdened by the urban pension program. In 2012 alone, the Hunan provincial government spent more than 3 billion *yuan* from the provincial fiscal budget to subsidize the pension program, which did not include Hunan sub-provincial governments' fiscal contributions (HNP0725131).

The Midland region is generally like Hunan/Hubei and scholars call it the “midland welfare lowland” (*zhongbu shebao wadi*) (Feng, 2006; Han, 2008). The discussion in this section shows that Hunan and Hubei are faced with serious pension fund constraints for two reasons: 1) very limited fiscal support from the center; and 2) the loss of pension funds as labor-exporting regions in the current decentralized pension administrative system. However, in order to stay competitive in the global capital marketplace, these provincial governments have to keep investors' pension burdens low. The resulting pension fund deficits need to be covered by fiscal resources of the provincial and sub-provincial governments. As a result, these regions only set a medium level pension contribution rate, and in return the governments become the most fiscally burdened of any by the pension program.

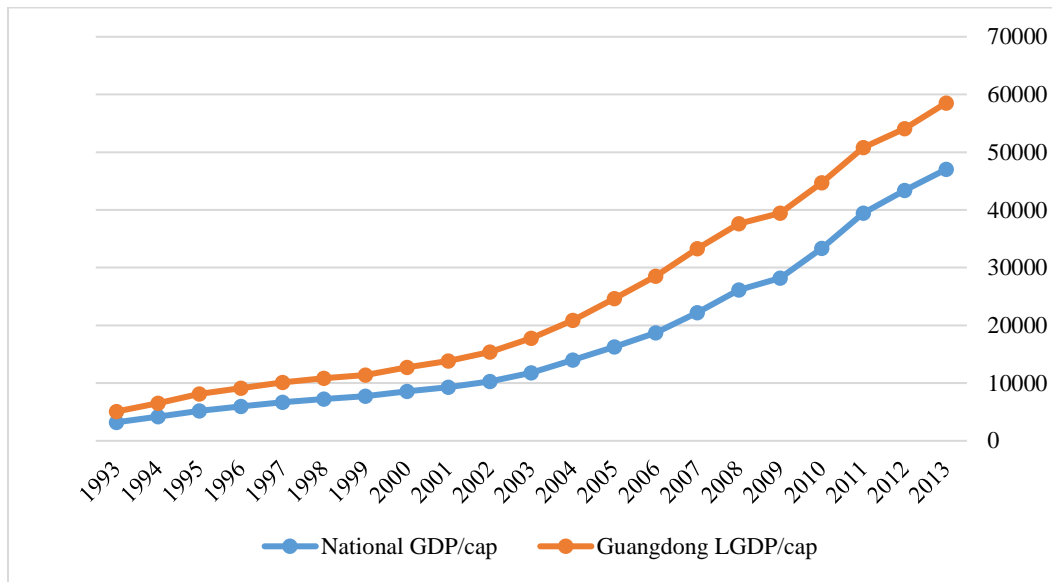
5.6 Guangdong – Enjoying the luxury of pension fund surpluses

Like Hunan/Hubei, Guangdong is low in political sensitivity and high in economic openness. However, Guangdong represents the engine of the Chinese economy emerging from

the economic transition, and given its fiscal abundance, enjoys complete financial independence from the central government. Since its economic opening-up, Guangdong has held an exceptional place in the imaginations of migrants, and millions of them have moved to Guangdong to find jobs. Its distinct economic and pension system demographic conditions deserve our special attention, so that we put regions like Guangdong in a separate category, a subgroup in Type Three, in our typology.

As the first province to open their door to foreign investment in 1979, Guangdong has become the powerhouse of China's market economic development in the past three decades. In the early 1980s, the center created special economic zones (*jingji tequ*) in four cities in Guangdong and Fujian Provinces to attract foreign investment and exercise an export-oriented development strategy. Trial market economic reforms were conducted in these localities, configuring the original SOE-dominated economic structure by promoting the service industry, and encouraging private and foreign investment. Guangdong's convenient geographic location with its geographic proximity to Hong Kong, and to more efficient market-oriented administrative system made Guangdong a rising star in the Chinese economy. Guangdong's total local gross domestic product (LGDP) has ranked first among all the 31 provincial units for 26 consecutive years (*People's Daily*, 2015). According to statistics from the *China Statistical Yearbooks*, Guangdong's LGDP has accounted for more than 11% of national GDP since 2001. Figure 5-7 compares Guangdong's LGDP per capita and the national GDP per capita from 1993 to 2013. Using the solid blue line of the national development level as the baseline for comparison, the figure shows that Guangdong's economy quickly took off in the 1990s, and carried its momentum over into the 2000s to secure its economic advantage over the rest of the country.

Figure 5-7 National GDP/cap and Guangdong LGDP/cap, 1993-2013 (unit: yuan)



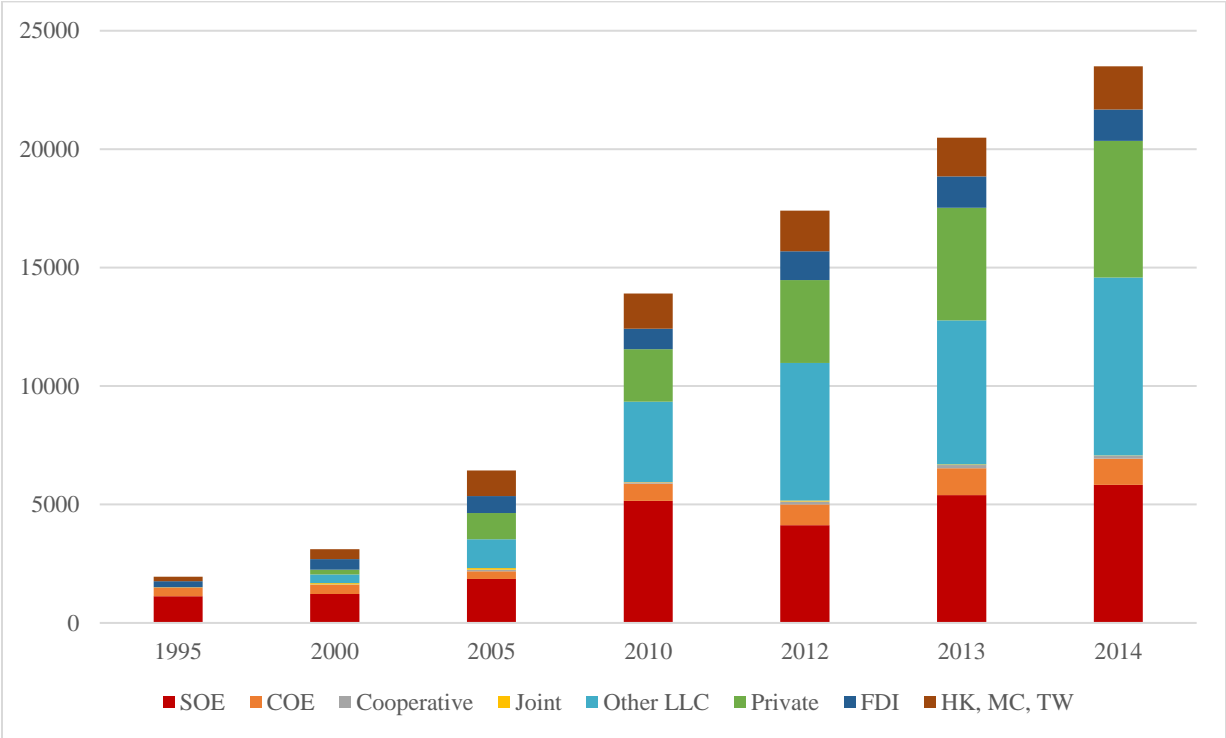
Source: *China Statistical Yearbooks* (various years).

Mainly due to the Guangdong government’s healthy fiscal condition, it is always excluded from the center’s earmark subsidy programs. In addition to Guangdong, seven other provinces, Beijing, Tianjin, Shandong, Shanghai, Zhejiang, Jiangsu, Fujian, are often called the financial G-8 by scholars in China, and are excluded from center’s fiscal subsidies in most cases (BJN0531121). As such, these provinces are truly “eating in separate pots” from the center, being financially independent. Given the lack of center fiscal support, the Guangdong government must act as an independent fiscal unit striving to increase local revenue and reduce expenditure, such as creating a more inviting business environment by reducing the pension burden of employers to attract more investment to come.

Figure 5-8 presents the composition of Guangdong’s economy by registered business ownership from 2006 to 2013, using the amounts of fixed asset investment received from various sources as a measure. The figure shows that by 2014 SOE investment accounted for less than a quarter of Guangdong’s total fixed asset investment. It reflects the increasing reliance of

Guangdong’s local economy on non-SOE investment, mainly private investment and investment from outside mainland China. Given the mobility of non-SOE capital, the dominant presence of non-SOE investors requires the government to grant favorable policies, including pension contribution reduction, to keep these investors from relocating. The interaction between the government and the business sector creates a virtuous cycle wherein favorable policies induce more businesses to come, and a resulting healthy ecosystem for economic development enables the government to carry out more preferential policies for the businesses.

Figure 5-8 The composition of Guangdong’s fixed asset investments by registered ownership, 1995-2014 (unit: 0.1 billion yuan)



Source: *Guangdong Statistical Yearbook* (various years).

Employers’ mean pension contribution rate at the provincial level in Guangdong has been well below the center’s proposed 20% of payroll. Government officials interviewed in Guangdong confirmed that in some areas, in particular the Zhu River Delta, the mean employers’ pension contribution rate has consistently been below 8% of payroll (GDP0421151). The mayor

in Zhongshan city once publicly discussed the idea of exempting employers' pension contribution as a strategy to attract more investment, and the provincial government was certainly aware of this proposal (BJN0619141). However, in the northern part of Guangdong the employers' contribution rate was set at 20% in order to guarantee timely pension provision (GDP0421151). The provincial government is now seeking to narrow the intra-provincial differences by gradually bringing contribution rates to a middle ground, 13% to 15% of payroll. An official from the Bureau of Human Resources and Social Security in Guangdong complained that enterprises were overburdened by pension contributions, and it would be unwise to increase the rate to meet the center's requirement (GDP0422151). An official interviewed noted that the province-wide rate adjustment move was not a response to the center's call for creating a nationally unified pension system, but was intended to improve the pension program's payment capability within the province (GDP0421152). However, this province-wide contribution rate adjustment plan has made little progress – even though the plan was supported by cities/counties in the north, cities/counties that would need to raise the contribution rate held firm ground against it. The progress of this plan is the epitome of what would happen if the center proposed to standardize the pension contribution rate across the country (GDP0422151).

In addition to the relatively lower contribution rate, the salary base for pension contribution in Guangdong is severely underreported. Underreporting salary base is a strategy commonly used by small private and foreign employers to evade pension contributions and yet stay lawful. Researchers find from the pension contribution records of local social security administrative bureaus in Beijing and Guangdong a considerable number of the records having the same salary bases, namely 60% of last year's local average wage level, which is the center's minimum requirement for public pension participation (BJN0531121). Because Guangdong

houses a very large number of small private and foreign companies, underreporting salary bases happens to a larger extent than in any other region in the country. Underpaying pension contribution has two effects: 1) at an individual level the pension participant will only receive minimum pension benefit payments upon retirement; and 2) at the pension fund level it reduces the government's pension revenue and may affect long-term sustainability of the pension fund. People often discount future benefits. Sometimes employees and employers reach an agreement to contribute the required minimum and employees may cash in the difference in contributions. However, in some cases, employers with the minimum wage level for establishing the pension contribution without obtaining permission from the employee, which later becomes a major dispute issue between employer and employee (BJN0402121).

Moreover, despite the compulsory nature of the program, a large number of employers evade pension obligation completely. Non-participation is very common among migrant workers and those employed in the informal labor market. A national survey on migrant workers found that, the participation rate of the public pension program was under 15% in 2012 (National Bureau of Statistics, 2013). One study found that 48.6% of non-participants reported that the main reason for nonparticipation was “do not know how to enroll”, 24.9% said “contribution rate is too high”, and 15.5% stated “employers do not want to enroll” (Sun et al., 2011). Although the center issued *The Labor Contract Law* in 2008, which was regarded as a milestone in China's labor relations, some employers, mainly those from small and private businesses, signed fake contracts with employees, without specifying social security protections, among other evasions and misstatements. Some employees were informed upon retirement that their employers did not pay for their pension contributions, and they would not be eligible to collect pension payments in spite of more than two decades of hard work. The contract they had signed did not have any

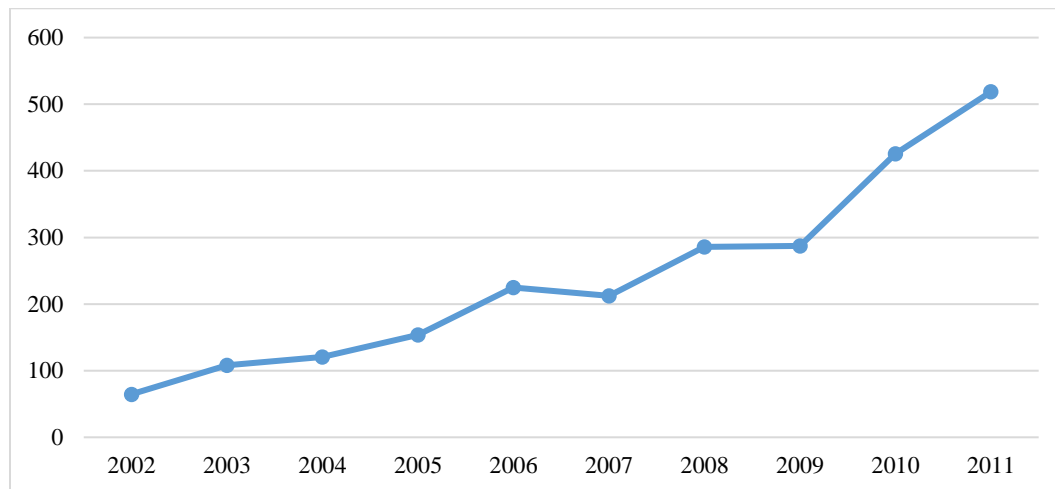
legally binding effect since the format of the contract did not comply with the Law. The concern and grievance over unsecured retirement life takes these employees to the streets and to strike action (Zhang, 2013; Zhu et al., 2014). A strike that took place in Dongguan, Guangdong Province in April 2014 gathered around 40,000 to 60,000 employees demanding that, their employer, Yuyuan Footwear Manufacturing – Nike’s outsourcing manufacturer, repay years of pension contributions (Qing, 2014). Strikes like that one certainly attracted eyeballs and the government intervened, but often such outcries become non-issues as soon as other events take their place to dominate the public’s attention (Baumgartner & Jones, 2009).

When asked why the salary base was well below the real wage level, and what explained the large non-participation rate, a government official in Guangdong answered that:

“Do we have more rats or more cats in the world? It is essentially impossible for cats to catch all rats. And those rats get shrewder over time, and they have come up many tactics to counter government policies. As long as the (*local*, the author’s note) pension fund is capable of providing current pension payments, we are content.” (GDP0421151)

Even with a low pension contribution rate and an underreported salary base, Guangdong’s pension fund reserve has the capacity to pay for over 50 months’ pension benefit payments, which makes it the most financially sustainable pension reserve among all provincial pension funds in China (Zeng, 2015). Figure 5-9 presents the changes in pension fund balance each year in Guangdong, aggregated at the provincial level from 2002 to 2011. It shows that the amount of annual pension fund surpluses had an eightfold increase over the period, quickly rising from 6.4 billion to 51.8 billion *yuan*. Cumulatively, during the ten-year period, Guangdong had surpluses of over 240 billion *yuan* in its pension fund.

Figure 5-9 Change in pension fund year-end balance in Guangdong, 2002 to 2011 (unit: 0.1 billion yuan)



Source: Zheng et al. (2013), p. 99.

Migrant workers' pension contributions explain a major part of the surpluses in Guangdong's pension fund. As mentioned, the migrant workers' pension entitlement issue is closely related to the limited portability problem of the pension program. As labor mobility increased significantly after the 1990s, China experienced a large-scale population movement, from inland provinces to economically more developed coastal regions. As Guangdong had three of the first four special economic zones in China, Guangdong has attracted more than 30 million migrant workers, over 95 percent of whom stayed in the Zhu River Delta (Zhang, 2014). As discussed earlier, when these migrant workers relocate or withdraw from the pension program, the nature of the localized pension governance structure makes it difficult for the public pension contribution portion to travel with them. The contribution would be deposited in Guangdong's local pension funds. The pension fund surpluses were essential for Guangdong's economic success in two ways – 1) they constituted a significant portion of local banks' circulating fund that supported local infrastructure development (GDP0422151), and 2) they give the local government more flexibility in alleviating enterprises' pension burdens by reducing employers'

pension contribution rates. We will return to the discussion of the limited portability problem in Chapter Six.

In January 2013, the Guangdong provincial government put forth an industrial transformation and upgrade plan – “Empty the bird cages and replace the birds: The Nirvana of the Phoenix”. The idea of this plan was to substitute labor-intensive industries with capital-intensive ones and thus to achieve an industrial structure upgrade. This plan precipitated a wave of industrial relocations from Guangdong to inland provinces. As was discussed in the prior section, inland provinces competed with each other to offer more favorable terms to attract these relocating businesses, and pension contribution reduction was one of the strategies. As Guangdong is embracing new businesses and labor force, it would be interesting to see how Guangdong’s pension program evolves over time as the industrial structure changes.

Guangdong represents the most economically affluent region in China, and its pension program enjoys many unique advantages. The Guangdong case has important implications for the center-local relationship in China. When a locality is economically well developed and fiscally independent from the center, the government has more policy autonomy to vary its pension policy. Meanwhile, governments like that of Guangdong have the power to define and create rules at the national level that can help them secure more benefits at the expense of the rest of the country. To a certain extent, with complete fiscal independence from the center, the Guangdong government more resembles an authoritarian welfare policymaker, making its own welfare policies for local situations.

5.7 Gansu – The obedience of an economically backward region

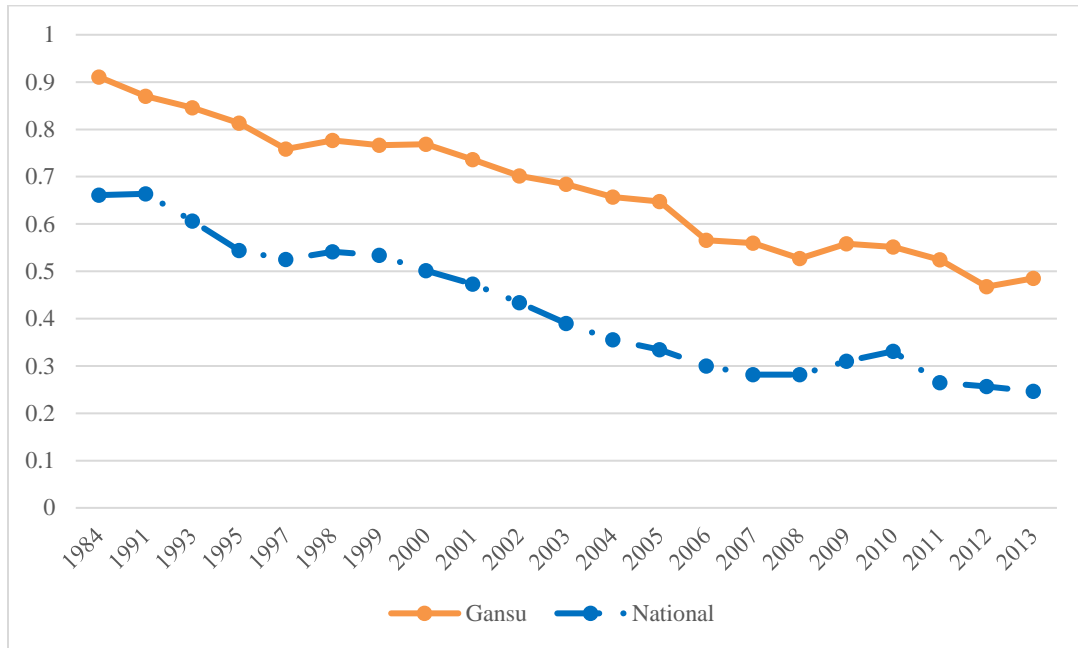
Gansu is located in the northwest of China, partly sitting in between Tibetan and Huangtu Plateaus. It is adjacent to Inner Mongolia, and Ningxia to the north, Xinjiang and Qinghai to the

west, Sichuan to the south, and Shaanxi to the east. Due to its strategic location, historically Gansu was a major corridor connected Great China and Inner Asia, and the famous ancient Silk Road passed through Gansu. Even though the geographic area of Gansu is the seventh largest in the country, the very mountainous landscape makes most areas in Gansu only sparsely populated. Its capital and the most populated city in Gansu, Lanzhou, is located in the southeast part of the province. Thanks to its mountainous landscape, Lanzhou's airport is located more than two-hour driving distance from the downtown, making it the most distant airport in all provincial capitals in China. During this two-hour drive, you would only see a few earthen houses sprinkled on a loess plateau, and signs of anti-deforestation and forestation experimental lands.

State investment has been the main economic resource in Gansu. Gansu's economy today greatly relies on mining of rare earth minerals, and on the nuclear base in Jiuquan. These two industries still heavily occupy by state-owned facilities. Therefore, market economic reforms did not interrupt Gansu's economic structure, nor did the reforms bring about waves of layoffs and early retirements, to the extent as occurred in other cases discussed above. According to official statistics released by the National Bureau of Statistics, the amount of foreign investments in Gansu was the third least among all the 31 mainland provincial units, only ahead of Qinghai and Tibet, and Gansu was ranked only ahead of Tibet in the amount of investment received from Hong Kong, Macau and Taiwan in 2013. Figure 5-10 compares the shares of state investment in total fixed assets in Gansu and at the national level. It again shows that state-owned units have played a major role in Gansu's economy, from over 90% of investment in 1984 to not under 50% in 2013. Despite the reduction across time, the share of state investment in Gansu has been systematically higher than that of the national average. The national average share of state-owned investments in fixed asset investments decreased from 66% in 1984 to less than 25% in

2013, from a majority shareholder in the economy to a minority, but in Gansu state-owned investments have remained the dominant capital source.

Figure 5-10 Shares of state investment in total fixed asset investment in Gansu Province and at the national level, 1984-2013 (unit: %)



Source: *China Statistical Yearbooks* (various years), and National Data Online.

Even including the center’s fiscal subsidies, Gansu is nevertheless challenged with a tight fiscal budget (GSP0409152). Unlike most provinces, Gansu does not have an office building for the Provincial Bureau of Human Resources and Social Security. The office space of the Bureau is divided into seven locations: six in different provincial office buildings, and seventh in a single floor rented in a small residential building. Given its very limited fiscal resources, no provincial leaders of the Bureau would take the risk of building a new office building, particularly when the center had strict control over spending items of its local governments (GSP0410151). Starting in 2010, the center required provincial governments that would like to apply for center fiscal support for their pension programs to submit operating budgets for the forthcoming year. Since then, the room for negotiating subsidy amounts with the center has become even more limited.

The officials interviewed from the Provincial Bureau of Finance did not seem to be particularly interested in the pension subsidy. They noted that, unlike the general fiscal subsidies that may be used as public financial resources, the special subsidy program for the pension is designated to fund only the urban pension program, and the amount received could only be invested in bank savings accounts (GSP0409151, and GSP0409152).

As Chapter Four's data on the center's pension program fiscal subsidies to each province revealed, Gansu does not in fact gain a high level of center fiscal support in comparison with other provincial units. The estimated expenditure for 2015 was 29.2 billion *yuan*, and the estimated pension program revenue was 29.3 billion *yuan*, including the center's fiscal transfer. In 2014, the center transferred 5.8 billion *yuan* to Gansu for the pension program, and the transfer amount for 2015 was expected to increase from the 2014 funding baseline (GSP0410151). With the center's funding, Gansu's pension fund could make ends meet, but Gansu really has a mouth-feeding fiscal budget – receiving the money with the one hand, and immediately spending exactly the same amount with the other (GSP0410153). According to an official from the Provincial Bureau of Finance, the amount of center fiscal support was determined in 1998 when the responsibility for providing pension benefit payments to retirees of center-owned enterprises was transferred from the center to local governments. The center granted fiscal support to compensate local governments for their additional spending for this new responsibility. The amount Gansu received in 1998 became a baseline, and each year the center simply applies an increase rate. The official commented that it would be impossible and unwise to seek to negotiate with the center for more fiscal support. The center must have its way in calculating how much fiscal support each province would receive (GSP0409151).

For years, Gansu had the highest mean total pension contribution rate among all 31 provincial units, more than 28% of payroll from employers and employees combined. Two top provincial officials interviewed stated affirmatively that, no discounted contribution rate was granted on paper as that would violate the center's policy, and the center would punish such a violation (GSP0410151, and GSP0410153). When informed that many other provinces had been bringing down employers' pension contribution rate in order to attract business to come and stay, most Gansu's government officials appeared to be seriously doubtful and surprised. An official from the Provincial Bureau of Human Resources and Social Security reported that, unlike eastern provinces that have a very favorable contributor-recipient ratio for the pension program, Gansu has only a much smaller pension contributor base. As such, the Gansu government really could not afford to reduce pension contribution rates (GSP0410151). Another official remarked cynically that, the strategy of reducing pension contribution to attract investments could never be sustainable (GSP0410153).

In addition to the high contribution rate, Gansu's salary base for the pension contribution is among the most consolidated. Gansu implemented a "dual salary base" policy for pension contributions. The dual salary base policy means that the salary bases for employers' and employees' pension contributions differ – employees' pension contribution base is their basic salary, but with the insured salary amount capped at between 60% and 300% of the average local wage level in the previous year; while employers need to pay 20% of total actual payroll, with no 300% upper limit of contribution. This policy only affects large profitable SOEs, such as those in the tobacco, petroleum, and telecommunication industries (GSP0410151), because only high-ranking corporate managers from these industries would receive salaries higher than 300% of the average local wage. According to an estimate of a government official from the Gansu Provincial

Bureau of Human Resources and Social Security, the average salary base for pension contributions for SOEs in Gansu was actually higher than 100% of the average local wage level for the prior year, and in some companies the base even exceeded 200% of the average salary (GSP0410153). The additional contribution collected due to this dual salary base policy has been crucial to ensure the sustainability of Gansu's pension fund. As a result of this policy, Gansu's real pension contribution rate from employers and employees combined is estimated to be higher than 28% of payroll and the highest in the country, even though Gansu's government officials acknowledged only a 28% contribution rate.

However, contrary to SOEs' generosity in inflating the pension contribution base, small private companies in Gansu found ways to evade pension responsibility, as shown in the other cases investigated. As a Gansu's official cited the words of President Xi, an average cannot represent a majority. SOEs' high pension contributions could not represent contributions by non-SOEs. The officials interviewed agreed that some small private companies may under-report their salary bases to reduce their pension burdens. For this pension contribution evasion tactic, an official seemed to be quite sympathetic: if they were not able to reduce their pension contributions, they would only go bankrupt in today's competitive business environment (GSP0410151).

Gansu's budgetary constraint misled its sub-provincial governments into expanding pension coverage to unqualified individuals in order to boost short-term gain on pension contributions. An official reported that more than 80% of petitions submitted to the Provincial Bureau of Human Resources and Social Security were associated with the public enterprise pension program (GSP0410151). Contrary to other provinces where petitions overwhelmingly focused on low pension contributions or non-participation, in Gansu petitions were more

frequently concerned with pension contribution back payments. The center specifically prohibits paying pension contributions in arrears (making back payments), as liability for benefit provision far exceeds the back payment amount collected. However, given the tight fiscal budget and limited pension contributor base, some sub-provincial governments in Gansu solicit people to enroll in the pension program to fulfill the annual recruitment quota for pension participants set by the provincial government. These solicited participants are often not qualified for the pension program coverage. They stop contributing to the pension program after a few months of enrollment. However, when they approach retirement age, they come to the Bureau and request to pay back the supposed contribution amount and to receive pension benefits. (GSP0410151).

Without much pension fund accumulation, the Gansu government welcomed the center's proposal to centralize the pension program. Gansu's individual accounts are completely emptied to ensure pension benefit provisions for current retirees. When asked about their thoughts on emptied individual accounts, an official answered, "Whoever takes over my position will find ways to resolve the issue". As long as we can afford to provide current pension benefits, I am fine with emptied accounts" (GSP0410151). Another official from the Provincial Bureau of Finance stated that the center should bail out pension deficits because the deficits are in fact transition costs. The center had promised to share SOEs' profits with sub-national governments to compensate them for the pension reform, but now the center seizes all the profits and sub-national governments are shouldering the responsibility of SOE retirees' pension benefit provisions (GSP0410152). However, despite their strong interest in centralizing the pension program, Gansu's officials thought this was an unrealistic (*bu xianshi de*) proposal. Gansu did not even achieve within-province pension pooling, and the current within-province pension fund

adjustment plan had encountered great challenges. To pool the pension program nationally at the center level would be a very appealing but unrealistic plan (GSP0409152, and GSP0410152).

With one of the highest pension contribution rates and the most consolidated salary bases for contributions in the country, the Gansu government still does not have much surplus in the pension fund. The government sees discounting the contribution rate as a violation of the central government's command, which makes a clear contrast to the other cases studied above. A substantial amount of pension contributions from large profitable SOEs in Gansu are crucial in sustaining its pension program. To move further, the government puts its hope on the center's plan on centralizing the pension program. The center's centralizing plan will be discussed in the next chapter.

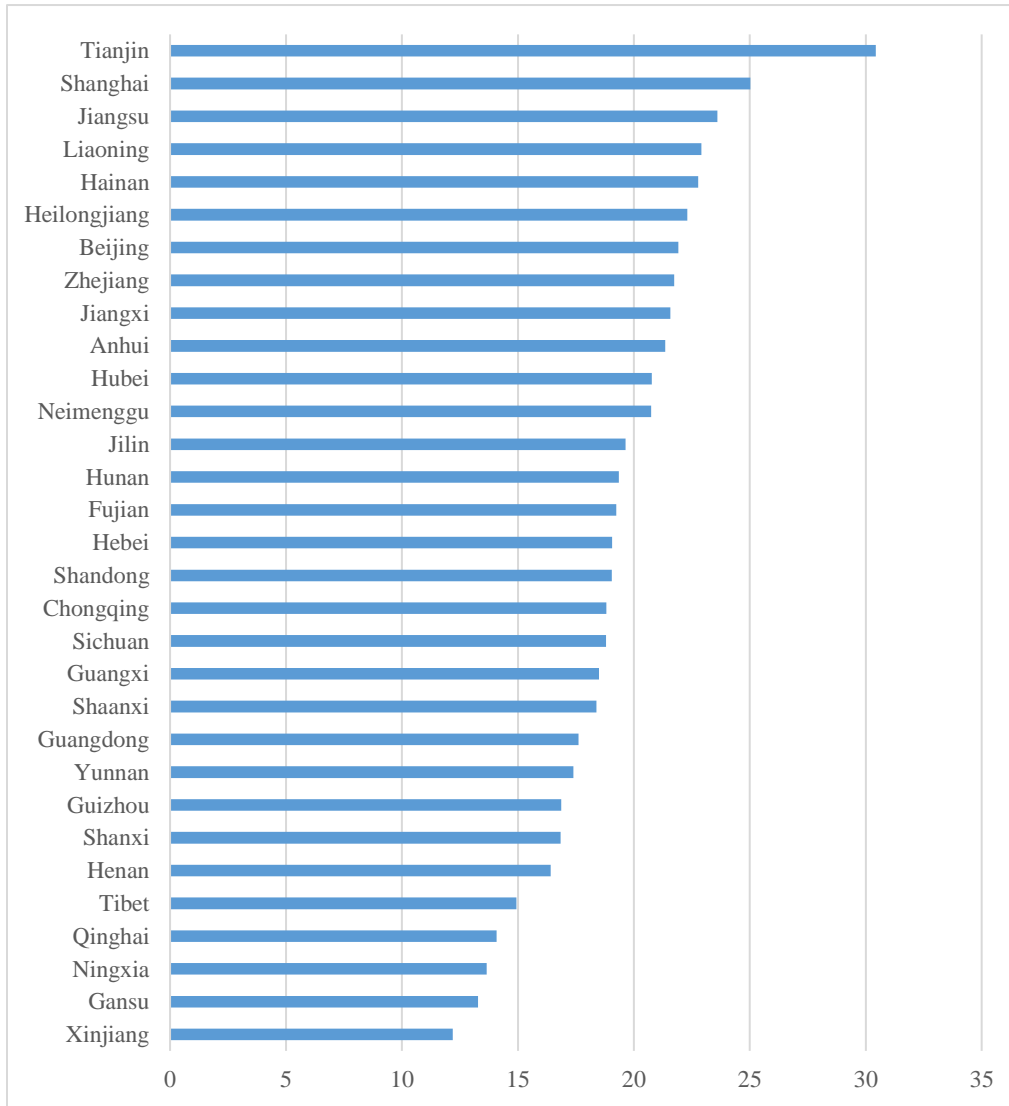
5.8 Discussion

Chapter Four tests the center's redistributive calculation, and this chapter discusses provincial governments' strategies in response to the center's decisions on pension subsidies. Given the fact that the ultimate purpose of the center's pension subsidy program is to promote individual wellbeing and prevent potential social grievances, it is worthwhile to ask whether the center-local interaction actually affects the generosity of individual-level pension benefits or not. In order to measure the level of pension generosity, this dissertation calculates the ratio of mean pension benefit relative to the cost of living in a particular region. The value of minimum living allowance set by each provincial government is used as a proxy of the cost of living in one locality. Dividing the provincial minimum living allowance value by mean pension benefit income aggregated at the provincial level offers an estimate of the living standards of pension benefit recipients – higher ratios indicate lower living standards, and lower ratios indicate the opposite. The data on minimum living allowances in 31 provinces come from the center's

nationwide survey from 2007 to 2013 (Department of Social Assistance, Ministry of Civil Affairs, 2014). The data on each province's pension benefit income are compiled by the author.

The results are presented in Figure 5-11.

Figure 5-11 Ratio of minimum living allowances to pension benefits, by province, 2008-2012 (unit: %)



Source: Department of Social Assistance, Ministry of Civil Affairs (2014), <http://www.mca.gov.cn/article/yw/shjz/llyj/201412/2014120073666492.html>, and the author's dataset. More details of monthly minimum living allowance in each province are included in Appendix Table 5-1.

The above figure shows the levels of pension generosity in ethnic minority regions (Type Two regions in the typology) are indeed higher than that of other provinces. As discussed in

Chapter Four, the center's major fiscal subsidies have played an indispensable role of promoting welfare development in ethnic minority regions. However, even though the center has channeled substantial fiscal support to old-industrial bases in the northeast (Type One regions), the figure tells that most center support did not arrive at the individual level. This chapter reveals that governments in old-industrial provinces such as Liaoning often see the center's pension subsidies as way to reduce social extraction and to fill historic pension burdens. As such, individual pension participants in these regions do not benefit much from the center's fiscal support. The figure also shows that in general coastal provinces (Type Five regions) only offer their retirees lowest levels of pension generosity. This is mainly due to the fact, discussed in this chapter, that these coastal provinces reduce businesses' welfare responsibility to attract investment, and individual pension participants bear the costs in this political and economic arrangement.

5.9 Conclusion

This chapter discusses five distinct types of fiscal structures for the pension program at the provincial level through systematic original case studies of five cases covering six provinces. This typology helps understand factors that shape subnational governments' redistributive incentives, and they depict how the pension program is funded and operated in subnational China. The findings of this chapter have two implications. First, despite the seeming strength of the Chinese central government, it has to rely on its sub-national governments to carry out its policies. Moreover, preferences of the center and local governments may not often converge. Local governments can make policy adjustments based on local economic and social situations to advance local interests. As for the urban pension program, the center puts forth general guidelines, but provincial governments are the real policy makers who make specific policy decisions based on provincial conditions and who implement those decisions at the sub-

provincial level. Second, regions that receive substantial fiscal support from the center are in the minority. For most provincial governments, funding the pension program is their responsibility. Variations in pension contributions and the imbalance in economic development across sub-national regions create a feeding loop. Regions with more advanced economic development levels can afford to reduce businesses' pension burdens and fuel further local economic growth, thus attracting more cheap migrant worker to contribute to local economies. Regions that suffer from economic backwardness lose manpower in the economies, and their governments need either to set high contribution rates to support the pension programs or to apply local fiscal resources to fund the program. A result of the fragmented urban pension system is increasing welfare inequality across sub-national regions in China.

What has the Chinese central government done to resolve the welfare fragmentation and what are the results, and what does the pension program contribute to our understating of center-local relations in China? These are the research questions of the next chapter.

Appendix Table 5-1 Monthly minimum living allowance, by province, 2008-2012 (unit: yuan)

	2008	2009	2010	2011	2012
Anhui	212	234	254	297	339.39
Beijing	390	410	430	500	520
Chongqing	231	231	256	299	326
Fujian	211	213	218	274	324.1
Gansu	157	171	189	207	251.29
Guangdong	256	244	254	286	313.98
Guangxi	178	217	228	241	270.48
Guizhou	158	170	212	271	308.04
Hainan	189	243	250	300	316.19
Hebei	196	245	265	310	335.01
Heilongjiang	201	217	240	278	323.67
Henan	169	186	202	233	271.76
Hubei	188	214	252	294	334.52
Hunan	180	195	214	243	304.52
Jiangsu	278	310	342	386	434.33
Jiangxi	193	194	244	308	345.93
Jilin	162	212	228	254	291.09
Liaoning	224	272	296	312	366.64
Neimenggu	195	241	299	344	407.7
Ningxia	187	204	212	244	252.5
Qinghai	188	223	232	236	310.83
Shaanxi	172	192	284	306	363.06
Shandong	235	262	286	314	364.12
Shanghai	400	425	450	505	570
Shanxi	200	213	231	268	308.48
Sichuan	190	196	210	242	276.73
Tianjin	400	430	450	480	520
Tibet	256	310	306	356	399.73
Xinjiang	143	172	183	200	261.29
Yunnan	198	199	206	248	284.42
Zhejiang	297	334	367	429	462.67

Source: Department of Social Assistance, Ministry of Civil Affairs (2014), <http://www.mca.gov.cn/article/yw/shjz/llyj/201412/2014120073666492.html>.

Chapter 6 Welfare federalism in practice

6.1 Introduction

The stories presented in the previous two chapters imply that the decentralized fiscal and administrative structure of the pension program has greatly empowered sub-national governments in China. As a result, the welfare capacity of the authoritarian Chinese central government is constrained by the level of compliance of its sub-national governments. While the Chinese central government has placed welfare development as its top priority, the provincial governments often modify the center's pension plan in ways that benefit their own interests.

Adjusting employers' pension contribution rates, as discussed in the previous chapters, is only one example of the conflict of interests between the center and provincial governments. What does the pension case contribute to our understanding of Chinese center-local relations in general? This chapter is set to discuss this question by addressing the following questions. How does the Chinese central government design policies and plans that motivate and also contain sub-national governments? Do center fiscal subsidy programs work to motivate sub-national governments and help the center achieve its desired policy outcomes? And how do provincial governments respond to the central government's commands while seek to advance their own best interests? Do we find any patterns of center-local relations in welfare politics in China?

We will answer these questions by investigating four cases of center-local interactions in the pension case: 1) the center's decision on funding the consolidating pension fund reform; 2) the center's policy to increase pension benefits every year since 2005; 3) the limited pension portability problem and the center's reform plan for transferring pension accounts across provinces; and lastly 4) the center's proposal for creating a centralized pension program, and its failures so far. These four cases also represent the four major challenges the Chinese government

faces with the current pension system – 1) emptied individual accounts and enormous future pension liability, 2) lack of a proper mechanism for pension benefit adjustment according to social and economic conditions, 3) limited pension portability, and 4) fragmentation of pension administration at the sub-national level, with low likelihood of creating a centralized pension scheme in the near future. The remainder of the chapter will unfold these four cases in turn, and the last section will conclude, and discuss implications.

A finding of this study is that the central government is aware that sub-national governments usually discount its commands. Policies the central government proposes often already reflect the discount sub-national governments may apply. Studies find that in a decentralized fiscal structure, higher-level governments often employ fiscal transfers as a tool to ensure lower-level governments' compliance and achieve their policy goals (Rodden, 2006; Treisman, 2007). This dissertation shows that the center's fiscal subsidies can motivate sub-national governments to deliver only part of what the center commands. Sub-national governments often utilize subsidy funding from the center to prioritize spending in other issue areas they desire, and oftentimes put local interests ahead of the national greater good. However, this does not mean that provincial governments can always challenge the center's decisions. Not all provincial governments are equipped with ability to negotiate with the center, not to mention publicly challenging the center's commands. Despite their strong inclination to advance local interests, sub-national governments are confined by the political and economic institutions in place. As a result, this study observes that provincial governments that are fiscally dependent on the center are relatively more compliant with the center's orders, and in particular that regions without much political importance to the center are the most obedient; but provinces with complete fiscal independence are more vocal and demanding. As a result, this study argues that

the center's fiscal support has only limited effectiveness in achieving the center's policy goals. However, without fiscal subsidies, the center can hardly obtain loyalty and compliance from sub-national governments at all. Here we use the term and concept of "welfare federalism" to describe center-local relations in the pension issue in China.

6.2 The center's subsidies for consolidating pension fund reform – *The squeaky wheel gets the oil*

As mentioned, individual pension accounts were emptied in practice to pay for current retirees' pension benefit payments. In 2001, the central government initiated a policy experiment of consolidating individual accounts, and thus a special fiscal subsidy program was created. Thirteen provinces in total participated in this experiment and ten provincial governments received special subsidies from the center beginning in 2001.

The Liaoning Province was the first provincial unit participating in the experiment, and they benefited most financially from it. In 2001 the center handpicked Liaoning as an experimental province to carry out the consolidation reform. The reform agreement between the center and Liaoning states that the center would cover 75% of Liaoning's annual pension fund deficit caused by the consolidation reform through fiscal transfers, and the Liaoning government was to pay the remaining amount. Simply put, the center would restore an amount equal to 75% of the 8 percent contribution which had been made by employees; Liaoning province was to cover the other 25%. The center's subsidy plan was called "fixed subsidies and continuous efforts of consolidating emptied accounts" (*jingtai bu zu, dongtai zuo shi*). The center used 2001 as a baseline year for calculating fiscal transfer amounts to Liaoning for this reform, and as the reform progressed the center's contribution was to remain the same as the amount given in 2001

(Lu, 2008). The amount the center granted for the experiment was 1.89 billion *yuan* in 2001 and every year thereafter (LNP1211132). As the number of pension participants gradually increased and the average wage level increased over time, the Liaoning government's fiscal responsibility for funding this consolidation reform increased over time, thus exceeding the initial 25%. In other words, as the experiment progressed, the portion of the center's investment in this experiment gradually decreased relative to that of the Liaoning government. In the eyes of local rulers, the center's arrangement of "fixed subsidies and continuous consolidation" was simply used by the center to fish for local fiscal resources (LNP1213131).

However, being the earliest bird, Liaoning was rewarded with a largest amount of fiscal transfer from the center for the consolidation reform among all participating provinces. As prior studies have pointed out, the Chinese central government often experimented in certain localities before putting forth national economic and social policies. This policy experimentation strategy is called "proceeding from point to surface" (*you dian dao mian*) (Cao, Qian, & Weingast, 1997; Montinola et al., 1995). Provincial governments have opportunities to apply for experimentation funding from the center, yet the differentiation between "point" and "surface" implies that the timing of participating in an experimentation makes a major difference. First experimentation cases, also called model experiments, are often rewarded with more attention and greater subsidies from the center. These cases are usually selected by the center to test the center's policy ideas. Therefore, with the formal or informal backing of the central government, these first experimentation cases rarely failed. As one scholar and policymaker reflected on effects of policy experimentation, it is hard to tell whether the success of an experiment is due to the effects of the policy design itself or to the center's strong fiscal support (BJC0413151). Spread of the experimented policy ideas from the "point" cases to other localities is called "expanding to

surface" (*kuo mian*). The experiment policy is often modified based on the lessons learnt from the first cases when applied to subsequent surface cases. In general, these surface cases are less favorably treated by the center.

In 2004 three years after Liaoning started its consolidation reform, the other two old industrial provinces in the northeast, Jilin and Heilongjiang, joined the experiment. Like Liaoning, Jilin and Heilongjiang also received substantial fiscal support from the center. However, according to the two government reports, *Jilin Province's Plan of Implementing the Improving Urban Social Security System Experiment* and *Heilongjiang Province's Plan of Implementing the Improving Urban Social Security System Experiment*, the center subsidized only 75% of the equivalent of 5 percent of employees' wages, thus subsidizing 3.75 percent of wages. The center again used the subsidy amount in the beginning year, 2004, as a baseline, and kept the same subsidy amount in the following years. Compared with the center's decision to subsidize 6 percent of wages in Liaoning, the center applied a 40 percent discount in Jilin and Heilongjiang. In addition, the center required Jilin and Heilongjiang to gradually increase the consolidating percentage by one percentage point each year, meaning consolidating 6 percent of wages in 2005, 7 percent in 2006, and reaching the 8 percent in 2007. In other words, as the reform progressed, Jilin and Heilongjiang provincial governments were expected to bear more fiscal responsibility in this reform than Liaoning did. The center transferred 2.1 billion *yuan* in total to Heilongjiang province for 2004 and 2005 two-year period (Yu, 2006), from which we may estimate the center's annual transfer amount to Heilongjiang for this reform was around 1.05 billion *yuan*, about a half of the amount Liaoning received.

The reform expanded to eight provincial units in 2006, Tianjin, Shanghai, Shanxi, Shandong, Henan, Hubei, Hunan, and Xinjiang. For local rulers, experimental projects mean

direct fiscal transfers and also other supporting funds (*peitao zijin*). Although local rulers disagreed with the center's idea that China should have a pension system with funded individual accounts, they still actively applied to be experimented cases (HNP0717132, and HNP0725131). Like the contract with the three northeast provinces, the divide of fiscal responsibility between the center and the eight local governments was 75% to 25%, but the funded amount was set to be equivalent to only 3% of employees' wages. Furthermore, instead of directly transferring the funding to local governments, the center designated the NSSF to invest the grant money on behalf of the local governments starting in 2006 for a five-year contract. The NSSF promised a 2.5% return rate on the investment (BJN0402121). A contract was signed between the Hunan government and NSSF in 2006, stating that all the subsidies and investment returns generated would be delivered to local governments after five years. However, after more than seven years, no settlement of the investment has been executed (HNP0724132, and BJC0612131). The center responded that provincial governments, midland provinces in particular, were technically incapable of managing and investing the pension fund, so these provinces would be better off if NSSF were to invest on their behalves (BJC0612131). When asked why local governments would not negotiate with the center to take back the money, an official from Hunan said, "We are very obedient, not like those coastal provinces" (HNP0724132). Though the Hunan government had not received any direct fiscal benefits for participating the experiment, they also had not set aside local fiscal resources for the promised 25% contribution to the consolidation fund as stated in the agreement. This means that the consolidation fund in Hunan still remains only notional in practice. However, on paper the reform in Hunan is still in progress. Therefore, the center government still transfers the due subsidy amount for the Hunan experiment to NSSF every year (BJC0612131). Hunan's government official interviewed also stated that when the center delivers

the promised fiscal support to their local pension account, they would have their promised portion ready (HNP0725131).

Shanghai was the only case that did not receive any fiscal support from the center in the 2006 reform wave.²⁰ In the agreement with the center, the Shanghai government promised to give local fiscal resources equivalent to 3% of employees' wages to the consolidation fund. According to the estimate, the Shanghai government was responsible for contributing about 5 billion *yuan* annually to the consolidation fund. In 2007 and 2008, the Shanghai government set aside 10.2 billion *yuan* in total to the consolidation fund. However, since 2009 the reserve amount in the consolidation fund increased by no more than 600 million *yuan*, and that increase came from interest payments on the investment made in the first two years (BJN0619141). By 2013 the amount reserved in Shanghai's consolidation fund was only 12.3 billion *yuan* (Li, 2015b), which suggests that the Shanghai reform in fact came to a complete pause after 2008.

In February 2007, the MHRSS and the MOF together issued a notice, *The Ministry of Labor 2007 Notice No.6*, to request that Zhejiang, Jiangsu, and Guangdong Provinces carry out the experimental consolidation reform 1) based on their local conditions and 2) using local fiscal resources. In 2008 the center approved Zhejiang's and Jiangsu's reform plan – the two governments would each contribute 5% of employees' wages in a few municipalities to start with, and the percentage would gradually increase each year. In 2009, Zhejiang and Jiangsu officially joined the reform. No further information was retrieved about these two experimental reforms. However, the Shanghai case shows that reforms without the center's fiscal subsidies would not go far. Even though the Guangdong government had sufficient pension fund surpluses to

²⁰ The center's subsidy plans for Tianjin's and Shandong's consolidation reforms were not stated in the agreements. The center only promised to subsidize their reforms, and transfer the money to provincial governments' accounts. However, the fiscal responsibilities of the two levels of governments were not clear. The center publicly stated only that no fiscal subsidies would be given to support Shanghai's reform plan.

consolidate individual accounts under its administration, in the end Guangdong did not participate in this reform. To carry out the consolidation reform using its own fiscal resources, the Guangdong government asked one pre-condition – the center would grant the Guangdong government the right to invest the consolidation fund, for example in the stock market, instead of depositing the money in bank savings accounts (Yin et al., 2007). Needless to say, the central government would not nod its head to approve this bold proposal. As a result, the Guangdong experiment plan fell through.

In 2008 the consolidation reform was deemed a failure. As stated, the consolidation reform required that the Liaoning government reserve the special fiscal allocation from the center and the provincial budget in a separate pension fund exclusively for future benefit payments from individual accounts. In other words, the Liaoning government was prohibited from using the money to pay for current retirees' pension benefit payments. However, as the Liaoning government's fiscal burden to carry out this reform gradually increased across time, the Liaoning government filed a report to the center, stating that to further this consolidation reform would compromise the "two ensures" policy in early 2008. The center noted that starting in 2009 the Liaoning government could borrow money from the individual account reserve to pay for current pension benefit payments, but Liaoning would need to repay the money plus interest. By 2015 the amount borrowed by the Liaoning government from the consolidation fund had reached 70 billion *yuan* (Li, 2015b). A government official from Liaoning commented, "Even though the center required us to pay back the borrowed amount, it is really another matter when it comes to when to pay the money back." (LNP1211132).

There are two main reasons that led to the failure of this consolidation reform. First, the very limited investment channels for the pension fund greatly constrains local governments'

incentives in creating a consolidated pension fund. Two, information about the center's plan to centralize the pension program leaked out, which caused sub-national governments to waver in their support of the reform.

First, because investment options for the pension fund are very limited, even policymakers at the center have not reached an agreement regarding the necessity of creating a consolidated pension fund of individual pension accounts. The central government allows sub-national governments to put the pension money only in national bonds or bank savings accounts, which yields less than 2% average annual return rate. The consumer price index (CPI) is a measure that estimates the price level of consumer goods and services. According to the official statistics, from 2005 to 2015 the average annual CPI increase in China was 3.0% (National Data Online). Therefore, a consolidated pension fund means depreciation of the pension money if the money sits only in bonds and savings accounts. Comparing the investment return rate of the pension fund with the CPI, Zheng Bingwen estimates that China's pension fund depreciated at least a hundred billion *yuan* from 1997 to 2015 (Hou et al., 2015). Thus, neither the center nor subnational governments had the determination to further push forward the reform.

Second, the preliminary discussion regarding centralization of the pension program became the triggering factor for the failure of the consolidation reform. In late 2007 the central government had informally solicited thoughts from scholars and policymakers on creating a pension fund centralized at the central level, and the news spread quickly. As soon as provincial governments heard the whispers, they lost any incentive to consolidate their local pension funds using their local fiscal resources. Sub-national governments simply did not want to further contribute their resources to the pension fund, if the money would be handed over to the center in the near future (BJN0603132). In the Third Annual Meeting of China Social Security Forum in

October 2008, the Minister of MHRSS, Yin Weimin, pointed out that the center would find an appropriate time to further promote to the rest of provinces the consolidating individual account reform. And in a follow-up interview, Minister Yin clarified that the appropriate timing would not be in 2009, since there were still difficulties in pushing forward this reform nationwide (Guo, 2009).

The center-local interactions in the consolidation reform showed that 1) the center again prioritized the northeast region via direct fiscal transfers; 2) center fiscal support was used to incentivize provincial governments to carry out the center's reform plan, and without the fiscal support provincial governments showed no motivation to obey the center's commands; and 3) provinces in sound fiscal condition had more power to negotiate with the center.

6.3 An inter-regional competition on raising pension benefits²¹

In 2005 the center decided to increase retirement benefits of enterprise retirees by "around" (*zuo you*) 10% every year beginning in 2005; in 2016, after twelve years, the center brought the policy to an apparent end. How effectively was this policy implemented during its life? One might have had good reason to suspect that the policy would not have been well received by provinces. However, perhaps surprisingly, most provincial governments participated in a race-to-the-top competition in increasing retirees' pension benefits. And most provinces raised pensions by more than 10% per year, resulting in a greater than 12% mean annual benefit increase at the national level in multiple years through 2013. As the center tightened its control over the increase rate, the annual benefit increase rate was cut back nationwide in 2014 and 2015 until the center finally put an apparent end to the 10% benefit increase plan in 2016. What

²¹ Part of this section was published in the *Journal of Contemporary China*, titled "Inter-Regional Competition in Retirement Benefit Growth—The Role of the Sub-National Government in Authoritarian China", November 2016, pp.1-18.

explains this inter-regional competition on raising retirement benefit level? And What does the policy life cycle tell us about center-local relations in China?

In Circular No. 26 issued in 1997, the center required provinces to develop “a mechanism for regular pension benefit adjustment”, though without giving specific instructions. In a follow-up regulation, Circular No. 38, issued in 2005, the State Council added, “The adjustment of pension benefits should be based both on the mean level of wages of current employees, and on price level variations.” Furthermore, the 2005 regulation mandated provinces to submit their specific adjustment plans to the MHRSS and the MOF for approval. Although Circular No. 38 identified two factors –the employees’ current average wage, and price level fluctuations – it failed to spell out a formula that clearly defined the relationship between these two and benefit adjustments. Thus, provincial governments continued to have considerable discretion to adjust provincial pension benefits according to local needs.

In 2006, the MHRSS announced a specific guideline for the benefit adjustment ratio: 60% of the rate of increase of local employees’ wages in the preceding year for the 2005 adjustment; 100% of that for 2006; and 70% for 2007. No explanation was given for how these ratios were arrived at. Over the period 2005-2007, the national average retirement benefit increased by 220 *yuan* per year, equivalent to an annual increase of 9.48% (He et al., 2012). The 2006 guideline was replaced by MHRSS Notice No. 43, released jointly by the MHRSS and the MOF in December, 2007, which proposed a 10% raise based on the 2007 benefit level for the 2008 retirement benefits adjustment. From 2008 onward, a 10% raise became the center’s standard recommendation for annual benefit increases. In 2013, the center put a strict limit on the increase rate of 10%, such that any increase higher than 10% may be subject to criticism and a cut to center fiscal subsidies. In 2016, after twelve years, the center brought the policy to an apparent

end. In the *2016 Central Government Work Report*, Premier Li Keqiang announced that in that year the retirement benefit increase rate would be around 6.5% (Zhao, 2016), bringing the decade-long “around 10%” annual adjustment of the retirement benefit to an end.

In order to motivate provinces to raise retirement benefits, the center decided to subsidize those regions seen as having difficulty diverting resources for such a benefit increase, excluding from the subsidies the eight provincial units located on the east coast -- Beijing, Tianjin²², Shandong, Shanghai, Zhejiang, Jiangsu, Fujian, and Guangdong. Of the aided provinces, the center promised to fully compensate provinces in the West for the costs of the benefit adjustment policy, while subsidizing those in the Midland region at 40% of costs. Whatever pension increase a province-level government might choose to provide, the center would grant them a subsidy equal to the full amount of the increase, if the province is in the West; 40% of the amount if it is in the Midland region; and nothing at all if it is in the East. With the center covering only 40% of their costs, provinces in the Midland region needed to tap their local pension funds or use general budget funds to finance the remaining 60%. Certainly, even with the center fiscal support, the West and the Midland regions would not raise the benefit level so high that they could not afford in the following year, as this year’s benefit level was to be used as a baseline for benefit increase next year.

The choice of a dividing line between the fully-subsidized West and partly-subsidized Midland region was not as clear-cut as that between the East and the others. It is worth pointing out that in employing the East-Midland-West geographic division for purposes of this subsidy, the center defined those regions differently from the way it had first defined them in 1986, in the Seventh Five-year Plan. Moreover, the division was subject to the adjustment by the center from

²² Tianjin is a borderline case. It is excluded from this center fiscal support for pension benefit increase, but it did receive more fiscal transfers on the pension program than the other seven eastern provinces (as shown in Chapter Four).

time to time. For instance, the subsidy level received by the three provinces in the northeast – Liaoning, Jilin, and Heilongjiang – was reduced once during the subsidy period from the “fully subsidized” category to the 40% level.

In order to calculate the annual adjustment rates actually implemented by provinces, this study collected data on mean retirement income per retiree at the provincial level for all 31 province-level political units for each year, 2008 through 2015. Annual increase rates for retirement benefits by province appear in Table 6-1, and mean monthly retirement income per retiree by province appears in Table 6-2, both discussed later.

The data on mean annual retirement income per person came directly from provincial governments’ annual work reports (for the majority of the data), government officials’ speeches and interviews, and news reports from major newspapers (often, [Province/City Name] *Daily/Evening*) and major online news portals (such as *Xinhuanet*, *Sina*, *Xiangrikui*, *163*, *Sohau.com*).²³ A cross-time analysis of pension benefits is not available. In addition, most prior studies have calculated annual benefit levels simply by using data from the *China Statistical Yearbook* on annual expenditure from each province’s pension fund; and number of retirees (e.g. Cai and Zhang, 2009; Xu and Han, 2006; Zheng and Mou, 2009). This method is flawed, as the Yearbook’s measure of annual expenditure from the pension fund can include outlays other than retirement payments, such as various subsidies, death grants, relief funds, and inter-

²³ For detailed sources, please see the Excel document at <https://sites.google.com/site/retirementbenefitsources/sources>. Most of the data are taken in the form of retirement income per person from the documents mentioned in the text. On some occasions, it has been necessary to infer the retirement income figure. For example, on some occasions the document will list the retirement income increase for a province for a particular year, instead of the level of retirement income. In such a case, the amount of the increase is simply added to the prior year’s level, or subtracted from the subsequent year’s level. The latter is preferable because the subsequent year’s increase is based on (and contains) the increase being measured. In a few cases the document reports the increase amount and the increase percentage rate; and the retirement income level is inferred from them. Actual data for 2014 were not available and for that year estimates appearing in the documents were used instead.

governmental transfer expenditures. Simply to divide the amount of pension fund expenditure by the number of retirees fails to yield an accurate or consistent measure for comparison across provinces. This study also used the official data from *China Statistical Yearbooks* on 1) annual pension fund expenditure by province, and 2) the number of enterprise retirees in the pension system by province, to calculate the mean monthly pension benefit payment per retiree by province, and the increase rate, as prior studies had done. The calculated increase rates range from 40% to negative 7% among provinces during the period investigated. The results confirm our concerns over the official data source, and demonstrate the need to compile an original data set, even if that meant using multiple sources.

Table 6-1 presents annual increase rates for retirement benefits in 31 provinces. The data show two distinct periods of the benefit increase plan, 2009–2013 and 2014–2015. During the first period, most provinces did increase their retirement benefits by more than the annual 10% rate sought by the center. For the period 2009 through 2012, the mean annual increase rate reached more than 12% at the national level until 2015, with some provinces showing annual adjustment rates greater than 15% in two consecutive years. Ironically, as a result of this behavior by province-level governments, in some localities retirees' retirement incomes actually became higher than their pre-retirement earned incomes, a phenomenon which has been called "retirement pay inversion" (*dao gua*) (BJN0408151). However, in the second period, the two years 2014-2015, a gradual decline in provincial governments' interest in raising retirement benefits could be observed. The mean annual increase rate in 2015 at the national level was under 10%.

Table 6-1 Annual adjustment rates for retirement benefits by province, by year, 2009-2015 (in percent for each year)

Province	2009	2010	2011	2012	2013	Mean**	2014	2015
<i>Eastern 8 provinces</i>								
Beijing	13.99	10.76	10.20	10.80	10.35	11.22	9.98	10.00
Fujian	12.75	12.19	10.63	16.94	17.65	14.03	10.34	10.17
Guangdong	9.24	10.01	6.09	7.85	8.35	8.38	9.79	9.43
Jiangsu	11.66	11.13	10.49	11.89	11.68	11.37	10.31	10.01
Shandong	11.70	10.54	12.53	13.92	11.44	12.03	N.A.	N.A.
Shanghai	11.33	12.09	9.88	13.02	13.33	11.93	11.38	N.A.
Tianjin	12.80	14.99	11.84	10.59	10.90	12.23	10.07	10.02
Zhejiang	9.47	9.61	9.35	11.76	11.00	10.24	11.63	10.00
<i>Mean**</i>	11.62	11.42	10.13	12.10	11.88	11.43	10.50	9.94
<i>Other provinces</i>								
Anhui	7.81	10.29	8.17	13.12	10.01	9.88	10.14	10.72
Chongqing	12.74	17.43	9.96	12.50	10.55	12.64	9.55	N.A.
Gansu	N.A.	12.70	15.70	12.11	5.43	11.01	N.A.	N.A.
Guangxi	10.69	11.16	11.17	14.00	12.34	11.87	N.A.	10.68
Guizhou	13.04	12.64	13.93	9.17	10.08	11.77	11.76	8.24
Hainan	12.94	15.83	17.80	15.11	10.14	14.37	9.87	5.75
Hebei	12.06	14.48	10.53	11.57	9.80	11.69	9.60	7.29
Heilongjiang	16.09	14.18	12.42	12.87	17.20	14.55	13.13	11.81
Henan	12.22	13.22	14.64	8.74	11.42	11.91	10.54	9.54
Hubei	11.70	12.38	16.95	16.23	13.47	14.15	10.05	10.03
Hunan	12.04	12.30	11.48	15.91	10.90	12.53	10.44	N.A.
Jiangxi	15.86	14.37	12.82	14.70	10.44	13.64	11.36	N.A.
Jilin	11.96	9.32	13.50	14.47	12.60	13.44	9.53	7.24
Liaoning	11.24	16.53	15.19	13.70	11.25	13.58	9.95	9.89
Neimenggu	12.70	14.45	15.69	6.66	10.23	11.95	10.02	9.82
Ningxia	10.55	12.72	12.41	11.15	9.33	11.76	N.A.	N.A.
Qinghai	13.02	12.33	14.35	13.24	9.78	12.54	12.13	10.10
Shaanxi	13.77	14.59	17.29	9.90	10.58	13.23	7.41	8.80
Shanxi	15.84	20.23	12.79	10.08	12.74	14.34	N.A.	N.A.
Sichuan	N.A.	N.A.	15.52	N.A.	N.A.	15.52	N.A.	N.A.
Tibet	15.13	10.69	10.62	12.73	7.63	11.36	11.10	10.35
Xinjiang	15.64	14.18	12.48	12.58	5.31	12.04	10.32	10.27
Yunnan	11.10	11.29	12.10	12.19	11.23	11.36	10.27	10.42
<i>Mean**</i>	12.74	13.51	13.37	12.40	10.54	12.52	10.40	9.45
Significance						0.023		

of difference between means, p value								
National Mean***	12.45	12.96	12.53	12.31	10.91	11.93	10.43	9.57

N.A. = Not available.

*: Xiamen is excluded.

** : Simple (unweighted) provincial means.

One important reason provinces increased retirement benefits was to compete for fiscal resources from the center. Center-subsidized retirement benefit increases constituted a perfectly acceptable vehicle for provinces to seek added fiscal resources from the center. Provincial officials in several locations stated that when their counterparts elsewhere were using the benefit increase opportunity to earn more funding from the center, it would have been foolish for them not to do the same (HBP0705132, HNP0724131, and LNP1213131). Provincial officials made a calculated decision: With a large number of retirees in a province, subsidies for even just a one percent increment to the pension raise would mean good fortune for the province. The raise in pension benefits would also increase disposable personal income level in a locality, which is a key indicator in the cadre evaluation system that measures government officials' performance according to government officials interviewed in Hunan (HNP0725131).

A close examination of Table 6-1 reveals that the eastern provinces set lower increase rates in general than did other provinces. The mean increase for eastern provinces between 2009 and 2013 was 11.4% while that for other provinces was 12.5%, more than a percentage point higher. The difference was significant at $p=0.023$. Guangdong in particular showed an increase rate which varied between 6% and 10%. As noted, the eight eastern provinces have been fiscally independent, covering the costs of retirement benefit increases with no subsidies from the center. When externalizing the costs of a welfare program is not an option for provinces, their incentives

to perform a welfare expansion task are often minimal. The differences in benefit increase percentages among provinces are not trivial. Every percentage point difference in the retirement benefit increase means a large amount of a province's fiscal budget. For instance, a 10% increase in Guangdong in 2010, benefiting 3 million retirees, cost their government 5.6 billion *yuan* (Liu, 2010). However, during 2014 and 2015, when the center tightened their control over the pension benefit increase rate, the grant-receiving provinces reduced their benefit increases, while the eastern provinces were able to show more consistency and resilience. As a result, the mean increase rate in the eastern provinces surpassed that of non-eastern provinces by almost 0.4% in 2015.

How then can the self-funded benefit increases in these eastern provinces, at above 10% in many instances, be explained, since their leaders would not seem to be highly motivated for self-financed expansion of welfare programs? Two major reasons were repeatedly offered by officials in two provinces in this category: First, they had constantly been compared with other provinces, mainly inland provinces, which had awarded more generous benefit increases (FJP0626131, and GDP0421151). For instance, a news report titled "Guangdong's retirement benefit level is lower than Gansu's" stirred heated discussions among the public (Cheng, 2014). Even though Guangdong has embraced more capitalist principles than most other sub-national regions, the apparent discrepancies between Guangdong's more advanced economic development level but lower pension increase pace put the Guangdong government to shame. Government officials in Guangdong and policy analysts had to respond to such news accounts by attempting to explain why Guangdong had a lower benefit increase rate, and promising more active benefit increase policies in the future (Cheng, 2014; *Southern Metropolis Daily*, 2014). Pressure based

on peer comparison pushed provinces without budget aid to match benefit increase plans of those with fiscal support.

The second reason offered was that officials in eastern provinces felt that retired persons' basic livelihoods would have been threatened by the price inflation that had occurred in prior years had no benefit increase been granted (FJP0626131, and GDP0421151). Price increases for major necessities of life in recent years had hit the lower income population the hardest, retirees included. While official central government data showed the consumer price index to have risen by only 2.6% in 2013, local food prices, and especially prices of vegetables and other basic goods consumed in large amounts by lower income people, could have risen much more (Xinhua News, 2014). As the pension provision formula does not provide a formal mechanism for automatic benefit adjustment across time, provinces have a responsibility to adjust benefit levels periodically to permit retirees to maintain an adequate level of living.

The retirement benefit increase had become so routine that the public had come to expect it to occur every year. Reports of the adjustment often make headlines in local newspapers. In order to put the benefit increase plan in context, reports often made comparisons, weighing their own increases against those of neighboring provinces. Provincial governments boasted of their retirement benefit increases as achievements "performing actual deeds for the people" (*wei min ban shishi*). In government work reports, local newspapers, and interviews, they claimed credit for the national ranking of their province's pension increase (e.g. Lin and Li, 2014; Liu, 2013; Zhang, 2014).

When they proposed the benefit adjustment plan and subsidy policy, the center certainly did not expect or desire an inter-regional race in pension increases. Because the center was fiscally responsible for fully or partially funding benefit increases in the West and Midland

regions, respectively, the inter-regional competition in obtaining more fiscal support from the center in fact increased the center's fiscal burden. To deter such competition, the State Council issued a special announcement in 2013 warning that any locality raising retirement benefits beyond the 10% target would incur a reduction in their regular fiscal transfer from the center; and a notice of criticism would also be circulated (HBP0705132)²⁴. Local officials certainly did not want to risk their political careers, but some still sought to test the center's limits by setting their locality's increase rate slightly higher than 10%. That the center's efforts to slow the growth were becoming effective is shown in Table 6-1, which reports that the mean benefit increase rate at the national level fell to slightly above 10% in 2014, and fell still further in 2015.

²⁴ Circulation of a Notice of Criticism by the State Council is a form of punishment of a local government and its officials.

Table 6-2. Mean monthly retirement income per retiree, 2008-2015, and retirement income replacement rate (RIRR), 2011, by province

	2008	2009	2010	2011	2012	2013	2014	2015	RIRR (2011)
<i>Eastern 8 provinces</i>									
Beijing	1630.0	1858.0	2058.0	2268.0	2513.0	2773.0	3050	3355	35.8
Fujian*	1004.0	1132.0	1270.0	1405.0	1643.0	1933.0	2133	2350	44.3
Guangdong	1298.0	1418.0	1560.0	1655.0	1785.0	1940.0	2130	2331	43.5
Jiangsu	1183.0	1321.0	1468.0	1622.0	1815.0	2027.0	2236	2460	43.0
Shandong	1214.8	1357.0	1500.0	1688.0	1923.0	2143.0	N.A.	2515	55.1
Shanghai	1501.0	1671.0	1873.0	2058.0	2326.0	2636.0	2936	N.A.	36.1
Tianjin	1171.8	1321.8	1520.0	1700.0	1880.0	2085.0	2295	2525	36.7
Zhejiang	1426.0	1561.0	1711.0	1871.0	2091.0	2321.0	2591	2850	50.0
<i>Mean**</i>	1303.6	1455.0	1620.0	1783.6	1997.0	2232.2	2481.6	2626.6	43.1
<i>Other provinces</i>									
Anhui	1037.0	1118.0	1233.0	1333.7	1508.7	1659.7	1828	2024	42.3
Chongqing	1099.0	1239.0	1455.0	1600.0	1800.0	1990.0	1990	2180	48.5
Gansu	N.A.	1260.0	1420.0	1643.0	1842.0	1976.0	N.A.	2168	58.7
Guangxi	982.6	1087.6	1209.0	1344.0	1532.0	1721.0	2043	2261.1	51.1
Guizhou	1014.7	1147.0	1292.0	1472.0	1607.0	1769.0	1977	2140	46.9
Hainan	850.0	960.0	1112.0	1310.0	1508.0	1661.0	1825	1930	45.8
Hebei	1103.0	1236.0	1415.0	1564.0	1745.0	1916.0	2100	2253	54.2
Heilongjiang	850.2	987.0	1127.0	1267.0	1430.0	1676.0	1896	2120	47.1
Henan	1005.8	1128.7	1277.9	1465.0	1593.0	1775.0	1950	2136	51.2
Hubei	940.0	1050.0	1180.0	1380.0	1604.0	1820.0	2003	2204	48.3
Hunan	914.0	1024.0	1150.0	1282.0	1486.0	1648.0	1820	N.A.	45.8
Jiangxi	883.0	1023.0	1170.0	1320.0	1514.0	1672.0	1862	N.A.	47.2
Jilin	920.0	1030.0	1125.0	1278.0	1463.0	1647.3	1804.4	1935	47.6
Liaoning	979.0	1089.0	1269.0	1461.7	1662.0	1849.0	2033	2234	47.6
Neimenggu	1087.0	1225.0	1402.0	1622.0	1730.0	1907.0	2098	2304	45.6
Ningxia	1280.0	1415.0	1595.0	1793.0	2044.0	2230.0	N.A.	2469	51.7
Qinghai	1306.0	1476.0	1658.0	1896.0	2147.0	2357.0	2643	2910	55.4
Shaanxi	1060.0	1206.0	1382.0	1621.0	1781.5	1970.0	2116	2302.2	51.8
Shanxi	1067.0	1236.0	1486.0	1676.0	1845.0	2080.0	N.A.	2630	50.0
Sichuan	1012.0	N.A.	1115.0	1288.0	N.A.	1525.0	N.A.	N.A.	43.9
Tibet	1699.0	1956.0	2165.0	2395.0	2700.0	2906.0	3228	3562	62.7
Xinjiang	1183.0	1368.0	1562.0	1757.0	1978.0	2038.0	2298	2534	53.2
Yunnan	1036.0	1151.0	1281.0	1436.0	1652.0	1792.0	1976	2182	51.7
<i>Mean*</i>	1062.3	1203.5	1336.9	1530.6	1734.0	1906.0	2094.4	2335.9	49.9
National Mean*	1124.6	1268.4	1409.9	1595.8	1801.9	1990.2	2194.3	2410.9	48.1

N.A. = Not available.

*: Xiamen is excluded.

** : Simple (unweighted) provincial means.

Table 6-2 shows mean monthly retirement incomes per retiree by province for 2009 through 2015. It shows significant variations in retirement income levels across sub-national regions. However, the validity of employing the level of retirement income as a measure of retirees' well-being in a province might be questioned, given profound inter-regional economic disparities. The retirement income replacement rate (RIRR in the table), which is the ratio of retirement income to pre-retirement earnings, is an alternative which measures the value of retirement income in relation to local economic conditions. As an indicator of the replacement rate, we use the average income per employee working in urban enterprises as a proxy for pre-retirement income. We divide mean retirement income by pre-retirement income for the same year to represent the replacement rate. The results, which are presented also in Table 6-2, confirm that substantial inter-regional inequality exists in the values of retirees' retirement benefits. The provinces with the highest replacement rates were Tibet, Gansu, and Qinghai; the provinces in the bottom were Beijing, Shanghai, Tianjin, Jiangsu, and Guangdong. Because of their higher benefit increase rates since 2008, provinces in the West and Midland in general have higher replacement rates than those in the East, contrary to what we may have expected.

The pension benefit increase case tells again that when it comes to incentivize sub-national governments to implement a welfare expansion policy, the Chinese central government has to rely on its fiscal subsidy program. On the one hand, through subsidy programs the center takes on partial fiscal responsibility for funding of welfare, which falls under sub-national governments' duty after the administrative reforms in the 1980s. On the other hand, the Chinese central government utilizes fiscal subsidies as its leash to push and restrain local governments. Meanwhile, regions that are fiscally independent show more autonomy in social policymaking.

6.4 Limited portability problem and the inter-regional pension transfer plan²⁵

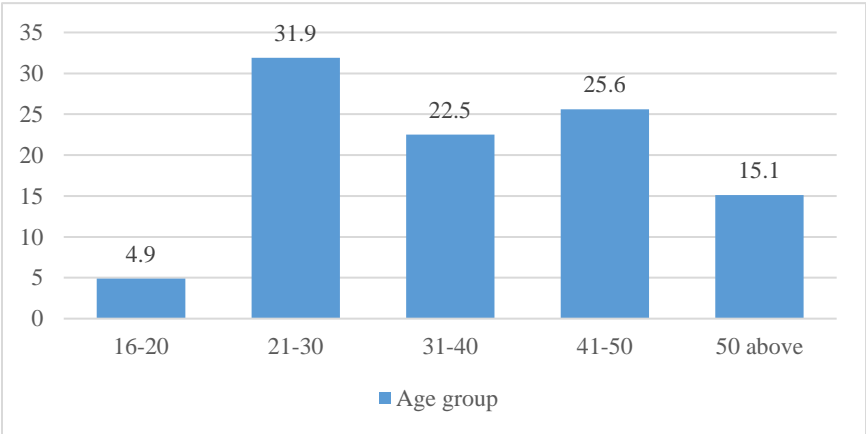
After relaxation of the restrictions of the *Hukou* (household registration) system, both rural-to-urban and inter-regional labor mobility increased dramatically. People are allowed to move from rural areas and stay in cities without carrying residence permits. As urbanization accelerated, the number of migrant workers multiplied quickly since the 1990s. Migrant workers have thereafter provided a cheap labor force for the urban economy, especially for labor-intensive industries, which are essential to China's economic success. However, their rural residence identity still keeps migrant workers from enjoying the same benefits of urban welfare programs as their peers with urban residence identity (Zhang & Wang, 2010). This section discusses the limited portability problem of the pension program, as exemplified in the migrant workers' pension entitlement issue, to show that beneficiary provinces of this limited portability problem have become a major obstacle blocking the center's attempts of further reforms.

Most pension administrative units incorporate participating migrant workers in the urban pension program, with minor revisions such as reducing contributions, and setting up minimum contribution length and withdrawal requirements to regulate migrant workers' participation. A few localities, such as Shanghai, Chengdu, and Dalian, set up separate welfare packages for migrant workers integrating old-age pensions, healthcare, and work injury insurance. The idea of creating a separate welfare package for migrant workers is less preferred, since it complicates the already fragmented system (Guo & Du, 2005; Li, 2014). The primary goal of the center is integration of migrant workers with the urban pension system. The focus of this section is thus on regions that include migrant workers in their urban pension programs.

²⁵ Part of this section was published in *Asian Social Work and Policy Review*, titled "Labor Mobility Without Pension Portability: Migrant Workers' Endangered Pension Entitlement in China", Volume 9, Issue 3, October 2015, pp. 269–81.

Several characteristics associated with economic migrant workers are crucial to our discussion here – they are often young or middle age, lower-paid, and willing to take on seasonal and temporary work. Figure 6-1 shows that in 2012 migrants in the 21 to 30 age group were the most numerous, at 31.9 percent of the total migrant population, and the 40 to 50 age group constituted the second largest migrant age group at 25.6 percent.

Figure 6-1 Age composition of migrant worker population in 2012 (unit: %)



Source: NMSRMW (2014).

A cross-time comparison indicates that the percentage of migrant workers who were in the 50 years and above age group gradually increased – from 11.4 percent in 2008, to 12.9 percent in 2010, to 15.1 percent in 2012. The average age of migrant workers was 37.3 in 2012, which was 3.3 years older than in 2008. These numbers indicate that more migrant workers are hitting retirement age. According to data released by the National Monitoring Survey Report for Migrant Workers (NMSRMW), fewer than 15 percent of migrant workers participated in the public enterprise pension program (NMSRMW, 2014). There are two main reasons that explain the low participation rate: 1) individual-level short sightedness of migrant workers leads them to choose cash salaries instead of participating in the pension program for long-term gain (Wang,

2011); and 2) employers' choice to maximize production profit by evading pension responsibility (Yang & Guo, 2006, p.111).

Even for those migrant workers who do participate in the urban pension program, the probability that they would receive pension benefits upon retirement remains quite low. The program requires participants to contribute for at least 15 years to be eligible to collect pension upon reaching retirement age. Furthermore, the decentralized administrative structure for pensions has caused the program to have very limited portability. The limited portability problem poses a particular threat to migrant workers' pension right, as they often engage in seasonal work and move from one locality to another several times a year. As the expression "floating population" – a term used to refer to these migrant workers – suggests, most migrant workers are not able to stay in one locality for a long time, certainly not 15 years. Therefore, this limited portability problem greatly constrains migrant workers' ability to transfer their pension accounts when they relocate, as their contributions were deposited in localities where they work. Every time when migrant workers relocate, their contribution records start all over again.

Cross-city/county pension transfers were highly unlikely before 2008, when almost all the 2,000 plus pension funds in the country were managed at the city- or county- level. The situation improved in 2009 when provincial governments began to set up intra-province transfer mechanisms that allow within-provincial transfers of public pension contribution. However, cross-provincial transfers still remain a major challenge. Inter-regional pension account transfers involve two parts of the contributions: to 1) pillar one, the public pension pool, and to 2) pillar two, individual accounts. The first part, the amount contributed by employers on employees' behalf to the public pension pool, is the major obstacle that keeps inter-regional transfers from going through.

Being frustrated by the transfer process, a considerable number of migrant workers have chosen to voluntarily withdraw from the pension program and cash in their contribution (*tui bao*) at the end of the year before returning to their home provinces for family reunions at the time of the Spring Festival (Li, 2014). By the end of 2013, the number of people voluntarily leaving the program accounted for 16.5 percent of the total number of participants in the pension scheme nationwide (Zheng et al., 2014). However, by terminating voluntarily, they can cash in only contributions to individual accounts, which means that they lose contributions to the public pool. The substantial pension contributions these migrant workers make to the public pension reserve, as a result, are deposited at the locality where they work. Migrant workers bring these work localities extra demographic dividends.

Guangdong, Zhejiang, and Jiangsu together with the three big metropolises, Beijing, Shanghai and Tianjin, are listed as top destinations for the migrant population (National Bureau of Statistics, 2013). Data presented in Table 6-3 confirm the skewed geographic distribution of migrant workers in more developed coastal regions. In addition, Table 6-3 also reveals an increasing concentration across time of migrant population at the Zhu River Delta area in the Guangdong Province. Migrants have constituted a large percentage of the population in Guangdong. Statistics from the Sixth Population Census carried out in 2010 revealed that Guangdong had 79 million long-term residents, 31 million non-residents staying in Guangdong longer than half a year, and 11 million non-residents staying in Guangdong for less than half a year.

Table 6-3. The geographic distribution of migrant workers by work place, from 2007 to 2009 (unit: %).

	Home city	Home province	Zhu River Delta	Yangtze River Delta	Bohai Rim	Others
2007	17.8	16.3	20.5	20.1	20.3	5.0
2008	16.1	16.7	26.5	25.0	7.9	7.8
2009	19.2	16.6	30.3	21.4	5.9	6.5

Source: The Statistics Division in The People's Bank of China (2012).

Table 6-4 reports the within-system old-age dependency ratio for each province, i.e., the ratio of numbers of recipients to contributors in the system, which may be called the "system dependency ratio." Instead of including only registered urban residents, the system dependency ratio also includes unregistered migrant workers. The system dependency ratio reflects the pressure pension recipients put on contributors who are economically active employees. The last column in the table presents the change in the system dependency ratios from 2007 to 2014, with a negative number meaning a decrease in system dependency ratio and a positive number meaning an increase in the dependency ratio. In 2014, the top five provinces with the highest system dependency ratios were Heilongjiang, Jilin, Hubei, Gansu, and Hunan; and the lowest five were Guangdong, Zhejiang, Beijing, Fujian, and Shandong. According to the data, a large majority of migrant-receiving provinces have substantially lower system dependency ratios than migrant-exporting regions and old industrial bases, thanks mainly to the influx of young migrant workers. In addition, the data show that many of these migrant-receiving provinces secured their advantage by attracting more young workers and enlarged the advantage of the young within-pension-system demographic structure across time. Migrant-exporting provinces and old industrial bases are the ones which suffered the most from high system dependency ratios, and their pension burden has greatly increased over time.

Table 6-4. System old-age dependency ratios, by province, 2007-2014 (unit: %)

	2007	2008	2010	2011	2014	Change 2007-2014
Anhui	37.6	37.6	36.1	35.6	45.8	8.2
Beijing	34.3	31.2	24.9	22.7	15.5	-18.8
Chongqing	48.6	47.5	49.1	51.5	30.1	-18.5
Fujian	23.7	22.6	21.7	20.5	17.3	-6.4
Gansu	41	40.8	41.6	47.8	64.6	23.6
Guangdong	13.1	12.6	11.8	10.9	10.2	-2.9
Guangxi	33.8	34.8	44.4	45.6	38.1	4.3
Guizhou	37.8	37.9	35.2	33.8	36.4	-1.4
Hainan	38.9	36.8	33.5	31.4	32.2	-6.7
Hebei	35.9	34.8	35.6	36.8	43.1	7.2
Heilongjiang	44.1	47.4	61.6	63.2	79.4	35.3
Henan	32.7	32.6	33.4	32.7	35.3	2.6
Hubei	36.1	37	40.9	44.3	66.2	30.1
Hunan	40.8	39.6	39.4	39.1	64.1	23.3
Jiangsu	28.3	27.6	28.4	27.8	32.2	3.9
Jiangxi	33.2	30.5	31.5	34.8	56.1	22.9
Jilin	41.8	42	52.6	55.8	68.0	26.2
Liaoning	45.8	44	46.2	45.5	53.5	7.7
Neimenggu	35.2	35.9	38.3	43.3	56.1	20.9
Ningxia	29.8	29.5	39.5	42.8	29.2	-0.6
Qinghai	38.1	37.4	36.8	44.7	53.1	15
Shaanxi	40.4	40.3	44.4	45.6	41.5	1.1
Shandong	24	24.2	24.2	24.3	24.8	0.8
Shanghai	57.5	58.7	59.7	41.6	48.0	-9.5
Shanxi	31.1	31.1	33.2	34.2	46.1	15
Sichuan	41.6	43.1	50.9	49.6	44.6	3
Tianjin	52.8	52.3	49.9	48	43.2	-9.6
Tibet	58.8	57.4	57.8	40	45.7	-13.1
Xinjiang	30.7	30.4	34.5	36	42.3	11.6
Yunnan	45.7	43.7	41	43.7	43.4	-2.3
Zhejiang	18.5	16.3	15.1	15.2	15.1	-3.4

Source: Zheng et al. (2013) p. 103, and Zheng et al. (2015) p. 35.

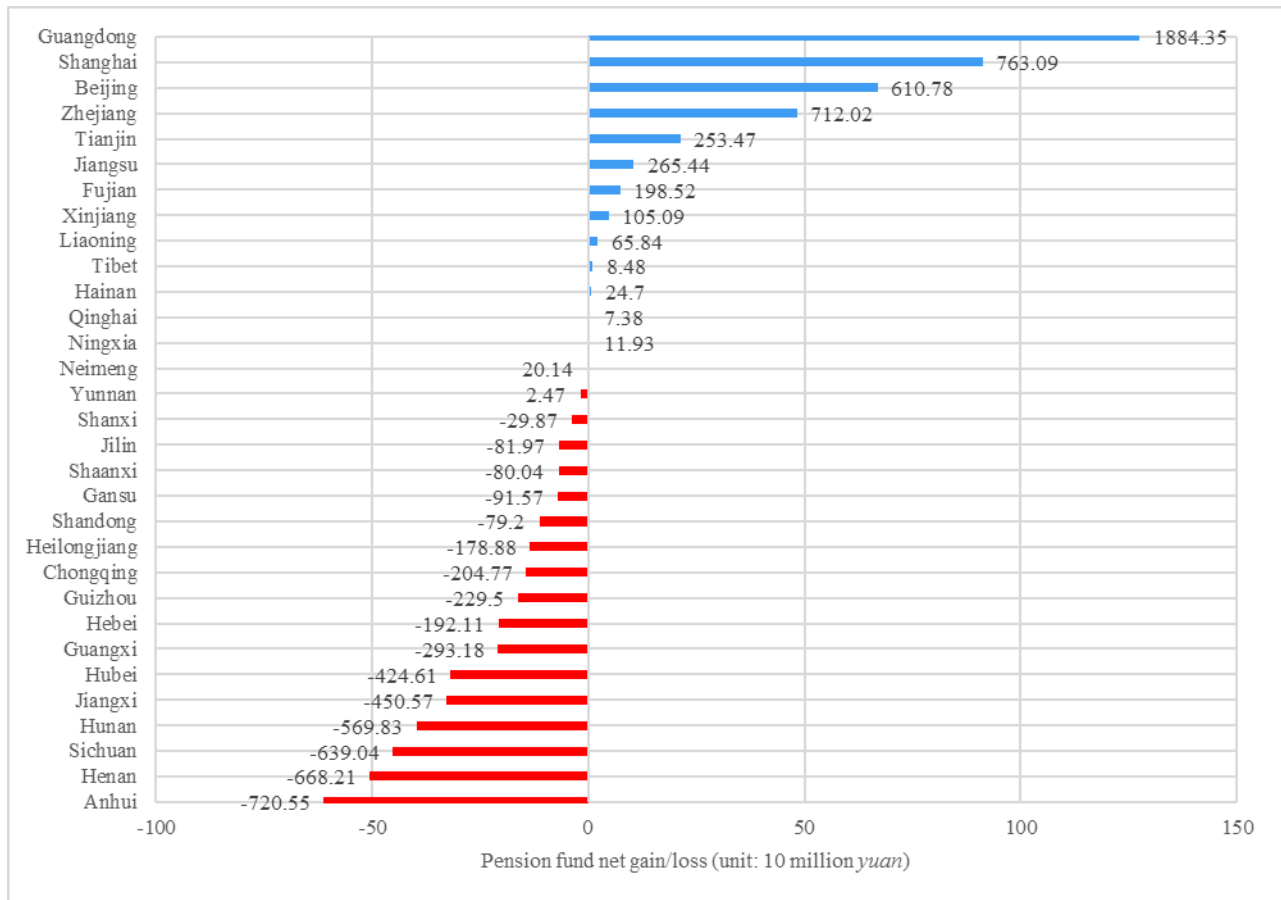
The concentration of migrant workers in economically more developed regions, especially in Guangdong Province, gives these regions 1) cheap manpower, and 2) pension

deposits that migrant workers are not able to transfer when relocating. As such, migrant-receiving regions, like Guangdong, have accumulated huge pension fund surpluses, which allow their governments to exempt or reduce pension contribution for investors. High-tech multinational companies, which are likely to bring in large investment packages and employment opportunities with them, are most likely to receive this favorable treatment (BJN0402121). The whole process creates a powerful virtuous circle that benefits these migrant-receiving provinces—the cheap labor force also contributes to the pension funds, and a pension fund with sufficient resources can afford to reduce extraction from businesses, attracting more investment to come.

Figure 6-2 (also see Appendix Table 6-1 in the chapter appendix for more detailed information) presents net gainer and loser regions in the labor movement in the single year 2010. In the figure, the numbers next to the bars tell the net flow of labor force in each province in 2010, i.e., the amount of labor inflow minus that of the outflow. The bars indicate the resulting gain/loss in the pension fund, blue indicating net labor-receiving provinces and red showing net labor-exporting provinces. According to the figure, 13 provinces were net labor-receiving localities and their local pension funds benefited from the population inflow. Among these labor-receiving provinces, Guangdong is the greatest beneficiary, gaining 127.45 million *yuan* in 2010. By 2013, the Guangdong pension fund has accumulated more than 400 billion *yuan* of pension fund surpluses (Lan & He, 2014). Even though the center requires that all pension-related funds, including local pension funds and the special fiscal account of center fiscal subsidies, should be exclusively deposited in national bonds or bank savings accounts, the Guangdong government has found ways to better utilize the pension fund surpluses. It is learnt from an interview that, the pension fund becomes a notional fund reserved at banks, and local banks are allowed to use the money as a circulating fund to support local infrastructural development (GDP0422151). When

the official interviewed was reminded of the center’s requirement of saving the money at savings accounts and bonds, the official responded that “That is stupid. Do you know what a billion fund means to local economies?” (GDP0422151).

Figure 6-2 Estimated gainer and loser provinces in labor mobility, and net change in pension fund by province, 2010 (unit: 10,000 persons; 10 million *yuan*)



Source: Zheng et al. (2013), pp. 129-31. For supplementary information on this figure, please refer to Appendix Table 6-1 in the chapter appendix.

Figure 6-2 also points out major labor-exporting provinces – Anhui, Henan, Sichuan, and Hunan. These four provinces lost more than 6 million workers net in 2010. The population outflow is estimated to cost their pension funds more than 400 million *yuan* in that year. As a direct consequence of being short of pension contributions from in-service employees, these provinces are often challenged by pension fund deficits. Moreover, as mentioned, compared with

labor-receiving provinces, these labor-exporting provinces are at a disadvantage regarding attracting businesses to come. These provinces are trapped in a vicious circle where they lose both manpower and investment because of the limited portability problem. The highly decentralized fiscal structure does not allow these labor-exporting provinces to claim the pension fund they are supposed to collect from labor-receiving provinces (HNP0724132). Therefore, government officials from these migrant-exporting provinces welcome the center's proposal to create a nationally unified pension system (BJN0603132, GSP0410153, HBP0706131, and HNP0724132).

The center has proposed two reform plans so far to address the limited portability problem: 1) an inter-regional pension transfer plan in 2008, and 2) a unified urban-rural resident pension scheme in 2014. However, neither of these two reform plans touched the crux of the problem, namely the fragmentation of pension administration. In 2008 the State Council issued a tentative inter-regional pension-account transfer plan, the *Interim Procedures for Transfer Renewals of Urban Enterprise Employees Basic Endowment Insurance Plan*. According to the plan, voluntary withdrawal from the pension program (*tui bao*) would no longer be permitted. To transfer pension accounts, 12% of taxable salary (60% of the recommended 20% enterprise contribution rate set by the central government) was meant to be the standard rate for public pension's inter-regional transfers. However, thus far the plan has not been effectively implemented. MHRSS noted that even though more than 1.1 million workers filed requests for inter-regional pension transfers in 2011 and 2012, only 20% of the applications went through in 2011 and 25% in 2012 (Zheng et al., 2013).

This reform plan was certainly not well received by migrant-receiving regions with pension fund surpluses. The plan raised strong opposition from government officials in

Guangdong, who argued that this inter-regional transfer plan was no different from inter-regional robbery (*kua di qiangqian*) (Pang, 2009). A Guangdong government official interviewed complained that the center may have good intentions, but it simply did not have a realistic assessment of difficulties of implementing the plan (GDP0421151). 2009 Spring Festival was expected to be the first peak season of inter-regional pension transfer applications after the inter-regional pension transfer plan was issued. As withdrawing from the pension program was no longer an option for migrant workers, an inter-regional pension transfer became the only way to save their public pension contributions. The Guangdong government required Minister Hu Xiaoyi from MHRSS to chair the transfer processes at Guangdong Provincial Bureau of Human Resources and Social Security. The reason for doing that was simple – the Guangdong government wanted the center to witness and participate in the whole process, and did not want to bear any responsibility if anything went wrong. Guangdong has over 40 million migrant workers. The Guangdong government does not have the ability to process all expected applications in a timely manner and ensure complete accuracy. In this situation, violence could easily break out. Minister Hu seemed to be quite resigned to the inter-regional transfer plan. (GDP0421151).

In addition, migrant-receiving provinces, like Guangdong, have set up additional hurdles for inter-regional pension transfers to go through. Transferring pension contributions in and out of Guangdong involves more than what is required by the center. Take the capital city of Guangdong, Guangzhou, for example. To transfer pension accounts into Guangzhou, the Guangzhou government requires applicants to contribute to the Guangdong pension fund for at least three years to demonstrate that they have indeed secured a job in Guangzhou. The provincial government explains that the purpose of this requirement is to make sure the transfer-

in option is not used by a worker to obtain better pension benefit payments in Guangzhou after retirement without having contributed to the local economy (GSP0410152). Moreover, the employers' average pension contribution rate in Guangdong was around 8 percent (Zheng et al., 2013),²⁶ yet inter-regional pension transfers require a transfer amount of 12% of payroll. Therefore, no provinces would accept pension transfers with less than 12% of payroll, because it is directly related to the sustainability of the pension fund to provide future pension benefit payments. It was learnt from the author's interview that transfers from Guangdong to other localities often result in rejection by transfer-receiving localities, requiring transfer applicants to provide further supporting materials or make additional pension contributions. The costs of transportation between the two provinces (Guangdong and the home province) to facilitate the transfer often exceed the amount requested for transfer, so many migrant workers voluntarily terminate their transfer applications (GDP0421151).

There are also some technical difficulties involved in the pension transfer process. Because direct fiscal transfer from one province to another is prohibited, every pension fund transfer must go through the central government's fiscal operating system before it arrives at the receiving end. Since each region uses its own online fiscal operating system, each pension transfer application in fact requires coordination among three different operating systems. Any problems occurring during the transfer process would require the applicant to reapply (GDP0421151). The lack of a nationally unified fiscal operating system and a unified pension management system poses unresolved technical challenges to ensure smooth inter-regional pension transfers.

²⁶ Zheng et al. (2013) estimated that Guangdong's average employers' pension contribution rate was between 4.5% and 6.7% of payroll from 2008 to 2011. My interviewees from the Guangdong Bureau of HRSS said that the current average employers' contribution rate was around 8% (GDP0421152).

Realizing the difficulty of implementing the inter-regional pension transfer plan, the State Council released an urban-rural resident pension scheme in early 2014. According to Minister of HRSS Hu Xiaoyi, migrant workers would be the largest beneficiaries of this new scheme (*Beijing Daily*, 2014). The main target population of this new pension scheme is unemployed urban residents and rural population. The creation of this new scheme allows migrant workers to participate in this new urban-rural pension scheme and the urban pension program at the same time. In doing so, in case of the denial of eligibility for urban pension benefits, migrant workers would still receive retirement benefits from this new scheme. However, compared to the pension benefits from the urban pension program, the benefits provided by this new urban-rural resident pension scheme are much more meager, as they do not seem to provide enough incentive for migrant workers to participate. On the other hand, this new scheme implicitly gives a green light to pension localization and fragmentation at the expense of migrant workers' pension benefits. Therefore, this urban-rural pension merger plan entails more political formality than real any welfare improvement for migrant workers.

The center certainly understands that persistence of the limited portability problem in the urban pension program could arouse serious social grievances and hinder economic growth (BJN0619141). A story of China's economic success would not be complete without mentioning exploited migrant workers. However, the insecurity these migrant workers experience about their jobs and social security entitlement has led groups of migrant workers to return to their home provinces, resulting in labor shortages in the export-manufacturing belt along the coastline (Chan, 2010). As compared with prior generations of migrant workers, besides earning higher paychecks, migrant workers today are also more eager to socially integrate into the urban environment. Despite the center's efforts to promote inter-regional cooperation, the limited

portability problem still remains unresolved as of 2017, with no end in sight. The decentralized pension administrative system is a main cause of the limited portability problem. And the intervention of powerful migrant-receiving provinces to defend their vested interests is the immediate cause of migrant workers' partial citizenship, and has become a major obstacle for potential centralization of the pension program.

6.5 The challenges of creating a centralized pension program

The patchwork pension administration system in China at the sub-national level has become the very core ("*niu bizi*") of many problems faced by the Chinese government with the pension system. Unlike private old-age insurance programs, the most apparent advantage of a public pension program should be to spread insurance risk across a broader group of individuals in the same pension pool, and also to lower administration costs substantially (Verbon, 1988). Although one main purpose of the center's 1997 reform was claimed to be creation of a "unified" pension scheme for urban employees at the national level, the resulting program is highly fragmented. There are currently estimated 2000-plus pension pools, mostly at the municipal level (BJN0828121). By 2014 only four provinces had pooled their pension funds at the province level; Beijing, Tianjin, Shanghai, and Shaanxi, three of which are province-level municipalities directly under the central government. It is ironic that the Chinese public pension system is so decentralized under a unitary political system as defined in the Constitution.

The MOF revealed that in 2014 aggregate pension contributions collected nationwide reached 2.3 trillion *yuan*, and the expenditure on the pension program was 1.98 trillion *yuan*, which means that the net surplus of the pension fund in that year was 347.6 billion *yuan*. In addition, from the 1997 landmark pension reform to 2014, there were cumulatively pension fund surpluses of 3.18 trillion *yuan* across the country. During the same period, the center's fiscal

subsidies in the public pension program to sub-national governments were around 1.87 trillion *yuan* (Guo, 2015). That means that if the pension program were centralized at the national level, the pension system would be able to sustain itself and have a 1.3 trillion *yuan* balance without utilizing the center's fiscal resources. However, over two-thirds of the national surpluses were concentrated in nine provinces, each of whose pension fund surpluses was 100 billion *yuan* or above. The remaining 22 provinces in total had a balance of less than 600 billion *yuan* in their pension funds. Due to the highly decentralized pension administration system, the center is not able to utilize the pension fund surpluses reserved in the nine provinces to pay for pension fund deficits in other areas, and thus it has to employ center fiscal subsidies. Why has the center allowed the provinces with pension fund surpluses to retain the pension money that is supposed to be the national reserve of the public pension program?

In fact, the central government has urged sub-national governments to work toward the goal of creating a nationally unified pension system, and stated that goal in policy papers as early as 1991, in the State Council Circular No. 33. By "centralization", the center meant that 1) the whole country would have a centralized pension fund pool and all participants of the pension program would be pooled at the central level, and 2) all parameters of the pension system would be standardized throughout the country, including contribution rates, retirement benefit formula, eligibility for benefit payments, and fund management. In its 1991 Circular No.33, the State Council urged municipal governments to turn over their pension pools to provincial governments for administration. The Circular states that, "Those areas that have not yet implemented province-level pools for basic pension insurance funds must actively create conditions to achieve that, and current city- and county-level pools must be gradually transferred to the provincial level." The same clause appeared both in 1995 Circular No. 6 and in 1997 Circular No. 26,

requiring provinces to consolidate pension pools and administration by having cities transfer these functions to the provincial level. Some progress has been made in the past two decades. Most provinces have achieved mechanisms for within-province pension fund accommodation. The accommodation system works as that every pension administrative unit (usually city and county) turns in a portion of their pension fund to the provincial level, and the provincial government use the accommodation fund to support units that have trouble providing pension benefits. Under this accommodation system, within-province pension fund transfers are smoother. However, having these within-province accommodation systems is a compromise step forward, still far from accomplishing the centralized pension system the centered intended to build.

As pension reform has progressed, the center has repeatedly expressed its strong desire to centralize the pension scheme, and lately this desire has been publicly announced as a formal plan. The *Social Security Law*, issued in 2010, requires that the public pension program should gradually become a nationally unified system. In the Twelfth Five-Year Plan for Social Security, the government promised that by the end of the twelfth five-years, i.e., by 2015, the government would have created a nationally unified public pension program (State Council Circular No. 28, 2011). The political significance of a centralized pension scheme was again brought up in the 2012 Eighteenth National People's Congress Meeting. In the Fifth Plenary Session of the Eighteenth National People's Congress in 2015, as the Twelfth Five-year Plan period was coming to an end, the government announced that by the end of that year it would release a reform plan to centralized the pension scheme. Premier Li Keqiang included "creating a centralized urban public pension program" as one of the government's tasks for 2015 in his *2015 Government Work Report*. The center invited nationally renowned scholars and international

organizations (the World Bank, and the Asian Development Bank) to draft feasible unification plans (BJN0413152). However, no even tentative reform plan has been released so far.

There are three major challenges in regards to create a centralized pension program. First, there are large variations in the employers' pension contribution rates across sub-national regions, as this dissertation reveals. Inter-jurisdictional competition in offering more favorable business invitation packages, including lower pension contribution rates, is heated. Creating a centralized pension system means implementing a nationally standard pension contribution rate regardless of business location or ownership. Without doubt, regions currently implementing lower contribution rates, mostly economically affluent coastal regions, would be the first to stand out and oppose this unification plan. Moreover, increasing pension contribution rates would be particularly unpopular in the current situation of economic slowdown in China. To accommodate these provinces, some scholars and policymakers propose that the center should allow provincial governments to gradually adjust the contribution rate, providing that the adjustment would not undermine the ability of pension benefit provision at the national level. Supporters of this proposal argue that allowing some flexibility would reduce oppositions to the unification plan, and help bring local governments on board (Li, 2015a). However, a national unification plan with flexibility given to certain regions might only indulge opponents and delay the unification plan.

Second, even if the center were to successfully implement a nationally unified pension contribution rate, the center would still face the classic principal-agent problem in operating the centralized plan. Collecting pension contributions is a long-term task that requires the center's constant supervision and auditing. How to guarantee that sub-national governments would collect pension contributions in time and in full, and turn over the contributions to the center, is a

major obstacle in the centralization reform (BJN0603132). Under the current pension administrative structure, it is the governments which collect pension contributions who are responsible for pension benefit payments. As such, local governments are motivated to collect pension contributions, and in the case of reducing contribution rates for investors it is the local government which would need to fill the deficit hole by using local fiscal resources. However, if the centralization plan were achieved, the center would be running the pension program, yet the sustainability of the center's pension fund would completely depend on sub-national governments' extraction capacity and their compliance with the center's commands.

In a country as large and diverse as China, the central government has to work with a set of sub-national governments with diverse economic conditions and political interests. The center suffers from a serious information asymmetry problem. In fact, the very purpose of decentralizing the old highly centralized administrative and fiscal system in the 1980s was to allow local governments who possess local information to run local economies and pursue their best interests, and thus to achieve a greater good at the national level (Montinola et al., 1995; Oi, 1995). The information asymmetry problem in this decentralized fiscal system was alleviated by creating state tax bureaus (*guo shui ju*) at the local level. In the 1994 tax reform, the center set up national state taxes in addition to local taxes, and created state tax bureaus at the local level in charge of collecting taxes which local governments are required to hand over to the center. The establishment of state tax organizations greatly advanced the center's grasp of local economic information. A nickname "state tax troop" (*guo shui jun*) is given by local governments to describe the power and intrusion of state tax organizations into local economies (GDP0421151). Unless the central government adopts a centrally controlled pension administrative agency at the local level, like the state tax bureaus, centralizing the pension program would greatly increase the

likelihood of subnational governments shirking the responsibility of collecting pension contributions and abusing the national pension fund for local interests.

Third is the allocation of local pension fund surpluses and deficits. As mentioned, some local pension funds are better endowed than others – a few provinces have huge pension fund surpluses, some are mouth-feeding funds with the center’s modest fiscal support, and some are challenged both by pension reform transition costs and current pension fund deficits. Obviously, if centralization and unification were to be achieved, the central government would bail out all pension fund deficits, including transition costs and current pension fund deficits, from its fiscal budget. The main debate is around the ownership of pension fund surpluses that a few provinces have accumulated. Certainly, provinces with fund surpluses would not easily let go of their balances. The difficulty of centralizing local pension funds with vastly different balance sheets was best manifested in Argentina’s pension unification reform case. In that reform, only regions with pension fund deficits participated in the centralization reform, and regions with fund surpluses refused to do so (Agarwala, 1997).

As mentioned, a substantial portion of pension fund surpluses in these regions came from contributions made by migrant workers under the limited portability constraint of the current pension program. A director of the Guangdong Provincial Bureau of Human Resources and Social Security shared his view on the possibility of handing over the fund surpluses to the center:

“The pension fund surpluses were achieved by contributions made by employees on Guangdong’s local economic market. The money is in the end our employees’ personal properties. Government officials are father-mother officials (*fu mu guan*) to the people in the locality, so they have the responsibility to protect their lawful rights. It would be absurd if the center would rob the rich to help the poor.” (GDP0421151)

Another government official in Guangdong noted that the center would not benefit from the situation wherein Guangdong's economy stumbles due to the withdrawal of the several trillion *yuan* pension fund surpluses (GDP0422151). In fact, the center learnt a costly lesson on collecting pension fund surpluses under the same condition of information asymmetry. In 1998 the central government decided to transfer corporate pension funds run by large center-owned enterprises to provincial governments. Upon announcement of this transfer plan, corporate pension funds with surpluses "consumed" the surpluses before the transfer could be carried out (Frazier, 2004; Jiang, 1999). The current centralization reform suffers from the same principal-agent problem. This seems to mean that, to centralize pension funds, the center is likely to be left with only one option –to leave pension fund surpluses at the subnational level, yet using its own fiscal budget to fill the multi-trillion-*yuan* pension fund deficits (BJN0603132).

The center is surely aware of the risk of local governments misrepresenting vital information. It was learnt from an interview that the central government convened a reform subcommittee in 2014 to investigate an appropriate pension contribution rate if a centralized pension program were to be realized. After a careful study, the subcommittee reported that a 12 percent contribution rate from employers would be sufficient, which would be an 8 percent reduction from the currently required 20 percent of payroll contribution rate. However, the central government replied that the contribution rate would need to be set at 15 percent or higher in preparation for discounts local governments may apply (BJN1115121). The center's concern was confirmed by an interview with a government official in Guangdong. The official noted that if the centralization was achieved, a sure thing would happen, that is, like the old saying goes "the higher authorities have policies, but we will find ways to get around it" (*shang you zhengce, xia you duice*). The official also commented that the MHRSS at the central level had always been

too conservative, and it would need strong leadership to carry out rigorous reform plans (GDP0421151). The central leadership may not be as weak as the Guangdong government official expected. The question is whether the welfare development issue is important enough for the center to overhaul the decentralized fiscal arrangement and penetrate its power directly at local pension agencies to overcome these challenges.

When asked about the prospect of the centralization reform, a repeated response given by interviewees, scholars and government officials at both the provincial and central levels, was that, the centralization reform would likely only stay as a formality and the implementation of the reform would be next to impossible, at least in the near future. Unifying the pension program within each province has gone through various difficulties, and has yet been accomplished. A nationally unified and centralized pension program would be a distant reality. Then we may ask, is centralizing the pension program the end goal of the government, or is it only a means for the center to address problems existing in the current fragmented pension system? Without addressing these problems, any premature centralization of the pension program would hardly yield any meaningful and long-lasting effects.

China's center-local relations in the pension case is exemplified in this long-overdue centralization reform. The reform is more a political reform that rationalizes center-local welfare responsibilities than a pension reform. Despite the urgency of creating a reliable welfare network for the people, promoting welfare development requires long-term efforts. Unlike some social and political events that involves time sensitivity, such as violent protests and accidents with large-scale casualties, welfare development does not often require immediate government response. Therefore, the center lacks the determination to exert its full strength to tackle the pension problem and bring about systematic reform. In this center-local interaction game, sub-

national governments always have better access to local information than does the center. As a result, sub-national governments take advantage of this fragmented pension management structure and play the game strategically. When the center has a reform plan, sub-national governments often have prepared counter-plans that could protect local interests. In particular, this section shows that governments with fiscal independence from the center have more power to challenge the center's decisions, and deter positive reform plans.

6.6 Conclusion

The discussion in this chapter is set to support the argument that the central government's capacity in promoting welfare development is largely constrained by sub-national governments, especially those from economically affluent regions. The four cases above also confirm the hypothesis that regions that are fiscally independent from the center have more policy autonomy than regions that are dependent on the center's fiscal subsidies.

In all four cases, the center's reform plans are compromised by sub-national governments to varying degrees – while regions counting on the center's fiscal support show more obedience, these regions still counter play the center's command to advance local interests; regions with fiscal independence are simply the most powerful negotiators with the center. In the first case, the consolidation reform, we witnessed three center-local interaction patterns. First, regions that received substantial fiscal subsidies from the center viewed center support as leeway to keep their pension contribution rates low and to increase business competitiveness. Instead of finding ways to consolidate pension funds, these provinces sought to borrow money from the reserved pension fund for the consolidation reform, to ensure current pension benefit provisions. Second, regions that did not receive direct center fiscal transfers did not spare local fiscal resources for the consolidation reform, as promised in their contract with the center. Third, the center

requested the Guangdong government to participate in the consolidation reform from Guangdong's own pocket, given that government's healthy pension fund situation. However, as the center did not allow the Guangdong government to invest the consolidation fund in the stock market, Guangdong refused to participate the reform.

Second, it is well-known to be especially difficult to expand welfare provisions in a decentralized authoritarian administrative system. To motivate provincial governments to implement the seemingly impossible pension benefit increase policy, the center granted fiscal subsidies to certain provinces. Subnational governments that received funding support from the center competed to increase pension benefits in order to secure more fiscal funding from the center. However, regions that did not receive fiscal support from the center, unsurprisingly, set lower pension benefit increase rates than regions with center support. The central government, perhaps alarmed by the consequences of its own policy, acted to bring the rapid expansion of pension levels to an apparent end in 2016.

Third, the outcome of the center's policy on facilitating inter-regional pension transfers was also far from the center's intention. As migrant workers often engage in seasonal work and move about with job opportunities, they rarely meet the requirement of retirement benefit payments. The limited portability problem of the pension program also restricts inter-regional pension account transfers. Despite the fact that in 2009 the center issued a policy facilitating inter-regional pension transfers, economically affluent regions as migrant-receiving localities set up extra hurdles for migrant workers to transfer their pension contributions when they relocate. Thus, these migrant-receiving provinces benefit from free pension contributions these migrant workers have made, and have accumulated a large volume of pension fund surpluses. In turn, in order to boost pension participation rates, regions with labor outflows induce returnees to enroll

in the pension program in their 40s and 50s. As a result, these migrant-exporting provinces bear a responsibility to provide retirement benefits to returnees without full pension contributions. Therefore, the fragmented pension administrative structure creates winner and loser provinces and enlarges inter-regional welfare inequality.

Lastly, a pension centralization reform has long been on the center's reform agenda. However, among many other difficulties, how to incentivize sub-national governments to contribute to the national pension pool is particularly challenging. While regions that suffer from pension fund deficits welcome the centralization plan, opposition from economically affluent regions with pension fund surpluses is the key obstacle. Therefore, despite the center's repeated emphasis on pension centralization since 1991, no tentative reform plan has been revealed so far.

The development of the Chinese pension system has been only incremental since the 1997 landmark reform. The center made a few reform attempts, but none of them yielded satisfactory results. The decentralized political institutions upon which the pension system is founded has put the pension system on a pre-set development path that is hard to divert. The policymaking and fiscal powers granted to sub-national governments in the 1980s have created powerful political actors with vested interests. Subnational governments often adjust the center's orders according to local conditions. In the current decentralized system, the center relies on fiscal subsidies as a tool to regulate its subnational agents. Sub-national governments enjoying complete fiscal independence from the center have more flexibility and autonomy than governments that count on the center's fiscal support. In other words, pension reforms are in the end always political reforms. The embeddedness of the current pension system in the political system means that without overhaul the whole decentralized administrative system, any pension reforms are likely to be unsuccessful.

Appendix Table 6-1 Estimated effects of labor flows on local pension funds, 2010

	In-flow labor force				Out-flow labor force				Net gain/loss (100 million yuan)
	% of the country's total labor inflow	# of people (10,000)	Fund inflow to annual local pension revenue (%)	Amount of fund inflow (100 million yuan)	% of the country's total labor outflow	# of people (10,000)	Fund outflow to annual local pension revenue (%)	Amount of fund outflow (100 million yuan)	
Anhui	0.73	52.26	0.55	2.88	10.79	772.81	12.16	63.89	-61.01
Beijing	8.86	634.25	13.05	68.57	0.33	23.47	0.29	1.51	67.06
Chongqing	1.16	82.84	0.91	4.77	4.02	287.61	3.63	19.07	-14.3
Fujian	4.85	347.12	3.52	18.5	2.08	148.6	2.1	11.04	7.46
Gansu	0.51	36.29	0.35	1.83	1.79	127.86	1.66	8.74	-6.91
Guangdong	27.33	1956.69	25.17	132.27	1.01	72.34	0.92	4.82	127.45
Guangxi	0.96	68.94	0.69	3.63	5.06	362.12	4.65	24.45	-20.82
Guizhou	0.77	55.41	0.55	2.91	3.98	284.91	3.62	19.02	-16.11
Hainan	0.69	49.46	0.44	2.29	0.35	24.76	0.31	1.65	0.64
Hebei	1.56	111.34	1.12	5.88	4.24	303.45	5.05	26.52	-20.64
Heilongjiang	0.58	41.5	0.39	2.05	3.08	220.38	2.95	15.48	-13.43
Henan	0.67	48.14	0.47	2.45	10.01	716.35	10.08	52.97	-50.52
Hubei	1.12	80.24	0.77	4.05	7.05	504.85	6.81	35.78	-31.73
Hunan	0.82	58.53	0.56	2.97	8.78	628.36	8.11	42.64	-39.67
Jiangsu	7.47	534.46	6.79	35.67	3.76	269.02	4.77	25.06	10.61
Jiangxi	0.65	46.53	0.41	2.14	6.94	497.1	6.62	34.81	-32.67
Jilin	0.52	36.93	0.34	1.8	1.66	118.9	1.6	8.4	-6.6
Liaoning	2.16	154.6	1.7	8.94	1.24	88.76	1.29	6.78	2.16
Neimenggu	1.48	106.29	1.15	6.07	1.2	86.15	1.19	6.24	-0.17
Ningxia	0.4	28.84	0.29	1.52	0.24	16.91	0.21	1.11	0.41
Qinghai	0.38	27.56	0.33	1.72	0.28	20.18	0.24	1.27	0.45
Shaanxi	1.14	81.97	0.88	4.6	2.26	162.01	2.17	11.39	-6.79
Shandong	2.55	182.74	1.92	10.09	3.66	261.94	4.06	21.32	-11.23
Shanghai	10.96	784.73	17.64	92.73	0.3	21.64	0.27	1.42	91.31
Shanxi	0.87	62.47	0.63	3.31	1.29	92.34	1.34	7.03	-3.72
Sichuan	1.26	90.48	0.91	4.81	10.19	729.52	9.5	49.91	-45.1
Tianjin	3.88	277.94	4.42	23.25	0.34	24.47	0.35	1.84	21.41
Tibet	0.18	12.97	0.22	1.18	0.06	4.49	0.05	0.27	0.91
Xinjiang	1.84	131.66	1.29	6.79	0.37	26.57	0.36	1.9	4.89
Yunnan	1.38	98.5	0.94	4.94	1.34	96.03	1.24	6.52	-1.58
Zhejiang	12.25	877.28	11.61	61	2.31	165.26	2.43	12.77	48.23

Source: Zheng et al. (2013), pp. 129-31.

Chapter 7 Conclusion

7.1 Summarizing the findings

Welfare development is often regarded as an intrinsic property of democracy. The current literature of comparative welfare politics is overwhelmingly Western- and democracy-centric, and the conventional wisdom often simplistically depicts authoritarian rulers as exploitative and repressive. This dissertation shows that authoritarian rulers use both sticks and carrots to advance their interests. The dissertation begins by discussing the benefits redistributive programs may give to authoritarian rulers to contribute to their ultimate goal of regime survival. Among various types of authoritarian regimes, one-party regimes appear most prone to welfare redistribution to secure their support base. Old-age public pensions are particularly relevant to this purpose as they register long-term citizenship and create strong state-society bonding effects, which increase the cost of overturning the regime. However, implementing redistributive programs is highly challenging in a decentralized political structure. As the incentives of the center and subnational governments often differ, the principal-agent problem surfaces. How the central government makes sure that its subnational agents carry out its vision faithfully is a well-known challenge. This challenge looms large when it comes to dividing fiscal responsibility between the two levels of governments for carrying out an expensive public pension program that requires substantial investment over decades. This study calls scholarly attention to the role of subnational governments in welfare politics, as the current mainstream discussion is focused mainly on governments at the national level. This dissertation differentiates redistributive incentives of governments at the national and subnational levels.

This study uses the public pension program for urban enterprise employees to investigate center-local welfare politics in China. As a one-party authoritarian regime with remarkable

economic achievements and political resilience, China provides an ideal case context. According to the Chinese Constitution, the Chinese regime has a unitary political system, with “all levels of subnational governments under the unified leadership (*tongyi lingdao*) of the Chinese central government”. Ironically, after the economic reforms, China has one of the most decentralized administrative and fiscal system in the world, and subnational governments are directly in charge of policymaking and implementation of policies related to social and economic development. In theory, the advantage of a public pension program versus private ones lies mainly in its ability to pool at the national level, across subnational regions and social groups. Moreover, being a universal entitlement program, the public pension program should theoretically have a uniform redistributive design across subnational units. However, despite the Chinese central government’s repeated emphasis on creating a nationally unified public pension program, the resulting program is highly decentralized and fragmented. This dissertation is motivated to explain the considerable subnational variation in the design of the public old-age pension program for urban enterprise employees in subnational China. This research uses rarely-found data and first-hand interviews to detail varying interaction patterns between the Chinese central government and various provincial governments in the pension program.

7.1.1 Authoritarian rulers’ redistributive incentives

This dissertation argues that the repressive apparatus is both politically and economically expensive for the ruler. First, it is very expensive to create and monopolize threat-trustworthy armed forces. Moreover, possibly contrary to expectation, use of the repressive apparatus is often unrealistic and counterproductive in resolving daily unrest. Second, the repressive apparatus may act as a double-edged sword, which is intended to protect the ruler but which may be used to fight against the ruler. The more power the ruler grants to the armed forces, the greater the

danger becomes for men with guns to intervene in politics. Third, heavy reliance on repression only intensifies the dictator's dilemma, wherein the ruler becomes completely insensitive to the public sentiments, and loses the initiative for preempting any upheaval. Lastly, for rulers whose economies mainly depend on labor force participation, repressing workers simply means disruption of the supply of the most important means of production, which is in direct conflict with the ruler's self-interests, both near-term and long-term.

Redistributive programs offer a great complement to the repressive apparatus. This dissertation points out two main reasons that redistributive programs are beneficial to authoritarian rule. First, redistributive programs increase the cost to the masses of exiting the regime, and encourage obedience to the current ruler. Redistributing economic benefits to the general public helps the ruler build a reservoir of support. This effect is particularly prominent when the program involves a long-term commitment from the government with distant payoffs to the public, such as a public old-age pension program, which creates a long-time bonding effect between the regime and the people. Second, redistributive programs that aim to incentivize labor participation and improve human capital directly contribute to the prosperity and sustainability of the economy. As many authoritarian regimes anchor their legitimacy in economic performance, the adoption of a redistributive program not only increases economic productivity but also helps justify rule without free and fair elections.

Among different types of authoritarianism, one-party authoritarian regimes are more likely to employ redistribution. Two main reasons that explain one-party rulers' preference for redistribution. First, given its vulnerability to opposition from outside the political party, one-party authoritarian rulers need to establish a reward/punishment system to create a broader support base and justify regime legitimacy. Welfare programs are an important ingredient in this

state reward/punishment regime. Second, the relatively higher level of institutionalization in one-party regimes extends individual rulers' time horizons, and thus political elites in one-party regimes are more likely to invest resources for future benefit than underinstitutionalized regime types such as personalist and military regimes.

However, whatever may have been the intentions behind redistributive programs, the center simply lacks the capacity to monitor policy implementation at the local level, especially in large states. In particular, in a decentralized policymaking system, the power of subnational units increases in relation to the center. The motives of the two may diverge, and as a consequence, policy decisions of subnational rulers may not always be in accord with the center's interests, particularly when it comes to funding expensive welfare programs. How does the national government supervise subnational governments to make sure that they faithfully carry out the welfare vision it desires, yet meanwhile grant local governments certain flexibility to tailor the policies to best serve local conditions? The urban pension program in one-party authoritarian China with a decentralized administrative and fiscal structure offers an ideal case to investigate this question.

7.1.2 Different incentive structures for Chinese national and local leaders

After a series of decentralization reforms in the 1970s and 1980s, the Chinese political system transitioned from a highly-centralized one to a decentralized fiscal and administrative structure. Provincial governments became nominally self-sufficient fiscal units, and *de facto* policymakers in China. Welfare policymaking and provision fall under subnational governments' responsibility. A classic principal-agent problem arises when the center and subnational governments have interests which do not coincide (Moe, 1984).

This dissertation argues that Chinese central and local rulers have different redistributive incentives. Two factors explain their differences: 1) ruler's time horizon, and 2) availability of external funding for redistribution. First, local governments have a shorter time horizon than the center does. If a ruler has stable interests in a domain over which his power is exercised, he is likely to have more positive future expectations and thus a longer time horizon (Wintrobe, 1998). Partly due to the personnel appointment system (Landry, 2008), local rulers' time horizons are often limited. Moreover, promoting local economies is weighted heavily in officials' evaluation schemes (Tsui & Wang, 2004). Sparing resources for long-term well-being of the people is in conflict with local rulers' immediate interests. Thus, subnational rulers often have fewer incentives for redistribution than central rulers.

Second, the availability of external grants for welfare development makes a major difference. Qian and Weingast (1997) contend that both central and local governments in China face hard budget constraints. However, Tsai (2004) argues that while the center has hard budget constraints, local governments can turn to the center for fiscal assistance when needed. This study demonstrates that the center relaxes fiscal constraints in certain strategic localities to motivate subnational agents and assist development. For sub-national regions that receive center fiscal support, welfare programs become less costly, and they are thus more willing to promote welfare development that the center desires.

How the central government allocates its limited fiscal resources strategically to subnational units is a political decision. This dissertation identifies two key factors that affect authoritarian central rulers' redistributive decisions across subnational units: 1) economy-induced political sensitivity (e.g., a high unemployment rate), and 2) politics-induced political sensitivity (e.g., a geographic concentration of ethnic minorities). First, during the economic

transition period, a high unemployment rate caused by massive layoffs and early retirements challenged the legitimacy of Communist one-party rule. The sudden increase in numbers of pension benefit recipients and a simultaneous reduction of pension contributors crashed the already fragile socialist-style pension program that workers held dear. To pacify public grievances, the center channeled substantial fiscal support to localities which had suffered most from economic instability, namely those with highest unemployment rates, to facilitate economic transition and maintain stability. Second, the Chinese government had always regarded ethnic minority issues as life-or-death matters for the regime. With no exception, ethnic minority regions received much favorable support from the center for welfare development. Pension programs in ethnic minority regions have been heavily subsidized by center fiscal support. Using both qualitative and quantitative methods, this dissertation confirms the significant effects these two factors have on directing the center's redistributive incentives.

7.1.3 A typology of fiscal structures of the pension program in subnational China

As mentioned, subnational governments are motivated to promote short-term economic growth, and are more reluctant to spare resources for welfare development. This dissertation further argues that subnational governments strategically choose economic entities with lower asset mobility to impose heavier pension burden, and yet reduce welfare responsibility for investors with higher asset mobility. As studies on inter-regional competition suggest, mobility of foreign and private investment means that investors can seek the best fit to locate their businesses. To attract mobile investments, governments often grant favorable terms to private investors, including reducing contributions to mandatory social programs (Garrett & Mitchell, 2001; Revesz, 1992). In contrast, locations of SOEs are often determined by political command. Therefore, fearing capital flight, local governments choose to tax SOEs more heavily than

private enterprises. Thus, the level of economic openness in a locality shapes subnational governments' redistributive decisions.

Combining these two factors – the level of political sensitivity and the level of economic openness in a locality, this dissertation develops a typology of five different fiscal structures of local pension programs. First, start with regions receiving major fiscal support from the center due to their high political sensitivity. As mentioned, the center is likely to grant subsidies to regions with economy- or politics-induced instability. Local rulers of these two types react differently toward the center's grants. First, for regions that suffer from economy-induced political instability, economic recovery helps those regions regain political confidence. In addition, economic recovery generates more employment opportunities and a larger payroll base for pension contributions, which together contributes to the pension fund and helps alleviate the immediate pension deficit crisis. To revive the economy, these local rulers often see the center's pension subsidy as leeway to lower the contribution rate to reduce the pension burden of investors and increase economic efficiency. As a result, even with the center's fiscal support, these regions often still suffer from huge pension fund deficits.

Second, instead of promoting economic growth in general as regions with economy-induced unrest do, regions with politics-induced unrest have a well-targeted set of groups, ethnic minorities, to reach. Rulers in these regions need to make sure that economic gains are equally benefited by all groups, or that minority groups who are particularly sensitive to relative deprivation along ethnic lines get an even greater share. Thus, these governments are likely to use the fiscal transfers from the center in the form of government subsidies to the targeted group. In addition, economic development is not as urgent a task in these areas as is in other parts of the country, because the governments, both the central and local, take a cautious approach to

assimilation of these ethnic minority groups. Therefore, politics-induced politically sensitive regions receive substantial fiscal support from the center, and do not tend to discount the pension contribution rate to boost local economic growth. As a result of sufficient local pension funds, the average retirement benefit level in these regions is often much higher than the national average.

There are also two types in regions that do not have a high level of political sensitivity and thus do not enjoy much center fiscal support. First, there are regions that face pension fund deficits, where provincial governments fill the deficits by themselves. Second, some regions have sufficient pension fund surpluses, and are not in need of center fiscal transfer.

In the first category, some regions have little support from the center yet constantly struggle to run the pension program. These localities have two options to solve the funding problem: 1) use local fiscal resources, or 2) extracting more from employers. In comparison with option 1, option 2 transfers the under-funded pension problem caused by the lack of center fiscal support to local employers. Recall the previous discussion on rulers' pro-economic growth strategies – that increasing the pension burdens of employers may divert investment away in an open economy, especially when the investment is mobile in nature, mainly the case for foreign investment. Therefore, this study finds that regions that are not politically sensitive yet have more open economies often discount contribution rates to attract investment and use local fiscal resources to fill in the pension fund deficits; while in contrast, regions that are similarly politically not salient yet with a lower level of economic openness are more likely to increase contribution rates to consolidate their pension funds.

In the second category some regions have accumulated fair amounts of pension fund surpluses, due mainly to the limited portability problem of the pension system. Thanks to the

marketization economic reforms, these regions were to first in the country develop vibrant market-economy business environments. The inter-regional economic imbalance brought waves of migration into these early-developed regions. Migrant workers (via their employers on their behalf) contribute to local pension pools. However, because of their high mobility, migrant workers often relocate before they become eligible for retirement benefit payments in one locality, and inter-regional pension transfers are notoriously difficult. Migrant workers leave these localities with huge pension fund surpluses. Governments of these migrant-receiving regions thus enjoy high levels of budgetary freedom to reduce employers' pension burdens, which helps further fuel economic growth. The connection between enterprises' production efficiency and economic competitiveness creates a powerful virtuous circle that encourages investments and further attracts a cheap labor force to come, which expands inter-regional welfare and economic inequality.

In summary, this research finds that local pension policy design is a response to 1) the level of local economic openness, and 2) the availability of center fiscal subsidies. The interaction between these two factors tells us the five different stories on how local pension programs are funded, as discussed above.

In addition, this dissertation notes that China has a dynamic asymmetrical form of welfare federalism. The distribution of the center's subsidies creates uneven center-local fiscal relations across subnational units. This study shows that the Chinese central government utilizes fiscal subsidies as a leash, to lead and restrain the provinces. For regions that are fiscally dependent, the center can vary the level of subsidies to advance its own goals. When the center detects localities' improper use of subsidies, it may reduce the subsidy level or mandate a rectification. In contrast, subnational governments with complete fiscal independence from the

center have more policy autonomy. Prior studies draw a similar conclusion, that the center maintains grassroots officials' obedience through fiscal transfers (Shih, Zhang, & Liu, 2010). Rather than arriving at the sweeping conclusion either that the center still maintains a strong hand over subnational governments or that Chinese subnational governments become gatekeepers of the center's development strategies, this dissertation finds that China's center-local relations in welfare politics are highly dynamic. As reflected in the pension case, both the center and subnational governments learn from each other's policy decisions, engage in constant negotiations, seek to push the boundaries, and then adjust future expectation and policy preferences.

7.2 Research ahead

This dissertation on the public urban pension program in China opens a new research arena that deserves future investigation. Moving forward, this study suggests the following three research areas: 1) the development of the current urban pension program; 2) the application of the theories developed in this study to explain other social policies; and 3) China's center-local relations.

7.2.4 Future development of the pension program

As population aging is progressing very quickly, the debate on reforming the current fragmented urban pension program has never been more heated. The future development pathway of the pension program has been under constant debates during the five-year period of this dissertation research. However, consistent with the findings of this dissertation, these high-profile debates have yielded very limited attempts at reform thus far. Based on a realistic assessment of the overall situation, this study notes that future development of the pension program will likely follow three directions: 1) continuing to remain highly localized, 2)

strengthening the connection between pension contributions and retirement benefits, and 3) exploring investment options for pension funds.

First, the decentralized pension management structure has been institutionalized, and any reversal of this trend requires an institutional overhaul. This decentralized pension system is a heritage of the fiscal and administrative decentralization reforms. The stickiness of this institutional setup has become a such decisive factor that any efforts at reversal in the near term would face great difficulty, and thus the decentralized nature of the pension system is likely to persist. This point is well manifested in the discussion in Chapter Six. Even though the center has made several attempts to centralize the pension program, and to create a nationally unified pension program, these attempts have all in the end deemed failures. The main purpose of a centralization plan is to encourage inter-regional redistribution. However, it is certainly a difficult task to redistribute resources among 31 highly diverse subnational units. Two subnational government coalitions are formed: one includes those provinces with complete fiscal independence from the center, and the other is loosely organized by provincial governments that are challenged by pension fund deficits. In terms of relative power, provinces with fiscal independence enjoy more leverage when negotiating with the center, as compared with those dependent on the center's fiscal support. Regarding incentives for any centralization plan, these fiscally independent provinces are highly motivated to defend their rights and properties. For fiscally dependent provinces, where the fiscal subsidy comes from, whether from the provinces with pension fund surpluses or directly from the center is not their major concern. Therefore, all provincial governments lack any genuine motive to push for a centralization reform. Moreover, not only provincial governments, but also powerful policy entrepreneurs such as scholars and journalists often exploit the uncertainty of a centralization plan. The uncertainty discourages the

center from making any risky reform moves, and thus they are instead being motivated to maintain the status quo.

As a compromise step forward, as a formality the center may issue a centralization reform plan to the public, yet subnational governments will still be granted substantial powers and rights to make modifications and adjustments. The discussion of centralizing the pension program has been given some urgency lately, particularly after the ambitious reform-minded Minister of Finance, Lou Jiwei, took office in 2013. Minister Lou used the slogan “we cannot wait” (*buneng zai deng*) to seek to push forward meaningful reform plans, including pension centralization reform (Ren, 2014). However, no tentative plan had been revealed before Minister Lou stepped down as the Minister of Finance in October 2016. Based on the author’s interviews with both central and subnational governments, it is a consensus that meaningful pension centralization reforms will likely be only a distant reality.

Second, the future is likely to see a strengthening of the connection between pension contributions and post-retirement benefits. It is the conventional understanding that without complete information, policymakers often make policies on a trial-and-error fashion, with an intention to make incremental policy revisions after they receive initial policy feedback (Lindblom, 1959). However, the “art of muddling through” policymaking processes is often challenged by unexpected consequences and resistance once a policy is implemented. The three-pillar pension program design was intended to capture the advantages of both defined-benefit and defined-contribution programs. The second pillar, individual accounts, was set up to encourage contribution to the pension fund and link retirement benefit payments directly to the amounts of contributed during active employment. However, as individual accounts are emptied in practice to fund current retirees’ retirement benefits, these individual accounts become only

notional. Payments that are supposed to be from these accounts in fact come from the general pension fund. Per current regulations, the pension program participants are entitled to receive retirement benefits from their individual accounts once they reach retirement age until they pass away. Monthly retirement benefit payments from individual accounts are calculated as the amount of pension fund reserve in the individual account at the time of retirement divided by 120. The assumption of this payment formula is that on average each retiree will receive retirement benefits for ten years after retirement. However, in fact the average number of months of retirement benefit payments per participant is over 190 months (Wu, 2015).

To address the burden of individual accounts, instead of having a one-size-fits-all benefit provision formula, the government may set up a number of alternative ways of benefit provision, such as one-time withdrawal of pension reserve in the individual account at retirement, or smaller monthly payments from the accounts individual participants notionally own. In addition, extending retirement age is one important solution to the problem. Even though for countries like China with such an unusually early retirement age – 47 is the average retirement age as mentioned in Chapter 1 – raising retirement age seems to be a well-expected move. However, this issue of extending retirement age has been on the center’s policy agenda since 2004. Yet after years of discussion no official reform plan had been revealed by the time this dissertation is complete in May 2017 (Shang, 2016). The sustainability of the second pillar and the three-pillar policy design both deserve scholarly investigation. Once a policy is introduced, the policy itself becomes an institution with beneficiaries and defenders, which makes any further changes, no matter how uninterrupted or necessary, very difficult. Thus, instead of having an incremental nature of policy change, policy development in authoritarian China is more in a fashion of punctuated equilibrium (Baumgartner & Jones, 2010). Furthermore, it would be interesting to

investigate why certain social policy reforms such as extending retirement age are more difficult to realize in authoritarian China than in democracies, as multiple democratic governments have successfully raised retirement age lately (Brown, 2012). What makes authoritarian Chinese rulers hesitant to make seemingly rational policy changes?

Third, as mentioned, by far most current pension reserves at both central and subnational levels are deposited in bank savings accounts and invested in national bonds, the investment return of which has been lower than the inflation rate (BJN0402121). The center strictly enforces this highly conservative investment strategy of pension funds. This strict control is partly a result of the 1998 Shanghai pension fund scandal, in which top Shanghai government officials diverted over 3 billion *yuan* from the local pension fund to real estate investment and infrastructure development. This strict investment prohibition is obviously an overcorrection to the 1998 scandal. As the Chinese central government argues, the Chinese stock market is too volatile for individual provincial governments to invest pension funds (BJN0408151). In 2012, an agreement between the center and the Guangdong government was made. The agreement set out that 1) the Guangdong government would put 100 billion *yuan* in the National Social Security Fund (NSSF) for investment in 2012; 2) the principle and potential future investment returns belong to the Guangdong government; 3) the center would bail out any potential losses to this investment; and 4) the center pays the NSSF for any fees incurred by this investment. According to the official investment report, from 2012 to 2015 the NSSF had obtained over 31.4 billion *yuan* investment return on the 100 billion *yuan* principle for the Guangdong government (Li, Xu & Xi, 2016). Obviously, over the past four years the investment return rate has been much higher under NSSF's management than in bank savings accounts. Shandong joined Guangdong and in 2015 became the second province that has used the NSSF investment plan, and they were allowed

to put in 50 billion *yuan*. The question is if the NSSF investment plan offers a much attractive investment option, why we have not seen a widespread adoption of the NSSF investment plan across the country, not to mention a comprehensive pension fund investment reform?

This study notes that any research which investigates the NSSF investment plan will not only reveal complex center-local politics, but also horizontal political battles between bureaucracies at the national level. The creation of an independent NSSF, directly under the State Council's leadership, was a thoughtful consideration to bring an end to the long-time competition between the MOF and the MHRSS for the right to invest the center's strategic pension fund. Instead of granting the investment right to either of the two powerful ministries, the center decided to create an independent entity directly reporting to the State Council, and appointed Dai Xianglong, the former President of the People's Bank of China, as the Director of NSSF. However, as this new entity was created, a new political actor with its self-interests emerged. As learnt from the interviews, being a new agency in charge of an important mission of pension fund investment directly supervised by the State Council, the NSSF has every incentive to outperform the government's expectation. After Guangdong became the first pension fund investor, quite a few provincial governments asked to join the investment plan (Xu, 2012). Some appeared to be quite desperate, using formal and informal channels through the State Council to press the NSSF to expand the investment plan. However, as a director in the NSSF commented, "We are highly selective in investment options, so the number of good investment opportunities is very limited. As we are a public investment agency, the last thing we want is to have a humongous fund and reduce our fund performance" (BJC0612131). The formation of the NSSF may partly resolve the long-time debate of who should oversee pension fund investment, yet it itself creates an unforeseen problem that ironically retards the progression of the pension

investment reform. In November 2016, the former Minister of Finance, Lou Jiwei, was appointed as the new Director of NSSF (Pengpai News, 2016). This move signals the center's preference of the MOF's proposed market-oriented reform approach over MHRSS's more conservative plan. This high-level personnel transfer is expected to facilitate more aggressive reforms. With the pressure of population aging pressure quickly approaching, the task of exploring reliable pension fund investment options is of great urgency.

7.2.5 Explaining other social policies

This study focuses on the public urban pension program for enterprise employees in order to understand center-local welfare politics. However, the findings of this study may help explain subnational variation in policy design and program benefits of other social policies, including another major welfare program implemented in China, the public urban enterprise healthcare insurance program (*yibao*).

China's social insurance system for urban enterprise employees is composed mainly of "five insurances and one fund" (*wu xian yi jin*), namely old-age pension insurance, healthcare insurance, unemployment insurance, work-related injury insurance, maternity insurance, and the housing provident fund. The center sets specific contribution rates for these six programs to be implemented in the subnational levels. They are: 28% of payroll (20% from employers, and 8% from employees) for the public pension program; 12% (10% from employers and 2% from employees) for public healthcare insurance; 3% (2% from employers and 1% from employees) for unemployment insurance; 0.8% (from employers) for maternity insurance; 0.2 to 2% (from employers) for work-related injury insurance, with the premium rate depending on the nature of work; and a cap of 24% of payroll (employers and employees each paying a half) to the housing provident fund. Taking these six programs together, the contribution rate in total nears 45% of

payroll for employers and 23% of wages for employees, which on paper makes China among the countries with the heaviest welfare taxes (Xue, 2016). Like the pension program, even though the central government has repeatedly sought to create a nationally unified social insurance program in all six programs, the idea of national unification is far from reality (Zhang, 2016). In fact, these high contribution rates provide a direct stimulus to evasion of welfare responsibility and inspire subnational governments to make policy adjustments according to local conditions.

The center's efforts to centralize these social programs seems to be more a slogan than an actual policy attempt. In 2016, the center officially gave a green light to reducing social insurance contribution rates, which may signal the center's concession to subnational governments on the idea of creating nationally unified social insurance programs. In the 1997 landmark social insurance reforms, the center specifically required subnational governments to work toward creating a nationally unified social protection net, with an exception of allowing regions that had real difficulty in funding welfare programs to set up higher contribution rates. While reducing welfare contribution rates was never an option officially permitted by the center, as we witnessed in the pension case, it was a fairly common practice that subnational governments lowered contribution rates to reduce enterprises' welfare burden. The center issued *A Notice on the Interim Reduction of Social Insurance Contribution Rates* in April 2016, and officially granted the permission for local governments to reduce welfare contribution rates. The notice permitted reducing contribution rates in the subsequent two-year period for four programs: the urban public pension, unemployment insurance, work-related injury insurance, and maternity insurance. According to the official rhetoric, the purpose of this contribution rate reduction package was to alleviate the welfare burden of enterprises in order to increase China's

competitiveness in the manufacturing sector on the global stage (National Development and Reform Committee, 2016). Individual contribution rates were not affected.

- Employers could reduce the contribution rate to the public urban employee pension fund to 19% if the asset reserve of the local pension fund could pay full retirement benefits for at least nine months.
- Employers could reduce contribution to unemployment insurance, which varies by locality, to a range of 1% to 1.5% from the original 2%.
- Subnational governments should further implement the State Council's decision in 2015 on a 0.25% contribution rate reduction on the work-related injury insurance, and a 0.5% contribution rate reduction on the maternity insurance (MHRSS Circular No. 36, 2016).

Similarly, this contribution reduction package proposed by the center was subject to subnational governments' modifications. As this dissertation noted in the pension case, subnational governments with fiscal independence have more policy autonomy than regions that have to rely on the center's fiscal support, and with greater autonomy these governments have more flexibility to reduce welfare burdens for investors to create a more attractive business environment. Subnational governments' varying reactions to this reduction plan once again lends support to this argument, which is demonstrated in the following two aspects.

First, not every province can afford to cut contributions, and the degree of compliance with the center's proposal has varied not only by locality but also by program. A message this reduction package sends is that regions with sufficient economic resources are allowed to further reduce enterprises' welfare burden to propel Chinese economic development. One clear result of this strategy is to increase inter-social group and inter-regional economic inequality. People in need of these welfare programs are exposed to higher risk of benefit reduction in near future.

Regions that suffer from welfare fund deficits are trapped in a vicious circle of high welfare contribution rates and lower economic productivity, as this dissertation argues in the pension case. In addition, among the four social programs subject to contribution reductions, the likelihood of subnational governments reducing contributions to unemployment insurance is greater than that of the other three programs (People.cn, 2016). It is worth investigating why the rate for unemployment insurance program is more likely to be cut than those for the other social programs.

Second, even though the public healthcare program is excluded from the center's reduction plan, a few provinces have announced plans to cut the healthcare contribution. Before the reform, the average employers' healthcare insurance contribution rate in Guangzhou was 8% of payroll, 2 percent points lower than the center's request. After the reduction package was revealed, the Guangzhou government announced that in addition to reducing employers' burdens on the four social programs, the healthcare insurance contribution rate would also be reduced, from 8% to 7%. Besides Guangzhou City, Shanghai, Shandong, Chongqing, Ningbo City and Wuxi City also announced cuts to employers' public healthcare insurance contributions (Li, 2016). These cities and provinces with no exception are all regions not receiving any fiscal support from the center.

Among these six programs, the public urban enterprise pension and the healthcare programs are most extensive. The Chinese central government places health development like the public pension as a top strategic priority. Economic reforms brought the old Soviet-type socialist healthcare program into question. Increasing layoffs and the expanding non-SOE sector called for a new public health program that would cover all urban employees regardless of the nature of enterprises. In 1997, the same year the landmark pension reform was revealed, the

government introduced the same concept of combining a public fund with individual accounts for the new public health program, and mandated contributions from both employees and employers. This reform similarly granted subnational governments the power to adjust the center's reform proposal to local conditions, subject to the center's review and approval (CCP News Archive, 1991). Statistics show that the government's overall healthcare expenditure has gone up significantly since the late 1990s (Tang, 2014, p. 1). In 2015 alone the central government transferred 54.1 billion *yuan* to subnational governments for subsidizing healthcare services, an 8.8% increase over 2014's figure, and an additional 14.1 billion *yuan* on medical assistance programs, which increased by 9.2% from the prior year (MOF, 2016). Like what we observed in the pension case, the central government prioritizes its limited resources for healthcare development to old-industrial bases (MHRSS No.52, 2009), and to ethnic minority regions and less developed regions in the West (CCP News Archives, 1991).

The public urban pension and healthcare programs for enterprise employees share many similarities. First, both programs are pooled mainly at the municipal level, with the provincial government establishing a within-province fund transfer mechanism to achieve a certain level of resource pooling and redistribution. Second, each healthcare administrative unit has the flexibility to adjust the center's policies, as considerable policy variation in both premium contribution rates and benefit calculation formulas exists across subnational units (Tan, 2016). Third, because of the prior two points combined, both programs suffer from a serious limited portability problem. Different from the life-term labor allocation in the command economy, labor movement across provinces in today's China is very common. In particular, as the number of rural migrant workers finding seasonal jobs in urban areas and constantly moving across administrative border lines has increased significantly over the past decade, how to honor these

migrant worker's contributions and benefits poses a challenge to this highly decentralized welfare administrative system. In the case of the public healthcare program, statistics show that 5 percent of all public-healthcare-participant inpatients received treatments in off-site hospitals, i.e., a hospital in a location different from where the participant is enrolled in the public healthcare program. A conservative estimate is that off-site medical costs accounted for 12% of total medical expenditure at the national level in 2015 (Min, 2016). Like the limited portability problem in the pension program, the current decentralized institutional setting offers many difficult hurdles for these off-site medical expenses to get reimbursement. Hainan Province has been the pioneer in addressing this limited portability problem, and they have reached bilateral agreements with each of the other 30 provinces/cities/counties for cross-province medical expenditure reimbursement in October 2016 (Chen, 2016). However, it is a long march for these bilateral agreements to become a national level endeavor.

The public urban pension program studied in this dissertation shares many very similar features and challenges with the other social programs in China. As such, lessons learnt from the pension case can easily travel to help us better understand other social programs. Using the arguments developed in this study to explain systematic subnational variations in other social programs hold promise.

7.2.6 Chinese central-local relations – Dynamic asymmetrical federalism in practice

How the Chinese central government ensures subnational governments' compliance with its commands is of crucial theoretical and empirical importance, and has attracted scholars' continuous research interests. The public pension case studied in the dissertation has two broad implications for this topic. First, the pension case shows that neither a strong top-down almighty central government model, nor a localized federalism model could actually depict a complete

picture of Chinese center-local relations. Instead, this study describes an interactive bargaining model between the center and subnational governments. Second, in this interactive bargaining game, subnational regions with fiscal independence from the center hold more power and resources against the center than the others, which exacerbates the landscape of inter-regional economic and social inequality.

A dynamic bargaining relationship between the center and subnational governments is the new reality in China's center-local relations. First of all, in spite of the definition in the Chinese Constitution of a unitary system of government, the center's power to lead as the unitary leader in the country declined after the decentralization reforms. The decentralized administrative and fiscal structures grant province-level governments substantial political powers, and over time subnational governments have developed capability and resources to at least sit at the policy-making table with the center. What is commonly regarded as a strong central government can sometimes find it difficult to get its policies out of *Zhongnanhai*; and that is notably the case with regard to welfare policies that are often associated with substantial long-term fiscal investments by provinces.

Many scholars assert that despite the decentralization reforms, the central government still holds firm control over subnational agents, as in the *nomenklatura* system the center has the power to appoint and dismiss key subnational rulers (Edin, 2003; Landry, 2008). The center designs the cadre evaluation scheme, which should serve as a guideline for its subnational agents to follow the center's lead and go through the maze of career path. Thus, according to this argument, being constrained by this political personnel evaluation and career promotion system, subnational government officials should be incentivized to carry out compliance activities.

Indeed, the center's power over the cadre appointment does still remain one powerful tool today to regulate subnational governments. Yet here we point out three problems revealed in the pension case, of employing the center's cadre appointment power to ensure subnational governments' compliance. First, dismissing its agents and parachuting in a new replacement is rarely a wise option. The center uses its dismissal right very cautiously and thoughtfully. To the center, projecting an image of political stability and justified legitimacy to the public weighs much more heavily than punishing misconduct of subnational agents on issues such as relaxing welfare policies. Hence, unless subnational governments violate major political disciplines, the center often chooses to turn a blind eye toward those minor misconducts.

Second, whoever sits in any position is likely to be shaped by political institutions and the momentum of historic development, and is likely to make similar policy decisions. There are on the other hand many cases where new officials appointed by high-level authority did not fit in local bureaucratic culture and were shunted aside and could hardly fulfill their political ambitions. Moreover, the cadre evaluation scheme is heavily economy-oriented. Scholars find that the center has made an effort lately to add cadre evaluation items other than economic terms, such as welfare development and environment protection (Zuo, 2015); however, as economic growth is more easily quantifiable than the other evaluation items, the current government officials' career promotion system is still dominated by assessing economic performance of the locality. In other words, the momentum of local institutions has set a rough development path for the locality, regardless who is in the top position of the locality.

Third, compared with subnational governments, the center is always at a disadvantage position in collecting accurate local information. Even for the evaluation scheme, the center relies heavily on information provided locally to evaluate its subnational agents (Huai, 1991;

Zheng, 2005). As the pension case demonstrates, although the center deems welfare development to be a major “strategic priority”, it has to count on provincial governments to carry out that grand vision. Subnational governments often find ways to relax the center’s regulations and modify policy guidance given by higher-level governments to best serve their interests. The center is certainly aware that subnational governments almost always discount its policies and regulations, but they can rarely forcefully require any substantial changes. Thus, the center’s cadre management power is less effective in regulating subnational officials’ daily practices than many may have expected.

Furthermore, this dissertation finds that the center’s policy goals and incentives are shaped by subnational governments. This implication is drawn beyond the context where, as some scholars observe, the center first carries out pilot local policy experiments before diffusing an idea to the sub-national level (Florini, Lai, & Tan, 2012; Marquis, Zhang, & Zhou, 2013). This implication suggests that the center also learns from local governments’ policy practices to revise current national policies. The center has more encompassing interests, which means it may often pursue multiple mutually-conflicting short-term goals at the same time, such as promoting welfare development and concentrating economic resources on propelling immediate economic development. For example, as this dissertation reveals, the center’s emphasis on centralizing the pension program was revised publicly after more than two decades of implementation. This interactive relation is also reflected in the pension benefit increase case discussed in Chapter Six. After observing an inter-regional competition to increase retirement pension benefits from 2008 to 2014, the center put an end to the 10% annual increase policy in 2014. These cases show that while the central government has the power to construct the cadre management system to foster vertical accountability between the center and subnational governments, the center may also

need genuine policy feedback from subnational governments to revise its policy goals at the national level. Deng's policymaking philosophy — “cross the river by feeling the stones underneath”— seems to describe this policy revision process quite accurately. This study suggests a reciprocal center-local interaction pattern, rather than a simple top-down centralized management style.

Moreover, though the cadre management system may be described as the center's “trump card” guiding its subnational agents' fundamental behaviors (Huang, 1999), this study notes that compared with the cadre management system, fiscal subsidies to subnational government offer a more effective and timely control of subnational officials' daily practices in grant-receiving regions. This dissertation shows that the center utilizes special fiscal subsidy programs to subnational governments to facilitate their compliance, and especially to counter their understandable disinclination to develop welfare programs. An uneven relationship between the center and subnational governments across subnational regions has emerged. Various cases in the public pension case discussed in this dissertation reveal the same finding, that is, the Chinese central government utilizes fiscal subsidies as a leash to lead and restrain the provinces, as a goodie bag to reward and punish subnational governments. As a result, subnational governments' reactions toward the center are divided into two categories – regions that do not receive any fiscal support from the center act more like independent policymakers, boldly signaling a much higher level of resistance to the center's reform agenda, and in some cases even introducing policies that counter the center's directives; regions that must count on the center's fiscal support, regardless the level of support from the center, act more cautiously and seek to cover any deviations from the center's commands. Instead of an overall erosion of the center's control over subnational governments about which some scholars worry (Bernstein & Lü, 2000; Goldstein,

1995; Tsai, 2004; S. Wang, 1995b), we observe the center's selective control over politically important regions.

A direct result of this unequal center-local power relations across subnational regions is growing inter-regional economic, welfare and political inequalities, and a highly challenging scenario for the center to coordinate subnational behaviors. Although a standard goal of welfare policy may be expected to be to promote a more equitable distribution of wealth to correct market failure, this dissertation shows that the Chinese retirement pension program in fact enlarges welfare inequality across sub-national regions. The high level of subsidies granted by the center substantially reduces or even wholly offsets the costs of welfare programs in some regions. With the option to externalize the costs of developing welfare programs, subsidy-receiving regions were able to promote welfare development than regions without center fiscal support. A direct result of this inter-regional welfare inequality is inter-social group inequality. While residents in subsidy-receiving regions are much better protected by these welfare programs, people in fiscally independent regions are exposed to larger degrees to market risk. (Lin, 2015; Lin & Tussing, 2016). As subnational governments continue to intervene in economic production, this political and welfare inequality surely translates to increasing inter-regional economic inequality.

A related question is the effects of China's center-local relations on boosting economic growth. Is empowering subnational governments to pursue economic reforms beneficial to the economy in the long run? Scholars argue that one key factor that differentiates the failures of Eastern European countries' transitions and the Chinese economic miracle is that the Chinese central government successfully mobilized incentives of subnational governments to facilitate the transition process by empowering them in the political sphere (Cao et al., 1997; Shirk, 1993).

More than three decades have passed since those Chinese market economic reforms. We are still in the process of evaluating this decentralization reform, based not only on economic achievements but also from the perspectives of political development and other social issues. Indeed, this devolution of power to subnational governments in China was an important institutional innovation to push through market economic reforms in a country theretofore subscribing to a socialist ideology. Subnational governments played an indispensable role in stimulating a continuous inter-regional competition of economic growth. However, empowering is much easier done than taking back the power. As Deng's slogan for the economic transition goes, "We should allow some people and regions to get rich first, the rest would be brought along, and we would achieve common prosperity". Inter-regional inequality may only be the interim phase. The real challenge of this development strategy is the latter phase, to narrow the inequality and achieve a harmonious society at the national level. Clearly, inter-regional inequality is a result of incomplete reforms; however, regions and people that benefit from these half-cooked reforms become highly motivated political actors to block further reform attempts and to defend the status quo. A market economy can achieve its highest efficiency if factors of production can move freely without barriers, such as in a unitary labor market, and economic units can compete equally under the same set of regulations. Coordination among subnational units to achieve this economic development goal is necessary. However, this study finds that the current fragmentation of the administrative and fiscal structures at the subnational level substantially curtails labor mobility, and greatly increases transaction costs, which impedes the great potential of China's large internal market.

As the Chinese economy and society have entered a difficult bottleneck development period, characterized by a slower economic growth rate at the middle-income level and a rapidly

aging population, any reform attempts at the national level without rationalizing this imbalance center-local relation would likely be short-lived. We also observed conflicting reform attempts from the center. On the one hand, we have seen the center seeking to centralize power and rights granted to subnational governments during the reform period to concentrate national resources in the face of these grand challenges ahead; on the other hand, we also find the center to be willing to relinquish some control to certain regional governments to slow down the economic downturn and possibly re-boost growth. It will be interesting to observe the progression of center-local relations amid current economic uncertainties.

Appendix 1. Interviewee List

The interviewee code is organized as follows. The two letters indicate the provinces in which the interview was conducted. The third letter indicates whether the interviewee is from the central level (with a letter “C”), provincial level (using letter “P”), or not applicable (using letter “N”) for scholars and journalists. The first six digits after the letters indicate the month, date, and year of the interview. This is followed by a digit indicating the order the individual interviewed on that day. To make interview subjects unidentifiable, I only identify the interviewees’ work institutions, without specifying their titles and departments. The table below identifies the interview subjects by level (where relevant) and type of workplace institution.

Code	Locality	Level	Institution
BJN0402121	Beijing	Scholar	Chinese Academy of Social Sciences
BJN0531121	Beijing	Scholar	Renmin University of China
BJN0715121	Beijing	Scholar	Chinese Academy of Social Sciences
BJN0828121	Beijing	Scholar	Chinese Academy of Social Sciences
BJN1115121	Beijing	Scholar	Renmin University of China
BJN0603131	Beijing	Scholar	Renmin University of China
BJN0603132	Beijing	Scholar	Renmin University of China
BJN0603133	Beijing	Scholar	Asian Development Bank
BJN0604131	Beijing	Journalist	China Business News
BJC0612131	Beijing	Central	National Social Security Fund
BJC0614131	Beijing	Central	Ministry of Human Resources and Social Security
BJC0614132	Beijing	Central	All-China Federation of Trade Unions
BJN0615131	Beijing	Scholar	Tsinghua University
BJN0619141	Beijing	Scholar	Chinese Academy of Social Sciences
BJN0403151	Beijing	Journalist	China Business News
BJN0408151	Beijing	Central	Ministry of Human Resources and Social Security
BJC0413151	Beijing	Central	Ministry of Human Resources and Social Security
BJN0413152	Beijing	Scholar	Renmin University of China
BJN0415151	Beijing	Scholar	World Bank
FJP0626131	Fujian	Provincial	Bureau of Human Resources and Social Security

FJN0630131	Fujian	Scholar	Xiamen University
GDP0421151	Guangdong	Provincial	Bureau of Human Resources and Social Security
GDP0421152	Guangdong	Provincial	Bureau of Human Resources and Social Security
GDP0422151	Guangdong	Provincial	Bureau of Human Resources and Social Security
GDN0423151	Guangdong	Scholar	Zhongshan University
GSP0409151	Gansu	Provincial	Bureau of Finance
GSP0409152	Gansu	Provincial	Bureau of Finance
GSP0410151	Gansu	Provincial	Bureau of Human Resources and Social Security
GSP0410152	Gansu	Provincial	Bureau of Human Resources and Social Security
GSP0410153	Gansu	Provincial	Bureau of Human Resources and Social Security
HBN0704131	Hubei	Scholar	Central China University of Science and Technology
HBP0705131	Hubei	Provincial	Bureau of Human Resources and Social Security
HBP0705132	Hubei	Provincial	Bureau of Human Resources and Social Security
HBP0705133	Hubei	Provincial	Bureau of Human Resources and Social Security
HBP0706131	Hubei	Provincial	Bureau of Human Resources and Social Security
HBP0708131	Hubei	Provincial	Bureau of Human Resources and Social Security

HBP0708132	Hubei	Provincial	Bureau of Finance
HBP0709131	Hubei	Provincial	Bureau of Finance
HBN0710131	Hubei	Scholar	Wuhan University
HNP0717131	Hunan	Provincial	Bureau of Human Resources and Social Security
HNP0717132	Hunan	Provincial	Bureau of Human Resources and Social Security
HNP0724131	Hunan	Provincial	Bureau of Human Resources and Social Security
HNP0724132	Hunan	Provincial	Bureau of Finance
HNP0725131	Hunan	Provincial	Bureau of Finance
LNP1211131	Liaoning	Provincial	Bureau of Human Resources and Social Security
LNP1211132	Liaoning	Provincial	Bureau of Finance
LNP1212131	Liaoning	Provincial	Social Security Administration
LNP1213131	Liaoning	Provincial	Bureau of Finance

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EDUCATION

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B.A. 2009, Renmin University of China, Beijing, China

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VISITING SCHOLARSHIP

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Advisor: Professor Xiaojin Zhang

PUBLICATIONS

1. **Lin, Jing**, and Dale A. Tussing (2016), “Inter-regional competition in retirement benefit growth – The role of sub-national government in authoritarian China”, *The Journal of Contemporary China*, November (8): 1-18.
2. **Lin, Jing** (2015) “Labor Mobility without Pension Portability: Migrant Workers’ Endangered Pension Entitlement in China,” *Asian Social Welfare and Policy Review* 9: 269–81.
3. **Lin, Jing**, and Jeffery M. Stonecash (2012) “Incumbent and Party Vulnerabilities in the House of Representatives,” *The Forum*, Vol. 10, Issue 3, Article 3.
4. **Lin, Jing** (2011) “State’s Role in Welfare Programs under Globalization” [全球化与国家社会保障职能的变动], *Teaching and Research* [教学与研究], Vol. 11, pp. 14-22 (in Chinese).

5. **Lin, Jing**, and Ye Tian (2010) “Labor Laws and Chinese Enterprises’ ‘Going out’ Strategy under International Labor Standards” [国际劳工标准下的各国劳动立法与中国企业“走出去”] *Oversea Investment and Export Credit* [海外投资与出口信贷], Vol.2, pp. 19-22 (in Chinese, by invitation).
6. Tian, Ye, and **Jing Lin** (2009) “International Labor Standards and Labor Governance in China” [国际劳工标准与中国劳动治理], *World Economics and Politics* [世界经济与政治] Vol.5, pp.1-16 (in Chinese).
7. Cao, Qi, **Jing Lin**, Lizhi Liu, Xue Wang, and Yang Yang (2008) “New Thoughts on the Mainland Policy towards Taiwan: A Statistical Analysis on the Articles about Taiwan in People’s Daily” [政治传播学视角下的大陆对台政策新探], *Hebei Academic Journal* [河北学报], Vol. 28, pp. 1-4 (in Chinese).
8. **Lin, Jing** (2008), “The Immigration Culture of Southern Fujian” [闽南移民文化] In *Conference Collection of Southern Fujian Cultural Forum*, edited by South Fujian Cultural Association and Xiamen Intangible Cultural Heritage, China Culture and History Press, pp. 274-278 (in Chinese).

WORKING PAPERS

1. “Authoritarian resilience and public perception of economic inequality – Findings from panel surveys in China” (with Tianguang Meng, in preparation for submission to a peer review journal)
2. “Advance with the time: The evolution of the Chinese government’s ideology of welfare”
3. "Internalizing International Institutions: The Politics of China’s Embrace of International Labor Standards" (with Ye Tian and Junyan Jiang).
4. “Authoritarian Rulers’ Redistributive Incentives – A Theoretical Discussion” (by invitation, in preparation for submission to *Tsinghua Review of Political Economy*) (in Chinese)
5. “Who stole civil servants’ prestigious pensions? – The end of occupation-based urban pension system”.

RECENT AWARDS AND HONORS

- EITM Scholarship, The Empirical Implications of Theoretical Models (EITM) Institute, 2016
- Dean’s Summer Fellowship, Maxwell School, 2015
- Travel Grant for the Annual Conference, American Political Science Association, 2013
- Summer Research Grant, Moynihan Institute, Maxwell School, 2013
- Roscoe-Martin Award for Dissertation Research, Maxwell School, 2012, 2013
- Global Young Leaders Academy Leadership Scholarship, Global Young Leaders Academy, 2012
- Teaching Assistant Scholarship, Syracuse University, 2009 - 2012
- Teaching Associate, Syracuse University, 2011
- Dean’s Summer Research Project Assistantship Award, Maxwell School, 2010
- Outstanding Thesis Award, Renmin University of China, 2009
- 3rd Place in National Undergrad Innovative Competition, Ministry of Education of China, 2009
- The Highest Prize in Originality Cup Contest of Social Sciences, Renmin University, 2008

INVITED TALKS

1. “Funding the Elderly – The Fiscal Structure of the Chinese Urban Pension Program”, Asian Study Group, Purdue University, April 29, 2015.

2. “Who Pays for China’s Pension Programs – Local Fiscal Structure of the Chinese Urban Pension Program for Enterprise Employees” [谁为中国养老? ——地方城镇企业职工养老保险的财政收入结构], Department of Political Science, Tsinghua University, Beijing, China, April 15, 2015.
3. “China’s Fragmented Urban Pension System”, East Asia Program, Moynihan Research Center, Syracuse, NY, September 20, 2013.
4. “A Long March to Fund the Elderly” [何以养老], School of Labor and Human Resources, Renmin University, Beijing, China, May 31, 2013.

TEACHING EXPERIENCE

Purdue University

POL141 Politics of the World	Fall 2016
POL141 Politics of the World (distant learning)	Summer 2016

Syracuse University

Environmental Policy and Politics (co-lecture, and review section)	Spring 2013
Comparative Politics and Governments (co-lecture, and discussion section)	Fall 2012
Environmental Policy and Politics (co-lecture, and review section)	Spring 2012
Political Theory (teaching assistant)	Fall 2011
Politics of Citizenship (teaching assistant)	Spring 2011
Comparative Politics and Governments (discussion section)	Fall 2010
Oil, Water, and War (teaching assistant)	Spring 2010
Comparative Politics in Developing Countries (teaching assistant)	Fall 2009

CONFERENCE PRESENTATIONS

1. Lin, Jing, and Tianguang Meng, “Authoritarian resilience and public perception of economic inequality – Findings from panel surveys in China”, 2016 Midwest Political Science Association Annual Conference, Chicago, IL, 4/2016.
2. Lin, Jing, and Dale Tussing, “Inter-regional Competition in Retirement Benefit Growth – The Role of Sub-national Government in Authoritarian China”, 2015 American Political Science Association (APSA) Annual Conference, San Francisco, CA, 9/2015, organizer and presenter of the panel on Chinese Welfare Politics.
3. Lin, Jing, “Funding the Elderly: Explaining Variations in Pension Contribution Rates in Sub-National China,” 2013 APSA Annual Conference, Chicago, Illinois, 8/2013, organizer and presenter of the panel on Welfare in Transitional Economies.
4. Estévez-Abe, Margarita, and Jing Lin, “The Real Varieties of Welfare Capitalism in East Asia: Continuities and Discontinuities”, Society for the Advancement of Socio-Economics 25th Annual Meeting, Milan, Italy, June, 2013.
5. Lin, Jing, “Funding the Elderly: Explaining Variations in Pension Contribution Rates in Sub-National China” 2013 New York State Political Science Association (NYSPSA) Annual Conference, Syracuse, NY, 4/2013, paper presenter.

6. Lin, Jing, "Varieties of Transitions: Pension Policies in Transitional Authoritarian Regimes," 2012 APSA Annual Conference, New Orleans, Louisiana, 9/2012, organizer and presenter of the panel on Welfare in Transitional Economies. (Conference was cancelled)
7. Lin, Jing, "Political Coalition and Pension Reform: A Case Study on the Chinese Pension Privatization," 2011 New York Conference on Asian Studies, Buffalo, NY, 9/2011, paper presenter.
8. Lin, Jing, "Changing Pension Policies in a Changing Society," 2011 APSA Annual Conference, Seattle, WA, 9/2011, organizer and presenter of the panel on China's New Welfare Politics.
9. Lin, Jing, "Privatization in a Socialist Regime: The Resilience of Chinese Communist Party in the Pension Privatization Reform," The 2011 Overseas Young Chinese Forum's Annual Conference, Canton, NY, 5/2011, paper presenter.
10. Lin, Jing, "Changing Pension Policies in a Changing Society: The Case of China," 2011 NYSPSA Annual Conference, Lewiston, NY, 4/2011, paper presenter.

PROFESSIONAL SERVICES

- *Invited Panel Chair*, "Political Economy of Authoritarian Welfare States", 2015 APSA Annual Conference, San Francisco, CA, 9/2015.
- *Graduate student representative*, Meredith Teaching Award, Syracuse University, 2013.
- *Graduate student representative*, East Asian Senior Faculty Search, Maxwell School, 2013.
- *Student Assistant*, Maxwell-China Executive Education Program, Maxwell School, 2010-2013.
- *Coordinator*, Chinese Book Collection at Bird Library, Syracuse University, 2011-2013.
- *Vice President*, Chinese Scholars and Students Association, Syracuse University, 08/2011 – 05/2012.
- *Discussant*, "Federal Education Policy and the Politics of Assessment and Accountability" (Sean Miskell), Political Science Research Workshop, SU Political Science Department, April 1, 2011.
- *President*, Model United Nation Club, Renmin University of China, 2007-2008

PROFESSIONAL MEMBERSHIPS

American Political Science Association
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 Midwest Political Science Association

LANGUAGE SKILLS AND ABILITIES

Mandarin Chinese, and Taiwanese (Hokkien) (native speaker)
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