

Property Rights and Economic
Reform in China

EDITED BY JEAN C. OI

and

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Contents

<i>Contributors</i>	xiii
1. Property Rights in the Chinese Economy: Contours of the Process of Change ANDREW G. WALDER AND JEAN C. OI	1
<i>Part One. Enterprise Ownership in Village Communities</i>	
2. Collective Enterprise and Property Rights in a Sichuan Village: The Rise and Decline of Managerial Corporatism GREGORY A. RUF	27
3. Local Institutions and the Transformation of Property Rights in Southern Fujian CHIH-JOU JAY CHEN	49
4. The Role of Local Government in Creating Property Rights: A Comparison of Two Townships in Northwest Yunnan XIAOLIN GUO	71
5. The Evolution of Property Rights in Village Enterprises: The Case of Wuxi County JAMES KAI-SING KUNG	95
<i>Part Two. Rural Shareholding Reforms and Their Impact</i>	
6. Shareholding Cooperatives: A Property Rights Analysis EDUARD B. VERMEER	123
7. Local Elites as Officials and Owners: Shareholding and Property Rights in Daqiuzhuang NAN LIN AND CHIH-JOU JAY CHEN	145

x Contents

8. The Regional Evolution of Ownership Forms: Shareholding Cooperatives and Rural Industry in Shanghai and Wenzhou SUSAN H. WHITING	171
<i>Part Three. The Transformation of Public Property in the Urban Economy</i>	
9. Backyard Profit Centers: The Private Assets of Public Agencies YI-MIN LIN AND ZHANXIN ZHANG	203
10. Bargained Property Rights: The Case of China's High-Technology Sector CORINNA-BARBARA FRANCIS	226
11. Producing Property Rights: Strategies, Networks, and Efficiency in Urban China's Nonstate Firms DAVID L. WANK	248
<i>Notes</i>	275
<i>Index</i>	339

claims in return for political and tax advantages, which make its property rights structure more, not less, complex and fuzzy.

5. The SHCS gives formal recognition to the claims of various stakeholders in collective enterprises, whose conversion to SHCs reduced some of the "vagueness" of collective property by establishing the value of the enterprise and converting various stakeholders into a definite number of shareholders with rights that are summed up in the company charter. The SHC legitimized or checked "gray privatization" by assessing the claims of contracting managers and employees and giving them recognition in the form of a definite number of shares and entitlement to dividends. The charters of SHC enterprises in which these rights were recognized had to pass formal political approval and constitute the legal basis for the solution of future disputes.

6. So far, the partial privatization under the SHCS has met with little opposition, either from investors (because collectives sold their most profitable enterprises first) or from the collective community (because political procedures were observed, and the community has little independent voice). However, as noted, at the time of conversion, inadequate and incomplete assessment of asset value and earning capacity was quite common. Usually, employee shareholders profited at the expense of the collective and received high dividends. Contracting managers profited most when they obtained large and legally protected shares. Because most enterprises did well, all parties seemed to be content with their share, but if the economic situation deteriorates, conflicts over ownership, share value, and entitlement to residual income will become more likely. In the light of current expectations, employee shareholders may refuse to accept a cancellation of guaranteed returns, let alone loss of share value.

One might argue that particularly in small-scale enterprises, and in periods of enterprise expansion, a certain degree of fuzziness of property rights is functional. Owners, managers, and employees are motivated by (not necessarily realistic) high expectations about their future share in earnings, and discouraged by a strict and limitative definition of their ownership or control rights. While this may be true, it is unlikely that the incentive of high expectations could be maintained in large companies and over a longer period, or in times of adversity.

Whether the SHCS will ever realize its pretense of cooperative management by employee shareholders is highly doubtful. Rather, the SHCS has been moving in the direction established by the Company Law. Its strength lies to some extent in its lack of legal clarity, which makes it useful to the Communist Party, government, managers and employees, and other stakeholders with widely divergent views in a period of economic boom and creeping transition from collective to private ownership.

Chapter 7

Local Elites as Officials and Owners: Shareholding and Property Rights in Daqiuzhuang

NAN LIN AND CHIH-JOU JAY CHEN

Rural China has been undergoing enormous institutional changes in the past two decades. Beginning with the self-responsibility system in the agricultural sector, and then extending to the nonagricultural sector, many innovative forms of organization have appeared, ranging from family and private businesses to joint-household enterprises, collective enterprises, and joint ventures involving foreign investments. A more recent form is the shareholding system (*gufen zhi*) or shareholding cooperative system (*gufen hezuozhi*). But the guidelines as to what the shareholding systems entail and how they should be run are limited. As we shall see, this vagueness and fuzziness are partly owing to multiple policy agendas. Some shareholding systems are intended to allow state enterprises to pool resources and capital, including foreign investments, and to become self-sufficient. Other systems aim to encourage households to form cooperatives instead of individual and family enterprises. Yet there is no guideline as to which existing enterprises are entitled to form a specific type of shareholding company. Given these encouraging and yet confusing guidelines and messages, many types of shareholding companies have emerged. Enormous variations can be found in (1) the existing enterprises (state, collective, households, individuals) or newly created enterprises that become shareholding companies, (2) the labels used, (3) the definition and distribution of shares, (4) the distribution of the residual income, and (5) the rights to transfer or dispose of the shares. Within the structural and policy constraints, different actors interpret these vague policies to construct rules and institutions in the creation of various shareholding companies that serve their particular interests. The

critical issue, then, is which actors take advantage of such opportunities and what motivates their actions.

We argue that *shareholding systems in areas of rural China represent deliberate action on the part of local families or local elites to transfer property rights away from the state and local governments into their own hands*. The success of a particular shareholding system is, therefore, to a large extent, contingent on its usefulness to the actors involved and on the lack of clarification and enforcement of rules by the central government. So long as the state does not provide clear guidelines and shows little enthusiasm in enforcing property rights, this transfer of collective rights into private hands will continue.

This chapter begins with a description of the fuzziness and uncertainties in various state policies and classifications of shareholding systems, which enable some collective and private (family or household) enterprises to join forces as shareholding companies while holding on to their property rights in those enterprises. The focus then shifts to the case of Daquzhuang in Tianjin, where the local elite are turning collective firms into shareholding enterprises and transferring the property rights of the enterprises into their own hands. Such subversion of the property rights has enormous ramifications because of the huge number and assets of collective enterprises in rural China. In 1994, rural collective (village and town) enterprises accounted for 31 percent of national industrial output and 70 percent of rural industrial output. Furthermore, 79 percent of the nonagricultural labor force in rural China was employed by collective (village and town) enterprises.¹ Transfer of the property rights of collective enterprises, if carried out extensively, would have significant ramifications for the socialist nature of the rural economy in China.

Shareholding in Rural China: Policies and Practices

Official Chinese documents specify three dominant types of shareholding system: (1) shareholding cooperatives (*gufen hezuo*), (2) limited liability companies (*youxian gongsi*), and (3) joint-stock limited companies (*youxian gufen gongsi*).

The term "shareholding cooperatives" (*gufen shi hezuo*) first appeared in Central Committee document #1 of 1985, which stated:

Some cooperative economies choose the method of shareholding management and dividend-sharing. Shares are obtained by way of investment of assets. They can also be obtained through assessment of productive materials and labor in the basic construction of the enterprise. Part of the profit can be paid out as dividends on shares. This method of management does

not change the entitlement of the property and avoids the fault of equating cooperative economy with the merging of properties and distribution of shares according to labor. Yet it merges various elements of production and more speedily establishes a new economic scale and accumulates shared assets.²

In other words, the state sees shareholding cooperatives as a way of allowing participating parties to invest and share profits, while allowing the state (or the "public") to hold on to the basic rights to the enterprise; namely, the rights of alienation and appropriation. The document provided general guidelines, with no specifications as to how this system could or should be implemented.

Further variations of shareholding emerged when the Company Law was approved and issued by the Standing Committee of the People's Congress on December 29, 1993, and enacted on July 1, 1994. The law identifies two types of corporations: the limited liability company and the joint-stock limited company.³ A limited liability company involves no more than 50 shareholders, limited assets (a minimum of Y500,000 for manufacturing or wholesaling firms and Y300,000 for retail firms), and restricted transfers of stocks. A joint-stock limited company issues shares of equal value to an unspecified minimum number of holders, may recruit holders publicly, has more flexibility in share transfers, and has a total share issue of no less than Y10,000,000. The shareholders may be exclusively the founding members of the corporation or include other publicly recruited holders.

Unlike the earlier regulation regarding shareholding cooperatives, which was intended to promote development of the communal form of economic organization, the limited liability company and the joint-stock limited company seem to encourage reconstitution of state-owned enterprises. The law specifically states that state-owned enterprises may become limited liability companies or joint-stock limited companies. However, the details of these transformations are unclear. It is stated that "the implementation procedures and specific measures for restructuring state-owned enterprises as companies shall be formulated separately by the State Council."⁴ Moreover, "where a state-owned enterprise is restructured as a joint-stock limited company, it shall be strictly prohibited to convert the state-owned assets into shares at a depressed price or to sell off them at a depressed price, or to distribute them to individuals without charge."⁵ Further, there is no information regarding how a collective (e.g., the town and village collective) might be reconstituted as a limited liability company or a joint stock company. The new forms of company thus open up the possibility of turning a collective enterprise into a stock company, but offer few guidelines as to how this should be accomplished.

As a result of the vagueness of regulations and the liberal interpretations of the documents, the actual use of a particular label, whether "shareholding cooperative," "limited liability company," or "joint-stock limited company," may bear little resemblance to its original intent. Systematic data on diverse types of shareholding enterprises are not available, but we have found four types in our fieldwork in Tianjin, Shanghai, and southern Fujian: (1) private enterprises disguised as collective enterprises (called "wearing a red cap"); (2) collective enterprises that have turned themselves into shareholding cooperatives so as to sell "social" shares to individuals; (3) shareholding companies formed by several collective enterprises, which hold shares in them; and (4) collectives labeled as shareholding companies.⁶

The first three types of shareholding enterprise represent no transformation of property rights. Shareholding is used here as a means to combine or absorb additional capital or to gain the advantages of being in the "public" sector. The original owners, whether local governments, collectives, families, or households, retain full control over the companies' assets and management, despite their nominal identification as shareholding companies. Only the fourth type shows signs of transforming property rights.

Converting Local Collectives into Shareholding Enterprises

When a collective enterprise transforms itself into a shareholding company, shares are only distributed within the enterprise. Control over assets, management, and residual income is nominally transferred to the shareholders. But because the enterprise itself retains the majority of shares, control of assets and management presumably remains in the hands of the collective, which thus retains property rights to the enterprise. The only new feature seems to be that the workers, as shareholders, are now entitled to shares of the surplus income and have greater incentives to work harder for the enterprise.

On the surface, this type of shareholding system seems similar to the first three types of shareholding. There is no actual transfer of property rights, in that the original owners (whether individuals, families, collectives, or some combination) retain control of the enterprise's resources. The key question, however, is whether the collective retains its control of the enterprise's assets and management. We argue that because of the fuzziness of the rules regarding how a collective can be turned into a share-

holding enterprise, subversion of the ownership is beginning to take place in many collectives turned into shareholding enterprises. The actual control of assets and management is being transferred from the village that used to own the collective to the shareholding enterprise. The subtle aspect of this transfer is that there may not be any change in the leadership of the collective or the shareholding enterprise. The same actors who served as principal managers and Party representatives in the collective remain as chief executives and Party representatives in the shareholding enterprise. But, instead of acting as agents for the village, entrusted with the task of managing the collective, these leaders now act as members of the board of directors and chief executives on behalf of the shareholding enterprise. The village no longer commands the assets or management of the enterprise. The leaders now take action on behalf of and in the interest of the enterprise, rather than the village. The village government is now a regulatory agency relative to the enterprise, rather than the next level in the chain of command.

However, in most cases, these same leaders retain some political and social functions on behalf of the village. They remain as Party secretaries of the enterprises, and often as Party secretaries of neighborhood committees. In these capacities, the leaders remain agents of the village government. This dual role enables them to avoid criticism for turning the enterprise over to private hands and at the same time permits them to ease control of the assets of the enterprise from the public sector (the local government) into their own hands.

We hasten to add that such transformations are only one particular form of privatization, in which the enterprise is rooted in a community (cannot be relocated) and is in the hands of a few powerful members of the local elite, who also retain their nominal leadership in the Party apparatus in the enterprise. There is also evidence that the political power (state control through cadres) initially embedded in the enterprise gives way to economic and social power (local families) as reflected in the succession of the leadership in these enterprises.

Nor is this a sudden or "big bang" phenomenon. Typically, the process evolves over time, involving two stages: (1) local cadres gain control of the local economy and create enterprises that combine the features of collectives (with clear village ownership) and a market orientation (self-management and distribution of surplus value), with themselves or family members installed in the management, and (2) local enterprises are turned, by local cadres turned entrepreneurs and their family members, into shareholding companies, where they themselves obtain the majority of shares by both representing the collective shares and claiming a large

portion of the shares given to the managers for their "contributions" to the enterprise. A third stage, still evolving, is a plan to accumulate sufficient noncollective capital for the shareholders in the enterprise to "buy back" the collective shares. When and if this third stage is completed, which may take years, ownership of the enterprise will have been transferred from the public sector to the private sector with the tacit consent of the state. These transformations reflect a process of interaction between what the local elite recognize and interpret as allowable by state guidelines and what rational actions they can take to acquire the property rights themselves. This process of property rights transformation is illustrated below by the case of Daqiuizhuang, regarded by some as the richest village in China until recently, when it was "promoted" to town (*zhen*) status.

Our data for Daqiuizhuang come from various sources: local informants, a participant observer, and extensive local and informal documents.⁷ The senior author has visited the community numerous times (at least once a year) since 1988, most recently in the spring of 1996. During these trips, he conducted interviews with local leaders (including the village Party secretaries and heads), enterprise executives (including several directors and deputy directors of the boards and the CEOs), key actors (including Liu Wanmin, the steel worker who helped start the first plant), and workers (both local and hired hands from outside). Journals were kept for all interviews and voice-recordings were made whenever it was allowed. A key external informant was a researcher from the Tianjin Academy of Social Sciences who spent two years stationed at Daqiuizhuang conducting intensive research on the organization of and changes in the village, as well as serving as an advisor to the local leaders. He accompanied the senior author on most of his trips as well. Many figures are derived from actual documents from the village, estimates calculated by the Tianjin Academy of Social Sciences, and reports in the media. Inconsistencies were found in different documents. Most of the inconsistencies, we felt, were owing to the lack of sophistication and imprecision of calculations in the accounting system in earlier years, and the habit of using rounded numbers, rather than to deliberate falsification. In such cases, we use the figures reported in the most recent documents and estimates repeated in different documents. Errors are inevitable and the figures should be seen as illustrations of general trends rather than precise estimations. Other information (e.g., the number of hired laborers—the outside workers—and their working conditions; the actual benefits received by the top managers and relationships among them) is not documented and had to be obtained from informants who had proven generally reliable. At best, these estimates provide only the general picture and trends. In all cases, we have striven to report only reliable information.

Local Market Socialism in Daqiuizhuang

Daqiuizhuang, about 50 kilometers southeast of Tianjin, with a population about 3,886 (in 1989), became the richest village in China by the mid 1980s under the dictatorial leadership of Yu Zuomin, its Party secretary and corporate boss. In 1988, the village produced output valued at Y403 million, equivalent then to about U.S.\$100 million, resulting in a net income, after tax and deduction of costs for administration, school, materials, and depreciation, of Y18 million.⁸ Total assets stood at Y90 million. Average household savings were about Y7,500 annually, and total household savings exceeded Y2.5 million in 1988. In 1990, the per capita income of Y3,400 was ten times China's national average. By 1991, this had risen to Y8,400. Estimates of gross output value and net income were Y450 million and Y25 million respectively.

The achievements were astonishing for such a small village and for such a short period of time.⁹ Rumors that it had been a designated model village, like Dazhai, in which heavy state and local investments were made for the sake of show-and-tell, are false. Since details of Daqiuizhuang's rise and development are available elsewhere,¹⁰ it will suffice to briefly recapitulate here.

It all started in 1968, when Daqiuizhuang faced starvation. Yu, the village's Party secretary, was in a desperate situation; his position was vulnerable. Through a retired villager's connection, Yu found out that Tianjin City needed bricks for construction. So he started a brickyard, with a hand-built oven and local clay, producing more than 3,000 bricks a week. In 1969, a construction team in Tianjin needed bricks worth Y30,000, and again, through connections, Yu made a deal with the team, whereby it lent him Y6,000 to buy a second-hand ventilation machine. As a result, production increased to several thousand bricks a day. While the brick-making business made some money, the real breakthrough came in 1977, when a local peasant named Xie started a steel-pressing business. It was a hot-pressing operation and did not make much money. Another villager, Liu Wanmin, a retired worker who had been employed by a steel mill in Tianjin, pointed out that cold-pressing would be cheaper. Yu sent him to his old factory to find out the possibilities. Then Yu and others went to Tianjin and through Liu's connections and introductions met and dined with some older workers. Upon their advice, it was decided that they could put together three steel-pressing machines with old parts for Y300,000. Liu figured that they actually needed only Y100,000, if he could persuade some of his old friends to work for minimum wage. Yu decided to take the risk. He collected contributions from the villagers and borrowed money from the

county (through a relative's connections) and other villages. The factory was built in 1977, with an investment of Y 160,000. It went into production in 1978 and turned in an income of Y 200,000 the same year.

Yu continued to reinvest the income into other factories and imported skilled technicians and young workers. By 1989, the Daqiu Zhuang Agricultural-Industrial-Commercial United Corporation owned 117 enterprises, manufacturing over 300 products in 20 industries. In 1992, Yu stepped down as the CEO (the general manager, *zongjingli*) and became the chairman of the newly created board of directors (*dongshihui*). His second son, Yu Shaozheng, took over as CEO. The corporation was split up into "Four Big Groups," each of which had its own subcompanies and enterprises.¹¹ Each group retained independence in management, financing, personnel, and marketing, while making annual contributions to the corporation—the village itself.

Property Rights During the Yu Era

Underneath its economic organizations, Daqiu Zhuang has a social structure not unlike those of many other villages in China. Of the Four Big Groups, Liu's brother, Liu Wanquan, was the CEO of the first; Yu's cousin, Yu Zuoyao, was the CEO of the second; Yu's son-in-law, Zhao Shuzhong, was the CEO of the third; and Zhang Yannian headed the fourth. A fifth group, in charge of all agricultural production, was in the hands of the husband of Yu's niece. Yu's mistress, a woman named Shi Jiamin,¹² was the director of the administrative office, and members of her family ran the electricity office, the electronics company, and Daqiu Zhuang's branch offices in Tianjin and in the Development Zone on the coast. Figure 7.1 shows these networked relationships among village and enterprise leaders.

Earlier work has characterized Daqiu Zhuang as an example of local market socialism.¹³ The village retained the ownership of all its enterprises, and yet allowed them to compete freely in the marketplaces of their choosing. Contributions from the enterprises were used to maintain public services and social welfare. In the final analysis, Yu was in total control, heading a local elite network dominated by his family.

In terms of property rights, Daqiu Zhuang and its economic groups in the late 1980s can be characterized as follows. First of all, the ownership of the economic groups was officially in the hands of the "public"—the village. Daqiu Zhuang was itself incorporated as the Daqiu Zhuang Agricultural-Industrial-Commercial United Corporation, which owned all the enterprises, as well as all other units in the village. While each enterprise was allowed flexibility in the allocation of its residual income

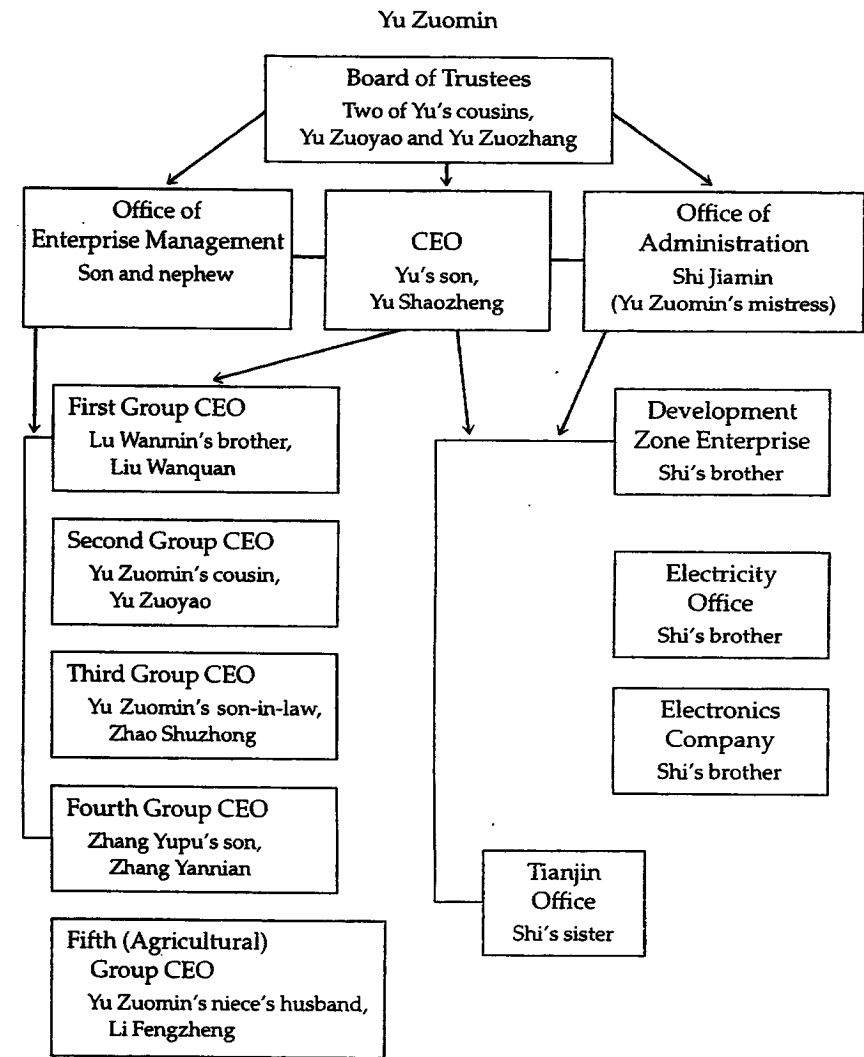


FIG. 7.1. Family Network Penetration in Daqiu Zhuang, 1990

and management decisions, the assets themselves belonged to the United Corporation—and, therefore, to the village collective. Secondly, Yu, as the chairman of the board of the United Corporation, as well as the secretary-general of the local Party and village head, had supreme authority over all enterprises. To a great extent, the enterprises contributed to the redistribution process imposed by Yu for the village. A significant portion of the

surplus income from each enterprise was handed over to the village for the general welfare of all residents and the village itself. All housing, schools, infirmaries, nursing services, infrastructure (e.g., roads, bridges, electricity, tap water), and other public services (scholarships for students, the security force, fire stations, retirement pensions, television and radio stations, etc.) were supported by surplus income generated by the enterprises and redistributed through the village corporation. In sum, the ultimate control of the enterprises was in the hands of the village corporation, a public, collective entity, and nominally under the continuing command structure of the state, through the county, to the village government and Party apparatus. In reality, Yu, as the local leader of the Party and village, commanded the enterprises; that is, *the political apparatus controlled economic resources*.

The Transformation of Daqiu Zhuang Enterprises

DEMISE OF THE YU EMPIRE

The fortune and fame of Daqiu Zhuang took a dramatic turn in 1992. It all started with the first group (Wanquan). In December 1992, a controller with the group, Wei Fuhe, was accused of doctoring accounts and was not able to explain a certain missing sum (about Y29,000).¹⁴ He was put under "company arrest" and subjected to interrogation and physical abuse. In the end, Wei died, probably accidentally. It was not the first time that a person had died in Daqiu Zhuang under the corporation's coercive interrogation. In 1990, a man named Liu Yutian had been beaten to death.¹⁵ However, Wei was not a Daqiu Zhuang resident. His family began to investigate and pursue the matter. Rumor had it that after getting nowhere in Daqiu Zhuang, they approached a relative who happened to be a police chief in a city in the northeast, who, in turn, contacted the police chief of Tianjin City. When an investigative group was sent to Daqiu Zhuang, probably in February 1993, it was met and stopped by village security forces at the entrance to the village. Yu, though not personally involved in the interrogations, instructed the security forces not to allow the investigative group to enter the village. After negotiations, Yu finally relented and the investigators entered the village. However, Yu forbade villagers to cooperate with the investigators, who were then not allowed to leave the village. When the news reached Tianjin, the mayor had to intervene and demand their release. With armed police surrounding the village, Yu gave in. At this time, in March 1993, the Eighth Congress of the People's Political Consultative Conference was in session, and Yu, as a representative, ap-

peared at the meeting. The state suppressed further reporting of the Daqiu Zhuang incident while the congress was in session. Soon after the meeting was over, however, a work team from Tianjin, along with armed police, stationed itself in the village, essentially taking control. On April 15, Yu was arrested, along with several other village and group officers, including one of his sons, Yu Shaozheng, the Party secretary of the corporation.

On August 23 and 24, 1993, Yu and seven others were found guilty and sentenced to jail. Yu was convicted of concealing the four persons accused of beating Wei to death, organizing and commanding innocent villagers to interrupt legal investigations, and bribing an investigative officer. He was sentenced to twenty years in prison. His son was sentenced to ten years, and Miss Shi to one year; five others received sentences ranging from two to four years.¹⁶ On August 27, eighteen more people were sentenced, including one with a death sentence (to be delayed for two years), two with life sentences, and others ranging from five to fifteen years in prison.

THE POST-YU TRANSFORMATION OF DAQIU ZHUANG

In November 1993, Daqiu Zhuang was "elevated" from a village to a town. The official explanation was that this elevation "was inevitable due to Daqiu Zhuang's social, industrial and economic developments."¹⁷ Thus, it had earned its new status. Regardless of the reason, the major political consequence is that as a town, all top officials, including the head of the village and the Party secretary, would be appointed by the county government.¹⁸ The change in administrative status allowed Jinghai County to send in one of its vice mayors as the new town head. Moreover, it abolished the corporation, and the Four Big Groups were converted into four "administrative streets" (*jiedao*) similar to the street committees in cities and towns. On paper, therefore, by the end of 1993, local market socialism in Daqiu Zhuang seemed to have received a death sentence. With the county government directly in control, the corporation gone, and the groups turned into street committees, state socialism seemed to have returned in full force.

What has happened since, however, has been a surprising process of transformation, no less dramatic than the initial rise of Daqiu Zhuang. The first inkling of the survival and continued prosperity of Daqiu Zhuang became public when in February 1994 *People's Daily* carried an essay entitled "Daqiu Zhuang—the Charm and Color Continuing."¹⁹ In it, the reporter described visiting teams from a Shandong Laiwu Steel Company that had just signed a joint project with Jinhai (the Daqiu Zhuang fourth group) with an investment of Y650,000,000 to produce hot-pressed steel

tubes with an annual production target of 120,000 to 150,000 tons. "Every group [in Daqiu Zhuang] efficiently managed its subdistrict; there was truck traffic everywhere, shops were full of goods and consumers, dance halls and karaoke clubs were everywhere in the evening, and more and more new managers and technicians are arriving every day," the article noted. "Production, from a low in July and August of 1992, started growing again, with the 1993 production target of Y5 billion accomplished, realizing a profit of Y430 million." Although the Four Big Groups had been reorganized into street committees, the article revealed, "all the original cadres, assets and operations were retained." Nowhere in this report were these groups identified with the local political structure.

In other words, the Four Big Groups continue to exist, despite the change of official title. Business is going on as usual. Moreover, the groups not only are now in full charge of the economic enterprises, but have also taken over administrative responsibility for the residential neighborhoods. What, then, is the role of the town government and its relationship with the Four Big Groups? Fieldwork in 1994, 1995, and 1996 (at the time of the most recent visit by the senior author in May 1996) reveals the following transformations.

Before the series of incidents in December 1992 that led to Yu's arrest, the general manager of the fifth, agricultural group (the husband of Yu's niece) suddenly died. It was discovered that the group had debts exceeding Y300 million, since it was in the midst of constructing a number of new factories, including a joint venture with a Danish firm to build a fertilizer plant. After the reorganization, it became clear that the group could not survive without substantial infusions of capital. Yu convened the leadership of the Four Big Groups and came up with a solution: the thirty-some enterprises in the fifth group would be absorbed by the Four Big Groups, which in return would take over its debts.

Before this plan could be realized, the death of the accountant occurred that eventually led to transformation of the village into a town under the control of the county. When County Vice Magistrate Wei, who had been appointed the new Daqiu Zhuang Party secretary, arrived, he was immediately faced with the problem of the Y300 million debt. The Four Big Groups balked at keeping the agreement they had reached when Yu was in control, and the county itself was totally incapable of paying the debt. In fact, the town found itself in difficulty, because with meager county support, it could not even function properly in managing the huge, thriving industrial complex and meeting its enormous obligations in public services (maintaining schools, hospital, utilities, communications, etc.). The county and Wei realized that the only way to prevent the collapse of this system was to maintain the status quo. Wei accordingly negotiated with

the Four Big Groups, which agreed to absorb the enterprises of the fifth group, as Yu had planned; furthermore, the land allocated to the fifth group would also be turned over to the Four Big Groups. The share depended on the proportion of the population under the jurisdiction of each street-group. Furthermore, all the groups would keep their original titles (Wanquan, Yaoshun, Jinmei, and Jinhai) and social and economic identity. Each street would have its own chairman (street administrator), CEO (economic head), and Party secretary.

In the end, most of the original cadres and officials except those in prison retained their positions and titles. In three of the groups, a single person became chairman, CEO (general manager), and Party secretary. In the other group, because the designated successor, a son of the CEO, was imprisoned, authority was delegated to a trusted family friend.

A brief account of these elites and the web of their social networks is useful here. In the first group, Liu continues to serve as CEO, chairman of the board, and Party secretary. (His older brother was the retired steel worker who helped start the first enterprise in Daqiu Zhuang.) Liu's son, the deputy CEO, was implicated in the "incident" and sentenced to four years in prison. Zhang Yuying, who is a cousin of Zhang Yupu, a prominent figure in the village, who preceded Yu Zuomin as the village's Party secretary and was himself "rehabilitated" earlier from some "mistakes," the nature of which we never found out, serves as executive deputy CEO. This arrangement allowed the Liu family to hold on to the group, while for the time being delegating the running of the group to Zhang. Liu's son Liu Yonghua has since been released from prison and reinstated as a deputy CEO. However, as Zhang had proved his managerial skills and loyalty to the Liu family, he has continued to serve as the executive deputy CEO. The second group, the largest of the Big Four, has Yu, a cousin of Yu Zuomin's, as its CEO, chairman, and Party secretary. The third group is headed by Zhao, Yu Zuomin's son-in-law. He remains the CEO and is assisted by Li Fengzhuang, a younger brother of Li Fengzheng, who, until his death, was the husband of Yu Zuomin's wife's niece. The fourth group also retains as its CEO Zhang Yannian, son of Zhang Yupu. These networked relationships among the leaders of the groups are depicted in Figure 7.2.

With the abolition of the Daqiu Zhuang General Corporation,²⁰ the Four Big Groups thus essentially became four independent corporations, each with its own neighborhoods, land, enterprises, and population. Each is dominated by a single family. Two of the four corporations are still connected with the Yu family, while the other prominent family in the village, the Zhangs, are involved in the two other corporations. The local familial network of elites remains strong, as does the market orientation of each corporation. Socialism has now descended from the village-town level to

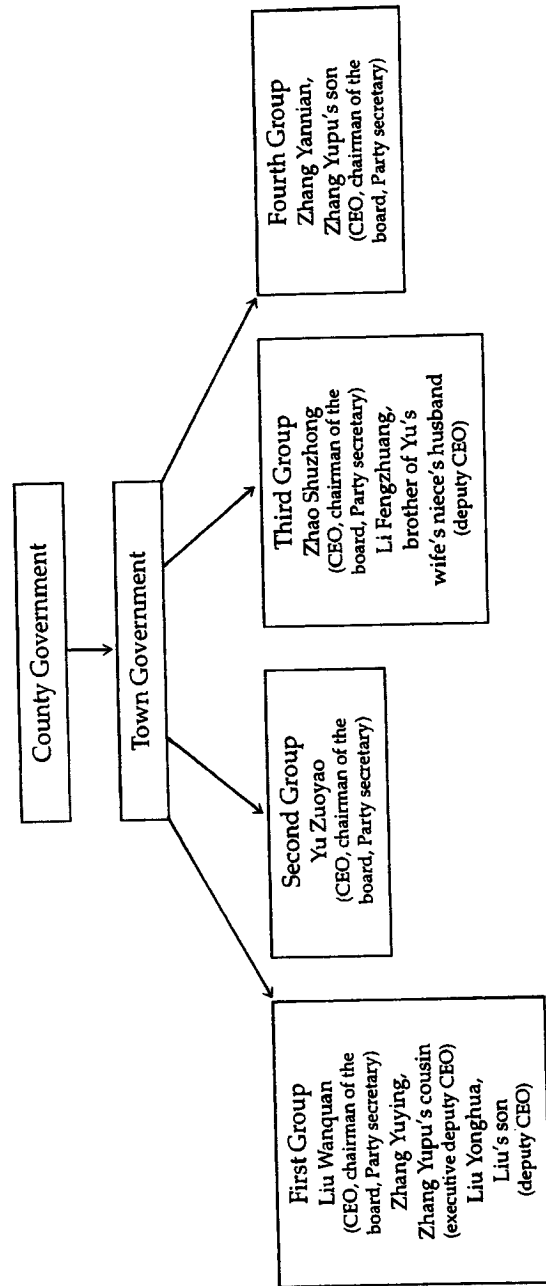


FIG. 7.2. Post-Yu Zuomin Networks in Daqiu Zhuang, 1996

the corporation level. Each corporation becomes its own socialist system, responsible for the welfare of its population. Each corporation runs its own infirmary and schools (nurseries and elementary schools), cares for its senior citizens, and hires its own managers, technicians, and outside workers.²¹

The town government is responsible for security, justice, banks, accounting, auditing, environmental protection, a junior high school, utilities (electricity, water supply, heating, gas), roads, and legal services. Each corporation-street is charged an administrative fee of .30 percent of net profits, of which 33 percent is retained by the town government and the rest goes to the county government. The town government has ten cadres, five of whom are sent in by the "state" (i.e., from the county government), while the other five are from Daqiu Zhuang. In addition, the county government has nineteen cadres on site. The town government, in other words, plays only a peripheral role in the social, economic, and political lives of Daqiu Zhuang's inhabitants. Within a year (in April 1995), Wei was replaced as Party secretary by Wang Qingwu, another vice mayor from the county.

In the meantime, the corporations continued to grow in productivity. Production value reached Y2 billion officially (but unofficially may have reached Y4 billion) in 1992, Y4.5 billion in 1993 (unofficially Y5.6 billion), and Y7 billion in 1994 (with a profit of Y5 million). In 1995, the enterprises employed 23,000 outside workers.

Another important event in the history of Daqiu Zhuang occurred in 1995: the land in the center of the town was divided and allocated to the Four Big Groups. While all the farm and industrial lands had been divided and allocated to them by 1993, the center of the town remained in the hands of the town government. In March 1995, however, it was divided into four portions and given to the four corporation-streets. The town government was left with only its headquarters, the junior high school, and the buildings occupied by the police and environmental protection agency. In essence, the four corporations have largely taken over the functions of local government, along with its land, population, buildings, residences, and industry. The town government provides only things that each corporation itself cannot, such as utilities, police, the middle school, and other functions under the direct control of the state (communication, roads, taxation).

In sum, the transfer of resources (i.e., land, population, many of the social services and social welfare functions, and the enterprises themselves) from the town to the groups represents a clear shift of property rights from government to the corporation. In contrast to the Yu era, when Yu, as the paramount Party leader of the village, exercised total control

over the resources invested in and produced by the enterprises, as well as the land, the population, and all public services and social welfare functions, the town Party and government now have little control over these resources.

Practicing Shareholding and Gaining Control over Property Rights

The next question is what has happened to the enterprises within the groups themselves. Nominally, the enterprises remained collectives, and their assets, built up over the years with investments of public (village) capital, were to remain under the control of the public, which after the reorganization should have been the town. This did not occur, however, because of a transformation of property rights that began taking place in 1992, by which the enterprises in each group were turned into shareholding companies.

The evolution of the shareholding systems in two of the four groups at Daqiu Zhuang is described below. Our understanding is that a similar transformation was occurring in the other two groups as well. Data are based on interviews with key administrators of each group and with informants in fieldwork conducted in 1995 and 1996. Information provided to us by officials of each group is adduced to convey the trial-and-error nature of the transformation process.

GROUP Y

In 1992, stock-sharing first appeared in Daqiu Zhuang, beginning in the second group, henceforth referred to as Group Y. The largest and strongest group, with assets of 1.4 billion yuan by 1995, Group Y has 46 enterprises and a workforce of 8,000, with a production value of Y 3.6 billion and net income of Y 180 million. Group Y is proud to be recognized as the third most efficient village and town enterprise and the second-largest village and town enterprise in China, ranking 143d among the country's 500 largest industrial enterprises.

Group Y reorganized itself as a limited stock company (*gufen youxian gongsi*) in 1992. (Since the Company Law was not formally enacted until 1994, it was apparently ahead of its time.) It had two types of shares. The group held 70 percent of the shares (the collective shares, *jiti gu*), and the rest were "social" or public shares. Each share had a base value of Y 1 and was sold for Y 2. Each share earned a fixed annual dividend of 20 percent

of its value. No transfer or sale was allowed. A total of 45 million shares were issued. The fixed 20 percent dividend was believed to represent little risk, because the group's profits were expanding at a much greater rate. For example, the group's assets of Y 1.6 billion in 1992 had increased to Y 2.9 billion by 1995, and thus almost doubled over a span of four years. Thus, it was simply a fixed-interest investment plan; the group generated cash and shareholders split the profits. Since the group held 70 percent of the shares, there was no transfer of property rights from the collective to private shareholders as far as the group was concerned.

Beginning in 1993, the group replaced this setup with a joint-stock company (*gufen hezuo gongsi*).²² Again, shares were divided into two types: collective shares, accounting for 70 percent of the total, and individual shares. Individual shares, which were only available to group and enterprise employees, were further divided into two types: "position" (*gangwei*) shares and individual or cash shares. Position shares were distributed at no cost to persons holding top managerial positions in the group and its enterprises, including the directors, the CEO, deputy CEOs, other leaders at group headquarters, and top managers in each enterprise. On average, there were three times as many position shares in each group and each enterprise as there were cash shares. Again, each share received a dividend of 20 percent of the share value each year.

The joint-stock company differs from the original limited stock company in at least two aspects. For one, the latter sold shares to the public and anyone could buy them, whereas the shares of the former are sold to local residents who are employed at the group's enterprises and to non-resident workers who are at or above the team leader level (*banzhang*). Shares can be transferred within the enterprise, but because of the guaranteed dividends, few such transactions have occurred.²³ Secondly, position shares are distributed to only a small number of high-level managers, at no cost to them. Thus, the elite of the group gained control of three-quarters of the individual shares at no cost.

Group officials claim that no transfer of ownership has occurred, because, in accordance with guidelines from the Ministry of Agriculture, the collective holds at least 70 percent of the shares. In reality, however, the collective shares are represented exclusively by group and company officials (the board of directors and top-echelon managers). Neither the town or county government nor the Party have any representation. Thus, by representing the collective shares and by holding the overwhelming majority of the individual shares, group and company officials have gained complete control of management and distribution of surplus income.

Nevertheless, the originally invested assets of the enterprises remain

public. Even if state policy were to allow the group to buy back the collective assets in shares, it would be prohibitively costly. However, a plan has been set in motion that may eventually change the most fundamental property right—that of ownership. In 1992, the group reorganized itself into a so-called General Group and divided its enterprises by industry into five groups: two for steel tubes, one for other steel materials (construction materials), one for nonferrous metals (copper, aluminum, transformers), and one for light industry (e.g., foam, paint, lumber, tires, and pumps). Following the Company Law, it then “decentralized” authority to each group; the General Group only “concerns itself with macro-management, policies, and strategies, but not micro-management. It is in charge of assets, not management.” In 1995, it set a production goal of Y 2 billion and a profit target of Y 120 million by year 2000 for each group. Thus, the General Group is expected to generate Y 10 billion in production value and Y 600 million in profits by 2000. In other words, the goal is to double the General Group’s assets and profits in five years.²⁴

While no official would reveal to us what the motivation was behind the “urgency” of doubling the assets and profits in five years, and why the decentralized system was devised to charge each enterprise with specific production and profit targets, we can offer a hypothesis: *these plans indicate a decision by the General Group to eventually “buy back” the collective shares.* Since collective assets are so enormous (representing 70 percent of current shares), they may have to be bought back in segments rather than as a whole. By allocating the collective shares down to each group and each enterprise and charging each with production and profit targets, the General Group has opened up the possibility that some groups will achieve their goals earlier than others and thus be able to buy back the collective portions of their shares sooner.

Thus, we speculate that the General Group may be preparing itself to exercise two options by year 2000: either, if state policy by then permits, buying out the original public assets so that each group, and eventually the General Group, becomes entirely private (in the hands of the individual shareholders), or, if state policy does not permit, each group returning the original assets (in equipment, capital, and other factors) and emerging as a separate privately held firm. There is no guarantee that either option can actually be exercised, since the state may not permit such options in the near future. However, the General Group leaders have set specific production goals and devised ways to accumulate capital so as to exercise these options if and when they become available. If either option is carried out, control will fall outright into the hands of the General Group elite, who hold the overwhelming majority of the individual shares in every group and enterprise.

GROUP J

For the third group, referred to hereafter as Group J, the shareholding system began to emerge in 1995.²⁵ According to the key administrator, Daquzhuang “had too many assets and too much property. It is impossible to buy it and the baggage cannot be thrown away. So we adopted a temporary measure—a contractual system for a period of five years.” The group and each of its enterprises agreed to make a “risk deposit” guaranteeing the doubling of the enterprise’s assets in five years. If the asset-doubling “contract” was accomplished, then returns would be doubled, trebled, or quadrupled. If it were not accomplished, the deposit would be forfeited. “And no bonuses.”

The risk deposit, as far as we could find out, was roughly the equivalent of one-tenth of the assets of an enterprise. In other words, if the assets of a factory totaled Y 1 million, the risk deposit would amount to about Y 100,000. This risk deposit amount was used to calculate and claim shares. The deposit was calculated for each of the enterprises, as well as for the second-level companies. In each unit, 30 percent of the deposit was considered the collective share, and the remaining 70 percent became individual shares to be bought by the leader, managers, staff, and workers of the unit, as well as by leaders of levels above, including the leaders of the group. The principle was that the number of individual shares to be bought was calculated according to position and seniority. The group leaders (the chairman of the board—CEO, the trustees, and the deputy CEOs), holding the highest positions and being the most senior, claimed the largest shares. Leaders of the second-level company claimed the next largest shares. The leaders of the enterprise (the plant director, the station manager, and the team leader) then claimed their shares. The remaining staff and a few technical-engineering workers brought from outside who had made “significant contributions” and had “important skills” were also allowed to buy shares.

In their capacity as officials of the collective, the group leaders voted the collective shares (30 percent) of each enterprise as well as their own. Since they also received the largest number of individual shares, they held an “overwhelming majority” of the shares in each and every enterprise. The officials we interviewed refused to reveal the exact proportion to us, and none of the other informants seemed to know either.

The “contract” goal was to double assets in five years. Thus, for an annual deposit of Y 100,000, the expectation was to make Y 200,000 in annual profits. If the net profit was less than Y 200,000, the deficit was covered by the deposit. If the net profit was over Y 200,000, this surplus (over Y 200,000) was divided into two parts: 30 percent to the collective

and 70 percent to individual shareholders. This plan was intended to encourage production, thus increasing the shareholders' dividends. But it would not challenge the collective ownership of the enterprises. In fact, the greater the production and profits, the stronger the collective would become, as the shares of the profits for the collective shares would increase proportionally as well.

In May 1996, when the senior author returned to Daqiu Zhuang and reinterviewed the key administrator of Group J, his opinion and enthusiasm for the risk deposit system had waned dramatically. While acknowledging that it was "an extension of the self-responsibility system but with deeper practice," he saw no direct connection to shareholding.

There were serious shortcomings and problems. Motivation was low, and mobilization insufficient. There were conflicts. The collective belonged to Daqiu Zhuang. After the village became a town, the collectives belonged to the four streets [committees]. Still, it belonged to everyone and it belonged to no one. It became a state enterprise at the village [street] level, with all the interest relationships, property rights, and management problems. Under this system, the assets still belonged to the collective, which benefited. We need to find a more practical way with better effects.

In other words, the group leaders and workers were reluctant to work hard for the benefit of the collective. The risk deposit system was terminated after one year. In order to compensate for possible gains in the second to the fourth year, those enterprises suffering losses in the first year were not penalized, and their deposits were returned.

In the second half of 1995, a new system was developed. After six months of deliberations, the group leaders came up with two alternative systems: the limited liability company and the joint-stock system. After consulting with "experts from Nankai University and Beijing, and lawyers," by the end of 1995, the limited liability company system was adopted, group leaders hoping in this way "to achieve all the goals in a single step." Each enterprise became a limited liability company. The steps taken were as follows. First, a thorough accounting of assets was carried out. The accounting office, along with the county accounting affairs office, took almost six months to come up with a detailed total valuation. Second, an accounting of net assets (assets minus debts) was made. Third, the net asset value was reported to the village government (nominally, the street committee, but in reality the group), to guarantee that no assets of the collective would be lost.

After the above steps were completed, each enterprise formed a limited liability company in line with the Company Law. A board of directors was created, and the largest shareholder became the chairman of the board. The collective accounted for 25–30 percent of the shares, varying by enter-

prise: "The better the enterprise, the more the collective shares." The remainder were real cash shares. Total investment amounted to Y 20 million. The shares held by directors of the group represented "50, 60, or up to 75 percent" of the shares, and other individual shares were held by the enterprise's staff and employees who were Daqiu Zhuang residents, as well as by some technicians who had been allowed to settle in the town. Likewise, the second-level companies would become corporations with registered cash assets of from Y 3 million to over Y 6 million. In total, fifteen limited liability companies have been established.

In the fifth and last step, the General Group signed a lease agreement with each company, on a rental basis. Each enterprise thus became an independent company, able to buy back its assets in the future, with no upper supervisory corporation: "The more independent the better."²⁶

Underneath the rhetoric, and despite their seemingly different paths, Group J ended up with a system very similar to the one devised by Group Y. It has estimated its collective assets (steps 1–2), made them a matter of public record (step 3), and given each enterprise the autonomy to set production goals (step 4). However, noticeably different from Group Y, Group J estimated its collective shares at only 30 percent of all shares, making it easier to possibly buy them back, as the General Group boldly encouraged each enterprise to do (step 5). Ultimately, then, each enterprise has the option of becoming completely privatized in the future.

This does not mean, however, that the General Group has only a contractual relationship with each enterprise and merely collects rents. The leaders of the General Group in fact participate as shareholders in each and every enterprise. Directors of the General Group represent collective shares in each enterprise. Furthermore, they own individual shares. For example, Zhao, the CEO (who earned a salary of Y 760,000 in 1995), Li, the executive deputy CEO (who earned Y 200,000), and five deputy CEOs all have individual shares in each enterprise company. Because the shareholders control top appointments, the large holders (i.e., the General Group leaders) have a decisive say about management in every enterprise.

To increase the individual shares relative to the collective shares, the profits in the first three years will be turned in part into additional shares, and only a small portion of cash will be actually given to shareholders. When shares are expanded, they will proportionally go to the shareholders as bonus shares. In essence, the unequal distribution of shares between the large holders and small holders will increase over time, with the bulk of new shares going to the General Group leaders.²⁷

In sum, Group J has also used the shareholding mechanism to shift the control of management and surplus income for each enterprise into the hands of the General Group elite. It has devised a plan to increase produc-

tion and profits and turn the profits largely into new individual shares. The collective shares, currently standing at around 30 percent of net assets, will correspondingly shrink relative to individual shares. Given the opportunity, the General Group and its enterprises will be in a position to buy back the collective shares in the next five years or so.

Further Analyses

In retrospect, then, the demise of Yu Zuomin, instead of leading to the end of the semi-autonomous local enterprises, may have further eroded local government power. When Yu was in charge, he was a ruthless entrepreneur, but also a powerful cadre. He had absolute control over the enterprises and was known to collect money from the enterprises for specific projects at a moment's notice. The village had the best social welfare and social services in rural China, and no enterprise or CEO would have dared to think of, let alone implement, any plans or system without his approval. In other words, Yu's system was to allow some enterprises and individuals to become rich fast, and yet to maintain and enhance the collective level of well-being. In terms of property rights, the village retained ultimate control of the assets of all enterprises, and Yu, as representative of the Party and village, controlled the economic resources from his political position. In other words, *political power controlled economic and social resources*.

Now, after becoming a town, the local government has, for all intents and purposes, become a powerless and resourceless entity. It does not control the enterprises, does not manage the residents and neighborhoods, and does not even control any land. All the property rights, except those involving infrastructure and services, have fallen into the hands of the groups and their elite leaders. The town government literally lives off handouts from the corporate (i.e., group and company) leaders, who, in fact, are the same ones as when Yu was in charge. The only difference is that there is no longer any Yu to control them. They are now held together by kin and local networks.

Transformation of property rights has gone through two stages in Daquizhuang between 1992 and 1996. In the first stage, the Four Big Groups were able to pull resources away from the town by incorporating and dividing the population and the land. This process was possible because, first, the town was without the political or economic resources of its own to sustain the social services and welfare systems. It had to rely on the Big Four to provide the financial resources (a portion of the tax the groups pay to the county government is returned to the town government) to support town expenditure. Second, and more important, the town and the county

were in no position to handle the enormous debts of the fallen fifth agricultural group and had to plead with the Big Four to assume the debts. To entice the Big Four to make such contributions, the town, in return, made the compromise of offering political (Party) and administrative (street, *jiedao*) power to the Big Four.²⁸ Thus, the leading actors of the Big Four (chairmen of the boards who also are the CEOs) were made the political leaders (branch Party secretaries) and administrative leaders (directors of the street committees). "There is a separation of politics and economics [*zhengjing fen zhi*] at Daquizhuang. The town will be in charge of politics, and will not take care of economics [*buguan jingji*]," the town's Party secretary announced. But the fact that the group leaders were also in charge of the Party apparatus and the street committees, as well as the land and the population, has left not much of the town for the town government to administer. As a result, the real economic, political, and administrative resources have clearly shifted from the town to the Four Big Groups.

During the second stage, the Four Big Groups reorganized ownership of the assets of the enterprises. Using the shareholding mechanism, the assets of each enterprise were turned into equities. Three types of shares appeared: collective shares, position shares, and individual shares. A significant portion of the shares (anywhere from 25 percent to 70 percent) belongs to the "collective" or the public. Since the corporate leaders represent the collective, they vote on behalf of the collective shares. Of the remaining individual shares, another significant portion consists of "contribution" or "position" shares distributed free to those who have made significant contributions to the enterprise—namely, for the most part, the leaders themselves. Finally, the remaining individual shares are sold to all qualified persons (usually the group and enterprise staff and workers who are local residents), proportional to their contribution and position shares. In other words, the greater their contribution/position shares, the larger the number of the cash shares they can buy. Finally, in most cases, only local residents affiliated with the enterprise are allowed to own or transfer shares. A few outside technicians who were invited to work in the enterprise have been allowed to move in with their families and to own shares. This exclusion rule inhibits possible subversion of the power of the local elite from outside. These rules seem to assure that property rights are being slowly but surely transferred from the town into the hands of the corporate leaders.²⁹

Finally, we suspect that plans have been set in motion to accumulate sufficient individual shares to buy back the collective shares if the opportunity arises. The groups are dividing the collective shares down to each enterprise, where production and profit goals are set in the next five or so

years to make this possible. Since the group leaders control the majority shares of each enterprise, they and their families would gain control over the assets, management, and surplus income if and when enterprises become privatized.

These local corporate elite leaders have thus molded the stock companies and interjected their own interpretations of state laws and regulations, while serving their own interests. They see and use the shareholding system as a method of diverting the rights of control and use of the collective enterprises from the town into the hands of the shareholders, even though the proclaimed reason was to provide incentives to the thousands of workers.

Furthermore, there is the process under way of transforming the power base of these leaders from their political assets to their local and family networks. These corporate leaders wear several hats. They are simultaneously corporate executives, Party secretaries, and village administrators. It is clear, however, their primary role is as corporate leaders. Except during the crisis period when Yu Zuomin and his subordinates were being prosecuted, political and Party ideology clearly take the back seat to running the enterprises and attending to the needs of the workers and their families. Corporate leaders are all grooming members of their families to succeed them as the next generation of leaders, working in a network of local families. These prominent families support and promote one another, as can be seen from the interlocking leadership in the various groups and enterprises, described above. Neither the county and town governments nor local residents—the other shareholders—challenge their positions. In short, the elites of the Big Four now use their economic and social power to control political and administrative resources.

Conclusions

Based on these observations and analyses, we argue that the shareholding system has become one means by which local elite actors have wrested control of collective assets from the public sector. It is clear that property rights subversion is taking place. Those in control of the corporations are gradually taking away the power (control of resources) from the local government and, at the same time, keeping it from the workers. At this point, the worker stockholders have little say in how the shareholding is operationalized or implemented, and the local government seems either unable or unwilling to wrest the power from the corporate elite leadership. The particular shareholding mechanisms adopted in each location are aimed at implementing this subversion.

One visible trend is the convergence of the corporate elite leaders and local elite family networks. The shift of the property rights of the corporations also signals the gaining of power by members of the local elite, who combine social and political capital rooted in their local origins and networks. Shareholding is the means by which they are shifting their power base from a largely political one (as cadres in the local government and the Party apparatus) to a largely social one (through a network of powerful families).

What remains to be seen is whether this subversion will become a stable form of control over local corporations. Our speculation is that this emerging form of property rights will remain viable if it meets the following conditions: (1) the corporate elite leadership merges with local elite families to form a strong local basis of power, (2) the corporation remains profitable, so that workers feel that there is continued improvement in their quality of life, and (3) local cadres and their families participate in the power structure and/or stock-sharing. Through this cadre-elite co-option and profit-sharing, local government will be rendered ineffective or indifferent to the erosion of the public ownership of the corporate assets.

The stage is now set for the next phase of property rights transformation for some of the local "collective" stock-sharing enterprises. Plans to quickly increase production and expand individual shares are being implemented. There will soon come a time when many of the enterprises will have the resources and strong incentive to buy back the collective shares from the state and local government. Should this occur, how would the state respond? If the state wishes to maintain the public character of these enterprises, it could face significant production slippage or even stoppage. If it permits such buyouts, then the public or "socialist" character of a huge portion of the rural economy might be lost forever. On the positive side, it would mean an infusion of substantial cash income, which the local government could probably use to meet increasing welfare and other demands. Depending on the tax revenue situation and the demands of national projects, the state government might desire such capital input as well.

The major stumbling block is the political ideology regarding the public ownership of the collective enterprises. State intervention to alter this transformation might yet occur. However, unless a better stock-sharing plan can simultaneously assure continued control and returns for the local elite leadership and cadres and the continued productivity and profitability of the corporations, the state is seen as unlikely to risk intervention where it would be met by resistance and further subversion, leading to further erosion of its command over local areas.

One scenario to preserve the socialist character of collective enterprises

might be to allow the public (the state and local government) to receive full or partial cash compensation for collective assets and still retain, without cash contribution, a significant but minority portion of the shares (say, 25 to 30 percent) in a shareholding enterprise. The immediate cash inflow could come in handy as the state and local governments face increasing pressure to fund welfare and infrastructure expenditures. The public would continue to benefit from the rents (dividends) from these shares. Yet the enterprise would remain market-oriented, inasmuch as it works for the majority of the shareholders. Should the enterprise go bankrupt, the public would not need to manage issues such as layoffs and liquidations. After all, in the "socialist" market system, there is no specification of how much of a socialist character each economic entity needs to preserve.

Chapter 8

The Regional Evolution of Ownership Forms: Shareholding Cooperatives and Rural Industry in Shanghai and Wenzhou

SUSAN H. WHITING

As a major initiative in the reform of property rights in rural industry, shareholding cooperatives (*gufen hezuo qiye*) have filled the headlines of newspapers and the pages of reform-oriented journals and books in China in recent years. This chapter draws on comparative case study evidence from Songjiang County, Shanghai, and Yueqing County, Wenzhou, to analyze the significance of this reform initiative, and it makes two main arguments: First, shareholding cooperatives are a transitional form of ownership that has evolved in response to partial and incomplete changes in the legal and market environments for rural industrial enterprises. Second, local officials have used the shareholding cooperative framework to support very different combinations of public and private rights over assets.¹ The varied dispositions of local officials toward public versus private property rights can be explained by an analysis of the institutional incentives and constraints under which local officials function.

The first part of the chapter lays out the factors shaping the evolution of ownership forms in rural industry. Subsequent sections show how and why shareholding cooperatives have evolved in Yueqing and Songjiang. In Yueqing shareholding cooperatives have provided a framework in which private investors have flourished, while in Songjiang they have been used to perpetuate government dominance of rural industry. The conclusion highlights the forces driving incremental change in property rights in China's transition from planning to the market.

37. Average holdings of managers and common workers differed by a factor of 6 in Zunhua (Y 35,800 and Y 6,000 respectively) and a factor of 4 in Zhoucun (Y 14,170 and Y 3,540 respectively). In Zunhua, workshop heads, technicians, and accountants formed an intermediate layer of stockholders, with averages of from Y 10,000 to Y 12,000. In Zhoucun, these three categories owned little more than the common workers; technicians and workshop heads averaged less than Y 5,000 and accountants about Y 6,500. It should be noted that some of the largest shareholder-managers (one with over Y 1,000,000 in shares) refused to be included in our sample. Because of our small sample size, the few large shareholder-managers had a great effect on the Zhoucun and Zunhua averages.

38. Art. 6 of the State Council rules on rural collective enterprises, dated June 3, 1990, states: "Provided the collective ownership form is not changed, rural collective enterprises may absorb investment that is put into shares."

39. "Because individual shares cannot be sold, transferred, mortgaged or circulated, they are not ordinary private property, but a form of socialist private property," notes Shi Yueqin. "Guanyu Shenzhen Henggangzhen gufen hezuozhi de kaocha baogao" [Investigation report of the SHCS in Henggang town in Shenzhen], *Nongye jingji* 10 (1995): 28-29.

40. "According to regulations, the collective should own half of the shares. . . . Some places convert the collective assets at current market value to create a share fund, and allow employees to buy shares. This belies the principle of one-man one-share. Other places distinguish between two types of allocated shares, one on the basis of capital and another per person. This is wrong, too. . . . The SHCS is characterized by the equal combination of labor and capital, and should have one share per employee in order to stimulate the workers," states Shi Yueqin. "Dui nongcun jiti qiye tuixing gufen hezuozhi jigé juti wenti de renzhi" [Understanding of some concrete problems in the promotion of the SHCS for rural collective enterprises], *Nongye jingji* 11 (1995): 23-24.

41. The sequence of profit distribution, after compensation for losses, is as follows: (1) 10% of after-tax profits to the public accumulation fund, as required by law; (2) the common welfare fund for collective employee welfare; (3) priority shareholders; (4) public accumulation fund, according to company regulations and decision of the shareholders' meeting; (5) ordinary share dividends (Zang and Cha, eds., *Nongcun gufen* [cited n. 31 above], pp. 6, 257-59).

42. Zhoucun ruled that 50 to 60% of profits should be retained by the enterprise for reinvestment, 10% should go to welfare, and 30 to 40% should be distributed as dividends (to a maximum of 20% of the nominal share value). Malanyu zhen (in Zunhua) ruled that this ratio should be 4:2:4. Zunhua County had ruled that about 25% should be retained, 30% distributed as a cash dividend, 30% paid as a stock dividend, and 15% allocated to employee bonuses and welfare. Interviews with municipal officials, Sept. 1995.

43. Wenzhou ruled that 15% should be retained in the public accumulation fund, 50% should be distributed in stock dividends, 10% should go to welfare, and a maximum of 25% should be paid in cash dividends (including interest). Some places in Wenzhou allowed share capital to be paid back to investors before taxes (this went at the expense of tax revenues). See Yu, Wen and Zhang,

eds., *Jiushi niandai*, pp. 3-7, 13-18, 23; Han Yuanqin et al., "Nongmin," p. 30; Zhoucun interviews.

44. In principle, no dividend should be paid if there are no profits. However, shareholders may decide to distribute a maximum of 6% of the nominal share value from the public accumulation fund, as long as it does not drop below 25% of the registered capital. See Zang Rihong and Cha Xhenxiang, eds., *Nongcun gufen hezuozhi qiye kuaiji hesuan yu caiwu guanli* [Accounting of budgets and financial management in rural SHC enterprises] (Beijing: Zhongguo nongye chubanshe, 1995).

CHAPTER 7 Lin and Chen, Local Elites as Officials and Owners

1. Calculated from data in *Zhongguo tongji nianjian, 1995* [Statistical yearbook of China, 1995] (Beijing: Zhongguo tongji chubanshe, 1995), pp. 85, 375.

2. *Zhongguo nongye nianjian, 1985* [Agricultural yearbook of China, 1985] (Beijing: Nongye chubanshe, 1986), p. 2.

3. See "Company Law of the People's Republic of China," in *PRC Year Book, 1995* (Beijing: PRC Year Book Ltd., 1996), pp. 138-87.

4. Art. 21, in *ibid.*, p. 140.

5. Art. 81, in *ibid.*, p. 147.

6. Information from fieldwork conducted by the second author, 1996. See also Xie Zifen and Ling Yaochu, *Xiangzhen qiye yunxing jizhi yanjiu* [Research on the operating mechanisms of township and village enterprises] (Shanghai: Shanghai Academy of Social Sciences, 1994).

7. See, e.g., Yu Zuomin, "Zongjingli de baogao" [Report of the CEO] (Daquizhuang: mimeographed, 1988); "Daquizhuang jueqi de mimi" [The secrets of the rise of Daquizhuang] (Daquizhuang: mimeographed, 1988); "Sishinian de zhuiqiu" [Forty years' pursuit] (Daquizhuang: mimeographed, 1988); and "Shijian he gouxiang" [Implementation and conceptualization] (Daquizhuang: mimeographed, 1989).

8. All figures are based on reports produced by Daquizhuang or verbal reports by the various officers and informants interviewed. There has not been any external validity check, and the figures can only be seen as rough estimates.

9. This section is based on a personal interview with Liu Wanmin, June 1994.

10. See Nan Lin and Mai-shou Hao, "Getting Rich First: The Story of Daquizhuang: A Case Study of Rural Development in China" (MS, Department of Sociology, Duke University, Durham, N.C., 1991); Nan Lin, "Local Market Socialism: Local Corporatism in Action in Rural China," *Theory and Society* 24, 3 (June 1995): 301-54.

11. A fifth group was later created for the agricultural sector.

12. See Nan Lin, "Local Market Socialism," n. 90.

13. See *ibid.*, and Nan Lin and Mai-shou Hao, "Getting Rich First."

14. One report suggested that he uncovered corruption and intended to report on Yu (*New York Times*, Mar. 31, 1993), but this cannot be confirmed from other sources.

15. *Shijie ribao* [World journal], May 7, 1993.

16. *Renmin ribao* [People's daily], Aug. 28, 1993.
17. Interview with Wei Zongjin, the newly appointed Party secretary of the town, June 1994.
18. The central command system only reaches down to the town level, where all officials are directly appointed from the county government.
19. *Renmin ribao* (overseas ed.), Feb. 22, 1994.
20. The name Daqiu Zhuang Agricultural-Industrial-Commercial United Corporation was changed to Daqiu Zhuang General Corporation in the early 1990s.
21. All workers since the mid 1980s have been from outside the village; all Daqiu Zhuang residents had become managers by then.
22. All the original shares were apparently bought back for their original cash values.
23. From the description of the Company Law, both these systems (the limited liability companies and the joint-stock limited companies) fit the description of the joint-stock limited system, in that individual shares are issued, all shares are of equal value, and total assets exceed the minimal requirement. The variation is that one system allows shareholders to come from outside the company, whereas the other only distributes shares to insiders.
24. The figures given and the claims made do not coincide. They are presented here to indicate the economic scale and the effort entailed.
25. In 1993, Group J produced 170,000 tons of steel. In 1994, it produced 360,000 tons, and in 1995, 600,000 tons (even excluding a new factory, which produced 100,000 tons, it still increased production by 140,000 tons). In 1995, it made a profit of Y 120 million.
26. It is not clear to us what the General Group proposed to do with profits from sales of the collective shares over time. We doubt that it would have returned the money to the town or county.
27. Group Y is also exploring another method: the joint-stock system. For the bigger, more profitable enterprises, the joint-stock method would be used to absorb more cash and technology. For example, the group's steel plate plant attracted twelve outside companies as customers, who contributed Y 230,000,000 of the total of Y 660,000,000 yuan to establish a second thin-plate steel plant with a production goal of 120,000 tons per month. Another company, the JinMeng Steel Tube Plant, has amassed assets of Y 120,000,000 in cooperation with an Inner Mongolian company. This system has no individual shares.
28. As of May 1996, the Big Four had not yet committed to any formal plan regarding payment of the debts left by the fifth group. In interviews, group officials all demurred about any such plan.
29. Ostensibly, it could be argued that the elites of the groups represented the street committees, and therefore the collectives. But the reality is that they controlled the collective shares representing the enterprise, rather than the street committee. It is clear to everyone in Daqiu Zhuang that the Big Four, not the street committee or the Party, controlled the streets, the population, and the land. The elite identified themselves first and foremost as leaders of the Big Four, and only secondarily as directors of street committees and Party secretaries.

CHAPTER 8 Whiting, *Regional Evolution of Ownership*

1. For a definition of property rights, see Chapter 1 of this volume.
2. Promotion, status, and job security were among the top priorities of leaders in two sets of village surveys, as shown by Scott Rozelle, "Decision-Making in China's Rural Economy," *China Quarterly*, no. 137 (Mar. 1994): 99–124.
3. Space limitations preclude a full treatment of the incentive structure of local officials. For a detailed analysis, see Susan H. Whiting, *Power and Wealth in China's Rural Industry: The Political Economy of Institutional Change* (New York: Cambridge University Press, forthcoming).
4. Under the incentive structure outlined above, local officials might be expected to prefer collective enterprises, all else being equal. While the township government was paid taxes and fees by all rural enterprises, as the owner of township-run collectives, it also received profit remittances from these firms. Furthermore, as owner, the local government faced lower information costs in extracting revenue from these firms.
5. John M. Litwack, "Legality and Market Reform in Soviet-Type Economies," *Journal of Economic Perspectives* 5, no. 4 (Fall 1991): 78.
6. Douglass C. North, *Institutions, Institutional Change and Economic Performance* (New York: Cambridge University Press, 1990), p. 6. See also Donald C. Clarke, "Regulation and Its Discontents," *Stanford Journal of International Law* 28, no. 2 (1992).
7. Yang Chungui, "Make an Effort to Grasp the Dialectics of Socialist Modernization—Studying Comrade Jiang Zemin's 'Correctly Handle Several Major Relationships in the Socialist Modernization Drive,'" *Renmin ribao* [People's daily], Nov. 6, 1995, trans. in FBIS-CH-95-241 (Dec. 15, 1995): 17.
8. See also Victor Nee, "The Emergence of a Market Society: Changing Mechanisms of Stratification in China," *American Journal of Sociology* 101, no. 4 (Jan. 1996).
9. A vast secondary literature has emerged on the Wenzhou model; among the best accounts are He Rongfei, ed., *Wenzhou jingji geju* [The structure of the Wenzhou economy] (Wenzhou: Zhejiang renmin chubanshe, 1987); Zhang Renshou and Li Hong, "Wenzhou moshi" [The Wenzhou model], in Zhang Liuzheng, ed., *Zhongguo nongcun jingji fazhan tansuo* [An exploration of China's rural economic development] (Beijing: Zhongguo jingji chubanshe, 1990), pp. 88–179; and Zhang Renshou and Li Hong, *Wenzhou moshi yanjiu* [Research on the Wenzhou model] (Beijing: Zhongguo shehui kexue chubanshe, 1990). For a full set of references, see Whiting, *Power and Wealth*.
10. *Songjiang xianzhi* [Gazetteer of Songjiang County] (Shanghai: Shanghai renmin chubanshe, 1991); and *Yueqing sishi nian* [Forty years in Yueqing] (Yueqing: Yueqing xian tongjiju, 1989).
11. For a more detailed treatment of this issue, see Whiting, *Power and Wealth*.
12. Zhang and Li, *Wenzhou moshi yanjiu* (cited n. 9 above), p. 32; and *Yueqing sishi nian* (cited in n. 10 above), p. 107.
13. These guises included household firms affiliated with collectives (*guahu*), joint-household firms (*lianhu*)—considered a type of cooperative (*hezuo jing-*