
On Governmental Reform in China: Two Suggestions from Japanese Experiences

Guirong Mao, Meijigakuin University (Japan)

Over the past two decades China has promoted the transition from a traditional planned economy to a market economy, but has tried to make this transition with poor administrative efficiency and large government. The Chinese government has introduced and carried out comprehensive reforms, and we have seen the results of their policies in the great changes throughout the country. Rapid economic growth and great social structural change have created a powerful impetus for an efficient modern government. Through a bold redefinition of government—the separation of government from business, decentralization, the establishment of a civil service system, and numerous structural reforms—the Chinese government expected to transform into an efficient modern government. It is safe to say, however, that governmental reform has not been the success story that economic reform was. This paper explores two of the necessary further reforms, targeting the basic problems of government size and poor central-local government relations. The purpose of this paper is to introduce two ideas promoted and practiced in Japan, the ceiling control system and the fusion system for intergovernmental relations. For this argument, a short summary of Chinese governmental reform is given in the first section, followed by a description of the two practical frameworks in Japan. Finally, in section 4 the relevance of these frameworks in China and their application through a revision of current reform

practices are discussed.

Government Reforms in China

Government reforms were implemented three times in the Mao era (1952, 1958 and 1961), followed by four reforms in the post-Mao period (1982, 1988, 1992 and 1998). There followed the economic reforms initiated in the 1980s, at least three important governmental reforms, accompanied by a slogan of government function transformation. All of the reforms occurred after the appointment or re-appointment of the Prime Minister. The main focus of governmental reform has been: 1) the functional separation of the Party and the government; 2) the functional separation of the government and business, transformation of governmental economic functions to a market mechanism; 3) cut backs or downsizing (the number of departments and commissions in the central government have been cut from 52 in 1982 to 29 in 1998); 4) the establishment of a civil service system; 5) decentralization; 6) the implementation of a legal system for administration (Liu, et al., 1996; Mao, 1999b).

Following the reforms of the post-Mao period, especially with the transference of economic management powers to local governments and the market, the structure and function of the government underwent drastic changes. But, as many have

Abstract: This paper explores the, as yet unresolved, crucial question of how best to conduct reforms aimed at controlling government size and improving relations between central and local governments. It suggests two ideas widely promoted and practiced in Japan, the ceiling control system and the fusion system of central-local relations. I argue that China could set up a ceiling control system to fix the total number of governmental departments and commissions and the maximum number of staff, and establish an institutionalized "fusion system" to promote decentralization. The paper demonstrates how these can be implemented to revise current reform practices.

indicated, in China there are two basic historical trends: 1) a “mysterious circle” (*guai quan*) between decentralization and centralization, especially with regards to economic management; 2) a “mysterious cycle” (*guai quan*) of expansion-cutback in government size. It’s well known that the “mysterious circle” was at work during the Mao era as well (Liu, 1998; Liu, et al., 1998; Ma, 1996; Mao, 1999b; Xin, 1994; Zhongyan jigou bianzi weiyuanhui, 1993).

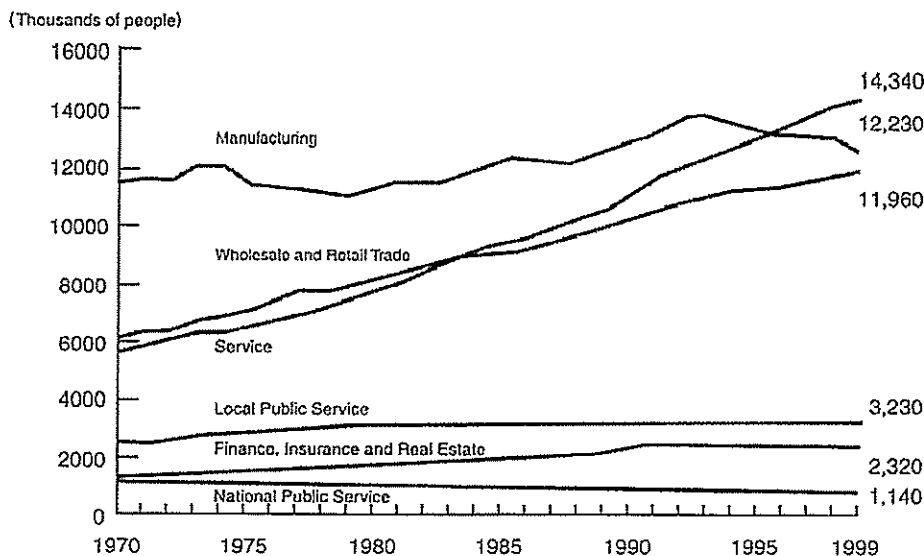
Throughout the 1980s, many government reforms were implemented in China, but the size of the central government did not shrink at all. The last government reform in 1998 proposed to cut administrative staff in half, but this was never carried out (Brodsgaard, 2002). Moreover, as administrative demands increased, as with the establishment of a social security system, the size of the central government began to expand again. It seems that the “mysterious circle” (*guai quan*) of cutback-expansion will invariably continue. Controlling government size is still one of the basic problems in China (Liu, 1998; Xin, 1994).

In regards to central-local government relationships, reforms often oscillated between centralization and decentralization in the Mao era

(Dong, et al., 1996; Hao & Lin, 1994; Liu, et al., 1998). In the post-Mao reform period, central-local relations improved somewhat with the introduction of the new tax system (the tax-sharing system, or *fen shui zhi*) in 1994 (Wang, 1997; for the discussions in China, see Dong, et al., 1996). However the basic problem remains unresolved. An instructive case of the problems of (de)centralization is that of investment: decentralization promotes economic development towards a “hot” economy. It then becomes excessively “hot.” To adjust the “hot” economy, retrenchment policies are enacted, recentralizing economic management powers and, in turn, producing economic slowdown and recession. The so-called “*yi shou jiu si, yi fang jiu luan*” phenomenon, meaning that vitality is lost with centralization while it becomes a complete mess as with decentralization, is still very relevant (Hao & Lin, 1994; Wu & Zhang, 1995).

To counter the two “mysterious cycles” discussed above, here I would like to introduce two frameworks constructed and practiced in Japan for controlling government size and improving central-local government relations. I contend that China could introduce the ceiling control system used in Japan to

Figure 1 Number of Employees by Industry (1970-1999)



Source: National Personnel Authority, 2000, p. 6.

Note: National Public Service includes Central Government Personnel, Self-Defense Forces, and Employees of Government Enterprises.

fix the total number of departments and commissions, even bureaus within the central government, as well as the maximum number of total staff in the central government. Within this kind of ceiling control system, the central government will transfer more economic affairs to the market and transfer more administrative affairs to local governments. In addition, China could introduce the "fusion system" of central-local government relations, also practiced in Japan.

Controlling Government Size

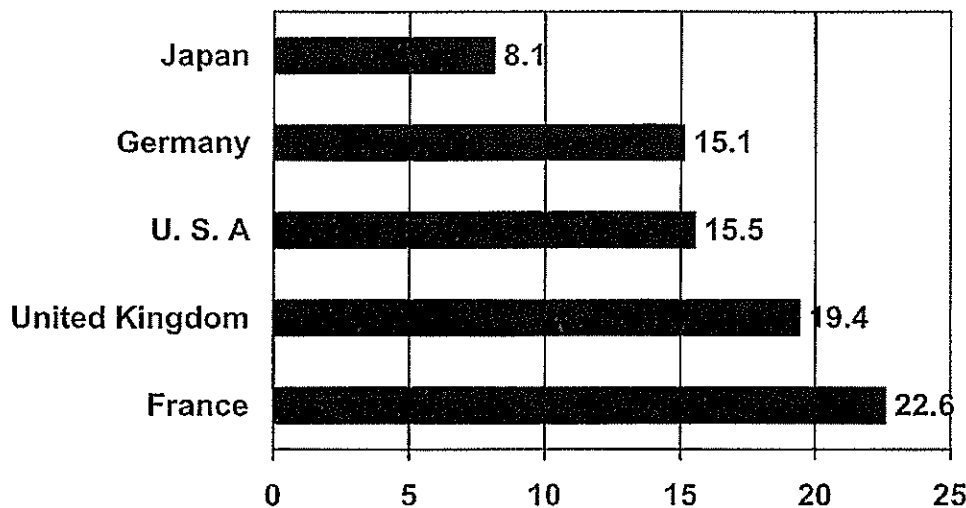
Postwar Japan has maintained a very stable and small-scale government. Japan has been largely ignored in the study of comparative government (Rose, et al., 1985; Rowat, 1988). Here I will cite some data by the Japanese government. From Figure 1, we see the decrease in the number of national employees, which includes the Self-Defense Forces, and a slight increase in the number of local public employees, which contrasts with the growth of employees in other industries. If we compare the total number of public employees, including employees in national, local governments and public corporations, with those of other developed countries, we find the size of the Japanese government to be the smallest. Figure 2

shows that in 1990 the ratio of public employment to total employment in Japan was almost half that of Germany and the USA, and less than half of the ratio in Britain and France. Of course, some may attribute that to the fact that Japan does not have a full-fledged defense force. However, Figure 3 provides additional data from 1998, comparing each country's public services to the total population, excluding defense forces. Japan's figures are still the smallest.

Moreover, as we focus on the central government, we see that from 1957 to 2000 the entire number of national government employees increased a little, under the high pressures of the high economic growth period, but it has been gradually reduced and kept stable since the late 1970s (Figure 4), despite their adoption of the welfare state model in 1973. In addition, throughout the entire post-war era, as shown in Figure 5, there has been no notable increase in the number of government ministries and agencies (1952 to 1999). How to measure the size of the government is a difficult problem, but from some of the standard measurements taken, we can safely describe the Japanese government as small (see Tanz and Schuknecht 2000, for the same conclusion with different data).

How have the Japanese managed to keep their government so small? One of the reasons is the "ceiling control system" (*zongliang guizhi*). In 1967,

Figure 2 Ratio of Public Employees to Total Employment (1990,%)



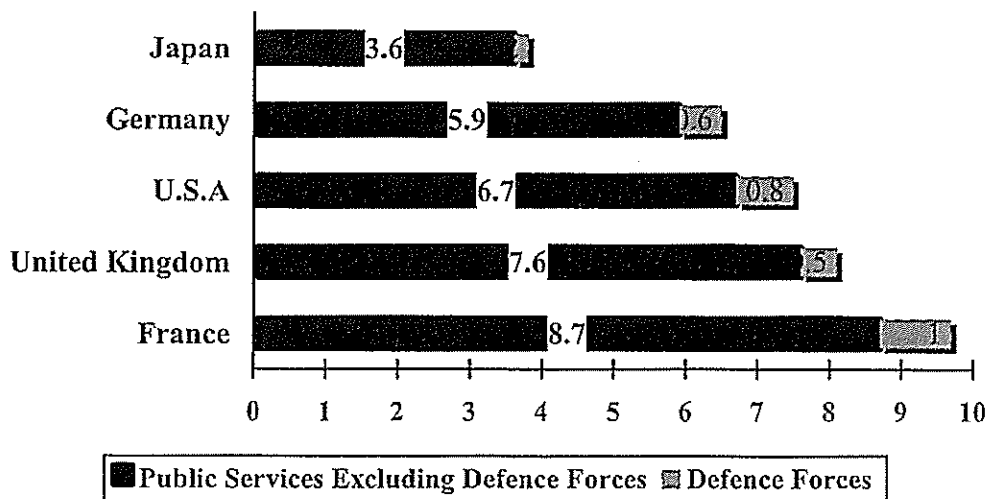
Source: National Personnel Authority, 1996, p. 4.

Note: Public Services include National Public Service, Self-Defense Forces, Local Public Service, and Employees of Government Enterprises.

a program was initiated to reduce the number of public staff, and in the same year a law entitled “Fixed Number of Personnel of Administrative Organs (Total Staff Number Control Act)” was passed. It set a ceiling for the total number of staff in the Japanese central government. The Total Staff Number Control Act sets the total number of employees for central government organizations. For instance, the revised Total Number Control Act in 2002 set the maximum number for central government ministries at 534 thousand. Then, the cabinet allots each ministry or agency a fixed number of employees within the total number set by the Control. Each Ministry or Agency in turn has the discretionary power to control the allocation of staff within their fixed allotment. This system is designed to allocate or reallocate employees between government organizations within the fixed numbers (Masujima, 1997; Tsuji, 1984). The reduction of personnel, in sectors with declining administrative demands or high administrative efficiency, creates a “pool” from which employees can be reallocated to sectors with increasing administrative demands. The reallocation occurs through the annual request of ministers and agencies for increased employees in the expanding sectors. As shown in Figure 4, the number of officials in the central government started to decrease in 1967. Until 1984, the Management Agency and, from 1984-2001, the Management and Coordination Agency considered the various agencies’ requests, together with budget set by the Ministry of Finance. Today the process is overseen by the Soumusho (MPHPT).

We can see the same ceiling control mechanism in other areas as well. The number of State Ministers was limited to about 20 by the Cabinet Law. For a long time, the Japanese government was called a “one Prime Minister’s Office, 12-Ministry system.” Besides the 12 Ministries, there are many Agencies and Administrative Commissions (increased from 29 in 1952 to 33 in 1999), yet only a few Agencies (increased from 5 in 1952 to 10 in 1999) headed by the Ministers of State have a formal status equivalent to a Minister serving as a member of the Cabinet. In fact, it was a 20-department system (and now a 12-department system, after 2001). During the economic growth period, while some new agencies like the Environment Agency and the National Land Agency, were established in the Prime Minister’s Office (now the Cabinet Office), the total number was largely maintained (see Figure 5). In addition, a policy of reducing one bureau per ministry (or agency) was adopted in 1968 when the ceiling control system was first implemented. After that, the so-called “scrap and build principle” was established. Under this system, any ministry or agency requesting the creation of a new unit had to abolish one of its existing units. The number of bureaus in the government is kept under 128. Even under the increasing demands of the administrative service during the high economic growth period, the size of the central government was strictly controlled. To institutionalize this practice, the National Government Organization Law was revised in 1984, giving the government the discretion to review organs below the bureau level, but setting a

Figure 3 Ratio of Public Employees to Total Population (1998, %)



Source: National Personnel Authority, 2000, p. 7.

ceiling on the total number of bureaus (128) within the central ministries and agencies. We also see the same ceiling control mechanism in the budget system and in the local governments. We will not go into the details here, however.

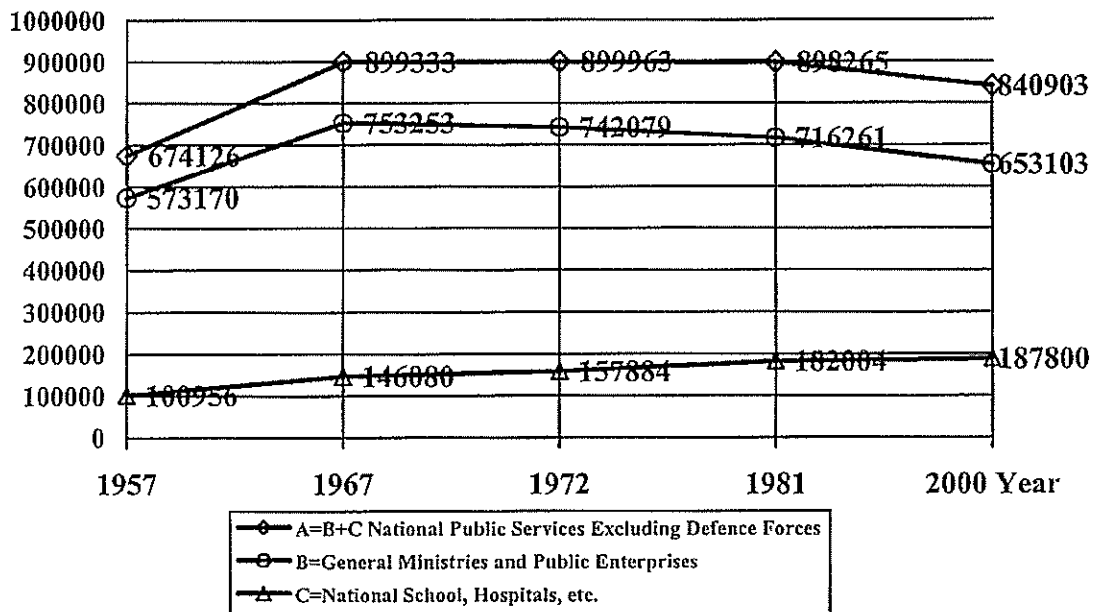
Through the control of the number of public employees and government organs, we can see how the mechanism of the ceiling control system has been formulated in the Japanese government. This mechanism is an artificial one. It is in itself not a rational system, but it provides a good means to control the size of the government (Mao, 1999a, 2000). It should also be noted that this system combined elements of both flexibility and rigidity in staff allocation and organization (bureau) setup. On the one hand, it fixes the total number of staff and organs (bureaus), but at the same time it gives the government the discretionary power to reallocate the staff and set up new organs following the "scrap and build principle."

I should note that there are some other reasons for Japan's "small government" that are worth noting. One is the "big-room-ism." In Japan, there is no position-classification system. All of the staff for

each division shares one big room. Not even the division chiefs have separate rooms, nor do they have private secretaries. This group-oriented working style lets the people in the same division share duty without increasing staff. There are undoubtedly responsibility problems that arise from this sort of group work situation. If everyone shares responsibility, than no single person takes on special responsibility, even the person who is in charge. This is a very probing question in Japanese administrative studies, but the method has kept each division small (Mao, 1994a, 1997; Nishio, 1998).

We should also acknowledge that there is a functional relationship between the small central government and the developmental state, regulations, administrative guidance and centralized central-local government relations. Through delegating its affairs to local governments and keeping control through involvements with and regulations over local governments, the central government is able to implement its administrative functions without increasing its size. The consequence of this was that local government employees increased by one million from the 1960s to the 1980s. After the high economic

Figure 4 Change in the Number of Central Government officials (1957-2000)



Source: Institute of Administrative Management, 2001, p. 54.

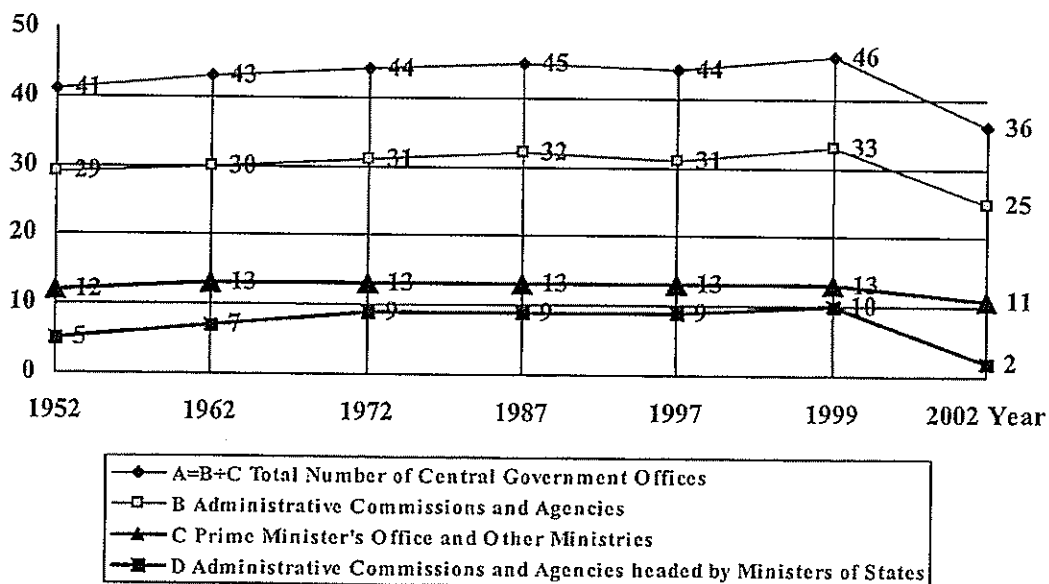
Note: National Public Services include Central Government Personnel (above 500 thousand), Government Enterprise Employees and other staff. For the total number of national employment, including the Defense Forces (about 280 thousand), see Figure 1.

growth period, these numbers stabilized, and have decreased in recent years through ceiling control for local governments. Regulations (more than 10,000 items) and administrative guidance contribute to the existence and maintenance of the small government as well (Mao, 1994a, 1999a; Okimoto, 1989; Vogel, 1996). Moreover, we should indicate that advisory councils and public corporations (cf. Figure 4) increased during the high growth period, all of which can be explained through their links to "small government." We can find the same roles in the intermediary associations in the business sector (Kim, et al., 1995; Mao, 1994a, 2002a). The cooperation between government and business (Evens, 1995; Johnson, 1982; Okimoto, 1989) is another one of the important factors in keeping government small. In precisely this sense, scholars of Japanese bureaucracy have indicated that the Japanese government system is a "maximum mobilization system." Stemming from the competition between government ministries and agencies, which had been criticized for its sectionalism, each ministry or agency mobilizes resources that they can get in their jurisdiction, including the cooperation of the private sector, for economic growth and modernization (cf. Kim, et al., 1995; Tsuji, 1984). The ceiling control system works as a constraining system to push the government to look for and mobilize all possible resources.

More interesting for us is that this system has persisted through recent government reforms. The cutback of government functions has been an

important issue in recent government reforms in Japan (as well as in other countries). There are many aspects to these cutbacks, such as deregulation, privatization of operations and projects, and transfer of administrative functions from the government to the private sector (Mao, 2000). Also, the reforms have involved a revision of the "ceiling control system." The total number of personnel and government organs will continue to be tightly controlled. The new central government initiated in January 2001 was reorganized into a 12-department system (one Cabinet Office, 10 Ministries, one Self-Defense Agency), and the number of State Ministers was limited to a maximum of 17 (Cabinet Law). It was also decided in the Central Government Reform Law that, in large ministries, the number of internal bureaus per ministry should not exceed 10. The total number of bureaus in the central government was drastically cut back, from a total of 128 in 2000 to be reduced to 96 in 2001 and to 90 in the near future. The total number of divisions in the internal bureaus of ministries and agencies, which was counted at about 1,200, has now been reduced to 1000 and will be further reduced to 900 in the near future. Within those limits, government organs have discretionary power to reform or reorganize, as they deem appropriate. In addition, the Total Staff Number Control Law was revised in 2001, and a new plan for staff reduction was formulated. In the first 10 years of the plan, overall government staff shall be reduced by a minimum of 10 percent (Mao, 2000, 2002a, 2002b).

Figure 5 Change in the Number of Ministers, Agencies and Commissions (1952-2002)



Source: Institute of Administrative Management, 2001, p. 41 (added data of 2002).

From this, it is quite clear that the “ceiling control system” has been one of the most important frameworks for controlling government size in postwar Japan (Mao, 1999b) and has been used for more than 30 years. As we have seen, the Japanese government, especially the central government, is not a big government, and will soon become even smaller. The ceiling control system is a useful framework for controlling government size. I will argue that this system can be useful for cutting down government size in China. Before turning to China, we first move to an analysis of the central-local government relations in Japan.

Improving Central - Local Relations

The central-local government relationship in the Japanese system is called the “Centralism-Fusion” system. I believe the central-local fusion system is useful for China to resolve the “*guai quan*” (mysterious circle) of the decentralization-centralization cycle. First, we should review central-local government relations in Japan.

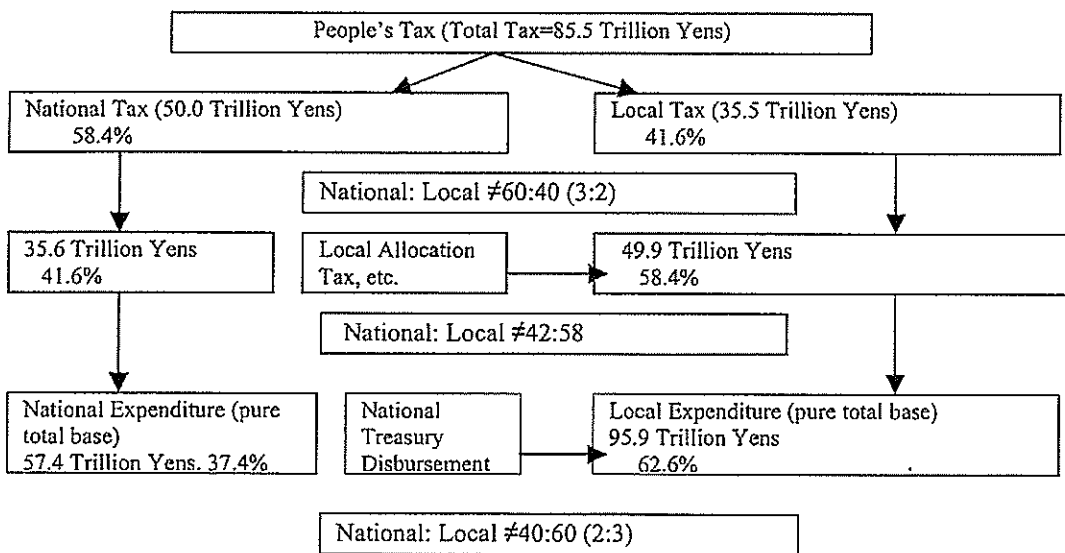
Before 1945, Japanese local governments were firmly controlled by the Ministry of Home Affairs, and the Home Affairs Minister appointed and removed the local governors and mayors. During the Occupation period, the GHQ abolished the Home Affairs Ministry (although a new Ministry of Home Affairs was re-instituted in 1960), and most powers

were placed in the hands of the local governments. Local government structures are based on the American idea of the separation of powers, combined with a parliamentary system. Most of the relevant positions were changed to elected posts, including the members of the local education boards. The elected local authority is a vital element in Japanese democracy (the Local Autonomy Law, 1947).

However, the share of taxes kept by the local government was for a long time about 30% (now 40%) of total taxes. From this, local autonomy in Japan is criticized as a “one-third local autonomy” (cf. Koike, 1998; Reed, 1982). In contrast, the taxes kept by central government account for a significantly larger share, over 60% of total taxes. On the other hand, over 60% of the total government expenditures go to local governments (Figure 6). Thus, there is a sizable gap between tax revenues and expenditures in local governments. It should be noted that the amount of local tax revenues is not as low as in many other countries; indeed, it is almost the highest of any unitary state (Lijphart, 1999).

Due to this gap between revenues and expenditures, local governments receive a local tax, allocation transfers, national treasury disbursements, grants-in-aid and subsidies from the central government (Figure 6). Ideally, the financial resources of a local public organization should be covered by local tax revenues collected by that organization. However, it is argued that, in reality, tax revenue resources are scattered unevenly throughout

Figure 6 Distribution of Tax Resources between Central and Local Governments (2001 Fiscal Year)



Source: Ministry of Finance, Japan.

the country, and most local governments in rural areas are financially weak. So it is necessary to have a system to guarantee financial resources for local public organizations and to ensure equal public services to all local governments. This is why a system like the Local Tax Allocation was established. It was created to ensure the equalization of local government revenues. So, despite the apparent 3:2 tax ratio between central and local governments, the central government redistributes money to local governments through the Local Allocation Tax, national treasury disbursement and other aids, in order to balance the scale of financial resources among the local governments. As a result, the final ratio of expenditures becomes 2:3, as shown in Figure 6.

Connected to the tax allocation and other fiscal transfers is the "delegated affair system," through which central government ministries assign certain services to local governments to fulfill. This system was held over from the prewar control system by the Ministry of Home Affairs. There are two types of delegated affair systems. One is the "agency delegated affairs system," in which central government ministries delegate their affairs to local governors and mayors. The politically elected local governors and mayors handle the delegated affairs as local agencies of the central government. The other version is the "local public entities delegated affairs system." The difference is that the local Assembly cannot intervene in the "delegated affairs," because in this system the local government is not regarded as a local agency of the central government. The first system is significantly more common. In the appendix to the Local Autonomy Law of Japan, there were about 600 items listed as "delegated affairs," largely criticized by the advocates of local autonomy. Related to the "delegated affairs" system are the many central government regulations (*kisei*) and involvements (*kanyo*) in the local governments, of which there are over 3000. Administrative involvement or control is the basic tool for inter-government coordination (Institute of Administrative Management, 1997; Nishio, 2001).

This kind of central-local governmental relationship is called the "centralism-fusion" system in Japan. The basic idea is that, the degree of centralism or local autonomy is judged through an analysis of taxes, power allocation and other such measures. In addition to this perspective, we should also consider the linkage of the central and local governments, mostly based on how the central government handles their affairs. There are two possibilities. In one case, the powers of the local government are designed in a limited, detailed enumeration. In this system, the relationship between local and central governments is prone to separation, so that central government

ministries and their local branches handle their affairs entirely on their own, and local governments do not handle the affairs that do not belong to them. We call this form of linkage "separation." The other is the case in which the powers of the local government are described through a general delegation, in a short summary style. Here, the separation of local government and central government is not so clear. In this case, the central government can delegate its affairs to local governments, fusing them with local government affairs. In short, the linkage of central and local government can be considered on a spectrum from separation to fusion. If we combine the two dimensions (i.e. from centralism to local autonomy and from fusion to separation) we can imagine four interacting factors, as shown in Figure 7.

There are two basic "patterns," No. 1 and No. 4, as shown in Figure 7. Logically and practically, if the central-local relation is defined by centralism, than the local governments most likely will be subject to the central government. If the basic relation is separated, the local government will certainly have greater autonomy. Local governments then will not handle the affairs that do not belong to them, and the central government will handle services by itself or through its local branches. Pattern No. 1 is called the "centralism-fusion system," practiced in Western Europe and Japan. In these countries, we find strong Home Affairs Ministries, coordinating local affairs with administrative regulation or control as the basic tool. Pattern No. 4, known as the "local autonomy-separation system," is practiced in Britain and in the local governments in the USA. We see a "Home Affairs Ministry" that is weak or nonexistent in those countries. If there are conflicts between the central and local governments in pattern No. 4, the basic mechanism for coordination is judicial control, rather than administrative control (Nishio, 2001).

Comparing local governments in the two patterns, especially the powers and affairs of basic local units, we see some interesting differences. Many who advocate local autonomy favor the "local autonomy-separation system." Local autonomy is preferred in Japan, and so the phrase "one-third local autonomy" is used in a negative sense. However, in pattern No. 1, local governments have less or low autonomy, but handle many administrative services including many affairs delegated by the central government. In this case, we can refer to it as quantitative, comprehensive local governments. In pattern No. 4, local governments have great autonomy, but without so many administrative services. Usually they are small governments. We can refer to it as qualitative rather than quantitative, local autonomous governments. Which one is better? It is not so easy to answer. If we support the tendency of local autonomy in central-

local government relations, pattern No. 4 is better. But in pattern No. 1, local citizens can receive many services directly from city hall, even if those are central government services they're receiving (Mao, 2000, 2002a).

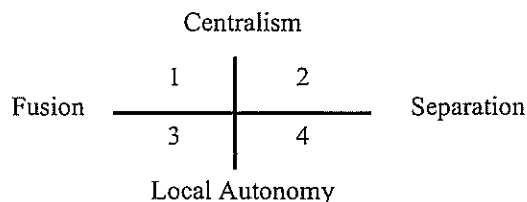
Moreover, as in the case of Japan, there is a very important reason for the fusion system in inter-governmental relations (i.e. the equalization of local services). Although it is desirable for local authorities to provide their services using their own revenues, there is a very large difference in the financial capabilities of local governments. In order to equalize government services among each local government and keep a standard level of public services throughout the country, some public services are delegated and regulated by the central government and implemented by the local governments, and a certain portion of financial receipts collected as national tax are transferred to local governments. Usually in Japan, the amounts for the respective local governments are calculated proportionally to their lack of revenues, taking into consideration the standardized financial receipts or revenues (formula-based calculation) and the demands of individual local governments. In addition, the national government disbursements in Japan are provided for enabling local governments to maintain a certain level of administration and gain sufficient revenues for large-scale construction works; the grants-in-aid from the national government comes with a view to support, encourage and promote certain functions of the local governments. These are very important mechanisms for the equalization of local services.

Interestingly, recent reforms of central-local governmental relations in Japan continued the fusion system. After the Diet passed the Decentralization Promotion Law, the Decentralization Promotion Committee started its work in July 1995. It presented five reports, with most of the recommendations for establishing an "equal and corporative relationship" between the central and local governments implemented. In total, 475 laws were reviewed, and the new local government system was implemented on

April 1, 2000. The basic idea of this reform is that the central government and local governments have an equal partnership. Following the first report recommendation, the "agency delegated affairs" system was abolished, and a new classification of inter-governmental functions was determined. These are: (1) the "autonomous affairs" of the local governments; (2) the "entrusted affairs by law" (or "legally commissioned affairs") of the local government; and (3) central government affairs. The "entrusted affairs by law" are local government affairs to be implemented by the local governments under the direction of the central government. In all, 45% of the "agency delegated affairs" have been transferred to the "entrusted affairs," and 55% of the "agency delegated affairs" to "autonomous affairs." Local governments are now expected to carry out these administrative affairs independently, so that their operations will fit the actual conditions of individual local sectors (Koike & Wright, 1998; Mao, 2000, 2002a, 2002b; Nishio 2001).

The reforms in the re-classification of intergovernmental functions, the abolition of "agency delegated affairs," and the transfer of "agency delegated affairs" to "autonomous functions" are very significant developments for central-local governmental relations in Japan. As the concept of the "entrusted affairs by law" has suggested, administrative involvements and regulations with bureaucratic discretion will be limited. The set up of third-party organs, to serve a judicial function for the adjudication of inter-governmental conflicts, was proposed and implemented. Administrative involvements and regulations will be transformed into judicial control within the system of central-local relations (Nishio, 2001). The Ministry of Home Affairs was abolished in 2001, and some of the affairs transferred to a new Ministry, Soumusho (MPHPT). Also, local governments will have greater local tax revenues and local taxing power. As noted before, the ratio of the final expenditures between the central government and the local governments is approximately 2:3, while the ratio of the tax revenues

Figure 7 Basic Patterns of Central-Local Relations in Unitary States



Source: Mao.

paid by the people between the central government and the local government is reversed, 3:2. There is a wide deviation between the final expenditures and the share of tax resources. Japan is considered to be a mature society: the location of tax resources and capacity for providing services are not unevenly scattered as before, and the tax collection is stable. It is necessary to reduce the deviation as much as possible by the substantial assurance of local taxes.

With all these reforms in central-local governmental relations, we seem to be dealing with a new system. Pattern No. 3 (local autonomy-fusion system) is currently being formed (Mao, 2000, 2002a, 2002b; Nishio, 2001). The judicial procedure, a third-party organ that is a mechanism for judicial control rather than administrative control, was established, and the Home Affairs Ministry was abolished. In keeping with the earlier discussion, we can say it is a new pattern, at least in terms of institutional formation. This is a totally new system, unprecedented elsewhere in the world. But for our purpose here, the most important thing is that when Japan promoted decentralization toward more local autonomy, they did not choose the "separation" arrangement, but rather the "fusion" system (Nishio, 2001). The "entrusted affairs by law" are the affairs of local governments delegated from the central government (legally they are not the affairs of the central government). It is a fusion system.

In my opinion, this is a better system for countries such as China, where uneven development persists, to improve central-local relations (Wang & Hu, 1999). Through China's reform period, we have seen the beginnings of decentralization and the appearance of the so-called "feudal princeling economies" (*zhuhou jingji*). We cannot allow reforms to take us back towards centralization and into the "mysterious circle." One reform option for China is for the central government to delegate economic management affairs and other public affairs to local governments, but with unified regulations set up by the central government. This kind of fusion system could maintain a unified policy, while giving local governments positive initiatives. In the next section, I will further examine this suggestion, if it can be done, and how to do it.

From Japan to China

In this section, we turn to the question of the feasibility of the two suggestions discussed above for China. China already has some practices that resemble those two Japanese frameworks, but they are notably different and require further revision to better implement reforms in China.

The Chinese reforms of 1998 emphasized the functional transformation of the government, and, as a result, governmental structure has changed significantly in recent years. This change has entailed an increase in the macro-economic agency and a decrease in the traditional agencies of industrial ministries. At the heart of recent Chinese reforms is the transformation of government. Functions that are not essential parts of the state should be discarded or delegated to the market or society. The reforms have focused on redefining the functions of the state and government organizations, and shedding those functions deemed non-essential, as seen in the privatization of state-owned enterprises. The separation of state function from the market and society has become a reform slogan. The "small government and big society" model was first instituted as an experiment in Hainan province, and then became the prototype for reform in local governments,

Moreover, during this reform process, targeting the "mysterious circle" of cutback-expansion-cutback, China showed interest in the Japanese control system and reduction plan (Liu, et al., 1998; Zhongyang Jigou bianzhi weiyuanhui, 1993). China invented a similar means for reducing government size, but in a very different framework. The key concept in size control is the so-called *san ding* (three limitations). The first of these three is a limitation on the functions of government or government organs. It follows the reforms on changing the function of government, the separation of government and enterprises, the separation of government and party, and the separation of government and market, based on the idea that many state functions should be transferred to the market and society.

Following this functional transformation of government, the second and third limitations are targeted at the reduction of organs and staff at every level. Basically, the number of government organs is based on a decision as to which functions the government should be responsible for. Based on whether or not the government should perform the function, a given organ will find itself sustained, reduced, or abolished. Clearly, the three-limitation control system is a means of streamlining government, and it looks like the Japanese ceiling control system. The difference is that the Chinese system is focused on controlling function—that is, whether or not certain affairs should be handled by the government. This is a very rational system for reforming government, but it is problematic as well. From where does the incentive to discard superfluous government affairs and decrease government organs and staff come? During the high economic growth period, economic development is the primary goal. There is no imperative incentive to reduce government, even if it

has become an obstacle to development. So, despite intentions to streamline, organizational size and staff have kept growing (Liu, 1996; Liu, et al., 1998).

During the period of the planned economy, businesses were appendages of the state organization, generally classified as administrative organs. This has changed over the course of the reform era, but still many business owners and managers are deeply connected to the party and government. There is a prevalent phenomenon of Chinese state organs, from party organizations to the military and police and to the judicial department, establishing their own enterprises. It is argued that partnership between government and business, the bureaucratic umbrella, is important for economic development, especially for local industrial development. The institutionalized incentives of bureaucracy, such as revenue generation, inspired the creation of new regulatory institutions and affiliated organizations. Similarly, local governments have a clear incentive to maximize the revenue through the control of businesses under their jurisdiction. This is well known to be a cause of great corruption in China (Baum & Shevchenko, 1999; Kokubun, 1998; Oi, 1999; Yang, 2001).

This mutual cooperation turned out to be fertile soil for expansion, with few or no incentives to streamline government. The government reforms did cut back on some bureaucracy, as well as upgrading the professional and technical qualifications of government officials and business managers. But the proliferation of new economic entities and growing economic complexities have prompted central and local governments everywhere to expand these new regulatory agencies and staff. This justified the *chaobian* (i.e. the new agency) or expansion of staff beyond the set three-limitation regulations (Brodsgaard, 2002). It is far easier to setup new agencies than to cut back existing ones, and so there is no mechanism to keep the government small.

China is experiencing drastic changes in the relations between state and society, government and market. We may keep pushing the functional transformation, but it would be far more effective to revise the three-limitation system so it entails a regular reduction mechanism. The basic difference between the three-limitation system and Japan's ceiling control system is that the ceiling control system is not based on functional determination. Of course, the situations are quite different in China and Japan. China is experiencing a high economic growth, and Japan is more stable now. However, as discussed before, the ceiling control system worked very well during Japan's growth periods at resisting the pressure for administrative expansion and the creation of new governmental organs. The size of the Chinese government will only continue to grow; it is time to

push for a redefinition of state functions and government structures.

What's interesting here is that China has a limited form of the ceiling control system. One of the methods for reducing government established in the 1998 reforms was the three-year support period for government affiliate organizations (*shiyè danwei*). After the three-year period, the governmental organs—with certain exceptions, such as universities—were to receive no new budgetary allotment, but rather rely on market support (Yang, 2001). This is not a rational method for reduction and limitation, and it bears a striking resemblance to Japan's reduction of one bureau per ministry. In addition, each new Prime Minister has initiated his term with a new round of governmental reforms, downsizing the ministry-level and other organizations (1988, 1992, 1998, and 2003). Now each new government has fewer and fewer ministries than its predecessor. The 1998 reforms reduced the number of ministry-level organs to 29. Now the latest government has proposed a plan to again reform China's government agencies, further reducing ministries and commissions to 28. The reform package established a state property regulatory and management commission, a commission to regulate and supervise the banking industry, a commission to reorganize the State Development Commission, and a commission to fuse the State Economic and Trade Commission and the Ministry of Foreign Trade and Economic Cooperation into the new Ministry of Commerce. The Ministry of Commerce and the other new organs seem to exemplify the "Scrap and build principle."

These may not all signify an intentional use of a ceiling control mechanism, but this explanation is quite plausible. Moreover, what's needed in China now is to make this kind of reform an institutionalized procedure in a consciously formalized way. The real number of Chinese public personnel is still unclear, as there are military forces, Party organizations, mass organizations (such as the women's federation), and many service organizations (*shiyè danwei*)—such as hospitals, schools, universities, research institutes, and working units—beyond standard government organizations and staff. There is a great deal of data attempting to ascertain these figures (cf. Brodsgaard, 2002; Burns & Bowornwathana, 2001; Liu, et al., 1998). It is reasonable to say that the number is much higher than most counts, and lower in the ratio to population than most other countries, taking into consideration that China has a huge population and is still in a developing stage. Regardless of the exact figures, China can implement the ceiling control mechanism through the following procedures.

The first step is the separation of central and local government staff, local and national civil service

systems, party and government, government and business, government and social organizations, and mass organization, in conjunction with the functional separation policy. Secondly, the government can decide the total number of government organs and the total staff under the State Council. Within this limit, the State Council has a free hand to reallocate staff and reorganize the ministries. The State Council can also give discretionary power to the individual ministries within their allotment. In addition, the "scrap and build principle" should be kept for further reform. China currently has 28 ministries, though we should be aiming for 20, which is standard in most countries. Surely ceiling control could be implemented collaboratively with the deepening economic reforms. Many functions need to be transferred to the market, business associations and other social organizations, with the ceiling control system as an embedded mechanism to push functional transformation.

Chinese governmental reforms have a long way to go before we have a truly open and efficient modern government. What I have introduced and described here is one of the options for constraining and reducing the size of the government. The ceiling control could become an automatically embedded instrument for government size control. Now let us turn to the next topic, an institutionalized fusion system in central-local relations.

Central-local government relations are changing drastically, and the bargaining processes have been well documented (Lieberthal & Lampton, 1992; Lieberthal & Oksenberg, 1988; Shirk, 1993). Post-Mao reform has been incremental, pragmatic and consensus-oriented, not guided by an explicit vision of society (Kenneth & Oksenberg, 1992; Lampton, 1987; Shirk, 1993). However, there has been an irrefutable trend towards decentralization in the reform era. Some even say there is now a behavioral federalist system in China. But the establishment of federalism in China is not a feasible institutional option; even central-local relations lean more towards balanced power relations (cf. Montinola, et al., 1995; Oi, 1999; Wu & Zheng, 1995; Yan, 1992; Zhongguo xingzheng quhua yanjiuhui, 1995). Decentralization and economic reforms have undermined central government capacity, of which tax extraction power is a key indicator (Wang, 1994). On the other hand, scholars argue that there has been an increase in the central government's political and administrative powers (Edin, 2003; Huang, 1995, 1996, 2002; Li, 1997). The economic, fiscal decentralization has been accompanied by a reinforcement political control system and cadre management. Local officials are, in fact, appointed by the central government, and only in the formal procedures selected or elected by the local

people's congress. Examining the fiscal relations, let us see if there is a possibility for the fusion system or decentralization-fusion system in China.

The local government's share of taxes and other revenues in the Mao era, even with oscillation between centralization and decentralization, constantly exceeded the central government's share. The central government's expenditure during the Mao era usually exceeded that of local governments (Dong, et al., 1996; Yang, 1994). So in the Mao period, local governments collected more taxes, but the central government spent more. This is the opposite of the Japanese case examined earlier. In the post-Mao era, this basic pattern has been changed. The central government's revenue share declined to 30-40%, and local governments' expenditure share increased to around 60% in 1990. We have also seen a decline in central control of investment during the reform era. Many studies show that local governments now collect more, use more, and use it with more discretionary power (Chung, 2001; Wang, 1994; Yang, 1994; Zhang, 1999).

Here, the most important thing is not only revenue, but also expenditure and resource and investment discretion. In the reform era, the local governments have become more and more development-oriented and entrepreneurial, and the central government is far more tolerant of the freedom of local governments in economic matters (Oi, 1999; Su & Yang, 2000). With the dwindling intergovernmental fiscal transfers from the central government, local governments have become financially more self-reliant, and so local governments are driven to employ a wide array of tools to obtain resources. But with the decline of its capacity, the central government lost control of aggregate investment demands and the national economy, resulting in growing regional inequality (Dong, et al., 1996; Wang, 1994; Wang & Hu, 1999; Yang, 1994). In 1994, China saw fiscal reform and establishment of the tax-sharing system (Shirk, 1993; Wang, 1997; Yang, 1994). The reform was targeted at increasing the share of central government revenue to 60%, in which 40% (two-third) was to serve as central government expenditure and 20% (one-third) as transfer grants to local governments. This means local governments have a 60% share, with 40% collected by themselves and 20% transferred from the central government (Yang, 1994). It is not a move back to the Mao era. The interesting thing is that the target ratios are almost identical to those in the Japanese case (see Figure 6).

In this new system, taxes are divided into three different categories: central, local, and shared taxes. The central and local governments' revenues have different coverage. The central and local governments have parallel systems for collecting taxes

independently, and the shared taxes are collected by the central government and then divided between the central and local governments, according to certain formulas. This reform was implemented to replace the discretion-based revenue-sharing system with a new rule-based system. After the reform was applied, the collection of taxes by the central government reached one-half, up from one-third of the total. Adding the remittance from local governments, the central government's share is argued to reach about two thirds. But here, the central should refund the local governments for revenue losses, as stated in the 1994 system deal. After this refund, the central share of total revenue is about 20-30% (Wang, 1997).

Officially, there is a separation of the local and central expenditures according to their different governmental functions, but this is not truly a rule-based system (Wang, 1997). There is no constitutional arrangement to constrain the central government. So, for instance, there is an ambiguity concerning the division of expenditure responsibility. The central government could transfer the responsibility to a local government without grants or subsidies. Also, the central government still has the power to decide the rates and the base of all taxes, including local ones, so local governments have no independent taxing power. The central government could take back the rights of the local governments at any time. As it stands, there are still discretionary powers wielded exclusively by the central government, and transfer arrangements are complicated by local remittance for the central government and central subsidies for local governments.

So while there is a transfer function in the central-local relations, it is not clear on the receipt of the transfers. In a sense, the tax-sharing system has just dressed-up the old system, because it relies on the central government to guarantee each local government a minimum base revenue. They used the 1993 tax revenue to establish the baseline-figure method (*jishufa*) in determining the allocation to local governments. Many have argued that it needs to be changed to a formula-based factor-analysis method (*yinshufa*) (Chung, 2001; Wang, 1997). Most important for the discussion here is that if we see this as the direction of reform, then we can predict further decentralization (or local autonomy), and the fusion system could quite easily be implemented.

Although it is desirable for local authorities to meet their expenditures using their own taxes and other revenues, there is a very large difference in the financial capability among local governments (Dong, et al., 1996). In order to equalize revenues among local governments and keep a standard level of public services, the central government should redistribute resources and grant a certain portion of collected

finance as national tax to local governments. Regional inequality is a serious problem in China now, where it is said that the First World and Third World coexist. Unless the central government is able to regain control over the redistribution of resources, the trend of divergence is unlikely to be reversed. Government intervention is imperative for promoting balanced regional development (Wang & Hu, 1999). The new strategy for development in the western region is an excellent example.

The regional policy for even development should be carried or coordinated by the central government. This does not mean the central should do everything, but rather in some cases the central should coordinate regional policy. The central government should manage and finance the economic development program, but let the local governments implement the program. The way for enhancing state (central government) capacity is not through the recentralization of resource allocation, nor the recentralization of discretionary power, but through unifying standards for local governments. Under those standards or directions, local governments shall have discretionary powers appropriate to local conditions and able to meet local demands. This is known as "local adaptation" (*yindi zhiyi*) in China. The revenue could be collected by local governments and used by the local governments, while some could be collected by local governments and transferred to other local governments. The conditioned or restricted transfers will be used for purposes mandated by the central government with unified rules. This system has even been used in federalist countries. Total separation of central and local government is not an ideal structure, and it is not possible even in a federalist system.

Moreover, a strong central government is capable of enforcing all kinds of policies, including those exacerbating regional inequality by favoring the rich regions. The central government has strengthened its political and administrative power (Edin, 2003; Huang, 1995, 1996, 2002); however, those central regulation powers and resource allocation powers could be influenced by the local powers (cf. Li, 1997; Reed, 1982; Su & Yang, 2000). This is another reason why central-local relations have been increasingly marked by bilateral bargaining and compromises in China. Strong local interests can be transmitted to the central government by influencing those very channels through which the central government controls local governments. Local influence of the center is similar to the Japanese system, but different in formation. The so-called interdependence -(mutual dependence between central and local governments) does not inherently entail equality between central and local governments and between each local government. So it is probable in some circumstances for greater

resources to go to those provinces that boast greater representations in the center. Therefore, it is important to have institutional arrangements free of such biases (Su & Yang, 2000; Wang & Hu, 1999;).

As stated before, in China there is no clear division between the responsibilities of the local and central governments and no constitutional arrangement to constrain the central government. So we can argue that China is actually functioning with a fusion system of central-local governmental relations. This feature can be seen in most of the unitary countries. So, what China needs is an institutionalized intergovernmental relations system, in which the central government delegates public affairs to local governments with unified forms and rules. Standardized public services should be provided through all local governments, whose even development should be guaranteed in institutional arrangement by the central government and delegated to local governments. This is not a unique idea. In fact, an arrangement entailing the delegation of government affairs to local governments, with a legal and institutionalized form, has been discussed before (Li, 2003). With this kind of reform, the decentralization-fusion system would very probably be adopted. It should be noted that the local autonomy of local governments (*difang zizhi*), in constitutional sense, has never been formally recognized in China, except in certain ethnic areas.

In Japan, as in many other countries, those administrative policies governing the infrastructure of most people's daily lives, such as those related to welfare, education (elementary schools), fire protection, roads and waterways, are generally implemented by local public organizations with their local budgets. Local public organizations are at the forefront of issues, such as enhancing community welfare. With an aging population, welfare services will expand and service delivery will mostly depend on the local governments, even if it will be financed or regulated by the central government. The Local Allocation Tax system in Japan was put in place by the national government, to equalize revenues among each local government and keep a standard level of public services.

For reforms of Chinese intergovernmental relations, the agenda should now focus on the institutionalization of resource redistribution, the assignment of expenditure responsibility, and the rule-based delegation of public affairs. Revenue allocation to local governments should be changed to a formula-based, factor-analysis method, with an equalization effect. In addition, there is no department or commission in the central government for the overall coordination of policy planning and implementation over local development, although there is some informal interagency policy consultation and

coordination and policy input and analysis by the think tanks (Lieberthal & Lampton, 1992). There is no central agency in China to coordinate local government affairs, such as a local government affairs ministry or commission. This lack of coordination is exacerbated by the cleavages in demarcation of functions and boundaries (*tiao-tiao and kuai-kuai*), corresponding to the different hierarchical chains (Lieberthal, 1995; Unger, 1987). This has certainly contributed to the complicated negotiations and bargaining. The control of local government affairs should not depend on ad hoc negotiation by central ministries, but on an institutionalized coordination system by a comprehensive department or commission.

Concluding Remarks

I have tried to show in this paper that to eliminate the two "mysterious circles," the two frameworks constructed and practiced in Japan for controlling government size and improving central-local governmental relations could be practiced in China. China could introduce the ceiling control system to fix the total number of departments and the maximum number staff. Under this kind of ceiling control system, the central government will transfer more economic affairs to the market and society, and transfer more administrative affairs to local governments. The ceiling control will work as an embedded constriction mechanism. In addition, China could introduce the "fusion system" in central-local governmental relations that is practiced in Japan. Surely these two aspects, government size and central-local relations, are intrinsically related, as local bureaucratic expansion has taken place both horizontally and vertically. By adopting the suggested reforms, the two "mysterious circles" will be eliminated, the Chinese government will be leaner and more rule-based, the frameworks for generating further reforms will already be in place, and China will be closer than ever to having a modern, efficient government.

Guirong Mao is Associate Professor at Department of Political Studies, Faculty of Law, Meijigakuin University (Japan)

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