

“Functional Socialism” and “Functional Capitalism” — The “Socialist Market Economy” in China —

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Based on a framework that conceives of ownership (property rights) as “a bundle of rights,” We propose four types of ownership system, build concept models of “functional socialism” and “functional capitalism,” and then try to clarify the reality of China’s “socialist market economy.”

We reached the following conclusions. First, we schematize the correspondence between “functional socialism” and “functional capitalism.” Second, we show that a process of land ownership reform and state-owned enterprises reform corresponded with a schema of “functional capitalism.” Third, we found that the ownership structure of the “socialist market economy” in China is now separated into three different sets of rights regarding ownership (property rights). Finally, we show that the reality of the “socialist market economy” is not a free market, but a market controlled by the Communist Party.

Keywords: market socialism, state capitalism, property rights approach, land ownership reform, reform of SOEs (state-owned enterprises)

1. Introduction: analytical viewpoint¹⁾

Following the remarkable rise of China’s economy, there has been an increase in discussion about the diverse forms that capitalism can take.²⁾ However, when one considers that China calls its own system a “socialist market economy,” one may wonder if it is better to think about the multiple forms that socialism can take. In

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1) For more on this section and the next, see Takeshita (1992), pp.1-6.

2) For more on the discussion regarding the diversity of capitalism, see Boumol, Litan, and Schramm (2007).

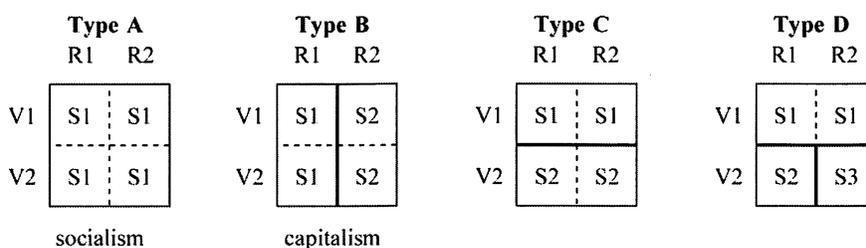
this paper, we intend to present two ideas of “functional socialism” and “functional capitalism,” as tools by which to understand the diversity of economic systems; in order to check the validity of these ideas—especially the latter, “functional capitalism”—we intend to clarify the actual state of China’s “socialist market economy,” while focusing on the system of ownership, which is the main factor in an economic system.

In *Comparative Economic Systems*, economic systems are generally classified by two axes: ownership system and resource allocation system (or mutual coordination system). The focal point of ownership system is private property or state property (public property), and that of resource allocation system is market or planning. As a result, there are thought to be four kinds of economic systems: capitalist economic system (private property and market), socialist economic system (state property and planning), planned capitalist economic system (private property and planning), and market socialist economic system (state property and market). According to this schema, contemporary China’s economic system is a market socialist economic system of state property (public property) and market—or, as they call it in China, a “socialist market economy.” The definitive split between capitalism and socialism is found in their ownership system—that is to say, whether ownership is private or state (public). In reality, in contemporary China, the “socialist market economy” is structured with a public property system at its core. In other words, the “socialism” of the “socialist market economy” is secured by putting a public property system at the core.

In this way, the largest factor regulating the “socialist market economy” in contemporary China is thought to be the ownership system. We would like to consider the reality of China’s “socialist market economy” from the viewpoint of the ownership system and understand ownership rights not as a question of the “real sphere,” but essentially as a question of the “control sphere.”³⁾ However, in the “control sphere,” “control-ability” in general is not equivalent to ownership; in the “control sphere,” even within “control-ability” in general, ownership rights become equivalent to “control-ability” only after having overcome harsh conditions. In other words, the notion of ownership is equivalent to a more limited (and stronger) idea of “control-ability.” As we attempt to clarify the peculiarities and points in question regarding ownership systems, our starting point will not be an ordinary degree of “control-ability,” but the concept of ownership in this meaning.

3) The idea of the “real sphere” and the “control sphere” comes from Kornai (1971). Furthermore, “control-ability” as a basic category of property rights (ownership) comes from Yoshida (1981). Again, for a fuller discussion about ownership system frameworks, including these, see Takeshita (1987) and Takeshita (1992).

First, I would like to raise five points (elements) that provide a basic overview of analytical frameworks, through which to consider systems of ownership: subjects, objects, contents, belonging, and justification (reason). For the first, subjects of property, we may consider different systems of classification: for example, private individuals, collectives, and corporate bodies; corporate bodies, natural persons, and unincorporated groups; or higher-ranked subjects and lower-ranked subjects. For the second, objects of property, we may consider material resources, information resources, human resources, and relational resources. The third, contents of property, encompasses a set of multiple rights that comprise the content of ownership, including the right of exclusive possession, right of use, right of revenue, and right of disposition, as well as multiple concrete rights that fall under each of these larger rights (i.e., a bundle of rights). The fourth, called belonging of property, is a little more arcane, but relates to when the contents of property concerning the object of property belong to the owner, and depends on whether that belonging is exclusive or non-exclusive, whether or not there is a time limit, and the length of such a time limit, if there is one; generally, exclusive, unlimited belonging leads to stronger ownership, and non-exclusive, short-term belonging leads to weaker ownership. The final point, justification of property (reason) concerns whether specific ownership is socially accepted in the society concerned, in consideration of any social norms or social values (e.g., freedom, equality, or efficiency).



Note: S, R, and V represent subjects of property, objects of property, and contents of property, respectively. Additionally, the dotted line shows "comprehensiveness," and the solid line shows "division."

Source: Yoshida (1981) p.232, edited and revised.

Figure 1: Four types of ownership system

To understand what kind of ownership systems could be considered in practice, we can draw the four types of ownership systems (Figure 1),⁴⁾ by focusing on the

4) Yoshida's (1981) "Theory of property rights structure" conceives of itself as part of "Theory of social system" and asserts that the concept of "social control-ability" is positioned as basic category of "theory of

four points of subjects, objects, contents, and belonging. To simplify, here we will assume that the property contents of the property objects belong entirely to the owner (i.e., completely exclusive belonging). Furthermore, although subjects, objects, and contents of property in Figure 1 have been portrayed as limited, in reality, this is not the case. Above all, in the analysis of ownership systems, it is important to keep in mind that, as pointed out above, the contents of property can be very diverse.

In figure 1, Type A represents objects-comprehensive and contents-comprehensive ownership. As a concrete example, in the notion of centrally controlled socialism, state ownership is thought to apply. In this situation, S1 is the state (or collectives). Type B absolutely epitomizes the absolute modern property rights in a modern civil society: they are objects-divisible (i.e., division of the tangible entity) and contents-comprehensive (i.e., freedom of usage, enjoyment of yields and disposition), with comprehensive belonging (completely exclusive belonging without time limit). Type C represents objects-comprehensive, contents-divisible property rights—for example, the separation of ownership and management typical in a modern capitalism (V1 = stockholder's right, V2 = right of management; S1 = the shareholders, S2 = the manager). Type D represents objects-mixed and contents-divisible ownership, as seen in the decentralization of socialism, with state ownership and management by state-owned enterprises. In this instance, V1 is superior authority (ownership), V2 is for middle to lower level authority (management rights), S1 is the state, and S2 and S3 represent state-owned enterprises. Logically, objects-divisible and contents-mixed ownership are conceivable, but this is not shown, because in reality there has been a mix of Type B and Type C; absolutely no other type of ownership has manifested.

2. “Functional socialism” and “functional capitalism”

In this paper, contemporary China's “socialism market economy” is understood by using the idea of “functional capitalism.” First, we will explain the idea of “functional capitalism” and show how it relates to the analytical framework and typology of ownership systems.

First, we deliberately present here the idea of “functional capitalism” as a response to the idea of “functional socialism.”⁵⁾ The idea of “functional socialism” was itself initially introduced in the 1960s and 1970s, when the illusion of approaching a

property rights structure.” In this paper, what is described in “theory of property rights structure” as “a simple formation model of ‘the first structure of control-ability’” is used as “the four types of ownership system” (Figure 1) to simplify the discussion.

5) For more on “functional socialism,” see Adler-Karlsson (1967).

socialist economic system was still strong, as a way of thinking where there was no need for revolution in order to establish socialist ideals, and that there would be no harm to the form and essence of capitalism, or its accomplishments. In other words, there was the thinking that it was possible to substantially implement socialist functions peacefully and gradually. This way of thinking is explained by Swedish economist Gunnar Adler-Karlsson (1967) as “functional socialism,” through the partial socialization of various functions; he does so by using the idea of ownership, wherein “ownership is usually viewed as an indivisible concept, … ownership should instead be viewed as a divisible concept which covers a number of functions which an owner potentially may exert over an owned object,” that is, “ O equals functions a plus b plus c , etc. or $O=a+b+c+\dots+n$.”⁶⁾

This way of thinking is similar to the perception of the property rights approach as one in which property rights (ownership) are understood as “a bundle of rights.”⁷⁾ According to this way of thinking, fundamentally, when various rights completely and exclusively belong to specific individuals, this constitutes modern ownership (Type B in Figure 1), and when exclusivity is weakened, or attenuated, various property rights connected to the implementation of various functions spring up to proportionately weaken it again (Type A, Type C, and Type D in Figure 1). “Functional socialism” could be described as being on the line of this perception of ownership.

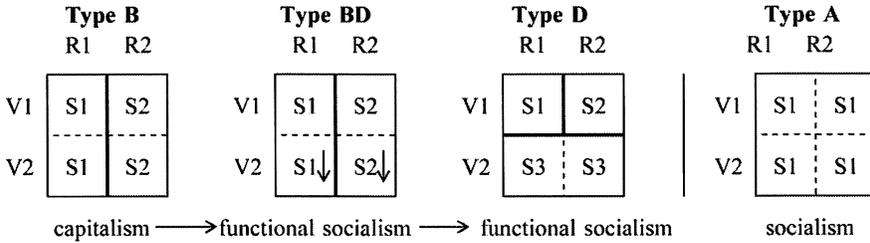
In the 1960s and 1970s, the idea of “functional socialism” was a guiding principle of social democratic parties in Scandinavian countries such as Sweden, which were implementing social democratic policies. The “functional capitalism” way of thinking is a response to this idea of “functional socialism.” Accordingly, “functional capitalism” is the implementation of what are for all intents and purposes capitalist functions, while preserving socialism as a structure. Expressed in response to the aforementioned “functional socialism,” it may then be understood as a way of thinking whereby capitalist functions are implemented by partially privatizing various functions that had been held by the socialist state, and transferring them to private sector (individuals and private enterprises).

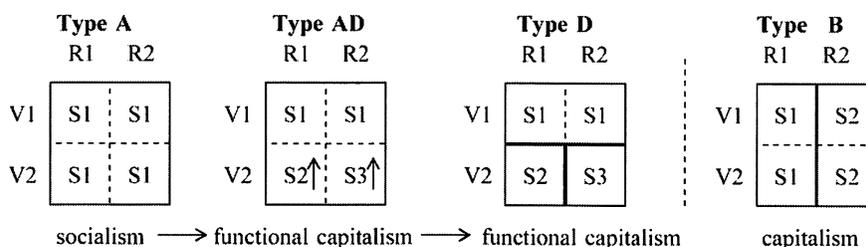
In order to understand at a basic level the relationship between “functional socialism” or “functional capitalism” and the analytical framework of ownership systems, the first thing to understand is that in this framework, the functions such as a , b , c , constituting ownership in functional socialism, are equivalent to “contents of property.” To “socialize parts of the functions” means that the contents of property

6) Adler-Karlsson (1970) pp.37, 50 ; Adler-Karlsson (1967) pp.25, 65 (in Japanese version).

7) For a good example of this way of thinking, see Barzel (1997).

are divided, the divided portions are possessed by different subjects, and the “exclusivity of belonging” is restricted (to that extent, it means to weaken ownership). To schematize this using Figure 1, “functional socialism” can be depicted as shown in Figure 2.





- Notes: 1) The meanings of the abbreviations and dotted/solid lines are the same as those in Figure 1. Arrows pointing upwards show the strengthening of appropriate contents of property (V)—in other words, the strengthening of the exclusivity of belonging. Regarding other contents of property, completely exclusive ownership applies.
- 2) S1 in Type A, Type AD, and Type D represents the state or collectives (groups), while S2 and S3 represent individuals. In Type B, S1 and S2 also represent individuals.

Figure 3: “Functional capitalism”

In Figure 3, the Type A on the left side type shows state property (public property), which is the typical form of ownership under socialism. “Functional capitalism,” as shown in Type AD, generally tries to provide incentives and strengthen the functions (V2) of the individual or private enterprises (S2, S3) under the condition that there would be no damage to the system of state property (public property). Additionally, as shown in Type D, property contents are divided into those (V1) where the system of state property (public property) has been maintained and those (V2) where it has not been maintained; the former (V1) are left with the state (S1), and the latter (V2) are transferred to individuals or private enterprises (S2, S3). In this way, “functional socialism” and “functional capitalism” can be understood in similar terms within the framework of the ownership systems, if one acknowledges that reforms are moving in absolute opposite directions. Logically, as with functional socialism, functional capitalism does not switch over to capitalist ownership (Type B) as shown on the right side. However, in practice, in the former Soviet Union and in Eastern European countries, that line was crossed. How should one make sense of this? Could there be a crucial difference between “functional socialism” and “functional capitalism”? What is the current status in China, and how might we expect it to change over time? Using the analytical framework described above and with an awareness of these issues, the object of enquiry will now be the progress of China, organized and considered with a focus on the ownership system.

3. China's land ownership system: state ownership and collective ownership⁸⁾

In order to address the question of property rights (ownership) in China, we would like to start with the question of land ownership, which is the foundation for property rights questions on the whole. Modern China's land ownership system was established in the 1982 "current Constitution" (article 10) and 1986 "Land Management Law" (article 2), such that public property takes two forms: state land ownership (all people's ownership) in urban areas, and collective land ownership (farmers' collective ownership) in rural areas. There no private ownership is admitted. To understand these basic structures of state ownership and collective ownership, one starting point is to think about each of the five elements of ownership(property rights) that follow the framework for analyzing ownership systems, as described in section 1: (1) subjects, (2) objects, (3) contents, (4) belonging, and (5) justification (reason).

First, state land ownership are defined in law by the state as the right to the exclusive possession, usage, yields, and disposition of state land. Regarding (1) the subjects of property rights, state property is owned by all people (i.e., all people's ownership), and so all citizens of China have the right to exclusively own, use, derive yields, and dispose of their own land through the state. However, in practice, the subject of state land ownership is "the state as the representative of the will and interests of all people." Namely, the state is the subject that exercises ownership as the representative of all the people, by the trust of the people. In concrete terms, the State Council of the People's Republic of China—which is the government of the Chinese people—is the sole representative of state ownership, and each regional government exercises ownership as a representative of the state, as authorized by the State Council.

Regarding (2) the objects of property, in article 10 of the Constitution and article 8 of the Land Management Law, the objects are all land in each urban area, and land within urban city limits. Outside of this, the Law of Realty⁹⁾ makes clear that other three types of land are added as the objects of state property; land occupied by state-owned businesses, energy, transportation, waterways; land occupied by state-

8) For more on China's land ownership system, the studies of Oda (2002) and Oda (2004) are valuable, in that they systematically consider the history of China's land system and the problems and peculiarities of land reforms. Additionally, Wang and Huang (1996) and Fu (2006) also offer valuable information on the history, status, and problems of China's land ownership system. This section uses these studies for reference.

9) On the problems and peculiarities of the law of realty in China, as enacted in 2007, see the essays collected in Hoshino, Qu, Tanaka, and Liang (2008).

owned cultural, health, educational, and military facilities; and non-developed or otherwise-unauthorized land as collectively owned land.

Regarding (3) the contents and (4) belonging of property, property contents comprising exclusive ownership, usage, yields, and disposition belong entirely and exclusively to the state. In other words, state-owned land is eternally state property, and the state cannot transfer or renounce its ownership of state property. However, as will be mentioned later, in 1988, the Constitution and Land Management Law were reformed, and ever since the “land use rights system”—which allows for the separation of “rights to own (ownership)” and “rights to use (use rights)” land—it has been possible to transfer the use rights of state property, for a fee. Finally, regarding (5) justification, this is genuinely a major problem; however, here, undertaking a structural analysis of ownership is the main point of analysis, and so for the time being, we will simply state that the whole of communist ideology is the reason for justifying state ownership.

Next, collective ownership of land in rural areas is the right of farmers’ groups within the law to exclusively own, use, derive yields from, and dispose of their own land; the land is not entrusted to any individual within the organization, nor is it jointly owned by the members of the organization. In other words, because it belongs to the entirety of the organization, the land cannot be divided, and even if the membership of the organization were to change, there is no change to the ownership rights themselves. (1) The subjects of collective ownership is defined as “collective ownership” according to article 10 of the Constitution, as prescribed; however, there is no unitary subject of collective ownership as a whole of China, and it is influenced by its formation process and more complicated than the state land ownership. If one were to consult related laws such as the Civil Law Principles (article 74, clause 2), the Land Management Law (article 10), and the Agriculture Law (article 11), one would see that the subjects of collective ownership is one of three kinds of farmers’ groups: a “village farmers’ group,” a “township and village farmers’ group,” or an “economic organization of farmers’ group.” However, in each law, the organization and structure of these groups (collectives) are not clearly defined. In any case, in contrast to the unitary nature of state ownership, in each area and district, there are tens of thousands of farmers’ groups that are the subjects of property.

(2) The objects of property are land in farm villages and suburbs of towns and cities. Regarding (3) the contents of property, the owner more or less has the right to exclusive possession, usage, yields, and disposition of the collectively owned land, but collective land ownership rights are not complete ownership rights, and they can use the land only for agricultural production, while abiding by the state’s agricultural

policies and arable land protection policies. Additionally, (4) belonging of property is considerably limited; for example, the only way that land can be transferred is through expropriation by the state, and abandoned land automatically becomes state property. Considered from this perspective, it is understandable that collective land ownership has a lower position than state ownership. This point, as we will explain below, can be seen even in the application of land use rights for development purposes. Finally, regarding (5) the justification of property, although I would like to bring up communist ideology as the rationale—just as it was the reason for state ownership—I would still add one more point in relation to the fact that agricultural land was made into collective property, rather than state property. It is thought that agricultural land became collectively owned as a consequence of political compromises made with farmers: the success of the revolution was indivisibly connected to their support, because the Chinese revolution had developed from bases in agricultural communities.

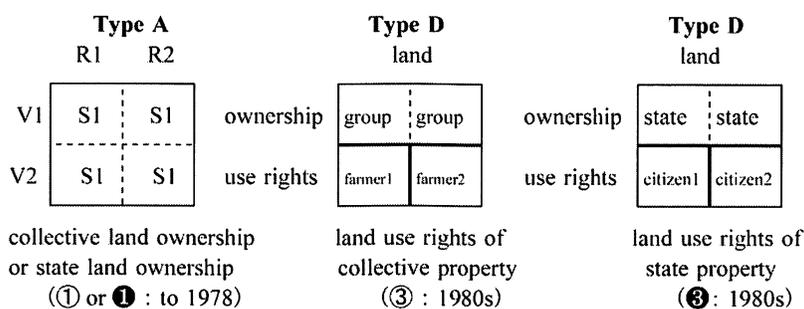
If one were to schematize the state ownership and collective ownership of land into the ownership system typology, although the ownership of the former would be superior to the latter, the types would both be considered objects-comprehensive, contents-comprehensive ownership (Type A), as shown in Figure 1. Of course, in that case, it goes without saying that the subject of property (S1) would be the state in state ownership, and farmers' groups in collective ownership.

4. Ownership and rights to use¹⁰⁾

In modern China, the two basic forms of public property system for land as defined in the current Constitution (1982) and the Land Management Law (1986) have not changed from the time of the Reform and Opening-up Policy until the present day; nonetheless, the contents of property rights have changed a great deal. In the 1988 reforms to the Constitution and the Land Management Law, based on the reality of economic activity after the Reform and Opening-up Policy (such as the farmers' household responsibility system) the "land use rights system" was established, recognizing a separation between "ownership" (rights to own) and the "use rights" of land. Since then, by maintaining and reforming laws relating to land, eventually, "Law of Realty" was established in 2007, and the current land tenure system with a separation of ownership and the rights of use (usufruct) appeared to be more or less complete. We would like to organize and investigate the fundamental struc-

10) This section also uses, as mentioned above, Oda (2002), Oda (2004), Wang and Huang (1996), and Fu (2006) for reference.

ture of the land ownership system under the Reform and Opening-up Policy (the structure of “separation into the two rights” of rights to own and rights to use) by comparing it to the fundamental structure of the land ownership system at the time that the Reform and Opening-up Policy went into effect.



Note: The meanings of the abbreviations and dotted/solid lines are the same as those in Figure 1. The word of “group” means the collectives as the subjects of collective ownership.

Figure 4: Land ownership and land use rights

To begin with, the basic land ownership system is a “land use rights system,” whereby the contents of property are separated into “rights to own” and “rights to use” land. First, regarding land ownership relationships under the socialist system of public property, the rights to use property approved formally for state property in urban areas are the “land use rights of state property” (use rights for building lots), and the rights to use approved similarly for collective property (“farmers’ group property”) in rural areas are the “land use rights of collective property” (rights of responsibility for collective property). The use of all land is controlled in order to ensure rational use; land resources have been separated into “agricultural sites” (farming areas), “construction sites” (urban areas), and “unused sites”; land use zones are defined according to a comprehensive land use plan; and restrictions on land use rights are agreed upon. Besides the land ownership rights mentioned in the previous paragraph, if one were to schematize “land use rights of state property” (construction site use rights) and “land use rights of collective property” (rights of responsibility for collective property) according to the ownership system typology, they would appear as shown in Figure 4. One can see how “functional capitalism” has progressed, if one looks at the correspondence between the Type A and Type D ownership in Figure 3, and the Type A and Type D ownership in Figure 4. In each case, there were two contents(rights) of property —namely, “land ownership rights of collective

property” ① and “land use rights of collective property” ③, and “land ownership rights of state property” ④ and “land use rights of state property” ③.

In Figure 4, both “state land ownership” and “collective land ownership” are shown as the same type of ownership rights as Type A (as mentioned above), and “land use rights of state property” and “land use rights of collective property” are also shown with the same structure. Therefore, at first sight, the use rights and ownership rights appear to be equivalent both in collective and state property. However, in practice, because originally in land ownership “state land ownership” has taken priority over “collective land ownership,” also in land use rights, “state land use rights” have taken priority over “collective land use rights.” For example, obtaining land use rights for new developments on land in urban areas is limited to land that has been defined as “construction sites” (“state land use rights”); this is made apparent by the fact that no “collective land use rights” have been approved for development. In the process for obtaining land use rights for development, there are “transfers” (disposal sale) and “allocations.” Land use rights for purposes such as urban infrastructure and land for military use are assigned (allocated) with an indefinite term of use, but for general residential, commercial, and industrial purposes, state land use rights are generally obtained through transfers. As a rule, it was decided to transfer land use rights not through consultation forms, but through a price competition process by means of bidding, sale, or public notification. However, in practice, there has generally been a consultation process in the same way as until now. Furthermore, when land use rights are acquired, retained, or transferred, taxes are paid—such as a sales tax (contract tax), a land use tax, or a land increase tax. On the other hand, when carrying out a new development in the suburbs of towns and cities, land must first be changed from farmers’ group ownership for agricultural use into state ownership, and then converted into a construction site, before going through the transfer process for land use rights.

The difference of position with regard to “land use rights of state property” (construction site use rights) and “land use rights of collective property” (rights of responsibility for collective property) has produced the characteristic phenomena in contemporary China.¹¹⁾ Although a great deal of land has been required for economic development and urbanization in China—which has undergone rapid progress since the Reforming and Opening-up Policy—the transfer and trade of “land ownership” is

11) In contemporary China, many problems have arisen in relation to land and politics, such as excess land development by regional governments—something born of the distorted land system and subsequent over-dependence on land finance, large agriculture site levies, farmers’ loss of farmland, and a sudden drop in the amount of available arable land. For more on these problems and an analysis that takes up “land politics” by using agency theory, see Ni (2012).

not permitted, as is to be expected in a country that still adheres to its socialist public ownership system. For this reason, a rapidly increasing demand for industrial, commercial, and residential land has been met by the obtaining of “land use rights”; although the only thing that can (legally) respond directly to demand in urban areas is the “land use rights of state property,” this is quantitatively inadequate. In practice, high demand is quantitatively and economically advantageous with regard to agricultural land on the suburbs of towns and cities; however, “land use rights of collective property” (rights of responsibility for collective property) cannot legally respond directly to demand. Because agricultural land is farmers’ group property, it is necessary to go through the process of converting it into a state property construction site. Under the Land Management Law, land registration, management authority, use authorization authority, and the authority for the disposition of illegal acts are all centralized—not at the central or provincial government level, but at the administrative level below the province (i.e., the city, prefecture, or village, especially the prefectural government). In other words, because various interests and rights are centralized at the city, prefecture, or village administrative level, a real-estate bubble has appeared in a way that is unique to the conditions of China.

In this way, on the one hand, it is clear that the different positions of ownership and use rights are connected to problems such as the real-estate bubble and land finance dependence of the prefectural governments, but on the other hand, it is also clear that the separation of land ownership and use rights is one of the keystones of the Reform and Opening-up Policy; this is part of what has driven the high rate of economic invigoration. That is to say, in the planned economy system before the Reform and Opening-up Policy, the separation of land ownership and use rights was absolutely never accepted, and the rational distribution and efficient use of land was obstructed in order to supply land, without compensation, for use by businesses or farmers, and for an indefinite length of time. In China’s public property system, the groundbreaking scheme and policy that helped resolve this problem was the establishment of the “land use rights system,” which separated use rights from land ownership. It would be no exaggeration to say that, subsequently, China’s progress to date from its Reform and Opening-up Policy, as well as its accompanying radical economic development, have been pushed forward by the separation of ownership and use rights—a separation associated with two sets of land use rights (i.e., land use rights of state property and collective property). Focusing on this point, in sections 5 and 6, we would like to discuss in detail the progress of land ownership system reforms in rural areas, and state-owned enterprise reform in urban areas.

5. Reform of the land ownership system (rural areas)¹²⁾

China's Reform and Opening-up Policy was started in December 1978 by the Third Plenum of the Eleventh Central Committee, under the leadership of Deng Xiaoping. The consistent directions of the Reform and Opening-up Policy were reforms towards marketization which include the removal or cutting of instructive factors from economic planning administration and the introduction of a flexible pricing system that reflected supply and demand; however, at the same time, in order for the market to function effectively, one precondition was a process by which to advance concurrent reforms to property rights. The property rights reforms in China included reforms to the land ownership system in rural areas, and reforms to state-owned enterprises in urban areas. Agricultural community reforms began with moving the administration units for agricultural production from people's communes to farmers, and introducing an "every house production contract system," to incentivize production increases. In the early 1980s, the production contract system spread rapidly and farmers' incentive to produce increased, bringing huge success. On the back of those results, from the mid-1980s, there was a rapid development in "township and village enterprises." During this time, coastal urban areas rapidly developed with the introduction of foreign capital, due to the policy of free-access zones; this rivaled the development of agricultural reforms and township and village enterprises, and even further advanced progress towards a market-oriented economy. Nonetheless, the reforms of the 1980s—especially those of the early 1980s—were primarily reforms in the non-state property and non-planning sectors; due to the success of the production contract system and the township and village enterprises, the gap between rural areas and urban areas was becoming smaller.

The movement to a market economy, which stagnated for a while after the 1989 Tiananmen Square Incident, was reignited in 1992 when Deng Xiaoping gave the "Southern Tour Lecture"; however, the central reforms that would lead to the establishment of a "socialist market economy" were finally moving into state property and planning sectors in urban areas. The progress of reforms in the 1990s and thereafter, along with rapid economic growth, led to a rapidly widening gap between urban and rural areas, and from the late 1990s to the early 2000s, the so-called Three Agricultural Problems emerged. Once again, the problems that agriculture, rural communities, and farmers faced were taken up on a grand scale, and full-blown

12) Oda (2004) is a most excellent work on the subject of China's agricultural land ownership system reforms. This section uses it for reference.

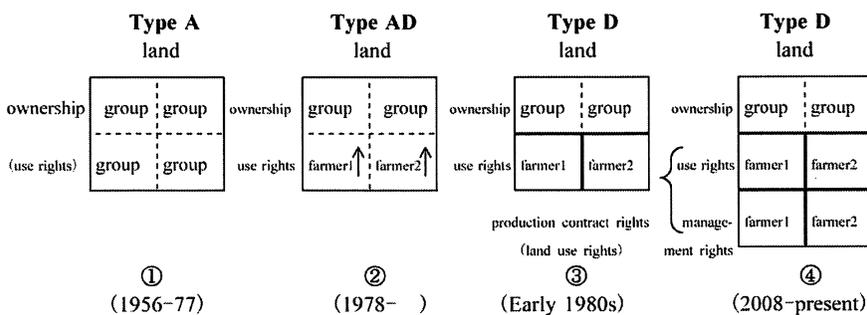
reforms were considered, leading to an acceleration of the reform movement. The Three Agricultural Problems—namely, the basic problems of agricultural underproduction, the decay of rural communities, and poverty among farmers—were in short due to the smallness of scale of agricultural management. In China's rural areas, given the limitations of traditional land ownership, the production contract system introduced in the early 1980s (rural use rights) had not been able to create sufficient change.

Land in China's rural areas (rural land) takes the form of "collective land ownership" (farmers' property system). From our perspective, collective property in rural China can be understood typologically, in the same way as state property in conceptual centralized socialism—namely, as an objects-comprehensive, contents-comprehensive ownership (Type A). The subject of property (S1) is the farmers' group (organization), and the farmers' group has the authority of disposition and management; although the individual farmers who comprise the collective (organization) have equal rights of use and yields under the collective, they do not hold shares and can neither claim a portion nor transfer that portion. Accordingly, even if collectively owned agricultural land were to have separate ownership and use rights, with farmers being granted use rights (production contracts), relocation of use rights would be subject to the consensus of opinion in the farmers' group to which a farmer belongs (i.e., a two-thirds majority of members or villagers' representatives). As a result, relocation of use rights (production contracts) and farmer's free choice of it would be greatly restricted. Even if relocation were approved, it would be exclusively for within one farmers' group. This peculiar characteristic can be attributed to the "principles of self-government and autonomy" approved in farmers' groups as a consequence of collective property, and across China, tens of thousands of such farmers' groups exist. To further complicate the problem, these "principles of self-government and autonomy" are, in reality, subject to a variety of regulations and restrictions, in line with the national government's "principles of guidance and guardianship." In rural areas that are engaged in this complicated state of affairs, the aggregation of agricultural land is not progressing; consequently, the farms are small, techniques are slow to modernize, production is low, and yields are not increasing. As a result, because many farmers are leaving the land for which they have use rights (contract) and seeking a considerably larger income in a town or city, agricultural land in China is decaying.

To resolve the Three Agricultural Problems, agricultural modernization policies have been advancing in recent years by virtue of the "fluidizing" of agricultural land

(i.e., making it easier for agricultural land to circulate).¹³⁾ This movement began in March 2003, when the “Agricultural Land Contract Law” was implemented, but real progress started in October 2008 when the “Central Committee decision regarding a number of great problems for the promotion of rural reform and development” was adopted by the Third Plenum of the Seventeenth Central Committee; thereafter, the relocation of farmers’ rights of management of land contracts was formally accepted for the first time. The most important aspects of agricultural modernization reforms due to the fluidization of agricultural land included conversion from a system of “two partitions” of land ownership and land use rights (contract rights) under “land use rights of collective property,” to a new system featuring the “three partitions” of land ownership, land use rights (contract rights), and land management rights; attempts to advance the aggregation of agricultural land and increases in farm size through the fluidization (circulation) of land management rights; and attempts to promote technological modernization. In other words, these new system reforms moved toward collective property, farming contracts, and pluralistic management, but since enforcing the “Farmers’ Specialist Cooperatives Law” in 2007, farmers’ cooperative organizations (e.g., farmers’ specialist cooperatives and farmers’ public limited companies, as well as trusts for incentives to promote land transactions) are now more frequently seen in several advanced regions, and there are now a variety of farm management choices available.

Using the ownership system typology, progress in land ownership system reforms



Note: The meanings of the abbreviations and dotted/solid lines are the same as those in Figure 1. The meaning of “group” is the same as that in Figure 4.

Figure 5: Reforms to the land use rights system

13) For more on recent movements in such agricultural modernization policies by means of the fluidization of agricultural land and the system of “three partitions” of rural ownership, contract rights, and management rights, see Guan (2008), Guan (2014), and *BTMU (China) Financial News* (2015).

in rural China following the Reform and Opening-up Policy can be presented schematically, as shown in Figure 5.

Figure 5 shows the process of moving from ① collective land ownership, via ② the stage of farmers' land use schemes with their original spontaneity, to ③ the stage of formally approved land use rights (production contract rights). This corresponds precisely to the "functional capitalism" in Figure 3. Furthermore, currently, reforms in collective land ownership in China are moving from ③ a "two partition" stage of ownership and use rights to ④ a "three partition" stage of ownership, use rights, and management rights, by a separation of management right from use rights. Namely, another step is being taken towards "functional capitalism," by separating management rights from "two partition" stage and attempting to increase liquidity and promote both rational distribution and efficient use.

6. Reforms to state-owned enterprises (urban areas)¹⁴⁾

Reforms to state-owned enterprises in urban areas also began with the Reform and Opening-up Policy, but the full-scale commencement of reforms to state-owned enterprises was spurred by the 1984 "Chinese Communist Party decision on economic system reforms." Although at first the reforms of the 1980s pushed progress in the direction of greater management autonomy while keeping the ownership system within state property, before long, these essentially limited and illogical reforms reached the limits of their efficacy. Thereafter, from 1987, a "contract system"—whereby profits delivered to the government are contracted in advance, and the excess amount is no longer returned to the government, but instead becomes the property of the enterprise—was implemented in almost all state-owned enterprises. However, even this had limited efficacy, in the wake of the unexpected Tiananmen Square Incident and a subsequent business slump. Reforms to state-owned enterprises in the 1980s were largely attempts to reproduce in state-owned enterprises in urban areas the success of the production contract system (land use rights) in rural areas; however, the contract systems of rural areas and state-owned enterprises were fundamentally different in terms of changes to the value of enterprise property, such that enterprise management can buy and sell enterprise property (e.g., land, buildings, equipment, manufactured goods, materials), whereas agricultural use rights did not involve the disposal of land itself.

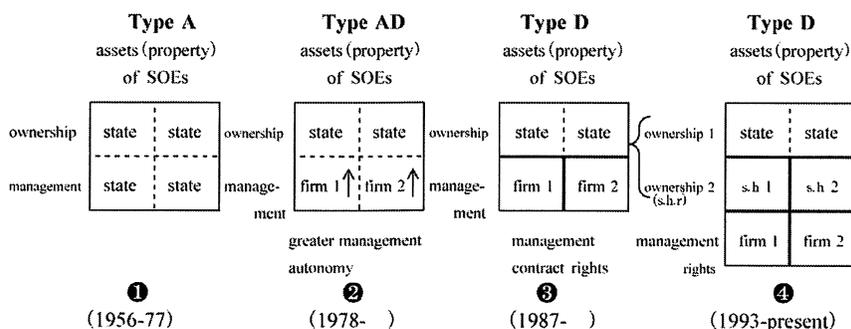
14) For more on the direction of reforms with regard to state-owned enterprises, see Xu (2008), Marukawa (2013), and Tanaka (2013)—in particular, chapters 8 (Complex governance of Chinese enterprises) and 9 (To protect state-owned property assets) of Tanaka (2013).

Reforms stagnated with the 1989 Tiananmen Square Incident. When they were revived by the 1992 “Southern Tour Lecture”—under a plan for “the establishment of a socialist market economy system” (the Fourteenth Party Congress)—a plan was set out for the establishment of a modern business system that contained “clarifying ownership, clarifying rights and responsibilities, separating administration and management of enterprises, and making management more scientific”. Attempts began at converting state-owned enterprises into public limited companies (i.e., the ownership reform of state-owned enterprises—namely, “shareholders’ rights” and “corporate property”). Having converted state-owned enterprises into public limited companies, there was a need for corporate law, which has two aims: the independence (efficiency) of corporate management by the separation of ownership and management, and the diversification of fund-raising. One consideration in the early stages of establishing corporate law was the introduction of shares (stocks) alongside a property system that ran on the principle of “putting a public property system at the core” and thus maintaining the predominance of the public property system. However, because the objective was set in 1992 for China to acquire World Trade Organization (WTO) membership, demand arose for the establishment of corporate law that followed global standards. As a result, corporate law was established in China in 1993 (and executed the following year); this was highly valued as a watershed moment in the history of law in China, as it removed differentiation in the ownership system by adopting the “equal treatment of shareholders.” However, regarding the problem of state-owned share management that could not be addressed with corporate law, new management stipulations were introduced by “temporary regulations on state-owned shares of public limited companies” (hereinafter referred to as temporary regulations), which was established in November 1994; it guaranteed that public limited companies reorganized from state-owned enterprises would, with some exceptions, have state-owned shares and be in a dominant position.

Since the establishment of corporate law, state-owned enterprises as parent companies have given rise to many public limited companies and their shares are listed on the Shanghai and Shenzhen Stock Exchanges (both established in 1990) and funds are accepted from any ordinary investor. Generally speaking, large-scale, state-owned enterprises have been made into groups that lie at the foundation of the Chinese economy. Almost none of the enterprises at the top of the groups have been made into public limited companies; either these top enterprises or the state retain the majority of shares in their subsidiaries and second-tier subsidiaries that have been made into public limited companies, and they thus reserve the right of management. Additionally, within Chinese shares, some circulate and some are non-circu-

lating. In public limited companies dominated by state-owned shares (e.g., state shares, shares of state-owned enterprises), the majority of shares are non-circulating. Furthermore, in legislation since the emergence of corporate law, there have been no laws that continue on this path, and even in the 2007 Law of Realty or the 2008 Companies' State-owned Assets Law, differentiation according to ownership was not removed; the latter seemed to elevate the status of the 1994 temporary regulations.

Chinese state-owned enterprises are divided into central enterprises managed by the central government (State Council) and regional enterprises managed by the regional governments, but save for affiliated finance companies (managed by the Ministry of Finance), the responsibility for the management of state-owned assets in practice falls on the State-owned Assets Supervision and Administration Commission of the State Council (hereinafter referred to as SASAC) and SASACs of each regional governments. Regarding the assets of enterprises managed by SASACs, this is prescribed by the Companies' State-owned Assets Law, but it has enlarged the scope of the stipulated business management of executive personnel, as the temporary regulations had specifically restricted the management duties of state-owned shares. In this way, while it might seem that corporate laws have removed differentiation within the property system, in practice, the dominance of the public property system (state property system) has suddenly been revived in tandem with the temporary regulations. From then until now, the principle of "putting the public property system at the core" has been firmly maintained, and it was an especially striking trend following the acquisition of WTO membership. This has given rise to a situa-



Note: The meanings of the abbreviations and dotted/solid lines are the same as those in Figure 1. s.h and s.h.r mean Shareholder and Shareholders' right, respectively.

Figure 6: Reforms to the ownership system of state-owned enterprises (SOEs)

tion in which one could say that “the state advances, and the private sector retreats,” rather than “the state retreats, the private sector advances.”¹⁵⁾

If the progress of ownership reforms after the Reform and Opening-up Policy regarding the above state-owned enterprises were to be schematized in terms of ownership typology, it would be as shown in Figure 6.

In Figure 6, Type A ownership ❶ shows obvious ownership of state-owned enterprises before the Reform and Opening-up Policy. State-owned enterprises existed only to carry out orders from the central government. Following the Reform and Opening-up Policy, the first movement toward reform was in the direction of increasing management autonomy in state-owned enterprises, thus aligning with stage ❷ of Type AD ownership. The next movement was toward a “management contract system,” introduced in 1987, that corresponded to the land contract system in agriculture; this aligns with stage ❸ of Type D ownership. To this point, it has proceeded in the exact same form as the movement in land ownership reforms in rural area, as shown in Figure 5. However, the stage ❹ reforms since the early 1990s did not, as with agriculture, create a separation between use and management, but fundamentally divided ownership itself. Following the establishment in 1992 of corporate law, the conversion of state-owned enterprises into public limited companies was promoted, but in centrally run companies and large state-owned enterprises belonging to the industries most important to the state, most of the stock in those state-owned enterprises that had been converted to stock was held by the state or by parent companies, who reserved the right of management. In centrally controlled enterprises and large state-owned enterprises, the state reserves control, because there are two types of stocks (shares)—namely, state-owned stock and non-state-owned stock. Moreover, there are circulating stock and non-circulating stock. On the other hand, small and medium-sized state-owned enterprises, the majority of which fell under the local government umbrella, were converted to stock, but because the local government participates in the board of directors of enterprises in which the majority of the stock is state-owned, the right of control is reserved; even if none of the stock is state-owned, not only will party organizations attempt to bridge the gap, but also the local government economic committee will become extensively concerned with technological innovation and fund-raising for management reform.

15) Although the data are a little old, according to the 2008 second industrial census, among the approximately 5,000,000 companies in China, about 75% of privately owned enterprises are outside the sphere of corporate law; the public limited companies within that sphere comprise no more than 15% of the total. Regarding privately owned enterprises, it is important to bear in mind that China has a system of public property for land; therefore, privately owned enterprises do not own land, and may obtain land use rights for only a limited period of time. For more on this, see Tanaka (2013), p.137 (see note 2).

In any event, with the reform of state-owned enterprises in a manner similar to that seen with the reform of the land ownership system in rural areas, steps ①–③ of the process shown in Figure 6 correspond to the process of “functional capitalism” shown in Figure 3. Movements toward stage ④ may be progressing or intensifying.

7. Conclusion

This paper focused on China’s ownership system—which constitutes the cornerstone of socialism there—in order to explain the realities of China’s “socialist market economy.” It also examined and considered the ownership system reform movement since the Reform and Opening-up Policy, based on the four types of ownership system and a five-point framework by which to analyze ownership systems. Four conclusions derive from this investigation.

First of all, based on these four types and five points, the main points of “functional socialism” and its corollary “functional capitalism” were schematized clearly (i.e., Figures 2 and 3, respectively). Between functional socialism and socialism itself, and between functional capitalism and capitalism itself, there exist large barriers that are difficult to overcome. That is to say, in focusing on the subject (SI) of Figures 2 and 3, it becomes clear that functional socialism (and accordingly, capitalism, which is its basis) is a society that fundamentally values individual freedom (self-determination), while functional capitalism (and accordingly, socialism, which is its basis) is a society that fundamentally values the guidance of the state. Therefore, it is natural that the barriers would be difficult to overcome.

Second, reforms to the land ownership system in rural China and reforms to state-owned enterprises in towns and cities were implemented at different times and in concretely different ways, but the path those reforms have taken to the present day accurately corresponds to the functional capitalism shown in Figure 3. In other words, the first stage of reforms and of functional capitalism is in separating the contents of property in socialist notions of property, to create “two partitions” of use and ownership, or management and ownership; the land ownership system reform, and the reforms to state-owned enterprises, followed the exact same process. The next stage pertains to the “three partitions” of management, use, and ownership—or, management, ownership 2, and ownership 1—and this construction of property corresponds to the stage of the “socialist market economy.” Accordingly, the construction of property, which constitutes the very foundation of a “socialist market economy,” is extremely unique to contemporary China; one could even say that a new construction

of property is being carried out there.¹⁶⁾ However, I would be unable but to say that these were created as desperate measures, while adhering to socialist ideology and maintaining the public property system.

Third, the three periods of Reform and Opening-up Policy correspond to land reforms and ownership reforms.¹⁷⁾ The first was in the 1978–84 period, during which only markets within the limits of a planned economy were permitted (planning > markets); in that planned economy, land ownership by allocation held a central position. The second was in the 1985–92 period, during which regulation and markets attained equal positions (planning = markets); this was a period established from the draft deliberation of the Land Management Law (i.e., arguments over the coexistence of allocation and transfer). The third period, running from 1992 to the present day, is the period during which markets clearly exceed control (planning < markets)—a period during which there is movement towards cancelling the coexistence of allocation and transfers. Periods 1, 2, and 3 correspond to stages ②, ③, and ④, or to ②, ③, and ④, of the Reform and Opening-up Policy, as shown in Figures 5 and 6; nonetheless, it is important to note that the final period of reform has not progressed as planned. In other words, it is not guaranteed that the “planning < markets” stage will move towards a suitable ownership system.

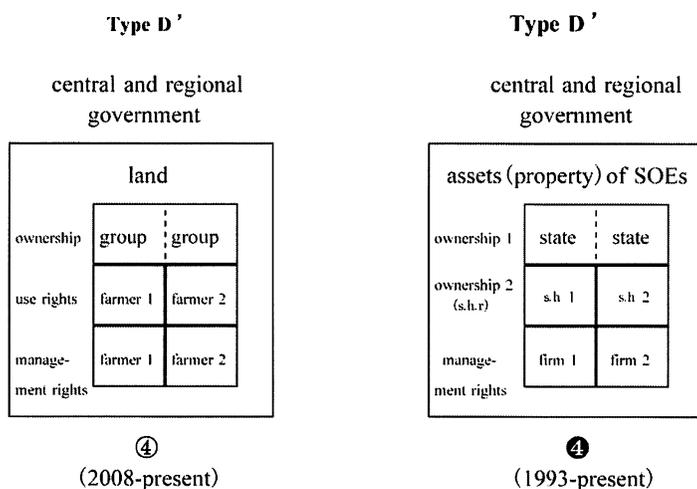
Fourth and finally, and closely related to the third conclusion above, while in the third aforementioned period the aspect of planning may have fallen in importance relative to the market, the reality of reforms to ownership in practice shows that the role of the government has not diminished: there still exist regulations on ownership that work to maintain the public property system. The principle of “the party being in charge of personnel” is rigorously enforced, and there is excessive intervention on the part of SASACs into the management of state-owned enterprises.¹⁸⁾ From this viewpoint, the third stage of the Reform and Opening-up Policy—namely, the condition of the “socialist market economy”—may be appropriately described as “planning < market < state (government).” Having revised this viewpoint on ownership rights to consider the problem of “control area,” if one were to schematize this a

16) For more on the possibility of diverse forms of capitalism following the collapse of socialism, see Boumol, Litan, and Schramm (2007).

17) For more on this separation into three periods, see Oda (2002), pp.62-3.

18) Xu (2008) focuses on the conversion of state-owned enterprises into corporate business enterprises, and points out that regional government provides guidance and plays a large role in enterprise management (e.g., technical guidance and fund-raising), regardless of whether it owns part of the company—even after they have been converted into corporate business enterprises. This is considered a “local development principle system,” and in Chinese society, where there is no spontaneous or autonomous system formation independent of the state, there is a need to leave room for government intervention with regard to enterprise management. For more on this, see Xu (2008), pp.172-4.

little provocatively, the condition of a “socialist market economy”—as the third stage of the Reform and Opening-up Policy (step ④ in Figure 5 and ④ in Figure 6)—can be seen in Figure 7.



Note: The meanings of the abbreviations and dotted/solid lines are the same as those in other Figures. However, the solid line of the central and regional government shows the government (party) guidance and intervention in collective-owned land and state-owned enterprises.

Figure 7: The reality of the “socialist market economy”

The above four points are conclusions that derive from this investigation and discussion.

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