

China: Oligarchy in the Forming and the Counter Movement  
Dr. Dale Jiajun Wen

Part 1: the Facts

China is evolving rapidly with its break-neck growth. Some people are getting rich at unbelievable speed; some interests are getting entrenched. The rapid polarization between the rich and poor is alarming. China's "Gini index", the measure of inequality commonly used, was below 30 in the 1980s, comparable to more egalitarian countries like Norway and Sweden; yet it has climbed to around 45 today, more similar to the US or Latin America countries. While the rich today comes from all kinds of social and economic background, there are worrisome signs that social mobility may be decreasing. For example, when one looks at the student composition of elite universities, the percentage of youngsters from rural backgrounds has dropped rapidly even after the urbanization rate is taken into consideration.

According to the newest Forbes China Rich List released in September 2011, the number of billionaires among China's richest 400 people increased to a record 146 from 128 a year earlier. The total wealth of the richest 400 people on the mainland is US\$459 billion, an increase of 8% from \$423.2 billion before, but only 4% in local currency terms. That is less than the 10% increase in China's GDP in 2010. The Forbes report commented that "Slowing growth in China's wealth is a warning sign for global luxury good suppliers". Well, a warning sign for luxury suppliers is actually a good sign for the average Chinese people, maybe not very significant, but still a positive sign.

It is not trivial to definitely say "who is who" about China's oligarchy in the forming. For individual billionaires, they are not quite entrenched and stable as in some other countries, say, the US. For example, Huang Guangyu, the number 1 richest person in China in 2008 according the influential Hurun Report, was charged with bribery and insider trading soon after. He was sentenced to 14 years in prison and fined 800 million Yuan (1dollar~6.5 Yuan). His case was not alone. In August 2009, Hurun Report issued a special report with following statistics: among the 1,330 Chinese millionaires or billionaires which had made the Hurun Rich List between 1999 and 2008, 16 had been sentenced into prison, 3 were waiting for sentence at the time, 10 were under investigation, 7 were missing or had escaped abroad with debt disputes or pending criminal investigation. Total 36 out of 1,330, or 2.7%, being rich is indeed a risky business.

While collusion of money and power is a usual and common feature of oligarchy, neither offers sure immunity from the law in China, at least for now. With the aforementioned Huang Guangyu case, 5 officials were sent into prison, with the highest ranking one a provincial level official (roughly equivalent to state heads level in the US). These 5 were the ones publicly announced, while it is commonly assumed that probably dozens of officials were implicated in Huang's case and ended up in prison. In 2010, 11 high-level officials (at least provincial or ministerial level) were sentenced into prison due to corruption and other charges, 4 with life imprisonment, 7 with death penalty with a suspension of execution (which would normally be converted to life imprisonment later).

With the rising income gap, theoretically progressive taxation should be one of the measures the government can deploy to address this issue. So far this vehicle has not worked so well. Chinese government started to collect personal income tax in 1980. There are 9 tax brackets, with tax rates ranging between 5% and 45%. People with low income are exempted from personal income tax, with the threshold previously set at 2,000 Yuan per month, but raised to 3,500 Yuan since September 1, 2011. With lots of economic transactions still done with cash, there is massive under-reporting. An

effective monitoring and taxation system is yet to be established. It is estimated that 84 million people paid personal income tax with the previous 2,000 Yuan threshold and only 24 million people will have to pay now with the new 3,500 Yuan threshold. A number for comparison is that automobile ownership has risen sharply in recently years, exceeding 70 million now. In a country where private automobile is not essential for most places, it is hard to believe that the majority of car owners actually earn less than 3,500 Yuan (~540 dollars) per month—this gap clearly illuminates the under-reporting issue. Personal income tax accounts for less than 7% of total government tax revenues in all of the previous 5 years, another sign that so far it is not an effective tool for wealth redistribution.

Yet in recent years the government has taken some concrete steps to address the rising inequality, most notably on improvement of the rural situation. The income and welfare gap between rural and urban areas in China have been enlarging since mid 1980s. As measures to address the ever-pressing rural crisis, all agricultural taxes has been eliminated since 2006, as well as tuition fees for all rural students for the first 9 years of education. Funds have been allocated to provide free textbooks and scholarships to poor students who need more help. Investment for rural infrastructure has been increasing at 20-30% a year. With all these measures, there are positive signs that the urban-rural gap has plateaued and is starting to decrease. Another very visible progress is in health care. The 2003 SARS outbreak exposed many problems of the health care system. It was estimated that about 80% of the rural population did not have any form of health insurance at the time. This sounded the alarm and sent the government into action. In July 2005, the Development Research Center of the State Council released an official document admitting that the market-oriented health care reform had not been a success. After that, a New Rural Cooperative Medical Insurance System was established as well as a Basic Medical Insurance System for Urban Residents. Now it is estimated that 1.27 billion people or 95% of the population have health insurance. While the new system needs more time and practice for fine-tuning and improvement, the positive sea change comparing to the situation mere 5 or 6 years ago is undeniable.

Needless to say, all these social programs need significant amount of resources to run. So it begs the obvious question: where does the money come from? Taxing multi-national corporations have proven to be difficult for all governments, including the Chinese government as well. As mentioned before, personal income tax makes up less than 7% of total tax revenues, so it does not provide significant resources for social programs. The answer, partly lies with the special role played by China's SOEs (State Owned Enterprises).

Before the reform era, with the socialist planning economy, all of China's enterprises were state owned and collective owned. With the market-oriented reform starting in the mid 1980s, the government allowed a private sector to develop aside the public sector. But starting from the mid-1990s, most of the small or medium-sized enterprises have been privatized; the remaining big ones also went through reforms and re-organizations, with almost all of them becoming publicly traded companies, but the state still holds the majority share. It is estimated that currently SOEs accounts for about 27%-30% of China's GDP, but they pay a disproportionately higher percentage of the corporate taxes.

For year 2009, the raw tax rate (tax collected versus profit) was 8.8% for SOEs controlled by the central government--these are normally the big ones like SINOPEC, 3.1% for SOEs controlled by local governments--these are normally smaller, and 3.1% for non SOEs (including privately-owned enterprises, joint-stock enterprises, foreign invested enterprises, etc.) When one calculates tax versus revenue, the rate was 3.2% for SOEs controlled by the central government, much higher than 1.9% for both SOEs controlled by local governments and non SOEs. For year 2009, SOEs paid 122,000 Yuan total tax per employee, while non SOEs only paid less than half of that, 56,000 Yuan per employee.

Unlike some MNCs like GE and Google, which paid zero tax in the US in recent years, by paying the lion share of corporate taxes which underwrite government social programs, China's SOEs are shouldering a disproportionately larger part of corporate social responsibility, even though many of them are only starting to learn buzz word like "corporate social responsibility" from foreign corporations.

To date, 61 of the Fortune 500 firms in the world are Chinese (up from just 12 in 2001), all but two of them state owned. Besides paying for much higher corporate taxes per employee, SOEs has started to pay dividends into government coffer like social security programs in recent years.

Another noteworthy fact is that when one looks at Hurun China Rich List or Forbes China Rich List, there is nobody from the top management of SOEs. It is another sign that the gains and profits from SOEs are more equally distributed to the employees and the population in general. Corruption scandals involving SOE officials do break out now and then. But all in all, the top management of SOEs are not getting filthily rich, unlike many of their counterpart in private or foreign enterprises. In some recent reform in Chongqing city, the government even starts to implement a rule that the salary of the top management cannot exceed 10 times salary of the lowest paid employee.

## Part 2: Discussion

With the growing number of billionaires, China's oligarchy is certainly in the forming. Yet the counter movement is equally strong. The total wealth of the richest 400 people on the mainland is US\$459 billion in 2010, a yearly increase of 4% in local currency terms, which is less than the 10% increase in China's GDP in 2010. This means that their percentage of wealth is actually decreasing slightly, not a trivial fact in our increasingly polarizing world.

The government has taken many active measures to address the income gap and consequent social ills. Some of these measures are not very successful, at least not yet--for example, the aforementioned personal income tax, whose theoretical wealth redistribution function has yet to be realized. Some other measures have achieved quite impressive results--for example, the increased spending for rural education and public health care. As mentioned before, about 80% rural population were without any form of health insurance in 2003, yet by 2011 95% of the population have been insured. The higher corporate taxes and dividends paid by the State Owned Enterprises play a significant role to foot the bills for such social programs.

Corruption has been a central issue for public discussion. While the marriage between power and money is a growing concern, this collusion is not as comfortable and secure as in some other countries, as exemplified by the number of millionaires/billionaires and corrupted officials who end up in prison and the non-trivial sentences they often get. As the case with Huang Guangyu showed, the number 1 richest person could still end up in prison, together with the officials he had bribed. Not a very common fact in some other countries.

With all these said, there is no delaying that the inequity in the country is still alarming and may explode if not further curbed. Within the country, there are different opinions and often heated debates about how China can further address its inequality and other social ills. One dominant school of thoughts, which has been mostly reported in the western media, can be summarized as following: the problems are always being blamed on China's past, and the solution is always further adoption of western rules and systems, and more specifically, the US system. Often times such narratives are wrapped in beautiful words, like China needs more transparency, more democracy and more rule by the

law; but the central idea is always the same: China would automatically get more of these good things if China could copy more of the US system. Yet with the ongoing financial crisis and the ongoing Occupy Wall Street movement, such narrative is increasingly being challenged, as it should be. As exemplified by many facts and examples in IFG's new report "Outing the Oligarchy", some part of the US system represents the pinnacle of crony capitalism and legalized corruption. What if "more transparency, more democracy and more rule by the law" in the US style actually means sanction of public asset stealing and more legalized corruption? With the reality on the ground in the US, it is a valid concern. For example, the recent IFG email broadcast "The Super Rich and Super-PACs: Oligarchs Find a Voice" shows alarming fact how money is eroding democracy in the US. There is no denying that China has learned lots of good things from the west in the recent decades; on the other hand, more and more Chinese are waking up from the blind superstition and unconditional confidence in the western system, and attempting to have a more informed and balanced view of the country and the world.

As a developing country, China still has lots of problems and challenges on its hand, as illuminated by Martin Khor's recent article "is China still a developing country?" On the other hand, some of its problems are not as bad as those in other developing countries or even developed countries, exactly because its system is not the same as the America's. For example, maybe the US can learn one thing or two from China about giving the poor health insurance; with the huge Wall Street bail-out, the US government should make sure those corporations pay taxes and dividends to the public like the Chinese SOEs.

In this time of global crisis, it is clear that US style free capitalism is not the end of history. People around the world need to have a fresh and honest look about our reality and work together to chart a better dream for humanity.