The Contractual Nature of City

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• Urbanization is the process of the concentration and rearrangement of property rights.

• This process involves huge amount of transaction cost with a large number of formal/informal contracts.

• How is transaction cost reduced to achieve efficient urbanization in the real world?
• Villages with similar locations, might
  – Remain rural
  – Urbanized by Government
  – Urbanized by Business Firm
  – Urbanized by Farmers

– Facing large transaction cost, why are there different types of urbanization?
• In China, most urbanization is dominated by government
  – Taking over farmers’ land
  – Land and city planning
  – Investing in infrastructure
  – Selling land use rights
  – Attracting Business

• Advantages
  – Fast, Large Scale

• Disadvantages
  – Farmers’ appeal
  – Less efficient use of land
• 民营城市：蛟龙工业港

• Jiaolong Industrial Park
  – Jiaolong Co. came to Shuangliu in 2004
  – Planning area 4.3 sq km, 0.12 million people
  – Yearly value of output 20 billion Yuan, 0.4 billion tax; 1000 firms
  – Invest in infrastructure by themselves
    • asphalt road, sewage treatment plant, water plant, transformer station, underground pipelines, apartments, office building, shopping mall, cinema, and aquarium.
• XiHangGang Economic Zone, run by gov’t
  – Planning area 80 sq km
  – 80,000 jobs
  – 1000 jobs per sq km
  – 1.4 billion tax
  – 23 million taxation per sq km
  – 1000 jobs
  – No business, apartments, just industry

• Jiaolong Industrial Park
  – Similar locations with XiHangGang
  – Planning area 4.3 sq km
  – 0.12 million jobs
  – 30,000 jobs per sq km
  – 0.4 billion tax
  – 0.1 billion tax per sq km
  – Urbanized with large business and apartments
– Compared to rural villages nearby, Jiaolong achieved urbanization.

– Compared to government-running city, Jiaolong has higher population density, more business, and larger taxation per sq km.

– Why could Jiaolong reduce large transaction cost in the process of urbanization? And why it could replace some government functions in transaction cost reduction?
• Hypothesis
  – Jiaolong Co. is a central contractor in the process of urbanization.
  – It signs contracts with government, farmers, business firms, apartment tenants (buyers), and schools.
  – As a central contractor, Jiaolong greatly reduce transaction cost in urbanization.
  – Yujiao Huang, as the entrepreneur, is the central contractor of Jiaolong. His vision with market plays a central role.
• Contracts with government

  – Defining Planning rights
    • “General Planning of Jiaolong Industrial Park must be consistent with the General Planning of Shuangliu County. Jiaolong Industrial Park makes planning and building itself, and recording (备案) in government.”

•

  – Tax Sharing
    • Shuangliu Gov. rewards Jiaolong “for 100 Yuan tax per sq-km promised by Jiaolong, (Gov.) rewards Jiaolong 25% of local taxation (指扣除乙方区内企业已享受优惠奖励扶持政策后的地方实得部分); for 80 Yuan, it is 20%.”
• Tax sharing
  – Solves the externality in the infrastructure investment of urbanization

• Planning rights recording
  – Most rural villages do not have ability or money to make planning
  – Gov’t planning is limited by government officials’ and experts’ vision, lacking cost measurement and efficiency.
  – Planning rights releases Yujiiao Huang’s vision as an entrepreneur.
  – Maximize land value and taxation.

• Tax sharing + Planning Rights solves the externality of infrastructure investment.
• Land rental contracts with farmers
  – Rent rather than conscripting village land
    • In the end of 2003, 8 villages (九江镇、东升镇的万年村、大渡村、石桅村、泉水八队) returns land contracts to the collective, and then the collective signed rental contracts with Jiaolong
    • Market price of 600 kg rice per year (5% increase every 3 years, bottom price 2.6 Yuan/kg), rental land use rights by 55 years.
  – Resettlement contracts
    • Build apartments for farmers, 0.42 million yuan in 2014.
• Factories, office building, and apartment rental contracts
  — Tax sharing 50%
    • 与工厂的合约：“企业每年两税总计应达到15万元/1000平方米建筑面积标准，若未达到以上收税标准，则乙方自愿同意甲方在原工厂使用费的基础上，按每月每平方米3元增收乙方一年的使用费”。

    • 与写字楼企业的合约：“每100㎡建筑面积单年完税超过10万元人民币的，即可享受税收奖励政策，即甲方对乙方单年完税超过10万元人民币/100㎡建筑面积的税收部分，按照县级留存部分的50%给予乙方奖励”。
Another way of tax sharing
For firms’ taxation passing some line, Jiaolong pays tuition for their kids. (primary and middle school, 2000-3000 yuan per semester):

- “一、入驻蛟龙港的企业，凡在园区年上交税收达到50万元以上的，每50万元解决1名企业在职职工的子女入学，享受蛟龙管委会的入学优惠政策，依次类推。”
- ...
- 三、在蛟龙港从事第三产业的个体工商户，在港年上交税收在5万元以上的，每5万元解决1名个体工商户的子女入学，享受蛟龙管委会的入学优惠政策，依次类推。”
- 《关于蛟龙港租金教育事业发展的文件》（成蛟字【2010】第074号），成都蛟龙工业港管理委员会，2010年7月31日。”
– County Gov’t, Jiaolong, and business firms formed multiple sharing contracts

- Cheung (2009): tax sharing is essential to understand county competition.
- Sharing contracts encourages each party to make investment, and increase efficiency.
- It encourages government to protect property rights.
- It encourages both gov’t and Jiaolong to reduce transaction cost in business registration and other services.
- Jiaolong promotes industry-upgrading by increasing business rent itself.
- With planning rights and sharing contracts, Jiaolong could maximize the land rent.
Given Chinese institutional and social structure, Jiaolong cannot replace all government functions.

- Discovered and attracted Huang to Shuangliu
- Gov’t provides police service
- Gov’t invest in major roads near Jiaolong
- Gov’t went to village to talk to farmers for renting land to Huang
- Gov’t protected Huang when the Land Administration went to inspect Huang
- Gov’t transferred part of land from rural-owned to state-owned.

Whether these phenomenon appears because of special Chinese institutions, or more fundamental, even in the U.S.?
• Contractual Nature of City

• Urbanization is the process of concentration and rearrangement of property rights, involving a large number of contracts.

• With non-zero transaction cost, how can a rural area urbanized by reducing transaction cost?
Government provides a lot of functions in the process of reducing transaction cost in urbanization.

Business firms could also provide the same functions replacing government in the process of urbanization.

Under which conditions, business firms could replace most government functions in reducing transaction cost and urbanization?
– Jiaolong reduces transaction cost by being the central contractor.

– The essential contract is the land rental contract with farmers, and the tax sharing and planning recording contract with gov’t.

– This institutional arrangement encourages government to define and protect Jiaolong’s property rights.

– It also provides Jiaolong, and esp. Yujiao Huang to use their vision and market signals to urbanize fast.
– Urbanization is the process of reducing transaction cost caused by a large number of contracts, which define and rearrange property rights.

– Whether more or less government functions is more efficient, depends on which could be more effective in reducing transaction cost. Neither gov’t nor business is definite for urbanization.

– The contractual structure is the essential to understand the comparative transaction cost of different urbanization paths.