Analysis on Capitalization of Rural Land Ownership in China by Law and Economics

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Abstract To find solutions for legal system for capitalization of rural land ownership in China, this paper studied and analyzed existing problems in rural land system and legal environment using legal theory and transaction cost theory. Results indicated that (i) the restriction of institutional condition upon property right and transaction is more essential, and key points include the relationship of entities of right formed jointly by the state, collective and farmers, accurate positioning of property right structure, and security for land appreciation income right and allocation mechanism; (ii) the land property right structure should select a legal structure with minimum transaction cost. It is concluded that entitling the ownership to a single entity is an economical method to eliminate current conflict of rural land right.

Key words Land capitalization, Land right, Law and economics, Transaction cost

1 Introduction

The capital value owned by rural land is incomparable to other things in the market economy, and the right conflict carried by rural land is area of gaming of rights. In China, usable land resources are less and less, but extensive land development is still widespread. How to realize reasonable use and optimum allocation of land and make farmers really enjoy land appreciation income are essential objectives of realizing sustainable rural development. Rural land capitalization (or exactly speaking, capitalization of rural land use right) is an only way for solving conflicts of rural land rights; rural land system and legal environment are essential guarantee for rural land capitalization and various rights; land right protection is one of essential requirements for further realizing agricultural modernization. We should respect farmers’ land right, reform and innovate upon existing land system and property right structure, provide and return rights to farmers from laws, and ensure continuation of income of land right entities from mechanism. In this way, it may actually realize synchronous, coordinated and harmonious urban and rural development.

2 Legal basis and problems of rural land capitalization

2.1 Land right and system Land right is core part of land legal system. The fundamental purpose of land legal system is protection and effective use of land resources. Adjustment objects of land legal system are ownership relationship, use relationship, circulation relationship, and management relationship of land. These series of relationship are interweaving, conflict and mediation of various benefits, willpower and act of land. The basic function of system is saving, in other words, making one or more economic men increase self welfare but not reduce welfare of other people, or make economic men reach higher target level under restriction of their budget(1). Existing rural land right system and institutions of China are products of historical development and influenced by political, economic and social reforms, thus it is required to combine social history and current national conditions when studying land rights within framework of the legal system(2).

2.2 Rural land legal system of China Article 10 of the Constitution specifies that "Land in the cities is owned by the state. Land in the rural and suburban areas is owned by collectives except for those portions which belong to the state in accordance with the law; house sites and privately farmed plots of cropland and hilly land are also owned by collectives. The state may, in the public interest, requisition land for its use in accordance with the law. No organization or individual may appropriate, buy, sell or lease land or otherwise engage in the transfer of land by unlawful means. The land use right can be transferred in accordance with laws. All organizations and individuals using land must ensure its rational use." Law of the Peoples Republic of China on Land Contract in Rural Areas clearly stipulates definition of rural land in Article 2; land in rural areas includes the arable land, forestslands and grasslands owned collectively by the farmers and by the State and used collectively by the farmers according to law, as well as other lands used for agriculture according to laws. The Law of Land Administration of the People's Republic of China stipulates in Article 10; In lands collectively owned by farmers those have been allocated to villagers for collective ownership according to law shall be operated and managed by village collective economic organizations or villagers’ committee and those have allocated to two or more farmers collective economic organizations of a village, shall be operated and managed jointly by the collective economic organizations of the village or villagers’ groups; and those have allocated to township (town) farmer collectives shall be operated and managed by the rural collective economic organizations of the township (town). Paragraph 1 of Article 59 in Property Law of the People's
Republic of China stipulates that the real properties and movable properties owned by a farmers’ collective shall be collectively owned by all the members of the collective. 2013 No. 1 document of central government Several Opinions of Central Committee of the Communist Party of China and State Council on Accelerating Development of Modern Agriculture and further Strengthening Development Vigor of Rural Areas stated that we should innovate upon agricultural production and operating system and encourage development of large specialized farmers, family farms and farmers’ professional cooperatives\(^5\). Besides, these laws set up rights for rural land, established legal basis for land circulation in various degrees, and confirmed subject status of farmers and their independent selection right for land capitalization. At present, these laws and related policies mainly provide rural land operating right, income right, and land capitalization of use right.

2.3 Existing problems Rural land public ownership and land contracting operation are fundamental rural land system at current stage. For rural land capitalization, it is a basic idea to adjust land use method according to market demand of economic development. Through analysis of these laws, it is not difficult to find following problems. (i) There are conflicts of rural land right subject, chaotic relationship, and fuzzy object (for example, it specifies that land ownership is possessed by the collective, but it is not definite for the legal relationship, legal status and scope of rights and obligations of the collective, the state and farmers). (ii) Land capitalization property right system is out of balance, the subject is dislocated and rights are in name only (for example, legal status and nature of rural land property right subject and land capitalization of land use methods). (iii) Allocation of rural land resources is improper, income allocation methods are incomplete, and supervision mechanism is vacant.

3 Rural land capitalization in the context of law and economics

3.1 Law and economics and transaction cost theory Law and economics is the application of economic theory (specifically microeconomic theory) to the analysis of law. Economic concepts are used to explain the effects of laws, to assess which legal rules are economically efficient, and to predict which legal rules will be promulgated\(^5\). Basic theorems of law and economics include Smith Theorem, Normative Hobbes Theorem, Coase Theorem, and Posner Theorem, etc. Law and economics takes personal rationality and individualism as basis of research methods, takes efficiency as core criterion, and takes cost-benefit and utility maximization as basic analysis tools\(^5\). This theory can be understood that any legal activity including legislation, judicial and legal system, the essential function is to allocate scarce resources and analyze and arrange corresponding legal activity by economical means. According to this theory, legal problems generated in the process of rural land capitalization can be analyzed and solved using theory and methods of the economics. The core issue of law and economics is transaction cost, and analysis of transaction cost has a series of proposition and important inferences\(^6\). Ronald Coase said that the size of the firm is dependent on the costs of using the price mechanism, and on the costs of organization of other entrepreneurs. These two factors together determine how many products a firm produces and how much of each. Polinsky stated that if transaction costs are zero, legal structure is of no account because it will bring about efficiency in any case\(^7\). In other words, as long as starting point of right is determined, market will realize Pareto efficiency of resource allocation through private transaction when the transaction cost is low and unblocked\(^5\). Namely, different property system will lead to different resource allocation efficiency. Transaction cost theory indicates that private transaction market can solve problems that can be solved only by government, and existence of transaction cost determines optimum system and law. In China, the precondition of zero transaction cost is impossible. However, Coase provided us a new idea and approach for solving legal and institutional problems through market mechanism.

3.2 Analysis of rural land capitalization

3.2.1 Land property right and structure of property right. According to opinions of Coase, as long as rural land property right is definite and transaction cost is zero (or very low), no matter the property right is given to any subject (for example completely owned by the state or privately owned by farmers), ultimate result of market balance will be effective and it will realize optimum Pareto efficiency of resource allocation. Assuming government turns land ownership to farmers (or completely to the state) and laws allow free transaction of land, it is unnecessary to make private and public balance and gaming of land right subject, and make either – or selection. Through market transaction, it is able to realize combination of rights and benefits, and both the state and farmers will believe that such combination is better than the initial right determination. Further, land property right should select a legal structure with minimum transaction cost, because such selection can save waste of resources, materials, time and manpower resulted from negotiation of land transaction.

3.2.2 Resource allocation and income allocation. From substantive laws to procedural law, from fundamental laws to common laws, and from written laws to unwritten laws, all current social laws have internal economic logic, to allocate resources in the way of being favorable for increasing efficiency, and ensuring optimum allocation and reasonable use of resources according to provisions of rights and obligations\(^9\). The core issue of economy is efficiency. According to requirement of economic efficiency, when selecting a system arrangement and right allocation, the criterion is minimum cost with maximum effect. According to Coase Theorem, the function of laws is to allocate rights to the party that attaches the highest importance to rights. If it fails to judge for which party it is more important, the criterion will be the party promoting realization of rights with minimum cost. According to this idea, land resource allocation right of rural land capitalization and the right of allocating land appreciation income should be turned to government, but it also should provide farmers with negotiation right and
land production and operation method selection right.

3.2.3 Land use and large scale operation. Farmers’ operating acts are a series of operating activities manifested in the operation direction, scale and methods selected by farmers for certain production purpose in certain economic condition (economic system, economic policy and regulation, etc)\(^{10}\). In rural areas of China, common land use modes are enclosure of land, laying farmland idle, letting farmland lie waste, and highly intensive use of land. Large scale operation is an active land use mode. In this mode, pure income of land use realizes great increase. The economy of scale is a production phenomenon that marginal cost or average cost monotonically decreases before reaching certain scale. If it fails to effectively obtain elements necessary for large scale production due to restriction of old system, the same type of production elements between new and old systems will lead to price difference, potential income flow will appear, and economic entities firstly making institutional innovation will receive excessive profit, and other economic entities will follow, so as to promote innovation of social institutions\(^{11}\). Large scale operation is a type of suburban land capitalization in developed rural areas of China. It is a trend and will promote institutional innovation and reform.

3.2.4 Policy recommendations. Theory of economics indicates that the restriction of institutional condition (especially legal rules) upon property right and transaction is more important\(^{12}\). In line with rural land capitalization of China, the state can carry out management and right allocation from macro-control and micro-intervention. At institutional level, it is required to take overall consideration in accordance with principles of "firstly migrating to cities, then transforming; distinguishing conditions and classified implementing; voluntary participation and turning profits to farmers."\(^{13}\) Specifically, it is feasible to make following legal institutional arrangements and environmental improvements. Firstly, it is recommended to build hierarchical compound property right structure. Land property right is the combination point for coordinating relationship of rural land benefit subjects, thus harmonious property right relationship is an essential factor for solving rural land right conflict and developing rural economy. Building hierarchical property right structure is to make clear definition of property right subjects, nature orientation, and relationship through the state, collective and farmers, and regulate the scope of land ownership at township and village committee organization, to restore rights and obligations. Secondly, it is recommended to institutionalize period and scope of rural land contractual right. In the new round of reform of land law system, it is required to specify period, scope of rights, and treatment method after expiration of rural land contractual right. Thirdly, it is recommended to legalize sustained benefit mechanism of rural land capitalization right subjects, to legally safeguard farmers’ land capital rights and interests and regulate protection of rights and interests of landless farmers. Fourthly, it is recommended to make clear scope of rights and obligations of all concerned parties, and determine property and income allocation rules and long-term responsibility mechanism.

4 Conclusions and recommendations

Based on current national conditions and legal environment and according to the above analysis of law and economics, we came up with following recommendations:

Firstly, it is proper institutional arrangement to adhere to the policy of rural land collective ownership, keep state ownership of land unchanged, and capitalize land use right, operation right, and income right. Secondly, property right ownership after rural land capitalization is a key issue in institutional innovation and reform and solving conflicts of rights. If the ownership is given to a single entity, no matter the state or the individual, it will play a great role in eliminating a series of current social conflicts. Thirdly, large-scale operation and specialized management of rural land are feasible ways of saving transaction cost, reducing information asymmetry, eliminating external barriers, optimizing use of land resources, and increasing economic operation efficiency. Fourthly, balancing economic efficiency and legal justice is an ideal institutional arrangement. In reality, it is difficult to balance these two points. It needs balance and selection according to social demands of certain stage. Nevertheless, it is recommended to advocate protecting rights and interests of the majority and making effort to reduce damage and losses to the minority.

References