

# *Analysis of the Strengths and Weaknesses of the Chinese Government's Governance Capacity in Different Areas under the Administrative Contracting System*

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**Abstract:** Based on the theory of "administrative outsourcing system", this article analyses the characteristics of the administrative outsourcing system and its impact on the Chinese government's governance capacity by comparing the hierarchical system with the outsourcing system from the three dimensions of the distribution of administrative rights among governments, material incentives, and superior-subordinate relations. On this basis, the article combines the administrative outsourcing system between upper and lower levels with horizontal competition among officials at the same level to analyse the deep-seated reasons for the great differences in the strength and weakness of the Chinese government's governance capacity in different fields. The combination of contracting between upper and lower levels and horizontal competition among officials at the same level helps to reveal the principles behind many features of the Chinese government's operation and social phenomena, and is of great practical significance in solving the current situation of the Chinese government's insufficient governance capacity in certain fields.

## 1. Introduction

In November 2013, the major proposition of "promoting the modernization of the national governance system and governance capacity" was first raised at the Third Plenary Session of the 18th CPC Central Committee. Since then, views on how to improve the governance system and enhance governance capacity have sprung up in academic circles. Tu Feipeng believes that there is a high degree of correlation between the government's governance capacity and the party's ability to govern, and that it should take strengthening the party's ability to govern as the basic point, give full play to the party's leadership of government reform, and steadily promote the construction of the government's governance capacity amidst the movement [1]. Ji believes that the modernization of the Chinese government's governance capacity must be achieved by removing the resistance of vested interest groups within the government, removing the government's administrative traditions and sweeping away the bureaucratic culture in the society as the starting point, and targeting and targeting to solve the above obstacles [2]. Liu Jiayi believes that the modernization of national governance capacity should be effectively promoted in the practice of auditing by strengthening the construction of the national audit system [3]. In the past, the views on strengthening the

construction of government governance capacity are incisive to explain the many programs to improve the governance capacity, but most of them start from the superstructure field, or are only limited to the study of government governance in individual regions; some of these views fail to fundamentally explain the determining factors affecting the strength of the government's ability to govern from the economic base, and some of them only study the individual cases of regional government governance, and can not be use the special to represent the general. This paper tries to use the theory of administrative contracting system to explore the reasons affecting the different strengths and weaknesses of the Chinese government's governance capacity in different areas from the economic foundation, and gives shallow suggestions. Exploring the factors affecting the strength and weakness of the Chinese government's governance capacity is of great theoretical and practical significance for promoting the construction of the Chinese government's governance system.

## 2. Concept and Characteristics of "Administrative Contracting Out"

The theory of "administrative contracting system" is put forward by Zhou Li'an, who synthesized the theory of "political tournament" summarized by him in his early years. The theory of administrative outsourcing system is a systematic description of the relationship between the upper and lower levels of government and the characteristics of government governance at all levels from both vertical outsourcing and horizontal competition, as well as an in-depth discussion of the underlying logic behind the phenomena of government governance, such as the contradiction of "centralization-decentralization" in China from both the vertical and horizontal perspectives of the system[4].

The concept of "administrative contracting system" is closely related to the two economic theories of contracting system and employment system. The contracting system corresponds to the transactional relationship between enterprises, while the employment system summarizes the relationship between upper and lower levels of domination and management within an enterprise. In terms of organizing production, if the enterprise finances the hiring of workers and provides the means of production, then it is a form of production under the hiring system, and if the enterprise only finances the contracting of production to other enterprises, then it corresponds to the outsourcing system. Based on cost and benefit considerations, how enterprises grasp the relationship between hiring and outsourcing, i.e., the optimal boundaries of enterprise production, is the core issue of economics enterprise management since Coase.

Two economists, Holmstrom and Milgram, make an essential distinction between the hiring system and the outsourcing system from three perspectives: asset ownership, incentive contract and task allocation. In the outsourcing system, the contracting company gives a certain amount of money to buy out the services of the contracting company, entrusts the contracting company to complete a certain goal, the task is all undertaken by the contracting company, then the ownership of the assets belongs to the contracting company, and because the contracting company only requires, and can only look into the results, so the contracting company's discretion is very large, how to produce by the contracting company to decide, and if the better the control of the cost, then the The higher the capital surplus incentive. In the employment system, the ownership of assets belongs to the contracting company, the company contracts out the tasks to the employees, and the material incentives are also relatively fixed, with relatively little discretion and surplus asset acquisition. Compared to the outsourcing system, the hiring system has fewer pay incentives.

Zhou Li'an developed and applied the economic system concepts of employment and outsourcing to the administrative field, and creatively put forward the concept of "administrative outsourcing system". The administrative outsourcing system is somewhat different from the

hierarchical system in the West and the outsourcing system in the commercial field. Administrative outsourcing is an ideal political system that combines hierarchy and outsourcing. It is the outsourcing of tasks within the government, i.e., under the authority of the central government, the superiors of each level of the government assign tasks to their subordinates. This is like the "land under the household" policy, in which the village distributes land to each peasant household on a per capita basis, and the peasants are free to decide what to grow and how to grow it, and after they pay enough rations each year, they get the rest for themselves. The household contract responsibility system did greatly stimulate the farmers' agricultural production.

Based on the three characteristics of administrative contracting put forward by Zhou Li'an, namely, the granting of administrative power, the distribution of financial power and hierarchical management, this paper will analyse the administrative contracting system in the light of the three characteristics of administrative contracting. On the basis of comparing the sectional system and outsourcing system in the administrative contracting system, this paper further elaborates the three characteristics of administrative contracting system: administrative power distribution, material incentives and internal assessment and management [5].

Firstly, in terms of administrative power distribution. On the one hand, the contractor, i.e., the higher government, has the supreme authority and arbitrary intervention power. For example, the contractor has personnel power, approval power, guidance power, veto power and arbitrary intervention power. This also shows that the contractor and the contractor are not equal in the outsourcing system of the contractual relationship of sale and purchase, the status of the upper and lower levels of the division is clear, which is precisely the "outsourcing system" before the name of "administration". On the other hand, the contractor has a high degree of discretionary power, that is to say, the contractor has given the decision-making power and the specific execution power to the contractor, and the contractor has a great deal of actual control, so that when the control of the contractor is weakened, officials similar to the "emperor of the land" may appear.

Second, in terms of material incentives. The contractor is faced with a situation of surplus material claims and strong economic incentives, i.e., the amount of welfare of the contracted administrative unit depends on its own efforts. From the point of view of claiming surplus, the contracting party and the contractor is a sharing relationship, that is, either to pay a fixed task target to the higher level, or the higher level from the total subcontracting results of a fixed proportion of the share, from this point of view, to give enough to the higher level, the rest of the wealth is the contractor's own, and it has the right to claim for the surplus information as a contracting return. In layman's terms, it means that the higher level government shares the power to the lower level government, and the lower level government utilizes the shared power to generate income and then shares it with the higher level government.

The other is that the higher level of government allocates funds or sets a certain budget for the lower level of government to accomplish specific tasks. Under this model, if the task can be accomplished at a very low cost, the remainder of the allocation will be the contractor's own. However, it can also face the situation of insufficient appropriation, self-financing and self-sustainability. Currently, the administrative activities of local governments in China are highly dependent on extra-fiscal budgets, especially with land contributions as the main source of finance, while transfers from higher levels of government account for a relatively low proportion of local government's financial expenditures. On the other hand, the revenue-generating capacity of the contractors determines their financial spending capacity, i.e., "one line of revenue and one line of expenditure". The administrative contracting system is close to the market-oriented model in terms of material incentives. In addition to the basic fixed salary, the amount of welfare of contracted officials depends on the amount of income generated by them, which is a high incentive model with the nature of sharing.

Finally, in terms of internal assessment and management, the administrative contracting system is result-oriented, focusing on the main role played by people in management, while the Western hierarchical system emphasizes the system and procedures, and there is a hierarchical difference. China has long used the "territorial responsibility system", that is, "whoever manages is responsible", that is to say, all the things that happen in the jurisdiction, no matter whether they are caused by the management of the jurisdictional organs or the improper procedures, are the responsibility of the jurisdictional organs and their main leading cadres. In terms of task assessment, the administrative contracting system mainly examines the completion of results, and because of the large amount of discretionary power at the local level, the contractor is unable to effectively supervise the entire process and details of the project, and therefore can only judge the heroes by the results.

The general characteristic of the administrative contracting out system is that tasks are contracted out in layers under a unified authoritative organization, similar to the introduction of market-oriented relationships within the government. Combining the characteristics of hierarchical and outsourcing systems, China's administrative contracting system has embedded the elements of "contracting" and "outsourcing" under the institutional framework of the hierarchical system, which means that the administrative contracting system has the appearance of a hierarchical system, while the core is the "contracting" system. In other words, the administrative contracting system has the appearance of a hierarchical system, but the core is "contracting out".

Further, the administrative contracting system is not as good as the hierarchical system in terms of overall and integrated collaboration, because localities have discretionary power, can to some extent indirectly confront the central government, and out of self-interest, cooperation with the same level of government is not effective, and the "local protectionism" also comes into being. On the other hand, the administrative contracting system is better than the outsourcing system because the relationship between the contractor and the contractor is fundamentally hierarchical and under one authority.

"The administrative contracting system takes into account the characteristics of the centralized system, while the outsourcing system is a representative system of decentralization. On the one hand, China is more centralized than any other country in major areas of defense science and technology, such as the construction of subways, which, objectively speaking, should be a local matter because of the stronger economic effect it brings to the region, but the approval of the construction of subways rests with the central government. On the other hand, in some areas, China is more decentralized than other federal countries. For example, laws and regulations designated by the central ministries have the same status as those designated by the provincial governments, which determines that the central ministries, to a certain extent, have limited binding power over the provincial governments, so the inspections are not as effective as they could be. Local governments do not cooperate, and many ministry policies are difficult to implement in the provinces. In addition, provinces are also not affiliated with each other, it is a cooperative and competitive relationship, so the effect of inter-provincial cooperation is also unsatisfactory [6]. For example, "food safety", "environmental protection supervision" and other social areas have long been difficult to achieve results because of poor coordination of remediation and lack of supervision.

### **3. The Proportion of Government Governance Costs and Administrative Risks Determines the Scope and Extent of Contracting Out**

The extent of contracting out is very limited in areas such as defense science and technology, petroleum, and electric power, while contracting out is done in layers in areas such as education, health care, and elderly care. This paper argues that the determinants of the scope and extent of

outsourcing are similar to the optimal boundary problem of enterprise production mentioned above, which is also a problem of risk and cost-benefit.

Business risks are mainly risks in the economic field, while administrative risks are richer in content but are mainly categorized into direct risks and potential risks. Direct risks are usually caused by a mismatch between the supply of and demand for public services. Public services are designed to meet the generalized needs of the public, specifically whether the legitimate rights and interests of the masses can be guaranteed, whether they can be treated fairly, and so on, and thus have a political nature. Private services, on the other hand, mainly focus on differentiated services. The supply side of public services mainly involves the cost of services, while the demand side of public services involves the assessment of the quality of government services and the resulting public pressure on the government, and as the public pressure on the government grows, the risk of domination also grows. An imbalance between the supply of and demand for public services can lead to the division of the country, mass petitions, revolutions, or other mass events that pose a direct risk to government rule. If the local government makes a mistake in decision-making, it can also cause economic fluctuations, increase the gap between the rich and the poor, social unrest and other potential risks. These direct and indirect risks were originally caused by the contractor government, but eventually evolved to be borne by the central government, i.e. the contracting party, through the fermentation and guidance of information technology.

The management cost of the government mainly refers to the management cost of the contracting party, that is, the central government. As mentioned above, if over-contracting is carried out, after local governments have too much autonomy, governance risks will inevitably arise, and the risks will eventually be transferred to the central government. On the other hand, if the central government reduces the scope and degree of contracting out, then the central government will have to directly play the role of the national governance regulating hub and fund allocation center, and its management and supervision costs will increase greatly, which will inevitably pose a huge challenge to the central government's finances.

In short, when social risk rises, the central government will gather power, and China's system is more inclined to the "hierarchical system", where the central government directly issues administrative orders and is solely responsible for national governance; while when the central government's administrative costs are too high, finances are tight, and governance risk is relatively small, China's system will shift to the "contracting system", where the central government directly issues administrative orders and is solely responsible for national governance. "contracting out system", where the task of governance is contracted out to the grassroots government [7]. The scope and extent of administrative contracting out is determined by the dynamic ratio of governance risks and administrative costs.

#### **4. Imbalance in Matching the Intensity of Vertical Contracting and Horizontal Competition Has Led to Significant Differences in the Strengths and Weaknesses of China's Governance Capacity in Different Areas**

In the administrative contracting system, in addition to the vertical contracting relationship between superior and subordinate levels, there is also a horizontal competition between officials, which Zhou Li'an called "political tournament" [8]. Vertical contracting is mainly about the issuer issuing tasks to the contractor; while horizontal competition is about competing for the political rewards from the issuer to the contractor. In the above discussion, the article starts from the relationship between the contractor and the offeror alone, and the default is that there is only one contractor; however, in reality, there is more than one contractor, and there is also horizontal competition among contractors, in other words, contractors also want to stand out from the crowd

and become the offeror. The following table (see table 1) is a combination of the two aspects of vertical contracting and the intensity of horizontal competition to divide the various fields of endeavor.

Table 1: Ranking of Degree of Contracting and Strength of Competition

Horizontal Competition \ Vertical contracting	Powerful	Weak
High	Investment, social stabilization, competitive sports, epidemic disease control, post-disaster reconstruction	Education, health care, environmental protection, social security, coordinated regional governance, food safety
low		Foreign Affairs, Defense, Aerospace, Customs, Railroads, Oil, Power, Salt

It is easy to see from the above figure that government governance is very strong in areas such as investment, competitive sports, epidemic control, and post-disaster reconstruction, where vertical contracting is high and horizontal competition is equally strong, as well as in areas where contracting is low and horizontal peer competition is weak, such as foreign affairs, defense, aerospace, customs, and railroads. This is because in areas of high contracting, where the political rewards are high and the resulting material benefits are equally generous, horizontal competition is strong and contractors are motivated to work for their rewards. On the other hand, areas with a low degree of contracting are usually critical areas that have a bearing on the nation's economy and people's livelihood, so they are usually directly under the central government's coordination and management, so as to minimize the probability of risks occurring in these areas, or even if they do occur, they can be dealt with in the first instance. Therefore, the degree of contracting in these areas is low, and since they are under the central government's management, they have less discretionary power, and the horizontal competition is also relatively weak. Such key areas are directly controlled by the central government and supervised by direct leaders, so the governance capacity is also very strong.

In areas such as education, environmental protection, health care, social security and food safety, where the degree of contracting is high but horizontal competition is weak, the government's ability to govern is far from satisfactory. The reason for this is that the political rewards that can be obtained in these areas are far less than those in other areas, and the material benefits are far less generous than those in other areas, so horizontal competition in these areas is relatively weak. In fact, these fields are also a typical representative of "the central government invites the guests and the local government pays the bill", that is, the central government decentralizes the management of these fields and asks for the strengthening of the construction of these fields, but these fields do not produce much economic benefit, so they do not stimulate the contractors very much, and the motivation of the management is not very high either [9]. Therefore, in areas where the degree of contracting is high but the economic benefits are low, the government usually generates its own income because it does not receive any official material incentives, so the phenomenon of embezzlement and bribery is particularly serious in these areas. Zheng Xiaoyu, the first director of the State Food and Drug Administration of the People's Republic of China, was sentenced to death for embezzlement and bribery, rent-seeking, and selling his office.

Further, areas with a low degree of contracting are usually the most important areas for the lifeblood of the country, and are usually managed directly by the central government, so the degree

of contracting is low, the discretionary power is small, and the horizontal competition is limited under the central government's pressure. Therefore, in the figure, the areas with a low degree of contracting and fierce horizontal competition are also blank, because stability is overriding in the areas under the central government, and fierce struggles will only bring instability. As for less important areas, the central government will contract its governance to the local, can produce significant economic benefits of the field, competition is fierce, governance enthusiasm is high, governance effect is good, governance capacity is strong; and produce economic benefits of the field is relatively weak, competition is less intense, governance enthusiasm is relatively weak, so the government's governance capacity is also relatively weak [10].

Combine the characteristics of the administrative contracting system with the determinants of the degree and scope of contracting mentioned above. From the central government's point of view, the regime is only secure if the key areas are in its own hands, and the key areas are the basis for maintaining stability, so more emphasis is placed on public welfare, while profit-making comes second, so to speak, regardless of the cost. As for other less important areas of light industry, if they are still managed by the central government in a unified manner, their management and supervision costs are too great, and may even exceed the economic benefits generated by these areas, so on the premise of not generating, or generating as little as possible, a crisis of governance, it is undoubtedly the optimal solution to contract out these areas to the lower levels of government, and to split the profits from them.

In general, in areas where the government's governance capacity is strong, either the central government operates at all costs or the contracting government is motivated by high returns to actively plan; for areas that are relatively less likely to generate high economic benefits and are less important, both the central government and the contracting government contribute less, so the government's governance capacity is relatively weak in these areas. In other words, governance capacity is strong in areas where there is a high degree of fit between "vertical contracting" and "horizontal competition", and relatively weak in areas where the fit is weak. In areas where contracting is high and governance capacity is weak, the only way to fundamentally improve governance capacity is to strengthen institutions, innovate working models, and then improve their economic efficiency.

## 5. Summary

On the basis of comparing "administrative contracting system" with "hierarchical system" and "outsourcing system", this paper elaborates the definition and characteristics of administrative contracting system, the scope and degree of administrative contracting and its determinants. On the basis of the comparison between the "departmental system" and "outsourcing system", the definition and characteristics of the administrative contracting system, the scope and extent of administrative contracting and the determinants of administrative contracting are explained, and the match between the degree of "vertical contracting" and the degree of "horizontal competition" is explored in-depth, and the influence on the strength of government governance in different fields is concluded. The conclusion is that governance capacity is strong in areas where "vertical contracting" and "horizontal competition" match, and weak in areas where they do not match. At a deeper level, areas with strong governance capacity are either so important that they are of national importance that the central government is personally involved, or they generate high economic benefits that attract contracting governments to work actively. On the other hand, for those areas with poor economic benefits and less critical importance, naturally no government is willing to take charge of them, and the government's governance capacity in these areas is naturally relatively weak. Only by improving the productivity of the whole society in continuous development,

allocating certain material benefits from the areas with strong governance capacity to those with weak governance capacity, and strengthening the relevant incentive system construction in the weak governance areas can the problem of imbalance of governance capacity in different areas of the Chinese government be solved fundamentally.

In addition, this paper does not provide a specific solution to the problem of weak government governance capacity in certain areas. This is because in terms of China's current stage of development, China is still in the primary stage of socialism, and this national condition means that the current social and governmental problems in China have to be solved by development. Therefore, in development, there is always the question of sequence; there is always a major and minor difference. Those areas where governance capacity is strong are the main priority areas for development, while those areas where government governance capacity is relatively weak are areas that can only be fundamentally solved after development has taken place. Therefore, the strong and weak government governance capacity in different areas also reflects the current era of China, and is a reflection of the objective process of development, so the problem of weak governance capacity in certain areas can only be solved by development, and there is no good solution to the root cause at present.

This article also does not dig into the political party factors behind the government, which is also the direction of future writing efforts.

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