

Congressional-Executive Commission on China Issues Roundtable
“Ownership with Chinese Characteristics:
Private Property Rights and Land Reform in the PRC”
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I am an American academic and lawyer specializing in real estate law, including leasing, finance, development and title issues. I have served in the leadership of the American Bar Association Section on Real Property, Probate and Trust Law for many years and have published eight books and scores of articles on American real estate issues.

Ten years ago I was invited to teach Real Estate Law at Peking University, and thus began an interest in the development of Chinese real estate law that I observed in its beginning stage at that time. Since then, I have traveled to China frequently and have invited Chinese scholars to collaborate with me in America. I have co-authored a book and a number of articles on Chinese Real Estate Law and have lectured on real estate topics at most of the major Chinese law schools. I have established academic programs for Chinese students in America and for American students in China. Recently, I have participated in the Center on Chinese Land Law and Policy at Peking University, which will develop a central source of information in English and Chinese, regarding developments in Chinese Real Estate Law, and to provide a resource of American expertise on real estate matters for Chinese practitioners and policy makers. I will serve as co-Director of the Center.

My book, *Chinese Real Estate Law*, published by Kluwer International Law Publishers, is the only book length treatment of this topic in English written by someone with background in real estate law practice. I attempt to synthesize the various sources of Chinese law to suggest the way Chinese law would address problems of concern to persons involved in market real estate transactions.

I do not speak or read Chinese, and my expertise is based upon collaboration with Chinese lawyers and academics who speak English. Although this necessarily is a limitation on my development of any true expertise, I can say that at the elite Chinese law schools I have been able to interact with students and academics from every part of China, have obtained insights that one might not obtain from government or business organs.

1. Overview of Chinese Real Estate System:

1.1. Introduction:

Until 1988, there was one simple law of real estate in China - the government owns everything. Although the government divided its control of the land resources in China into different compartments and vested various governmental elements with responsibility and control, there were no individual rights in land and any arrangements that had been made could be unmade by government fiat.

In 1988, China amended its Constitution to provide for the recognition of privately owned transferable rights in land. Although the Chinese Constitution does not have the same force of law that the American Constitution does, this change was an important symbolic step, and presaged an array of changes in governmental statutes and regulations that implemented a system of private ownership and exchange of real estate. The developmental process was slowed by political unrest in China occurring also in 1988, and when I arrived in 1992, China was just beginning to act on the development opportunities offered by the legal changes.

Since 1992, there has been real estate activity in China's cities on a scale perhaps unequaled in human history. Certainly the legal system that has been developed since 1988 has been a critical element in accomplishing this real estate activity, but the physical development has surged far beyond the legal development.

China has some law in place, and there certainly is recognition and protection of ownership. Private bargains can be struck with some degree of assurance that the law will enforce them. Lenders have some clarity of right to reach security given for loans. But there is little certainty, on a nationwide basis, that the rights technically recognized in the Chinese laws will be fully recognized by those who administer the Chinese legal system, although there is steady improvement in this area.

Perhaps more important is the fact that the Chinese real estate system has yet to undergo the test that will come when the "first bubble bursts" - when China's real estate market experiences the inevitable economic correction that must come as part of the cycle of economic activity. It is only then that we will know how well the rights and expectations created by the system will stand up to the pressures of political expediency. We have had the same "test of fire" of the legal system in this country a number of times during our history, and each time we have identified weakness that needed correction.

In short, the existence of a "rule of law" cannot be proclaimed. It must be experienced. It must be measured again and again as new pressures arise to test its stability. No social system is immune from such tests, and no legal system responds to these tests perfectly. Since the system of private rights was first established, China has yet to experience its first real test.

1.2. Basic Characteristics of the System:

The basic building block of the U.S. real estate economy is perpetual and relatively comprehensive ownership. The "fee simple absolute" is an ownership interest in land that can be transferred and inherited indefinitely into the future. It cannot be said to be "absolute ownership" because land rights in America are subject to rather extensive government regulation. But that which is not regulated or limited by the rights of other landowners is owned outright. This basic concept permits enormous flexibility in the American economic system. Those who hold such rights can divide and redivide these interests in thousands of ways, and our complex private economy attests to the inventiveness of American property owners to find the highest and best use of various aspects of land ownership.

By contrast, the basic element of ownership of Chinese land is far more limited. The "granted land use right" is given for an identified period - 40 to 70 years depending upon the purpose for the grant. Although, theoretically, there are some renewal rights, the time for renewal of any such rights is still well in the future, and the terms of renewal remain uncertain. The right is given by government only for purposes of implementing a particular use, and permission must be obtained to change the use. It should be noted, however, that in most cases these use restrictions are no different than use restrictions typically imposed in America through zoning and land use laws. A more important limitation is that speculation in raw land is restricted through the requirement that the user commence the required use within two years. If the property is not developed, it cannot be transferred and in fact it may be forfeited back to the government.

In addition, it should be noted that the land use right in China does not carry with it the extended package of rights to subsurface and above surface activities that American ownership typically has included. The Chinese government continues to control all mineral resources and air rights. Over time, the U.S. has moved to a significant restriction of these rights in American property as well, however.

The granted land use right is similar in some ways to the long-term ground lease that is commonly used in America to develop commercial sites. The difference is that the Chinese right is obtained from, and reverts to, the government, rather than a private owner, and the consideration for the right is paid “up front,” and is forfeitable if the property is not developed.

Chinese granted land use rights are protected from expropriation without compensation.

China has a reasonably reliable system of registration of land use rights that permits identification of the owners. In an important recent development, China has established that there shall be unrestricted public access to these land records nationwide - an important development that western investors have been seeking for some time.

Since the land use right can be transferred, China has developed a system of rules governing the leasing, mortgaging and sale of these rights. The rights can also be inherited and there are rules concerning division of the rights upon divorce. Generally speaking, the various legal rules that have been developed reflect the Chinese predilection to favor control and guidance from government over individual freedom of choice. Leases cannot be for more than 20 years. Lenders are strictly controlled as to how much they can lend against the value of the land.

Although the relatively new Basic Law of Contract proclaims that the parties are free to contract as they please and that their bargains will be upheld, it remains to be seen whether bargains will be upheld that create interests that are inconsistent with the many regulations of the Bureau of Land Administration or the Ministry of Construction. For instance, one Chinese mortgage rule requires that all leases continue to exist following a foreclosure of the landlord’s interest. In America, by contrast, there is extensive bargaining among lender, landlord and tenant with respect to the possible impact of foreclosure on the tenant’s rights, and a wide variety of outcomes are possible. Another rule gives lessees a “right of first refusal” to renew at the end of the lease term or to buy if the landlord should sell the underlying ownership of the land. It is unclear whether this right can be “bought out” in advance, although clearly many Chinese transactions attempt to do this.

The Chinese legal system still does not recognize formally many concepts that apparently are being developed within the transaction system. There is no clear “easement in gross,” for instance, so it is unclear under what rights parties can extend pipelines or power lines. Although hundreds of millions of Chinese have moved into condominium residences in the last five years, there is no clearly developed condominium law spelling out their rights and responsibilities toward one another.

There is a proposal to include a section on property rights (“rights *in rem*”) in the new Chinese Civil Code that is expected to be considered for adoption this year. There have also been proposals made by high Chinese leaders to amend the Constitution to provide better protection for property interests, but the nature of these new changes remains uncertain.

1.3. Other Property Rights and Expectations:

1.3.1. Homestead Rights:

There are some rights to “homestead properties” that have been recognized as traditional interests virtually since the establishment of the People’s Republic. These properties exist both in urban and rural areas. The nature and basis of the rights has always been somewhat uncertain, as has been their number. Homestead rights, however, have never been viewed as granted land use rights, and it is unlikely that they have much protection against appropriation by government. Some people with homestead rights have been able to convert them to granted land use rights and now have a protectable interest. Others lack the sophistication or resources to carry out such conversions, and their interests remain vulnerable.

1.3.2. Occupancy Expectations:

After the Cultural Revolution, many people found themselves residing in or using properties as to which there were no clear rights of occupancy. Records had either been destroyed or never produced. As development has progressed, many of these occupants have been forced to relocate. The granting of land use rights on property that has been occupied in this way usually has required that the grantee pay for the relocation of those on the land, whether or not they had any formal right to be there. Twenty years ago, these persons were given quite a lot of informal protection through the negotiation of the granted land use rights.

In recent years, the sale of granted land use rights has become an important source of revenue for local and provincial governments, and there appears to be less solicitude for “undocumented” occupants of property that is part of a granted land use right. Although in theory the government can require the grantee to pay the cost of relocation, I have heard that the bargains over such relocation have led to less generous settlements.

1.3.3. Household Responsibility System - Agricultural Land

The system of granted land use rights has been used primarily in urban areas and for industrial and commercial development in the countryside. Agricultural property in the countryside has been under the control of agricultural collectives who have reallocated the property under their control to individual peasants under a system known as the “household responsibility system.” Peasants live and work on their allocated farm plots and have some autonomy in the management of their agricultural enterprises. We have heard stories recently of the wholesale breakdown of this system in the countryside as opportunities have arisen to consolidate land for purposes of corporate farming or industrial or commercial development. It appears that the individual peasants may in many cases be relinquishing their household responsibility ownership voluntarily for these purposes, but we have heard many reports that they do thereafter receive benefit from the reapplication of the property to other purposes that one would have expected them to enjoy as members of the Collective.

This problem may be a problem of failure to enforce legal rights and it may be a problem of simple fraud and sharp dealing by leaders in these countryside Collectives. Reports are, however, that the phenomenon is widespread in rural China.

A very recent new statute addressing some of these issues has been passed, and is discussed by another panelist. It remains to be seen whether the statute will be effective to slow down what appears to be a widespread movement.

2.0. Problems with enforcement of legal rights.

2.1. The problem of diffusion of legal power:

It is important to recognize that legal power in China is widely distributed. The popular U.S. image of the all-powerful monolithic central government is not an accurate picture of China in the area of economic rights. It is true that there is a tradition of overbearing government control in China, and consequently when central government and local government interests coincide, or at least do not conflict, it would appear that the Central Government has the power to effect strong controls over the population.

But in the area of division and management of economic resources such as land, there often are conflicts between the Central Government and provincial and local authorities. The Central Government lacks the political and social strength to prevail in many of these conflicts. Thus, even when the Central Government proposes a system of legal rights and expectations that may be sufficient to form a basis for a successful market system, it is up to the Provincial and local governments to provide effective enforcement mechanisms to insure that the system really works.

In Guangzhou, Shanghai, Beijing, and other important commercial centers, there is recognition that a transparent legal system is vital to attracting investment capital and encouraging economic risk taking. Consequently, the legal system tends to follow the dictates of the Central Government rules, although extensive additional local control over real estate practices is commonplace. Often the local regulation in these areas, in fact, is benevolent, and assists in promoting effective market transactions by “filling in the gaps” of national rules.

This happy story of cooperation, however, is not repeated in many other areas. Local, County and Provincial governments control large sections of the taxing system and control the payrolls and other benefits that support courts and other agencies that are nominally organs of the Central Government. Consequently, when conflicts arise between local government interests and the interest of stability and predictability in the legal system, judges and administrators find themselves often under intolerable pressure. We have heard many tales of foreclosure proceedings delayed into exhaustion, of transfers of land use rights without regard to government-required plans and pursuant to special negotiations that might be viewed as inconsistent with concepts of fair opportunity.

If anything, the current frenzy of land development in China has increased the motive and opportunity for local leaders to ignore the rules in the name of expediency. Often this situation provides a breeding ground for corruption, and even more often individual property rights are frustrated by such activities. We saw similar abuses occurring during “boom time” periods in the development of our own country, and I suggest we should be neither surprised nor too dismayed that such things are now happening in China. Ultimately, as we have seen in the larger cities, a recognition is likely to develop that orderly process and clear rules will lead to greater economic prosperity. Egregious examples of corruption are periodically identified and dealt with, although cynics might argue that such activities are really ways of disposing of the most difficult political enemies rather than the most troublesome thieves.

2.1. Addressing the problems:

As I have suggested, to a certain extent, the problems observed in China are “boom time” problems that will disappear over time. But certainly an important factor in these problems is the lack of adequately trained lawyers and judges. Often departures from the national system of property management and destruction of property rights occur because no one in the local area really understands what the legal rules are.

Although there are a large number of Chinese judges, many of them lack formal law training and, unlike in America, even those with formal law training lack much experience in law practice. Further, there are few lawyers in many areas capable of insuring that their clients’ interests are protected by law. The concept of the rule of law has only lately arrived in many Chinese provinces, and established lawyers have been successful by paying more attention to cultivating friends rather than advocating legal principles.

There is a need to educate lawyers in many areas of China as to the nationally mandated rules and procedures involved in the creation, transfer and protection of property rights. There is a similar need to provide such education for judges. Further, there is a need to encourage capable graduates of China’s law schools (which have grown exponentially in recent years) to move into the outlying areas of China and to avoid the existing concentration in the major financial centers.

2.2. Special needs in the housing market:

In a recent meeting with leaders in China’s housing industry, there was general agreement on the need for several social or legal developments to occur to facilitate the continued growth and prosperity of private property exchange in China:

- A national system of reliable credit analysis and review.

- Development of autonomous and responsible owners associations in Chinese housing complexes.
- Development of an industry for the resale of residential property (now most Chinese housing is still occupied by the original owner.)
- Development of real estate specialization among lawyers, who now are poorly prepared to address real estate problems in the residential marketplace.
- Resolution of the many conflicting provisions of Chinese real estate law and greater contractual autonomy in the commercial marketplace.
- Meaningful consumer protection in the housing development, finance, and resale markets.
- Clear rules regarding bankruptcy.
- As discussed above - adherence to national laws and enforcement of those laws by courts and administrators.

2.3. The special problem of corruption:

China needs to continue to be vigilant in the suppression of corruption. In my years in China, public concern about corruption has become the single greatest complaint from the Chinese citizens I meet. Ask any Beijing taxi driver!!

Land use rights are sold and regulated by local officials. As public land now passes into private hands, there are enormous opportunities for profiteering on two fronts. First, Chinese officials who generate revenues from the sale of the land have power to allocate those revenues. In many cases, these revenues may be used to finance joint venture investments by which individuals make great profits through the exploitation of these government funds. Although a 1998 law requires that proceeds from the sale of arable land be reinvested in the development of more arable land, there is widespread belief that this law is being ignored in favor of diversion of monies into other enterprises of more direct interest to the specific public officials who control the sale of land use rights.

A second means of corrupt practice in the creation of land use rights, of course, is in the identification and regulation of those who receive land use rights. In some areas, concerns about corrupt practices in the awarding of land use rights to favored persons at low prices reached such a pitch that sale by auction was required. But almost as soon as the auction requirement was enacted, exceptions to the rules crept in that preserved the options of local officials in "special cases."

In some cases, the creation of a "political machine" may have the short run benefit of insuring stability where law may not accomplish that result. For instance, there is little question that most housing development is being carried out by favored developers who have the inside track on obtaining land use rights for these purposes. But the fact that they are on the "A list" may lead these developers to be extra cautious to insure that they actual produce the housing that is called for and that no scandals result in terms of shoddy housing or sharp practices that may jeopardize their ability to continue in their favored position. Indeed, we hear remarkably few complaints about consumer housing considering the size of the market.

Inconsistent regulation of land use development also can be a problem. Since the power of forfeiture for failure to develop is so draconian, it is likely that there is some extortion going on where the possibility of forfeiture exists. The Chinese likely would be wise to consider less drastic interim measures to cope with problems of slow development in order to ease the friction at this point in the system.

A country that lacks a free press is particularly vulnerable to corruption. Perhaps China's greatest challenge in the economic arena is to secure the confidence of its population in the fairness and openness of its system of economic regulation, and China's concern that unrestricted freedom of the press endangers stability in other areas makes the achievement of such confidence far more difficult.

3.0. The significance of property rights and human rights.

It should be noted at the outset that the recognition of property rights in China has occurred for economic reasons - to encourage individual responsibility for economic decisions that will fuel an effective marketplace and an adequate distribution of resources. China wants its population to have a better physical standard of living, and believes that market principles may achieve that result. In short, it can be said that the Chinese value individual property because this is in the best interests of the collective.

Although these considerations also are present in our political system, the recognition of property rights in America is more fundamental, and reflects a social and philosophical balance that is not necessarily a part of Chinese political philosophy. We tend to view our citizens as deserving of individual liberty and autonomy, and the recognition of private property is an important part of that personal autonomy. Consequently we view individual property rights as a distinct objective, and may sacrifice the interests of the collective in some circumstances in order to protect such rights.

In evaluating the progress of individual property rights in China, we should maintain our focus on why China is promoting these rights, and not expect more from China than it is reasonable to expect.

On the other hand, I believe that the development a greater degree of individual autonomy that inevitably results from the protection of property rights will lead, ultimately, to stronger individual rights in other areas of Chinese life as well. Those who have something to protect and preserve often seek a greater voice in government. Chinese government is not closed to the voices of the people. It is not as responsive to those voices as might be the case in a democracy, but neither is the Chinese government a despotic and uncaring parasite. But at present many Chinese citizens are “apolitical.” As citizens in China increasingly become aware that governmental policies will have a direct result on their opportunity to keep what they have and obtain what they want, they will demand a greater voice in government, and will demand that government respect their autonomy.

A significant problem in this development, of course, is the fact that the Chinese government’s second great goal, concurrent with economic development, is political stability. The development of greater citizen participation in government threatens those with entrenched power, and it is only a short step from perception of a challenge to ones power to the conclusion that government stability is in danger. But the development of individual property interests is so much a part of the economic system at present that it does seem unlikely that Chinese officials will take significant steps to frustrate such expectations. Accommodation of political change, therefore, is possible and it is likely that the change will be in favor of greater levels of individual autonomy.

Other institutions in the society that serve to promote the market economy - such as the development of trained lawyers and other social advocates, private trade associations such as brokers groups and owners groups, and the free exchange of information that necessarily flows through a market economy, will lead to social expectation of greater power and gradual reform.

Consequently, U.S. policy in the area of Chinese real estate ought to be to recognize that a healthy system of exchange of private real estate interests is likely to lead ultimately to demand for and realization of a greater individual autonomy and citizen voice in government in China, both goals that are critical to the greater development of human rights.