

The Solution of the Dependence on Land Finance with the New-type Local Taxation System

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Abstract

The Third Plenary Session of the Eighteenth CPC National Congress put forward again that we should adhere to the new path of urbanization with Chinese characteristics, which has attracted the attention at home and abroad. In the past, the urbanization of our country mainly demonstrated as "land urbanization", which led to the emergence of the local government land finance, widened the gap between urban and rural development, manifested interests contradiction between urban and rural areas. Therefore, it is necessary to guarantee that local governments have sufficient sources of fiscal revenue in order to break dependence on land finance for the purpose of making the construction of the new-type urbanization becoming the engine for the economic growth in China. The corresponding specific measures are: first, we should perfect the legislation; second, we should straighten out the fiscal power and the administrative authority between the central and local governments harmoniously; the last and most important one is that local governments are authorized to adopt the innovative measure of "municipal securities and local taxation system".

Keywords: New-type Urbanization; Land Finance; Local Taxation System; Overseas Experience; Legislation and Perfection

1. Introduction

Since the 21st century, the urbanization in China has made significant progress, while urbanized rate has increased from 36% in 2000 to 52% in 2012. However, the previous urbanization was mostly extensive and low-level development that focused on city scale and urban population. It's far from the intensive and high-level urbanization, which not only focuses on the upgrade of city scale and urban population, but also pays close attention to the integration of rural area and urban area, interaction between urbanization with cities, and the in-depth urbanization and synchronized development among industrialization, informatization, urbanization, and agriculture modernization based on rural-urban integration. Therefore, it has to take financial system building as source and "municipal government debt + local tax system" as innovative measure to guarantee sufficient financial support to urbanization, break the bottleneck of land-based finance and promote the Chinese characterized urbanization that is more appropriate for the development of social economic .

2. Materials and Methods

2.1. Land-Based Finance's Negative Influence Urbanization

Since the implementation of Tax Distribution System in 1994, China has gradually formed the asymmetric finance system in which financial power has gradually centralized to central government while administrative power has been gradually provided to the regional government, resulting in that the regional governments have to shoulder abundant responsibilities with insufficient financial support. Under such circumstance, in order to increase public finance income, regional governments raised finance from land development and got loans from local financing platform. Therefore, they needed to remarkably count on land-based finance, which led to the disorder expansion of urbanization and rapid growth of housing price, regional government financial debt risk and land financing risk and brought negative influence to the development of the real economy and economy reconstruction. As a result, we should pay more attention to it.

2.1.1. Land-Based Finance has Made Regional governments to Suffered Significant Debt Risk and Finance Risk

In recent years, in order to cover the significant expenditure in urban construction and civil project construction, regional government had to adjust the land-based finance mode, in which land served as the mortgage to get large amount of fund from financial system and caused that capital from commercial banks rapidly combine with the land capital.[1] According to the result of random investigation on 36 regional governments in 2012 issued by the National Audit Office in June 2013, the total debt of the investigated 36 governments has reached 3.85 trillion. Among them, the debt ratio of 16 regional governments has exceeded 100%, while the highest one reached 219.57%. How will the governments repay so huge amount of debt? Actually, since 1979, the land transfer fee has been the major source for regional government's debt repayment. Among the total 18 provincial capital cities in the random investigation, 17 cities promised to repay debts by land transfer fees. They totally needed to repay 231.573 billion RMB, around 1.25 times of total disposable land transfer income of the year (Chinese National Audit Office, 2013)[2], showing the serious situation that the revenue of regional governments ran behind their expenses. The scarcity of land resource had determined that regional governments that counted significantly on land transfer fee wouldn't have stable or sustainable land-based finance. However, the ability of land mortgage's debt-repaying ability is subject to regional government's ability in land business operation and public finance income, while the instable financial income and over-dependence on land-based finance have significantly increased the financial risk. It will be gradually transferred to national finance and finance system level by level.[3] As a result, in case that the land-based finance cannot be overcome, it will become the potential factor for regional government debt risk and financial risk.

2.1.2. Not beneficial to lower the remarkably high housing price

In recent years, the significantly high housing price issue was increasingly highlighted. Though the

State Council has issued stricter and stricter control measures to keep the housing price down while facing its actual rapid increase, each control measure finally turned out to be a catalyze for the new round of housing price increase and pushed to housing price to a new height. From 2003 to now, there are totally 43 macro policies related to real estate issued while the housing price has increased by 10 times(Xiaoyuan Zhou,2013)[4].Since the housing price is subject to land price, the high land price would surely result in high housing price.It's obvious that regional governments' noncooperation to the housing price control policies by creating new highest land prices, which is closely related to growing land price. According to door investigation executed by National Bureau of Statistics in urban population, from 2003 to 2010, the average annual growth rate of land price is 22.9% while the average annual housing price growth rate is 16.1% (Hongzi Wang,2013)[5].Meanwhile, the rapid increase land price has brought remarkable finance income. According to statistics, from 1989 to 2012, the ratio of income of land transfer in total local finance income has increased from 0.24% to 74.14 %, around 308 times of growth(Yejun Wang,2013)[6].Regional government' over-dependence on land-based finance has resulted in the convergence of interests between regional governments and real estate developers. The regional governments, by transferring land on open market and increasing the market price of land, indirectly increased the housing price. Therefore, it has gone beyond the central government's macro control power on housing price[7].As a result, once the issue that regional governments over dependence on land-based finance, there couldn't be any chance of drops in housing price.

2.1.3. Not Beneficial in Solving the Difficulty of Current Land Expropriation System

In recent years, the public issues caused by land expropriation have increased remarkably. The cruel dismantlement on the house of urban citizens and house owner's violent resistance to dismantlement occasions could be frequently read on media. Therefore, the public had keen requirement on modifying and improving the current land expropriation system. However, no achievement has been made up to now. The reason is that current land-based finance system in which the regional government runs the land business has become the financial basis for regional government[8]. Limited by the pressure from providing service support to the increasing public demand[9] and performance evaluation system, the regional government, as a rational economic entity, searches for the maximum benefit through land transfer in accordance with law. However, on one hand, the execution of land expropriation plan suffers no influence from land expropriation compensation and relocation dispute; on the other hand, regional government could transfer the expropriated land at the market price of urban construction land. As a result, the low compensation may violate rural people or resident's interest and therefore results in social disputes and instability. It's said that the over dependence on land-based finance will make land property right, land expropriation, compensation and lease system become the convenient legal door for regional government to acquire land transfer income. It's not beneficial in solving the difficulty of current land expropriation system and promoting the in-depth reform to current land system.

2.1.4. Stop the real economy development and economic structure update

Since real estate industry provides high profit, many capitals that could have been invested in real

economy were finally invested in real estate industry or participate in speculation of real estate for the sake of seeking for maximum profit. For example, Midea Group, which is famous for manufacturing housing electronic appliance, couldn't help joining the real estate development industry. Therefore, the prosperity of real estate industry has significantly prevented real economy from enjoying stable development. What's more, it adds more risks to the housing price bubbles. In the aspect of Finance System, the total amount of issued credit loans increases remarkably, while the whole economy is in the slowing down pace, since banks tend to issue their loans to real estate enterprises that enjoy high profit rate instead of manufacturing enterprises. Let's take Guangdong Province for example. From January to May 2013, the newly increased credit loans to real estate industry has taken up 33.1% of total newly increased credit loans, increased by 24.1% compared with last year(Haiyan Guo,2013)[10]. It objectively caused financing difficulties to manufacturing enterprise. As a result, the real economy suffered insufficient growth. In the aspect of consumption, China suffers imbalance economy situation of intensive investment and exportation but poor consumption. The reason is that social security system is relatively low. Citizens have to bear high retirement cost, medical cost and education cost based on relatively low income. As a result, people in China have to keep saving money for the sake of preparing for unexpected use, while the high housing price has further restrains Chinese people's consumption desire. Under the circumstance of high housing price, the demand on house won't simulate any consumption. Instead it further restrains people's consumption desire. Therefore it seriously prevents Chinese economy structure from updating.

2.1.5. Trigger disorder urban expansion

Encouraged by the land-based finance income, regional government, in order to collect more urban land using quota, significantly increases the city scale, resulting in a phenomenon that the land urbanization is much faster than population urbanization during Chinese urbanization [11]. In accordance with the demand in simulating regional economic growth and maintaining long term tax income, the current urbanized land is mainly used for production used, such as industrial development zone, housing improvement to current urban residents and the construction for supporting facilities, rather than creating living place for migrant workers(Ran Tao and Guangzhong Cao,2008). [12]Meanwhile, since regional government frequently expropriates land from rural people and transfer the land for gaining finance income, it finally causes that the speed of land expansion is faster than population urbanization and that urban land is being used extensively with low efficiency. On one hand, the disorder urbanization has caused mess in land use plan and waste of farming land. On the other hand, the waste of farming land restricts the sustainable development of land-based finance (Chinese Land Resource 12th Five-Year Plan Outline). As a result, regional government is trapped into a vicious circle.

2.2. The Reference of Foreign Urbanization

The land-based finance is not the unique phenomenon of China, but a common phenomenon for many countries during their urbanization. However, western countries mainly adopted the way of collecting building tax on existed land to compensate the regional finance income. It can not only provided tax

equality but also helped regional government in gaining relatively stable income. Especially in countries with developed market economy, they adopted the method of passing sophisticated regional tax laws to improve land tax system and adopted the method of issuing municipal bond to guarantee regional government have sufficient financial support to fulfill its other service functions.

2.2.1. Establish laws to classify the administrative power and financial power of central government and regional government

Regional Tax System refers to the organic system consists of diversified regional tax, clear taxation power, rational tax system as well as independent collection and management.[13]The fiscal federalism system between federal government and regional governments in developed countries adopted the legislation to determine the administrative power with equivalent financial power to provide system guaranty to the establishment of sophisticated regional taxation system.[14]

America is a county that adopts federalism and establishes three levels of finance system based on federal level, state level and regional level. In addition, it adopts legislation to clearly determine the administrative power, financial power and transfer payment for governments of different levels. It's the precondition for its taxation power classification. The Federal Constitution classifies administrative power into four kinds: the exclusive federal power, the non-fixed and shared responsibility of federal government and state government, responsibilities dominated by state government and responsibilities borne by regional government. In the aspect of financial power distribution, the financial powers of federal government, state government and regional government are independent, while their own part of tax collections are performed by the responsible government independently without inter depending on each other. Federal government will not interfere regional government and state government in the aspect of tax collection and expenditure (Martin Bronfenbrenner,2009).[15]

Japan is a country with single political system. However, it also classifies tax power into three levels based on central government, provincial government and municipal government. Meanwhile, it made regional government to be under the administration of central government. Japan centralizes the tax legislation and taxation into congress. However, regional government can establish extra regional tax, while central government has the right adopt tax veto system to limit regional government in collecting extra tax[16].Meanwhile, Japan adopts the principle of administrative responsibility and outstanding efficiency to determine the administrative power of central government and regional government by stating that regional government shall provide most public products and services while central government enjoys most financial income[17].In addition, the central government adopts large scale transfer payment to ease regional government in revenue pressure to maintain their balance. [18]

2.2.2. Legislate to regulate regional government's municipal bond issuing

Municipal bond is also known as regional government bond, which is issued by regional government or its authorized agencies. The collected fund will be used in constructing municipal or regional facilities, compensating the the municipal government's expenditure, covering the imbalance expenditure or seasonal fluctuation of finance tax income.

Allowing regional governments to issue municipal bond is the common way among countries with developed market economy. Meanwhile, it gradually becomes the policy focus among rising industrial countries and developing countries. Since the middle of 1990s, the regional municipal bond market enjoyed the trend of rapid growth in the world. In North American countries, European countries and Japan, the municipal bond played an important role in its financial income and bond market system. Among them, Municipal bond in America enjoyed the earliest issuing and largest scale, covering around 20% of total government debt. In developing countries, with the progress of urbanization, regional government's finance income was no longer sufficient to meet the huge investment demand of facility construction projects. Therefore, regional government had to keep improving resource utilization rate, strengthening its budget management and guiding private capital to invest in public service industry and facility construction. Therefore, the regional government shall adopt municipal bond to improve financing efficiency and promote the stable development of bond market.

Though issuing municipal bond is beneficial, it may trigger remarkable debt risk and finance risk in case that municipal bond is issued and managed in an inappropriate way. Therefore, many countries have gradually established risk prevention and supervision system by establishing corresponding laws and regulations. For example, the American Congress has established Security Act of 1933, Security Exchange Act of 1934 and Dodd-Frank Act of 2010. Meanwhile, the Municipal Bond Analyzer Association and Financial Official Association in America established a number of industrial self-disciplines to regulate information announcement. Therefore, America gradually formed the risk supervision and prevention system that takes laws and regulations as backbone, industrial self-discipline as assistance, information announcement as core and scale control, credibility ranking, risk prevention as well as risk solution and method to provide effective source guaranty in preventing systematic issue to regional government's issuing of municipal bond.[19]

2.2.3. Legislate to create land banking system

Land banking is that government or other public organizations or groups purchase land from private or other organization and reserve the land before land development projects, so that government could keep a low construction cost, control land market and realize the orderly development for land in future urban development, commonweal residence projects, traffic projects, green belt projects or other public products. Land banking system has long been formed in developed countries. In 1896, the Netherlands, in order to solve the issues of housing shortage while urban population grew in a rapid pace, firstly created the land banking system. Soon, it was adopted by most European countries and North American countries as well as the rapid rising Asian countries.

The comprehensive review on the land banking system in developed countries shows that it has below features:

Firstly, it could help government to execute policy for increasing social commonweal project and enrich land banking. Under this precondition, Congress in Sweden and other countries established different policies based on their own situation and purposes, including the policies to solve housing shortage due to sharp growth of urban population, the policies to control land market price and the policies to optimize

urban living environment.[20]

Secondly, Land banking management are mostly dominated by regional government while only a few of them are dominated by organizations under the administration of regional government or the land development companies held by regional government.

Thirdly, government mainly expropriates land by signing agreements with original residents. However, America is different, as it mainly expropriates land by exchanging or setting lease right. In order guarantee that the land in land banking will not affected by expectation factor, the government's expropriation will not be executed publicly so as to prevent sharp increase in land price caused by the expropriation project.

Fourthly, the fund source for land expropriation normally is mainly the assistance and loans from central government, fund collected by regional government's issuing of municipal bonds and regional tax income. The combination of above fiscal and financial measures is able to provide stable and reliable fund support to the effective land banking system.

Fifthly, a serial of laws on land price and tax were established to cooperate the execution of land banking, so as to release the fund pressure for land expropriation.

Sixth, the operations of reserved banks normally include both lease and sales. Some would be mainly adopted for lease while some will be mainly adopted for sales. The price for land lease and sales is not subject to expense that government invested in it but the land usage or purpose.

3. Result and Discussion

Surely, in order help regional government in completely overcoming the over dependence on land-based finance, legislation method shall be adopted with below measure: on the basis of clearly classifying the administrative power and financial power of central government and regional government, the regional government shall be authorized to adopt innovative measure of regional tax system + municipal bond to guarantee sufficient fund for regional government so as to enable it to overcome the over dependence on land-based finance

3.1. The taxation organization shall be reformed to build to harmonious relation between central government and regional government on administrative power and financial power.

The establishment of harmonious relationship between central government and regional government on administrative power and financial will guarantee that regional government can acquire corresponding financial income. The current experimental project of Changing Income Tax to Value Added Tax aims to adopt the VAT to replace the largest regional tax, the income tax. It accelerated the declination of local taxation bureau. As a result, the topic of integrating state taxation system and regional taxation system was put on the agenda again.

In the opinion of the author, the integration of state taxation system and regional taxation system meets the idea of deepening administrative system reform, lowering administrative cost and promoting the large ministry system reform put forwarded in the 18th CPC National Congress. Meanwhile, some places have acquired the authorization from central government for executing large ministry system

reform. Take Guangdong for example, the plan can be divided into Class 1, Class 2 and Class 3 strategies. The Shenzhen mode that combines regional taxation system with local financial organization while state taxation system is under the direct administration of central government is the Class 3 strategy. The Shanghai Mode that integrates Finance Department, State Taxation System and Regional Taxation System into the same organization with three different names is the Class 2 strategy. The comprehensive reform that integrates finance system, taxation system, custom system and even SASAC into the Finance System to form a Ministry of Finance based on Large Ministry Reform by taking taxation right and financial rights into comprehensive consideration to completely change financial power range and classification way between central government and regional government is the Class 1 Strategy.

Meanwhile, central government shall change its administrative power classification with regional governments, so that it could syn chronically promote the reform to the classification of the broad sense of financial power, administrative power and ownership (for state-owned enterprise) by taking taxation right, financial power and ownership into the comprehensive consideration of full financial power. As a result, the classification range and classification of financial power classification between central government and regional government can be clearly determined in accordance with law. In addition, the financial power can be provided at the ratio of 5:5 in accordance with its administrative power. The national finance income (tax income) will be collected by finance departments of all levels into the national treasury. After that the finance income will be audited in accordance with its source place within given time and returned to regional financial department in accordance with legal ratio, so as to realize that there is financial power with equivalent administrative power, responsibility with equivalent financial support for both central government and regional government.

3.2. The legislation shall be adopted to update regional taxation structure and build Chinese characterized regional taxation system

Only if the income distribution system reform between central government and regional government is deepened, can regional government have the financial power equivalent to its administrative power to gain sufficient financial support for handling the increasing heavy local duties. Meanwhile, it's shall be clearly determined that regional government cannot have any other incomes other than tax. In other words, the land transfer fee shall be canceled. The mode that regional government take land transfer fee as major income shall be gradually changed to the mode of regional taxation system established in accordance with law, for the sake of completely eliminating the foundation for land-based finance.

Firstly, the regional taxation system shall be established in accordance with law and regulation. Currently, there are only four laws on taxation, while most regulations are built based on administrative regulations which are inferior to law. They have insufficient authoritativeness and consistence. The unstandardized system is not effective in motivating the construction of a high quality and stable regional taxation system. Therefore, legislation shall be adopted to promote the construction of regional taxation system.

Secondly, the regional taxation system shall be improved. In the reform of Changing Income Tax to VAT, change to the financial power of central government and regional government has been made. How

to follow the trend of reform and optimize regional government's financial power so that it could be equivalent to regional government's administrative power, in the opinion of author, can be fulfilled by below change. Authorizing the regional government to impose individual income tax, property tax and consumption tax based on real estate property and land VAT to improve regional taxation structure. The reason why consumption tax was integrated into regional taxation system is that, since individual income tax and property tax is only in small ratio, taking consumption tax into regional taxation system could enable regional tax income to cover 60% of national tax income.

3.3. The innovative measure of issuing municipal bond shall be protected by legislation to guarantee that regional government has sufficient financial source

By learning from municipal bond issuing experience in developed countries with advanced market economy and taking China's experiment that central government issue bond on behalf of regional governments while Shanghai and Guangdong's regional government could issue government bond independently into consideration, under the circumstance of improving risk prevention system by issuing laws on central government and regional government, the regional government (of provincial level) can be authorized to issue municipal bond. It's the common method among countries that adopted tax distribution system and graded finance system. The repayment for regional bond comes the cash flow accumulated in land development during urbanization, including stable regional tax income, fees submitted by user of public facility and other service and the different kinds of tax income growth brought by economic prosperity. As a result, regional government can have sufficient financial income and no longer needs to collect benefit from land by competing with the public, so that urban land will become the carrier for migrant worker's residence and life and urban development will enjoy the benefit of huge amount of human resource in China to prevent of early arrival of Lewis Turning Point.

From the aspect of establishment of risk supervision structure system, in order to prevent and control regional government's debt risk, we shall carefully learn from the experience of countries with advanced market economy and strengthen system building to strengthen the supervision on municipal bonds. Meanwhile, we shall entitle the China Securities Regulatory Commission, China Banking Regulatory Commission and other market supervision organizations to establish corresponding regulations on information announcement and gradually form the risk supervision system that take laws and regulation as foundation, take information announcement as core and takes scale control, credit ranking, risk caution and crisis solution as method, so as to provide effective system guaranty to the prevention of systematic risk to municipal bond in the aspect of government and market supervision.

3.4. Reform the land transfer system and fulfill land banking's modification function

In the promotion of new urbanization, after taking thorough reform of finance and taxation system into consideration, in the opinion of the author, China's land transfer system shall be modified immediately. The original principle that the organization which offers highest price in land auction gets the land will always result in that the final price is always higher than actual price. Under the circumstance that land supply is dominated by government, it will always try to whoop up the land price

and therefore directly cause the rapid increase of housing price. As a result, the land transfer system needs urgent reform and modification.

Firstly, we shall improve land banking system and independent land transfer function. In China, the current system integrates land management and land operation function in one department. Therefore, it's hard to avoid illegal behavior in land market through power distribution. As a result, the land operation function can be separated by establishing an independent management organization to take charge of state-owned land operation in accordance with market principle under control and supervision of government. During this process, unless that state-owned land is expropriated for facility construction, public service projects and non-operation projects, government shall not participate in any land expropriation, so that the construction land demand and supply will be marketized. Correspondingly, government's land supply target shall be modified to meet the housing demand of growing urban population.

Secondly, the land transfer fee collection and distribution shall be reformed. The Chinese Constitution has clearly stated that land is owned by the country; therefore the benefit collected by independent land operation organization during its operation shall be submitted to the country. By submitting land benefit to the country could not only avoid the current regional government's over-dependence on land-based finance but also is able to fulfill land transfer fee's positive function in income distribution. [21]

4. Conclusion

In conclusion, it is necessary to guarantee that local governments have sufficient sources of fiscal revenue in order to break dependence on land finance for the purpose of making the construction of the new-type urbanization becoming the engine for the economic growth in China. The corresponding specific measures are: first, we should perfect the legislation; second, we should straighten out the fiscal power and the administrative authority between the central and local governments harmoniously; the last and most important one is that local governments are authorized to adopt the innovative measure of "municipal securities and local taxation system".

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