

Dear Comparative Politics Workshop participants:

Thank you very much for taking time to read my proposal! This is a draft of my dissertation prospectus, which will also serve as a funding application proposal. Generally, any suggestions on how to enhance my chances of getting funding are welcome! Specifically, comments and suggestions on the following aspects are appreciated:

1. How can I make a stronger argument to funding-providing institutes and my dissertation committee that I *CAN* finish this project?
2. In the theoretical model, ordinary people are totally ignored. Do you think I will gain some value-added by including a new player: the mass? Or should I keep the model as parsimonious as possible?
3. Is there an easier and more feasible way to measure the rule of law?
4. I am trying to come up with some alternative explanations, any ideas?

WHEN DICTATORS PLAY BY THE RULES: THE DEVELOPMENT OF THE RULE OF LAW IN CHINA

DISSERTATION PROSPECTUS - DRAFT

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I. Introduction

After the disastrous Cultural Revolution, China resumed its state building process in the late 1970s, in which institutionalization of the formal legal system is a crucial component. Today China has a nationwide court system including over 3,000 basic courts and almost 200,000 judges (Cohen 2005). The Chinese Communist Party (CCP) is mobilizing a mass campaign for rule of law.

However, there is a consensus among scholars that rule of law is too pie-in-the-sky right now in China. Even optimistic students of Chinese law have an endless list of flaws of the legal system (Peerenboom 2002). Clarke, Murrell, and Whiting (2008) point out that, an important feature of the Chinese judicial system that works against unity and consistent enforcement is the dependence of courts on local government. Lubman (1999) depicts China's legal institution as a "Bird in a Cage" which is struggling with formal and informal environmental constraints.

Although there is a strong national initiative, the development of rule of law is quite uneven across the country. A study I did in 2007 (see Shen and Wang 2007¹) showed that citizens' preference of the formal legal institutions varies greatly over space, and surprisingly, the variation cannot be explained by level of economic development (Figure 1). Data on performance of legal institutions is still lacking, but we can expect a similar extent of variation. *This project is an attempt to evaluate the performance of the formal legal institutions and explain the variations of rule of law at the sub-national level in China.*

[Figure 1 about here]

II. Two Puzzles and Two Models

This project is motivated by two puzzles:

1. *How do local state agents in China overcome collective action problems to provide a particular type of public goods: the rule of law?*

¹ We found that economic growth rate has a *conditional effect* on people's preference: in low level of development, economic growth rate has a significant positive effect, but this effect becomes smaller in highly developed regions.

The Rule of law has both features of a public good: it is non-rival and non-excludable. Consumption of a quality law or a fair court by one individual does not reduce availability of the good for consumption by others; and that no citizen can be effectively excluded from using the good. Provision of rule of law, therefore, faces collective action problems. Building the rule of law, which consists of quality legislations, ubiquitous enforcement, fair legal procedures, and consistent implementation of court decisions, needs cooperation among politicians. In a single-party authoritarianism, where local legislatures, local courts, and local bureaucracies are all under the autocratic rule of local communist party committees, why do local party leaders, instead of seeking a free ride, bear the cost to build a fair legal system?

2. *Why are local "dictators", with the means of repression in their hands, induced to make their own behavior predictable by building the rule of law?*

Unpredictability is an effective means of autocratic rule. Examples of unforeseeable policies are numerous in dictatorships. In summer 1957, Mao Zedong initiated the "Hundred Flowers Campaign" to encourage intellectuals to criticize the new communist regime. Professors started to speak out: from June 1 to July 17, 1957, millions of letters were pouring out. In mid-July, 1957, Mao ordered a halt to the campaign and started the "Anti-Rightist Campaign". An estimate of over 550,000 people who spoke out earlier suddenly became "rightists" and were humiliated, imprisoned, demoted or fired from their positions, sent to labor and re-education camps, tortured, or killed. No one dared to oppose Mao thereafter even when 30 million people starved to death during the Great Leap Forward. On June 3rd, 1989, Deng Xiaoping ordered the People's Liberation Army to enter the city and fire on protestors around the Tiananmen Square. Soldiers soon found out that the most effective way to clear the streets was *random shooting*: the odds of being shot were unpredictable to unarmed students and Beijing citizens. By 5:40 a.m. June 4th, the Square had been cleared. Why do dictators, armed with guns and tanks, constrain their discretionary behavior by promoting the rule of law?

To address these two puzzles, two models are developed. I assume that *local leaders in China are promotion-opportunity maximizers*, which means, they are willing to do *anything* to increase their chances of getting a promotion. Getting a promotion in the bureaucratic hierarchy in China means a higher wage, a bigger house, a more comfortable car, a better health care package, a more luxurious lifestyle, and above all accessibility to greater rents.

Like its Soviet counterpart, the Communist Party of China uses a *nomenklatura* system to regulate authority over Party and state "main leading cadres" and other important individuals (Lieberthal 2003). The Russian term *nomenklatura* generally refers to the lists of offices controlled by the various Party committees (Manion 1985: 212). In this *nomenklatura* system, the appointment, promotion, transfer and removal of leading cadres are based, in principle at least, on their qualifications and performance as assessed regularly in the *cadre evaluation system* (Manion 1985; Burns 1994; Huang 1995; Whiting 2000).

Whiting (2004) provides the most detailed accounts of the cadre evaluation system to date. A sample of the cadre evaluation forms is drawn from Jiading County, Shanghai. The first set of indicators in the local version of the cadre evaluation forms assigns highest priority to increases in the gross value of industrial output and industrial profits. The second set of indicators focuses on state procurement of agricultural and agricultural subsidiary products and the marketing of pork; it assigns highest priority to the sale of grain to the state. The third set of indicators covers party building. The fourth set addresses education and includes both the completion rate for compulsory education and an indicator of investment in education. The fifth performance indicator is the family-planning compliance rate. The final indicator is public order. In each locale, performance on these criteria was used to determine the bonuses of state cadres and the total salaries of collective cadres. In addition, local leaders' tenure in office and opportunities for advancement were to some extent determined by their performance as well. Generally speaking, local cadres need to undertake three challenging, yet often conflicting, tasks to maximize their "grades" in this GDP-centered evaluation form: (1) Promoting local economic growth; (2) Securing and expanding revenue sources; and (3) Maintaining social order.

How can they maximize their grades? Township & Village Enterprises (TVEs) and Foreign direct investment (FDI) are seen as major driving forces of China's economic growth in the 80s and 90s¹. In order to attract FDI and promote economic growth, local governments are expected to deliver and maintain consistent policies and put in place a legal environment in which contracts can be enforced and property rights established (Zheng 2007).

An effective legal system is also conducive to maintain social stability. As Diamant, Lubman, and O'Brien (2005) observe, "Today, we are witnessing an outpouring of grievances from, among others, people who lost money in the stock market, pensioners, veterans, unemployed laborers, disgruntled peasants, and unhappy couples. Yet, only a small proportion of these complaints spread to other sectors, lead to violence, or threaten the existence of the regime." (6) The formal legal institutions have played a notable role in channeling social discontent into moderated forums (Gallagher 2005, 2006; O'Brien and Li 2005).

Although it is generally believed that the rule of law is the key to economic growth and attracting investment either through protecting property rights (North and Thomas 1973; Acemoglu et al. 2001) or through increasing policy stability (Henisz 2000; Feng 2001), another school of observers, however, argues that government's obsession with attracting foreign investments will bring lax regulations. Such claims are based on competitive pressures: The mobility of MNCs, coupled with a desire to create jobs, produces incentives for governments to engage in cross-national "races to the bottom" (Drezner 2001). In addition, the experience of East Asian NICs further casts doubt on the assumed relationship between the rule of law and economic growth (Campos 2001; Rock and Bonnett 2004). Yet empirical studies do not lend support to the

¹ For the role of TVEs, please see Oi 1992, Walder 1995, and Qian 2003; for FDI, please see Gallagher 2002, Zweig 2002, and Huang 2003.

“racing to the bottom” argument (Wheeler 2001; Prakash and Potoski 2006; Mosley and Uno 2007), and the East Asian paradox only exists at the national level, once data is disaggregated at the sub-national level, the positive link between the rule of law and economic growth still remains (Zheng 2007; Huang 2008).

Based on the discussions above, local cadres’ probability of get a promotion is a function of economic growth rate and social stability, and GDP growth rate and social stability are functions of the rule of law:

$$\begin{aligned} (1) \quad & P_i = f(GDP_i, S_i) \\ (2) \quad & GDP_i = g(R_i, X_i) \\ (3) \quad & S_i = h(R_i, Z_i) \end{aligned}$$

where P_i stands for local cadre’s probability of getting a promotion in locale i , GDP_i the GDP growth rate of locale i , and S_i the level of social stability of locale i , R_i the rule of law, X_i and Z_i are some other factors that affect GDP growth and social stability. Local officials’ objective, therefore, is building the rule of law to maximize their probability of getting advancement:

$$(4) \quad \max_{R_i} f[g(R_i, X_i), h(R_i, Z_i)]$$

While the cadre evaluation system provides selective incentives for local officials to build the rule of law (which solves the first puzzle), model (4) cannot explain why some local leaders, similarly obsessed with GDP growth, *don’t* promote the rule of law. It also cannot explain, in this authoritarian system, why local “dictators” do not simply act predatorily and employ means of violence to force enterprises into production (the second puzzle). To solve the second puzzle, a simple game theoretical model is developed to capture the interaction between political actors and economic actors.

Wintrobe (1998) points out that dictators cannot solely rule by use of political repression, they also need people’s loyalty, and the common way to create loyalty is to stimulate economic growth. Economic stagnancy destabilizes dictatorships (Przeworski et al. 2000). It hurts dictators either through reducing the amount of private goods allocated to their winning coalitions (Bueno de Mesquita et al. 2003) or through empowering their opponents and making opponents easier to coordinate (Acemoglu et al. 2005). In the Chinese case, economic stagnancy may ruin local leaders’ political career by failing them on the cadre evaluation system. Therefore, in order to maintain economic growth and remain in power, dictators need cooperation. As Holmes (2003) contends, “the principle reason why people with power voluntarily agree to render their own behavior predictable is that even the most powerful people need cooperation to attain their ends.” (30)

To obtain the goal of stimulating economic growth, dictators especially need the cooperation of economic actors: entrepreneurs, merchants, foreign investors, bankers, etc. However, the bargaining power of economic actors varies. Economic actors’ power

comes from the *credible threat to withdraw* urgently needed cooperation. This point is vividly illustrated by the story of the Glorious Revolution. In 17th century England, the Crown needed money to wage their wars abroad. However, the rise of wool producers, merchants, and financial intermediaries who controlled assets that were very difficult for the state to tax significantly increased the bargaining power of the Parliament where these property holders were represented. In order to make a credible commitment to the Parliament that the Crown would pay back the debt, the Crown had to grant the Parliament veto powers which constrained the Crown's discretionary behavior in the future (North and Weingast 1989; Weingast 1997). Clark, Golder, and Golder (2008) formalized this story into a game theoretical model that they called the "Exit, Voice, and Loyalty game" (the EVL game).

I will use this model, with revisions tailored to the Chinese context, to capture the idea that political leaders in China need cooperation of economic actors to remain in power. The game tree is illustrated in Figure 2. There are two players in the model: a government (**G**) and a firm (**F**). The firm makes the first move: they can choose **exit** (withdraw the country or the area and move to a new place), **loyalty** (stay, produce, and pay tax), or **voice** (demand for a favorable legal environment¹). If the firm choose exit, the game ends with a payoff of **E** for the firm and **1** for the government, where **E** is firm's *exit payoff*. If the firm chooses loyalty, the game ends with a payoff of **0** for the firm and **1+L** for the government, where **L** is the value taken from the loyal firm by the government (e.g. tax). If the firm chooses voice, the government may respond by building rule of law or by simply declining the demand. If the government chooses accepting the demand, the firm's payoff is **1-C** ($1-C > E$ by definition), where **C** is the cost of using voice for the firm ($C > 0$ by definition), and the government gets **L**. If the government declines, the firm is left with two options: stay and pay tax (loyalty) or exit. If the firm chooses loyalty it gets **-C** and the government gets **1+L**; if the firm chooses exit she gets **E-C**, and the government gets **1**. The *sub-game perfection* of the game depends on the parameters **E** and **L**. $E > 0$ means the firm has positive exit payoff, which implies the firm can move to a new place and start over again; in contrast, $E < 0$ means once the firm moves it cannot survive. $L > 1$ means the government is *dependent* on the local economy, while $L < 1$ means the government is *autonomous*.

[Figure 2 about here]

Table 1: Outcomes of the EVL game

	L < 1 (Autonomous)	L > 1 (Dependent)
E > 0 (Mobile Assets)	The Rule of Man Stagnant Economy	The Rule of Law Booming Economy
E < 0 (Fixed Assets)	The Rule of Man Booming Economy	The Rule of Man Booming Economy

¹ Instead of pushing for democracy, the firm in the Chinese context only asks for a quality legal system. This assumption is consistent with empirical studies of Chinese entrepreneurs (see Dickson 2003) and foreign companies (see Gallagher 2002).

Derived from the EVL game, the equilibrium “the rule of law” is the result of a coupling of the firm’s credible exit threat and the government’s dependency on the local economy. By taking into account the interaction between political actors and economic actors and assuming economic actors have exit threat, the second model explains why local “dictators” have to constrain their predatory behaviors in order to seek economic actors’ cooperation to stimulate economic growth. The next section will generate several testable hypotheses and discuss measurement issues.

III. Measurement and Testable Hypotheses

Three key variables wait to be measured: the rule of law, capital mobility, and government’s dependency on local economy.

1. *Measuring The Rule of Law*

The research uses a definition that is widely agreed upon in the literature: “*the rule of law*” is present when the rules defining permitted and forbidden actions are not discretionary decisions of an individual, but rather take the form of laws that discipline every citizen, regardless of his or her power of status (Smulovitz 2003: 168). A concept as rich as the rule of law is hard to measure. Solum (1994) considers that the rule of law can be conceived as the conjunction of seven requirements: no extralegal commands are obligatory; actions by government and officials should be subject to regulation by general and public rules; the legal system should meet the requirement of publicity; the legal system should meet the requirement of generality; the legal system should meet the requirement of regularity; the legal system should provide fair and orderly procedures for the determination of cases; and the actions that the rule of law requires and forbids should be of a kind that persons can reasonably be expected to do and to avoid (122). To put the rule of law in the Chinese context, this research uses eight indicators to measure the rule of law at the sub-national level:

1. To what extent do local *government’s policies* contradict national laws and regulations?
2. To what extent do local *legislations* obey the principles of national laws and regulations?
3. To what extent do local *government enforce* national laws and regulations?
4. To what extent are *information* concerning local legal system public?
5. To what extent are *court decisions* implemented?
6. To what extent are *court procedures* perceived as fair?
7. To what extent do citizens *trust* local courts?
8. To what extent are local *legal system* perceived as efficient?

The first five indicators are objective and the last three are subjective measures. An index of the rule of law will be made to incorporate all eight indicators¹. It will be a continuum with one extreme being strong rule of law, the other strong rule of man.

2. *Measuring Capital Mobility*

One crucial component of China's reforms is privatization. Now there are basically four forms of ownership: state-owned, collective, private, and foreign (and mixed forms). In terms of degree of capital mobility: foreign > private > collective > state-owned². Mixed ownership will be coded according to the proportion of stocks or assets held by different owners.

3. *Measuring Dependency*

The degree of dependency on local economy is very much determined by local governments' fiscal conditions. If a large proportion of fiscal revenues comes from corporate tax³, the government is considered to be dependent on local economy; in contrast, if the governments don't rely on corporate tax (e.g. they can obtain a large amount of fiscal transfer from the national government⁴), it is considered to be more autonomous.

4. *Testable Hypotheses*

Based on the theoretical prediction in Table 1, two testable hypotheses can be generated:

1. When the proportion of corporation tax in government revenue is low (the government is autonomous), the effect of capital mobility on the rule of law is not significantly different from zero; as the share of corporation tax increases, *ceteris paribus*, the effect of capital mobility also increases and is significantly greater than zero;
2. When share of mobile capital in local economy is low, the effect of proportion of corporate tax is not significantly different from zero; as share of mobile capital increases, *ceteris paribus*, the effect of corporate tax also increases and is significantly greater than zero.

¹ I plan to do an expert survey to test the validity of my measures. Techniques of integrating these eight indicators depend on the dimensions of the index: if there are multiple dimensions, I will estimate each dimension in separate statistical models.

² This is a very coarse ranking; there is great variation across locales. In some places, it might be foreign > state-owned > collective > private. The mobility of state-owned companies depends on who owns them. A provincial level state-owned company can move wherever it wants within the province. And in some places, private enterprises might only have limited mobility because they are under the protection of local governments (see Wank 1999)

³ After the 1994 tax reform, tax from firms that are owned by the national government goes to the center, local governments can keep corporate tax from local firms.

⁴ Shaoguang Wang's study shows that fiscal transfers from the national government are biased towards areas with large proportion of ethnic minorities, like Tibet and Xinjiang (Wang 2002).

The expected relationship between dependency and the rule of law conditional on capital mobility is illustrated in Figure 3. The relationship between capital mobility and the rule of law conditional on level of dependency is illustrated in Figure 4.

[Figure 3 about here]

[Figure 4 about here]

5. Endogeneity problem

The model specified above suffers greatly from endogeneity problems. It might be the case that foreign investors only locate in places where the legal system is already sound. Although studies have shown that the arrow is mainly from economic development to the rule of law (Clarke, Murrell, and Whiting 2008), special cautions should be kept in mind when doing statistical analysis.

An instrumental variable will be used to deal with the endogeneity problem. A good instrument in this case should *cause* capital mobility and should be linked to the rule of law *only through* capital mobility. Naughton (2007) argues that the takeoff of private economy and FDI in the 80s mainly took place in coastal areas with the help from overseas Chinese. “Homecoming” of overseas Chinese who were financially successful abroad inaugurated China’s privatization reforms. Considering the legal system was completely abolished during the Cultural Revolution, and overseas Chinese’s investment decision was mainly based on their kinship connections in the Mainland, number of overseas Chinese in their hometowns qualifies for a good instrument.

IV. Research Design

The research will consist of three parts: case studies, data collection, and survey research.

1. Case studies

I plan to first of all carry out case studies in four Chinese counties (or county level cities). The first objective of case studies is to get a finer grained sense of how local Party committees, legislatures, governments, and courts work, and what their dynamics are. For example, scholars found that local governments usually selectively enforce national laws and policies (O’Brien and Li 1999), what is the rationale behind the selection? And also it is a Party rule that all major personnel decisions in the local court is made by the Party committee at the same administrative level, how do local Party bosses make personnel decisions concerning the court? What standards do they use to choose judges? It is also observed that local Party committees often interfere in legal affairs if the case is politically sensitive (O’Brien and Li 2005), but what constitute a “sensitive” case? In what way the party intervention will change the final decisions? Case study is a good tool to answer these micro-level questions.

The second objective is to collect data about the cadre evaluation system. Local officials' incentive structure is the starting point of this research. Without knowing the details of the cadre evaluation forms, we don't know how local cadres are motivated. So far, the most updated information about the system is provided by Whiting (2000, 2004), but her fieldwork was finished by late 90s. A lot of changes happened in the last decade, for example, in some prosperous provinces, local Party committees reduce the weight on GDP growth and put more emphasize on quality of economic growth and environmental protection¹, but does this change matter? How would this change of the incentive structure change local legal environment and officials' behavior? These questions all need to be addressed in case studies.

The third objective is to refine measurements of major variables in the model. In the preceding section, I proposed possible measures of the rule of law, capital mobility, and dependency, do they have both validity and reliability? I also have identified an instrument to deal with the endogeneity problem, but is the number of oversea Chinese a good instrument? Does it relate to the rule of law only through capital mobility? Case studies will also deal with these questions.

Table 1 offers a good guidance about case selection. Four cases will be selected *only* according to their level of capital mobility and dependency on local economy. . An estimate of two months will be spent on each site (overall eight months in four sites) to do interviews and data collection.

2. Data collection

After the first stage of case studies, I plan to collect data on major variables and some control variables (e.g. measures of local economic development, number of legal cases each year, etc.). Majority of the data exists in government documents, like yearbooks, government reports, and government websites. In order to do large-N statistical analyses, I need a sample of around 100 counties (the number is also constrained by the survey I was involved in 2004).

In the past three decades, China's National People's Congress has passed hundreds of laws. I constrain my data collection effort on three laws: the Environmental Protection Law (passed in 1989), the Administrative Litigation Law (passed in 1989), and the Labor Contract Law (passed in 2008). The rationale of the selection is that these three laws deal with different dynamics: the Environmental Protection law concerns the dynamic between governments and enterprises, the Administrative Litigation law deals with the relationship between citizens and governments, and the Labor Contract law involves citizens and enterprises.

3. Survey data

¹ Guangdong province reformed the cadre evaluation system in August 2008 to tailor different local contexts. For example, if a city is classified as an "ecological development area", GDP growth is no longer a major measure of performance. In general, measures of economic growth only constitute 30% in the performance "grades" in Guangdong after the reform.

Some subjective measures of rule of law also need to be collected, so survey data is necessary. I have access to two high quality data sets. I was involved in a survey “Institutionalization of Legal Reforms in China”. It was carried out by the Research Center for Contemporary China at Peking University¹ (RCCC) in 2004. It was a national random sample (7714 respondents residing in 100 counties) and survey questions covered broadly people’s legal behavior, legal attitudes, and opinions on other social issues. Some of my own researches drawn from the data either have been published (Shen and Wang 2007) or are forthcoming (Shen and Wang).

I am also working closely with Professor Mary Gallagher at University of Michigan on a survey she did in 2004 on the Labor Law. It was carried out in four cities: Foshan, Chongqing, Wuxi, and Shenyang. The same size is 4112. Survey questions focus on people’s experience and attitudes towards the Labor Law. I independently did a follow-up research in 2007 interviewing those people who were identified having labor disputes in the 2004 survey. Some preliminary results of the survey are shown in Gallagher and Wang² (forthcoming) and Stockmann and Gallagher (2007).

V. Theoretical and Applied Significance

Studies of dictatorships are surging lately (Wintrobe 2000; Acemoglu et al. 2005; Magaloni 2006; Brownlee 2007; Gandhi 2008), and the resilience of Chinese authoritarianism is still puzzling (Nathan 2003). This research seeks to talk with the broad comparativists community by shedding lights on authoritarian resilience through looking at an important mechanism dictators utilize to channel social discontent: law. It is noted that law has become a tool (rule by law) employed by dictators to consolidate their rule (Ginsberg and Moustafa 2008), this research argues that rational dictators as well have to constrain themselves within the legal framework to obtain cooperation. In addition, previous studies often assume that democracy is a necessary condition for rule of law (North 1981, 1990), yet this is not corroborated by empirical evidence (Barro 2000). This study provides both theoretical and empirical bases to point out that dictators might also be fond of rule of law, and the emergence of rule of law, instead of being a result of external imposition (Acemoglu et al. 2001), can be an endogenous process.

Existing measurement of rule of law is often subjective and cross-national³. One contribution this study will make is to create a dataset of measures of rule of law at the sub-national level within a nation.

¹ RCCC is the primary survey research center in China (<http://www.rccc.pku.org>). I worked at the Center in 2003-2006 as a research assistant and was involved in every process of the legal survey.

² We found that citizens’ political identity determines their attitudes towards the legal system: young, rural, and private-sector employees are often expressively motivated and care more about procedural justice, while old, urban, and state-sector employees are instrumentally motivated and put more emphasize on outcomes.

³ For example, World Bank’s Transparency International and UNDP’s Global Integrity.

There is also a recent resurgence of social science interest in Chinese law, especially people's legal behavior and legal attitudes (e.g. Diamant, Lubman and O'Brien 2005; Gallagher 2006; Michelson 2007). Legal scholars have been focused on China's legal institutions (Lubman 1999; Peerenboom 2002), their analyses are good at descriptions but often fall short of causal analysis. This research is seeking to fill this gap by bridging institutional analysis and behavioral studies and offers a micro-foundation for the development of rule of law in China.

The study also has great policy implications. China is entering several important international protocols, including the WTO, Kyoto Protocol, et cetera. After the national government signs agreements with the international community, previous failures of compliance call into question local governments' incentive to enforce these laws and regulations (Mertha 2005). This research will provide a theoretical foundation for policy makers both in China and abroad to enhance means to guarantee enforcement.

Figures

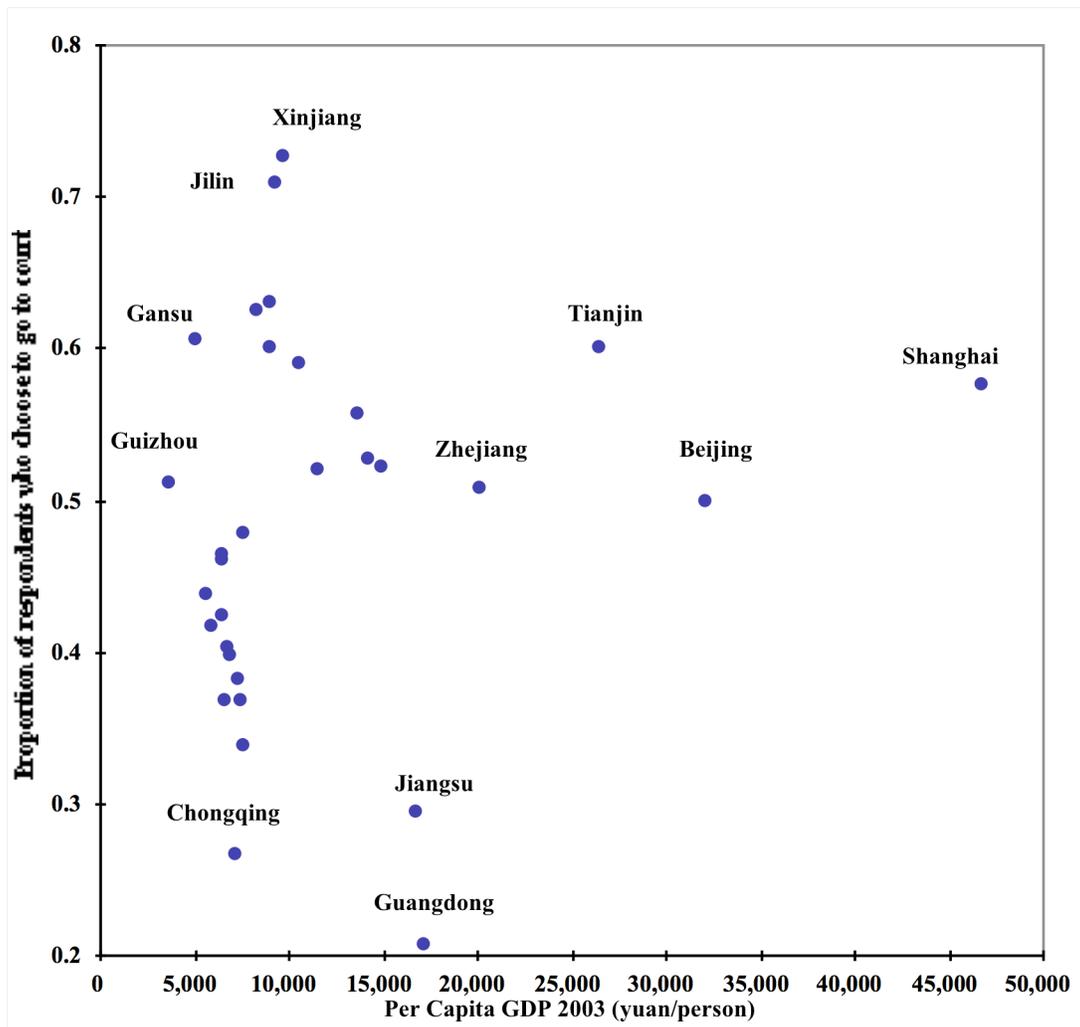


Figure 1: Using Litigation to Settle Disputes by Level of Economic Prosperity

Note:

1. Respondents included here are those with “agricultural hukou” only, N=6,116.
2. Per Capita GDP data is the provincial statistics of 2003, as our survey was conducted in that year.
3. “Proportion of respondents who choose to go to court” = “Respondents who choose to go to court in the province”/ “Total number of respondents of the province”.

Source: Shen and Wang (2007).

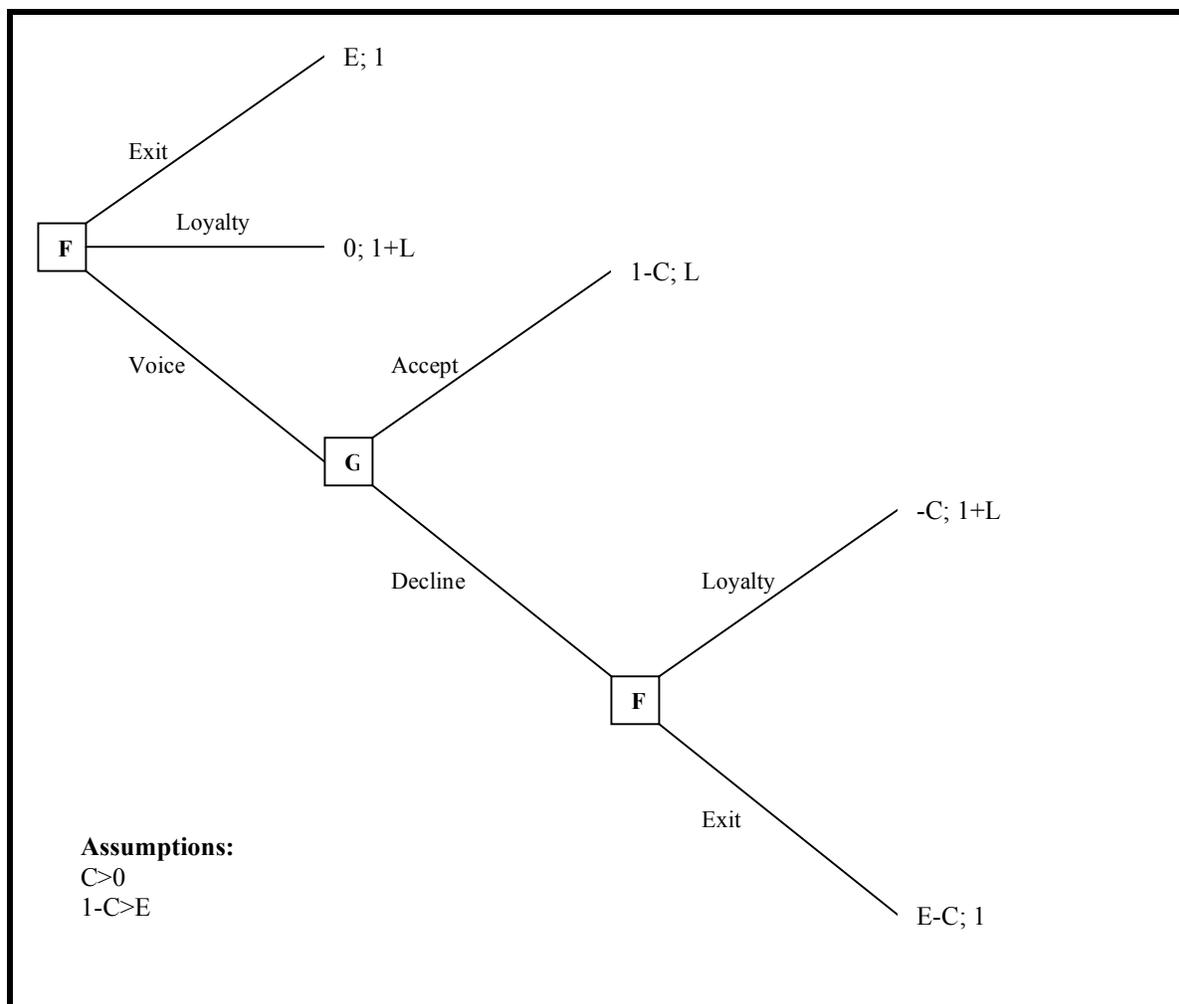


Figure 2: The Exit, Voice, and Loyalty game

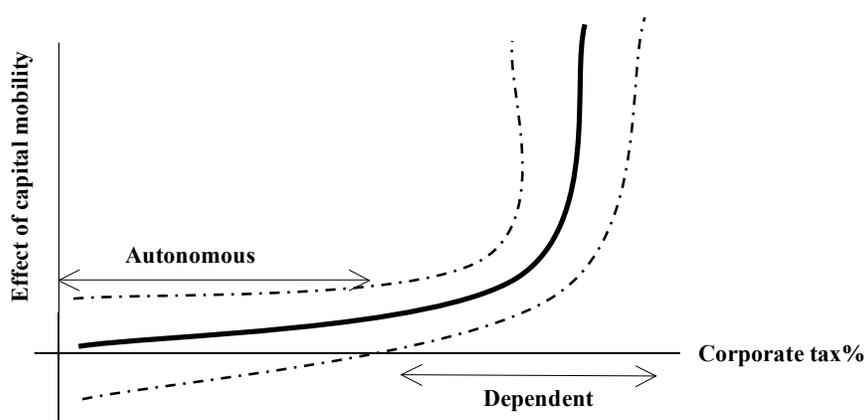


Figure 3: Effect of capital mobility on the rule of law conditional on corporate tax%

Note: The solid line is the effect, dotted lines are the confidence interval.

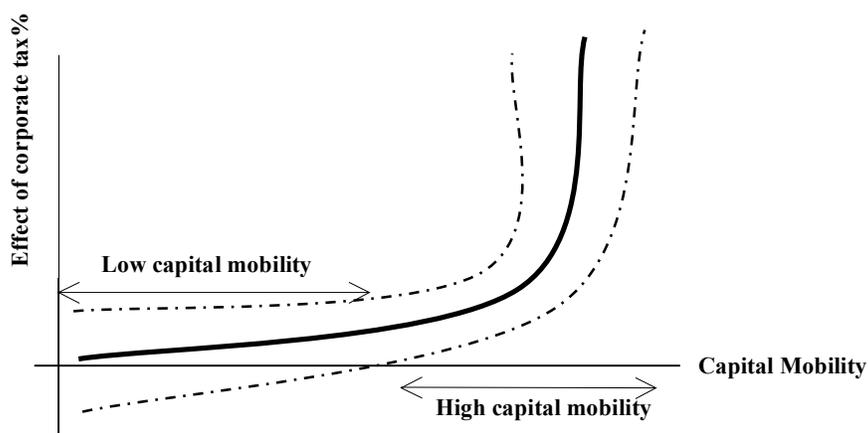


Figure 4: Effect of corporate tax% on the rule of law conditional on capital mobility

Note: The solid line is the effect, dotted lines are the confidence interval.

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