

## REFORMING SOCIAL SERVICES – ASIAN EXPERIENCES

## From Command Economy to Hollow State? Decentralisation in Vietnam and China

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*In Vietnam and China, decentralisation is a by-product, both by default and design, of the transition to a state-managed market economy. A dual process of horizontal and vertical decentralisation is occurring simultaneously in both the economic and political arena. There is an increasingly high level of de facto political/fiscal decentralisation, much of it occurring by default as local governing units try to meet rising demand for services. This is accompanied by the marketisation and socialisation of services such as education and health. Accompanying both of these processes is a trend towards greater 'autonomisation' of service delivery units, including the emergence of new 'para-state' entities. Most of these decentralisation processes are the by-product of marketisation, rather than part of a process of deliberate state restructuring in pursuit of ideals of decentralised government. The cumulative effects include a significant fragmentation of the state, a high potential for informalisation and corruption, and a growing set of performance accountability problems in the delivery of public services.*

**Key words:** *decentralisation, market reforms, transition economies, China, Vietnam*

The economic and political transitions currently under way in former command economies under one-party rule, such as Vietnam and China, produce a powerful set of forces leading to processes of decentralisation. In these societies, economic decentralisation is a key driving force, for marketisation entails dismantling the command economy (as well as creating new economic institutions), which, in turn, entails political and administrative decentralisation. In a transition economy, the two processes are intertwined and interdependent in a special way. My main argument here is that this 'dual decentralisation' is a particularly challenging process, creating its own kinds of problems and outcomes. To grasp this fully, we need somewhat different and unfamiliar tools of analysis beyond those generally encountered in the decentralisation literature.

Another way of conceptualising dual decentralisation is to draw a distinction between 'vertical' and 'horizontal' decentralisation. Vertical decentralisation is about devolving or decon-

centrating power and functions within the state; horizontal decentralisation is about shifting power and functions from the state to society (or, to use other terminology, from the public to the private sector). However, a further complexity in a transition economy is that this very distinction between 'public' and 'private' is in the process of formation. Moreover, in a command or transition economy, we encounter vertical devolution of economic power and functions within the state as well as the more familiar devolution of political and administrative power. When economic power is concentrated within a unified state (the command economy), the decentralisation of economic decision-making is a distinct process. It results in a more decentralised, but nonetheless state-managed economy. As Schurmann (1968:197) puts it: 'Economics in a Communist country means political economics, hence administration'. If, at the same time, horizontal processes of marketisation and socialisation are occurring (including the creation of both new forms of economic organisations and new forms of 'para-state'

**Figure 1.** Dual Decentralisation in a Transition Economy

	Vertical	Horizontal
Economic Power	1 Local Autarky	2 Privatisation & Socialisation
Administrative Power	3 Deconcentration	4 Cellularisation

organisations and activities) where (in both cases) the public/private distinctions are in the process of being worked out, the complexities of relationships and outcomes are multiplied.<sup>1</sup> Some of these complexities are the subject of this article.

Figure 1 combines these distinctions into a four-fold categorisation of types of decentralisation in a transitional economy: first, local autarky, where localities and/or regions have high levels of economic decision-making power; second, deconcentration, where there is a decentralised set of administrative and political structures; third, privatisation and socialisation, the transfer of activities from state to non-state sectors, both for-profit and not-for-profit; and fourth, ‘cellularisation’, or the emergence of a large ‘para-state’ sector in which state power (whether at the centre or in the localities) is horizontally diffused into arm’s-length quasi-autonomous entities that have varying and often uncertain legal and organisational forms.

These distinctions can be aligned with other, perhaps more familiar ones. Political devolution in the form of ‘local self-government’ sits in cell three of Figure 1, but is hardly relevant in the cases of China and Vietnam. Fiscal decentralisation, where this involves devolution of taxing powers to local general-purpose authorities, overlaps cells one and three. In a command economy, fiscal decentralisation is essentially about retaining the ‘surplus’ generated by state-managed economic activity at the local level, rather than passing it up to the centre. Administrative delegation and deconcentration within a unified administrative hierarchy are located mostly in cell three. New Public Management (NPM)-style ‘manage-

ment devolution’ also falls into cell three but may spill over into cell four, as devolved entities in various ways may become detached from the general purpose control of governments and acquire ‘fringe-body’ status. Decentralisation to various forms of mixed public-private arrangements and the phenomenon of ‘quangocracy’ (here, labelled ‘cellularisation’) fits squarely into cell four. Market decentralisation in all its forms, involving the transfer of ownership and/or provision of a service or function to a ‘for-profit’ commercial or business entity (whether or not government-owned) fits into cell two, as does decentralisation to the ‘third sector’ (non-government organisations that are not operating in a commercial environment, for example foundations or charities). However, some such organisations take on public functions and acquire para-state legal status, in which case they belong in cell four.

The discussion in this article looks at aspects of each of these types of decentralisation but focuses in particular on the horizontal dimension, where some of the more far-reaching changes and critical reform issues are evident. Vertical administrative and fiscal decentralisation in China and Vietnam has been subject to extensive analysis elsewhere (for example, Wong 1997; World Bank 2005a), but less attention has been given to the implications of horizontal decentralisation for the structures of public administration (but see Lam and Perry 2001; Lo, Lo and Cheung 2001; and World Bank 2005b). Parallel processes of privatisation or socialisation and the cellularisation of state institutions are occurring to a large extent through ‘bottom-up’ actions at the local level. Not every dimension or consequence of this ‘hollowing-out’ process is anticipated or under the control of central policy-makers, and this leads to a burgeoning array of problems for both national governments.

### Decentralisation: Process and Policy

Decentralisation is both a process and a policy. As a process in any historical or geographical context decentralisation reflects the unfolding of a power struggle between centre and

periphery. This process has characterised all attempts to create and sustain kingdoms, empires, and, latterly, the modern state. Sometimes the centre is in the ascendancy, in which case centralisation may be occurring; at other times, the centre is weakened, resulting in decentralisation.<sup>2</sup> In many states, long-run centrifugal forces seem to persist as a result of geography (eg, the existence of island communities or the sheer size of the jurisdiction) or due to the resilience of traditional forms of local social and economic organisation. In Vietnam, for example, an old saying still frequently heard – ‘the kingdom stops at the village gate’ – epitomises a long-standing tradition of local autonomy.

Decentralisation seems to be a common contemporary trend (White and Smoke 2005:1–5). In developing countries, national government shares in total public expenditure have tended to decline with increasing urbanisation and with economic and social development more broadly, suggesting, perhaps, that there is an administrative or fiscal logic to the decentralisation process associated with the demands of increasingly sophisticated services and infrastructure. As democratisation has taken hold in an increasing number of countries, political demands for greater local autonomy and better, locally delivered services have become stronger and more irresistible. This has encouraged not only political decentralisation but also a greater devolution toward civil society. In terms of market decentralisation, global pressures on governments to adopt more market-friendly policies such as privatisation have added another set of pressures to decentralise.

In part, the decentralisation process is a bottom-up one reflecting the unfolding of local as well as national demands for more control, but it may also be a top-down process where policies are promulgated to loosen central controls and to provide for more local autonomy and initiative. Nevertheless, while the centre may draw up decentralisation policies – political, fiscal, administrative, and economic – there is a fundamental paradox in the idea of decentralisation ‘policy’. Some of the preconditions for such a policy – namely, local demands for autonomy and local capacities to exercise it ef-

fectively – would seem to rule out the possibility of such a design. At best, a decentralisation policy would be about containing demands for local autonomy so that they did not create unmanageable diversity.<sup>3</sup> Conversely, if there is to be such a policy, the centre must have the capacity to implement it, in which case we may ask why the centre would voluntarily surrender power.

But perhaps this only highlights an obvious point about decentralisation reforms: just like any other set of public policies, they are part of a political process in a particular domestic setting. Decentralisation as a process reflects the distribution of political power in a particular society and is the product of political stratagems and battles between centre and periphery. Decentralisation as a policy often masks other goals and stratagems. The struggles may be conducted in multiple arenas – party, bureaucracy, civil society, and so on – and they shape national policy towards administrative and political decentralisation. These policies themselves are likely to be as much *post hoc* as *ex ante*, signalling the state of play in the political process of centre-periphery conflict. These centre-periphery political battles spill over between economic and political arenas and manifest themselves in contests over the nature of the state, the carving out of spheres of private activity within society, and the creation of new forms of state-society relations.

In both China and Vietnam, contemporary centre-periphery struggles are given expression not as demands for formal local political autonomy in the form of ‘local self-government’, but as demands for administrative deconcentration and devolution, usually associated with the struggle to retain or acquire economic resources, particularly those that were under central state control in the old command economy. Often, the demand for local autonomy is accompanied by manoeuvres to attract more central funds or to retain locally generated economic surplus or revenues. The interconnections between the politics of marketisation and the politics of centre-periphery are indissoluble; knowledge of each is essential for understanding the other. For the remainder of this discussion, we look at aspects of these

contemporary struggles and debates over decentralisation in Vietnam and China.

### **'Power Scattering' and Decentralisation in Vietnam and China**

In both Vietnam and China, while formal political devolution is 'off-limits' except in very constrained forms, it is generally argued that a process of decentralisation or 'power scattering' has accompanied economic reform (Vasavakul 1996:44–48; Gainsborough 2002:360). Power scattering is evident in the changing distribution of roles, functions, and powers among levels of government and a simultaneous shifting of the boundary between state and market, or 'public and private'. This process began before the reform era in response to failures of the command economy. In Vietnam a common series of events in the gradual introduction of marketisation was for local experiments to take place (sometimes without official sanction but often under the sponsorship of local officials), followed by an assessment by central officials and, in some cases, the adoption of the experiment as a wider 'reform' measure. Observers have dubbed this process 'fence breaking' (Phong 2004; Fforde 1993:300–301). Only in this way were a number of inherent crises and contradictions in the command economy surmounted.

In the era of marketisation, reforms such as restructuring of state-owned enterprises (SOEs) in the 1990s have also had a strong 'bottom-up' character. From early on, the central government in China gave some provinces a large amount of leeway to experiment and use their initiative in stimulating local enterprise and attracting foreign investment. New ownership forms, in which managers and other stakeholders acquired 'shares', replaced direct local government ownership and bureaucratic control. Many local officials exploited the relaxation of controls and the call for new ownership and control structures to acquire assets for themselves and their families: they effectively privatised state assets 'by the back door'. As markets have emerged for state assets, the income they generate has been diverted to a variety of private

as well as public ends. At the same time, some local governments have operated more or less independently in attracting foreign investment and making deals. Gainsborough (2003:72) has argued that in Vietnam a 'state business interest' of bureaucratic businessmen, with strong roots in provincial and local state or party circles, and with direct or indirect complicity in various kinds of informalisation, emerged as a powerful political force during the 1990s (see also Beresford 2001:226–229; Fforde 1993:308–312).

Local experimentation has also been evident in response to pressures to reform the public sector as marketisation has gathered pace – for example, downsizing and efficiency improvements. In China, Li (2004) has shown how in the Shunde city government in Guangdong province, local political leaders and city managers found ways to relinquish direct control and ownership of local business units, downsize the government bureaucracy, and undertake other initiatives to cope with the new market environment, getting tacit approval from provincial leaders to experiment with 'bold' reforms. This story is repeated in other cities and towns across China in areas such as housing reform and social service delivery. That is, the reform activities associated with marketisation set in train a process of both vertical and horizontal decentralisation as localities have taken it on themselves to experiment or adjust, with a view both to enhancing local administrative capacities and also to supporting local economic development.

### **Administrative and Financial Decentralisation**

In both Vietnam and China, there is a seemingly inexorable trend towards a greater sub-national share in service delivery and public expenditures. In China, sub-national expenditures rose from about 45% of the total prior to the economic reforms in the 1980s to close to 70%; in Vietnam, sub-national expenditures in the state budget increased from 26% in 1992 to 48% in 2002. One reason seems to be the changing composition of public expenditures rather than a deliberate process of devolution, a

process that is in part the result of economic reform. Local governments have inherited many 'collective consumption' service provision responsibilities (health, education, housing, and so on) that formerly fell to state-owned production units (responsibilities that have been shed as SOEs have been commercialised and subject to more market discipline).<sup>4</sup> The local taxing capacity of China's local governments has not kept up with the growth in demand for services, with about 45% of the sub-national expenditures being funded from central revenues. These grants and tax-sharing arrangements have been a constant source of conflict and have tended to be allocated according to political pressures rather than need, resulting in a high level of inequity between rich and poor regions, with local governments in the poorest localities often unable to meet their payroll bills.

In the course of this transition from central to local funding, local bodies have had to rely increasingly on their own resources. Centrally determined policies on standards and levels of provision coupled with local budget shortages have prompted local governments to look to alternative sources of finance, some of them outside the formal and legal channels. In both Vietnam and China, local bodies have increasingly relied on revenues such as service charges and fees, over which there has been quite loose central oversight (probably deliberately so), with local units operating many accounts and activities 'off-budget'. In China, these unofficial funds are called 'the three arbitraries' – arbitrary taxation, fines, and expropriation or apportionment – and the *ad hoc* local bank accounts in which they are held are called 'small treasuries' (Wedeman 2000; Gong 2005). In China's rural areas, this squeeze on the meagre resources of the rural population (the 'peasant's burden') continues a long tradition of harsh extractions (Bernstein and Lu 2003:20–47). One estimate is that extra-budget and off-budget revenues and expenditures amount to as much as half of total local government expenditures, although this is a matter of dispute (Wedeman 2000). Thus, whatever the amount, the proportion of local expenditures in the total state budget – official and unofficial combined – was certainly higher than officially reported.

The existence of heavy, often arbitrary local taxes and charges, coupled with corruption, has given rise not only to local protests but also to official periodic crackdowns on 'illegal fees'.<sup>5</sup> The struggle between centre and periphery has thus been manifested in the 'disciplining' of wayward local officials by the central authorities, while 'local autonomy' has come to be defined in part through its informality and rule-breaking. Centre-periphery conflicts over revenue and expenditure (both off- and on-budget) have also resulted in wholesale tax reform, including the recent 'tax for fee' reform that seeks to outlaw many local fees and replace them with new sources of funds (Yep 2004).

Aside from numerous cases of outright extortion, many of the fees and charges introduced by hard-pressed local service delivery units to plug the revenue gap have been legitimate user charges, that is, they are collected at the point of service delivery as a 'fee for service'. Thus, *de facto* fiscal and service decentralisation in the provision of services such as health, education, family planning and so on was at one and the same time a process of public service commercialisation.<sup>6</sup> That is, horizontal decentralisation has gone hand in hand with vertical decentralisation. This development was encouraged by the general climate of marketisation reforms in both countries. China now has a system of public service provision that may be one of the most commercialised and decentralised of any in the world.<sup>7</sup> Vietnam is not far behind. Recent official discourse in Vietnam has given growing legitimacy to the imposition of various forms of user fees and charges and, in parallel, a degree of semi-entrepreneurial fiscal decentralisation and managerial devolution (Painter 2005). In 2000, estimates from the national accounts showed fee revenues accounting for 22.5% of public hospital revenues nationwide, with accelerating growth since the early 1990s. Recent measures have succeeded in increasing that proportion (Socialist Republic of Vietnam and World Bank 2005:107). There is in general a clear expectation that service delivery units will become more self-reliant and hence remove the need for continuing 'state subsidy' – that is, there are strong pressures towards decentralised (both

deconcentrated and marketised) forms of service delivery.

However, it would be misleading to view these aspects of horizontal decentralisation – including ‘cellularisation’ as it is labelled in Figure 1 – as a complete break with the past. Service delivery units in both China and Vietnam have been considered as a separate set of state institutions, whether managed by central or local government, with a distinct identity separate from the line or administrative agencies (Lam and Perry 2001). The structure of the administration, while it is becoming more complex, still distinguishes between three types of entity: first, administrative agencies such as government ministries; second, service delivery units (in Chinese, *shiye danwei*, and in Vietnamese, *don vi su nghiep cong lap* or *don vi su nghiep co thu* [literally, ‘state organisations that produce turnovers’]); and third, state-owned enterprises. In 2002, China had over one million *shiye danwei* employing nearly 30 million people, many of them in the civil service (World Bank 2005b:1–2).<sup>8</sup> The largest sectors were in education and health. Administrative departments at all levels exercised the ‘state management’ function’ of supervising these bodies; in China, 65% were supervised by local governments. In China, reforms in the past decade and more to give these bodies greater managerial and fiscal autonomy included flexibility in recruitment and remuneration and provisions allowing delegation of activities to ‘social organisations’ and other new fringe bodies (Cheng 2001:322).

With this set of administrative structures already in place, and in the context of marketisation, contemporary decentralisation reform discourse in both China and Vietnam draws a direct link between service delivery reform and autonomisation, particularly coupled with commercialisation. A conception of the ‘core’ role of government has evolved as the arm’s-length coordinator and regulator of production units (‘steering’), without distinguishing between economic and social policy sectors: ‘those functions that do not belong to state management agencies will be transferred to SOEs and professional agencies, especially those functions of direct productive and

business administration and management and the provision of public services’ (my emphasis) (GSC 2000c:8). ‘Equitisation’ (transfer of SOE ownership) and ‘socialisation’ or ‘the transfer of government work to non-government agencies’ (Vasavakul 2002:10; GSC 2000b:18) are coupled together as part of the decentralisation (or downsizing) process. This ‘transfer of work’ requires the ‘people’s resources’ to be mobilised and an end to subsidy, or what is often labelled in Vietnam the ‘begging and giving mentality’ (GSC 2000a:15). In the old socialist economy, local communities were required to contribute labour and funds to local public works (indeed, in Vietnam this is still formally a requirement at the commune and ward level, although payment of a small ‘fee’ can be substituted). But in the reformed economy, families who generate income through entering the market can also contribute through user fees and charges to support local schools and health centres. In a strange twist, socialist doctrine has ended up sounding more like neo-liberal rhetoric.<sup>9</sup> In addition, Vietnam’s burgeoning non-governmental organisation (NGO) sector, which was subject to increasing regulation and political oversight in the 1990s, was viewed as a potential participant in the process of socialisation (Vasavakul 2002:43).

Income-earning public service units in Vietnam (as well as in China) have been increasingly subject to new decrees regulating their behaviour,<sup>10</sup> but at the same time new incentives and freedoms have been provided to encourage greater revenue autonomy in order to ‘help them become self-reliant for the funding of their operations, increase compensation for their workers and reduce amounts allocated from State Budget’ (Ministry of Finance 2002). The risks associated with potential abuses have been accepted, and countered with a set of new rules and procedures. However, the thrust of the new measures is to devolve powers and discretion to managers: increasing the budgetary autonomy of service delivery units, allowing greater flexibility in remuneration, permitting more entrepreneurial activity to raise revenue, and so on.<sup>11</sup> An Ordinance on Cadres and Civil Servants in 2003 spelt out additional flexibilities permitted in the terms and conditions of

civil servants in the 'productive' sectors as distinct from 'administrative' agencies (Joint Donors 2004:50). Moreover, in paying across-the-board salary increases of 38% in 2003 and 30% in 2004 respectively, local units were required to contribute at least half of the cost from their own resources (Painter 2006). This was one way of trying to consolidate and regularise some of the extra-budget funds and accounts, while continuing to encourage (indeed, compel) the practice of seeking new ways to raise money from the customer.

In the case of administrative as distinct from service delivery units, the decentralising trends have been more modest but still significant, involving lump-sum or one-line budget allocations incorporating incentives for efficiency improvements. Where this was first piloted in Ho Chi Minh City, it led to savings in administrative costs, stimulated restructuring and downsizing, and allowed for local increases in salary (Bartholomew et al. 2005). As in China (Wedeman 2000), savings from 'downsizing' and other efficiency gains have generally been devoted to staff salary increases. On the one hand, salary increases are long overdue, but in the absence of some regulating mechanism, an excessive proportion of funds is in danger of going to staff salaries alone instead of also improving service quality. This is one illustration of the potential gaps in performance accountability associated with financial and administrative decentralisation measures of this kind.

## Conclusions

In sum, the decentralisation process in both China and Vietnam is a dual process of vertical and horizontal transfers of power and resources. In this process, there is as much bottom-up initiative and experimentation as there is top-down design and planning. Much of the bottom-up initiative takes the form of rule-bending or downright illegal behaviour and is consequently the object of clampdowns and disciplining campaigns. These, in turn, become the site for central-local struggles. There is, however, a huge grey area between the rhetoric of disciplining campaigns and realities of marketisa-

tion. Local entrepreneurship growing out of the state feeds back into bottom-up decentralisation, hollowing out the state, creating new possibilities for local administrative autonomy, and producing new spheres of private activity. Some of the private activity is also the result of official policy as state service delivery functions are 'pushed into the market' or are handed over to a growing third sector of non-government service providers. User-charging and the growing commercialisation of service delivery, accompanied by abuses and distortions, are accelerating trends.

The outcome is an increasingly decentralised state where boundaries between public and private are more and more blurred. This is most obviously seen in the case of public service delivery, where a clear conception of the role of 'the public sector' seems absent (Cheng 2001). A growing gap is emerging between the clear need for expansion in service production and the declining capacity of the state to ensure accountability and to assure performance. More formal accountability mechanisms are critical in the long run if hopes for better services at lower cost are to be realised. Some experiments have been initiated. In Vietnam, for example, a system of 'citizen report cards' for local service delivery units was piloted in Ho Chi Minh City, and in China and Vietnam there have been some experiments in grassroots democracy through village and township elections. These are not the subject of this article, and it is too early in any case to say what impact they will have on accountability or performance.

In this context, 'performance monitoring' still tends to follow the traditional patterns: first, a set of 'mobilisational' targets and principles; and second, a set of disciplining processes, in which the party inspectorate suddenly descends on a hapless local officialdom that has run foul of a higher set of officials, and a spate of punitive actions follows. How and why such interventions occur in some cases, but not the countless others where similar deficiencies may exist is hard to say. Political devolution in the Western sense – which may be one route towards improved accountability – is not on the agenda. Much is left to the overburdened public complaints procedures to provide a channel

for citizens to exercise their 'customer rights'. The issue that will surely arise at some point is the policy capacity of the centre to assure basic service quality and accessibility in areas such as health care or education, as some increasingly autonomous local government units and decentralised, commercialised service delivery entities under-perform in the eyes of the public.

### Endnotes

1. The term 'socialisation' in this context refers to a range of measures to decentralise state activities to entities in society aside from those engaged primarily in economic activity.

2. However, the decentralisation-centralisation 'balance' is not simply a zero-sum game. For example, if local government occupies a previously unserved niche in service delivery, this does not mean the centre has given up or lost power.

3. Indeed, perhaps the purest form of a 'decentralisation policy' is not to have one, other than to let local initiatives bloom spontaneously without restraint.

4. In addition, costs of provision in labour-intensive areas such as health and education have tended to grow faster than costs in other government sectors and faster than the resources available in the total state budget.

5. However, the precise meaning of 'illegal' and 'legal' fees and fines was as much a matter of political expediency as being strictly legislated, just as the practice of holding 'off-budget' accounts was widely tolerated and only subject to sporadic, partly symbolic central interventions. Crack-downs on so-called local 'arbitrary' fees revealed that, in fact, many were officially sanctioned (Wedeman 2000:506).

6. User-charging by local service units such as schools and hospitals is often accompanied by competition for the customer so as to maximise revenues, particularly in urban areas. In rural

areas, extortion by the sole provider has been more common.

7. In the case of health services in particular (but also in other fields) there seem to have been deleterious effects: quality has declined for many (especially the rural poor), costs have escalated, and numerous inefficiencies have been introduced into the system (Socialist Republic of Vietnam and World Bank, 2005:110; Saich 2001).

8. Many services were also delivered by units directly under the control of enterprises. As the subsidies inherent in these activities were withdrawn, the burden fell on service delivery units under the control of administrative units.

9. It must be acknowledged that a driving force behind this development has been resource scarcity, namely, the absence of general purpose state revenues due to weaknesses in the tax system.

10. See, for example, Decision 70/1998/QĐ-TTg and Inter-Ministerial Circular 54/1998/TTLT/Bo GDDT-TC on school fees.

11. Decree 10/2002/ND-CP.

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