Delegation of Tax Collection, Local Elites, and State Capacity

Linke Hou
Center for Economic Research
Shandong University
abramhlk@sdu.edu.cn

Mingxing Liu
China Institute for Educational Finance Research
Peking University
mingxingliu@pku.edu.cn

Xiaobo Lü[1]
Department of Government
University of Texas at Austin
xiaobolu@austin.utexas.edu

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Abstract:

Tax cut is used to bolster popular support to the government, but few studies evaluate its unintended consequences on state capacity. We focus on the incentive structure of local elites, arguing that the removing delegation of tax collection as part of tax cut engenders the credible commitment problem in strategic interaction between the government and local elites, disincentivizing the latter to assist the state in enacting unpopular policies. We evaluate our argument based on a village-level panel dataset between 2000 and 2007 in rural China. We demonstrate that a tax reduction reform led to tax noncompliance and rising social unrest. We further show that worsening local governance was not the result of change in the domestic political environment, declining public spending, or rise of ad hoc taxes but disincentives of village elites to carry out state-preferred policies after losing fiscal autonomy and legitimacy through the withdraw of tax collection delegation.

1. Introduction

State capacity manifests in states' ability to penetrate civil society, transforming the intent of national political leaders into concrete outcomes (Lindvall and Teorell 2016; Mann 1984). Taxation (fiscal capacity) has been a predominant indicator of state capacity because extracting revenue from people is neither easy nor popular, and its success relies on a strong bureaucratic infrastructure. Furthermore, political leaders rely on tax revenue to achieve the outcomes necessary for their political survival—from public goods provision to coercion capacity building.

The importance of fiscal capacity has renewed scholarly interest in recent years (e.g., Beramendi, Dincecco, and Rogers 2019; Besley and Person 2009; Garfias 2018, 2019). These studies have significantly advanced understanding of sources of state capacity, yet two issues remain unexplored. First, these studies primarily focus on the roles of *national* elites, but the reach of the state often depends on the interaction between low-level bureaucrats and local elites, vital in the last mile of state capacity (Soifer 2015). Second, taxation is only one dimension of state capacity. It remains unclear if changes in fiscal capacity building may shape the state's reach in other dimensions, such as information collection and bureaucratic compliance (Berwick and Christia 2018; Lee and Zhang 2017).

In this paper, we fill the void by proposing a new mechanism of fiscal capacity building that enhances the state's reach. Although fiscal centralization is critical for state capacity (Dincecco 2011), the state often delegates tax collection to low-level bureaucrats and local elites. We argue that delegation of tax collection incentivizes local elites to assist the state in achieving unpopular policy outcomes. The incentives consist of two sources: 1) resolution of the credible commitment problem between the government and local elites, and 2) empowerment of local elites through fiscal autonomy and legitimacy.

Our arguments build on insights from theories of bureaucracy and delegation in a principal–agent framework by highlighting the commitment problem by the principal. We argue that local elites (agent) play a vital role in helping the state implement policies because they are socially embedded in the community and have better knowledge of local conditions than the government. To facilitate policy implementation, the government may *implicitly* delegate some authority to local elites in the form of discretionary policy enforcement. Notwithstanding, delegation is not credible *ex ante*—if the process of policy implementation generates undesirable outcomes, governments could deny and even renege on delegation, scapegoating local elites.

Delegation of tax collection could help incentivize local elites in two ways. First, it offers leverage to the local elites to punish a reneging government by exerting less effort in future tax collection, mitigating the credible commitment problem. Second, state-initiated taxation enhances local elites' political power through fiscal autonomy and legitimacy in fiscal extraction and public spending, which could be used as leverage in bargaining with local residents for compliance with various policies. When the state reduces or even abolishes local taxes, the tax cut inadvertently undermines the delegation of tax collection, thus undermining the incentives of local elites to assist the reach of the state.

To provide evidence for our arguments, we explore the relationship between delegation of tax collection and rural governance in China. China is a good testing ground because it has a strong fiscal centralization system, yet policy implementation in rural China relies on rural elites' cooperation (Tsai 2007). The Chinese central government initiated an agricultural reform since 2001, reducing and eventually abolishing agricultural taxes—the primary tax burden on peasants imposed by the state throughout China's history. Many argue that the tax reform strengthens fiscal centralization by the Chinese government (Oi et al. 2012). Although tax reduction has been widely

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used by governments around the world to garner popular support, we find puzzling the increase in tax noncompliance and rural unrest and the decline in peasants' tax burden, even though public spending has risen (Figure 1).

FIGURE 1 ABOUT HERE

We show that the surprising decline in rural governance after the tax reform is partly the result of the unintentionally removal of tax collection delegation to village cadres—the local elites—thus undermining their incentives to assist the state in achieving unpopular policy outcomes beyond tax collection. Our empirical strategy relies on a unique village-level panel dataset and the exogenous timing of the removal of tax collection delegation in our identification strategy. More importantly, our data consists of detailed measures of village elites' efforts and local policy outcomes (i.e., tax compliance and local stability).

Our empirical results suggest that tax reform increases tax noncompliance by 7.10 percentage points and mass petitions and mass protests by 18.1 and 13.5, respectively. We rule out a host of potential temporal and cross-section variations that could lead to rising social unrest and tax noncompliance such as changes in the Chinese central government's management of social stability, the level of public spending, the ad hoc tax burden, prior local stability, and the strength of informal institutions. We then provide direct evidence for our proposed mechanism. We demonstrate that village cadres exert significantly less effort in collecting taxes and maintaining local stability. Tax reform reduces their fiscal autonomy and undermines the legitimacy of village cadres, who reported difficulty dealing with villagers after the reform.

Our paper is relevant to two strands of literature. First, we contribute to recent burgeoning studies of state capacity and state building. Complementing existing studies by focusing on local

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elites, we propose another mechanism through which fiscal capacity building facilitates the state's reach. Cooperation from local elites is particularly vital for state building in environments with weak formal institutions in rural and peripheral areas (Baldwin 2013; Garfias and Sellars forthcoming; Gerring et al. 2011; Hassan 2020; Koter 2013; Mattingly 2020). Nonetheless, local elites are not always keen to become state agents (de Kadt and Larreguy 2018; Mattingly 2016), sometimes resisting the state's penetration in weak states (Lange 2004; Mamdani 1996; Migdal 2001; Shue 1988). Our paper highlights delegation of tax collection is an important mechanism for the cooptation of local elites because it resolves the credible commitment problem in delegation of authority. The mechanism we propose provides another reason that windfall revenues could undermine investment in state capacity: these sources of fiscal revenues fail to incentivize local elites to facilitate grassroots policy implementation.

Our paper also sheds light on the political consequences of agricultural tax reform in China. In previous studies this tax reform is viewed as a form of fiscal centralization, strengthening the central government's control of revenue collection and public spending at the expense of local governments (Chen 2014; Takeuchi 2014; Oi et al. 2012; Kennedy 2007, 2013; Smith 2010). These important insights are primarily based on an examination of *township* governments through the lens of fiscal contracting and revenue sharing. We offer a different argument, emphasizing the commitment problem in strategic interaction between township officials and village cadres. Our finding corroborates insights in Oi (1989) and Tsai (2007), who highlight the importance of village elites in assisting the state with policy implementation prior to agricultural reform.

Moving forward, we present a theoretical framework based on principal–agent models in Section 2. In our framework we highlight the ways tax collection resolves the credible commitment problem in strategic interaction between local government and village elites. Section 3

contextualizes our argument in rural China. In Section 4, we show consistent evidence that tax reduction since 2001 has undermined the state's desired outcomes—tax compliance and political order. In Section 5 we provide supporting evidence for our arguments by evaluating the impact of tax reduction on village elites' efforts to assist in implementing state policies. Finally, Section 6 concludes with implications.

2. State Capacity, Local Elites, and Delegation of Tax Collection

In this section, we offer a theoretical framework specifying ways through which the delegation of tax collection incentivizes local elites to achieve unpopular but desired state policy outcomes. Our theoretical framework is most applicable to political environments with weak formal institutions and state reliance on local elites for policy implementation (e.g., rural and peripheral regions).

2.1. The Set Up

Our theoretical framework builds on insights from theories of bureaucracy and delegation in a principal–agent model,[1] allowing us to specify the choice set and payoff behind strategic interactions between lowest-level government officials and village elites. In our framework, the former constitutes the principal and the latter are the agents. The principal has the resources and institutional power to make policy decisions but is ill-informed; agents have better information and the social network necessary to implement policies because they are socially embedded but lack sufficient power and resources to make policy.

To achieve desirable outcomes, the principal faces two choices in the strategic interaction with the agent—control or delegation. The control strategy entails the principal taking full control of

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[1] For a review of the formal models of bureaucracy and delegation, see Bendor, Glazer, and Hammond (2001) and Gailmard and Patty (2012).

policy implementation by relying on the agent for accurate information on local affairs; however, this strategy is not in the principal's best interest because the agent may falsify information. Even if the agent reveals accurate information, controlling policy implementation comes at a high cost to the principal, especially when managing multiple agents. Finally, taking policy implementation into the principal's own hands is potentially dangerous because he has to bear full responsibility for negative outcomes.

Meanwhile, the agent has two choices in strategic interaction with the principal—exerting effort or shirking. Specifically, the agent could exert effort by persuading local residents to comply with unpopular government policies. The success of the agent's efforts lies in moral authority as well as social embeddedness in the community (Tsai 2007); however, government policies are not always popular among local residents, making the agent's efforts very costly.

Alternatively, the agent could choose shirking, relegating the task of policy enforcement to higher-level government officials. Although the agent's shirking is likely to lead to failures in policy implementation, these undesirable outcomes hurt the principal more than the agent. Furthermore, the agent could use various excuses for lack of policy compliance and try to hide policy incompliance from higher-level governments. Because of information asymmetry, higher-level government officials have difficulty verifying the agent's claim and the degree of local policy compliance.

2.2. The Commitment Problem in Delegation of Policy Implementation

Fundamentally, the principal's ultimate goal is to "get as close as it can to its most preferred outcome, and by extension, to induce the agent to deploy its expertise as much as possible in the principal's interest" (Gailmard 2014:9). Hence, the standard principal–agent framework suggests that the principal should choose delegation for better compliance outcomes. In the context of weak

institution environments, delegation manifests mainly in discretionary policy enforcement, allowing the agent to selectively withhold law enforcement to achieve the broader objective (Holland 2016). Specifically, local elites with the power of discretionary policy enforcement may ignore local residents' minor legal infractions in some areas in exchange for compliance in other areas; or local elites may use coercion to carry out government policies.

Although delegation facilitates agents' efforts to carry out state policies, a credible commitment problem arises (Gailmard and Patty 2012). Specific to an environment with weak rule of law, delegation of power is not institutionalized, especially in the form of discretionary policy enforcement. Instead, delegation of power by the principal is implicit as long as the agent assists the principal in accomplishing tasks. Precisely because delegation of power is implicit, the principal may renege on and even deny delegation when the process of policy implementation generates undesirable outcomes, scapegoating the agent.

Blame avoidance frequently occurs among levels of government. Scholars have shown that the decentralization of policy implementation and state media bias induce Chinese citizens to give credit to the central government for good policy outcomes while assigning blame to local government for bad outcomes (Cai 2008; Lü 2014; O'Brien and Li 2006). Higher-level governments often blame village cadres' actions instead of policy design when undesirable outcomes emerge during implementation of such policies as shown in studies of the One Child Policy, environmental policies, and tax collection in China (Bernstein and Lü 2003; Mattingly 2020; Ran 2017).

Without safeguarding the commitment from the principal, agents have no strong incentive to use their information and social network to assist the state *ex ante*. Although contracting could help alleviate the credible commitment problem (Dixit 1995; Myerson 2015), the effectiveness of

the contract requires an objective and impartial third party to monitor and enforce contracts. This type of third party is often absent in developing countries where rule of law is limited. The principal could also use career incentives (e.g., replacing existing agents with new ones) to incentivize the agent; however, new agents are unlikely to possess the information and social network needed to deal with complex relationships among local residents. More importantly, a new agent faces exactly the same commitment problem as the previous agent. Hence, replacing existing agents is unlikely to yield better policy outcomes.

2.3. The Delegation of Tax Collection as a Solution

In light of the commitment problem in delegation of power, the delegation of tax collection serves as an external commitment device constraining the reneging principal. The logic of our argument is twofold. First, delegation of tax collection offers the agent leverage in strategic interaction with the principal, to whom tax collection is often an important task but to a lesser degree to the agent largely because the majority of tax revenues are relayed to higher-level governments. If the principal reneges on delegation of discretionary policy enforcement, the agent could punish the principal by exerting less effort in future tax collection, which hurts the principal more than it hurts the agent. Relying on the agent's continuous efforts in collecting taxes, the principal is constrained in reneging on the delegation of power.

Second, the effectiveness of delegation requires embedded incentives for the agent to use local knowledge and social networking to achieve the policy outcomes desired by the principal (Dessein 2002). With direct tax collection, embedded incentives entail fiscal autonomy and legitimacy to the agent. Specifically, local elites could legitimately collect other associated fees through the process of tax collection as the mandate of the state. Fiscal autonomy then offers an opportunity for agents to distribute public spending at their discretion, enhancing local elites' political power.

Finally, village elites could use tax collection as bargaining leverage with villagers for compliance in other policy dimensions.

The delegation of tax collection resolves the credible commitment problem and offers legitimacy as well as fiscal autonomy to local elites. When the state reduces or even abolishes local taxes, it unintentionally withdraws the delegation of tax collection from local elites. Consequently, they no longer have sufficient political power and incentives to assist the state to achieve desirable outcomes from unpopular policies. Our argument aligns with the insights of Kotsonis (2014), who observes that Imperial Russia never abolished taxation on peasants. Doing so would gave cut the only primary connection peasants had to the state (Kotsonis 2014: 244).

3. Agricultural Taxation and Local Elites in China

Before we present empirical evidence, we contextualize our argument in rural China. We briefly discuss the evolution of agricultural taxation in China, then detail the ways that delegation of tax collection shapes village elites' incentives to assist the state in achieving desirable policy outcomes.

3.1. The Evolution of Agricultural Taxation in China

Agricultural taxation had been a major source of state revenue throughout China's history. During the Qing Dynasty, for example, 70 percent of state revenue was collected from land and agricultural taxes (Zeng et al. 2013). After the founding of the People's Republic of China in 1949, agricultural taxes and later mandatory grain procurement fueled China's early industrialization (Oi 1989). Since China's economic opening and industrialization in 1978, however, the share of agricultural tax in government revenues has radically declined. By 2002, the share of agricultural tax accounted for only 2.6% of total government revenue (Wang and Shen 2014). Nevertheless, agricultural taxes remained an important revenue source for county and township governments

primarily because of enormous pressure to finance local public goods after the 1994 tax-sharing reform (Wong and Bird 2008).

Chinese peasants' tax burden falls into two categories: formal and ad hoc. The former consists of the agricultural tax (农业税, or *nongyeshui*) and associated fees (三提五统, or *santi wutong*) authorized by the central government. Based on estimated agricultural production, the agricultural tax is part of county and township government revenues. Meanwhile, associated fees are a subtax on the agricultural tax that remains in the hands of township and village to finance local public goods. Chinese peasants are also subject to an ad hoc tax burden, in the form of fundraising for village public goods projects, administrative fees even illegal fees and fines (Bernstein and Lü 2003). Supplementing the budgetary shortfall of local governments, it is legitimized by local governments' ordinances and policies but not by the central government's tax policies.

The Chinese central government initiated an agricultural tax reform in 2001 as part of the "Taxes for Fees" reform in Anhui province in 2000, fundamentally changing the nature of rural taxation in China. Importantly, the design of the agricultural tax reform was a top-down process. Despite mounting social unrest in rural China in the 1990s, the central government reacted tepidly to the peasants' burden even when it became a national policy issue (Göbel 2010). Eventually, elite competition in the central government, not bottom-up pressure, became the main driver of this policy (Li 2007).

This reform abolished formal taxes (i.e., agricultural tax and associated fees) previously authorized by the central government. Despite the abolition of agricultural taxes, peasants are still subject to ad hoc taxes and administrative fees imposed by local governments. The central government did not impose new taxes but used intergovernmental transfers to fill township and county governments' budgetary shortfall resulting from tax abolition. Consequently, the reform

relieved county and township governments' pressure to rely on agricultural taxes and fees to finance local public spending. By the end of 2002, another twenty provinces joined the policy experiment to reduce peasants' tax burden. Finally, the National People's Congress formally abolished the agricultural tax and fees for the entire country as of January 1, 2016.

3.2. Local Government and Village Elites in China

The formal organizational structure of the Chinese government is a nested hierarchy of political power, comprising four levels: province, municipalities–prefectures, counties–districts, and townships, the lowest level of the governmental system representing the formal state apparatus. Meanwhile, nearly one million villages are nested within townships in rural China, but their governing structure differs radically from the higher-level governmental structure. Since the enactment of the Organic Law of Village Committees (1987, amended 1998), the village committee, whose members are elected by villagers, serves as the main governing body in each village. Although village elections have granted villagers some political power, township governments and village-level party organizations remain important players in shaping rural governance (O'Brien and Han 2009).

In rural China, the last mile of state capacity hinges on cooperation between township officials and village cadres. Hence, the township officials can be considered the principal in our theoretical framework; village cadres, the agent. Although township officials have resources and institutionalized political power to make policy decisions, the implementation of these policies relies on cooperation from village cadres. Serving as dual political brokers for both the state and peasants (Chen and Liu 2020; Duara 1988), many village elites, who serve on village committees and in party branches, come from families or clans with extensive political power in the village; and they play an important role in facilitating or undermining the state's policy implementation.

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In particular, village elites play an important role in enforcing unpopular policies, such as tax collection (Duara 1988; Oi 1989; Tian and Zhao 2008; Wu 2007) and the One Child Policy (Mattingly 2020).

To entice cooperation from rural elites for policy implementation, Chinese rulers have always used various fiscal incentives to tie the fate of local elites to the state. The Qing Dynasty in China purposely allowed local bureaucrats to keep extra, unmonitored taxes in order to ensure bureaucratic compliance (Ma and Rubin 2019). In contemporary China, village cadres were entitled to a share of associated fees (i.e., santi wutong) to finance village projects, incentivizing them to assist in collecting the state's agricultural taxes. The scheme of revenue-sharing and fiscal contracting was the basis of local state corporatism because they incentivized county, township, and village governments to promote economic growth in rural China in the 1980s (Oi 1992).

4. Empirical Evidence

We describe our data and identification strategy and report the main results, showing that the removal of delegation of tax collection led to greater tax noncompliance and social unrest in rural China. We further evaluate a number of potential channels for the rise of social discontent and demonstrate that the main finding was driven chiefly by tax reduction but not by other potential channels.

4.1. Data

Our data are based on the *Rural Survey of Land, Migration, and Local Governance*, carried out by the Center for Chinese Agricultural Policy at the China Academy of Sciences. The survey involved a multistage stratified sampling procedure. First, the researchers who conducted the survey divided the entire country into six regions, in each of which they randomly selected one province, resulting in the selection of Fujian (Southeast), Hebei (North Central), Jilin (Northeast),

Jiangsu (East/Central Coast), Shaanxi (Northwest), and Sichuan (Southwest). They then sorted all counties in each province into five quintiles based on their gross industrial output per capita. One county was then randomly selected from each stratum. Next, researchers randomly selected two townships in each county based on per capita rural net income (one above the median and one below). Following the same procedure of township selection, they randomly selected two villages in each township for a total of 120 villages in the panel. Data collection in several villages was disrupted because of flooding in 2005 and the Sichuan earthquake in 2008. Hence, the data analyzed in this paper are based only on 113 villages in 53 townships during 2000, 2004, and 2007, thus creating a balanced panel dataset. Figure A1 in the appendix illustrates the geographical locations of the counties where these villages are located.

These survey data are particularly useful and reliable for two reasons. First, they were designed and collected by academic researchers, not governmental agencies, overcoming potential bias in government statistics. Second, the data are comprehensive, offering fine-grained measures of key concepts specific to our argument before and after the tax reduction. For instance, the survey includes an extensive set of objective questions on local governance, ranging from details on the tax burden from formal and ad hoc sources, tax noncompliance, and social unrest (i.e., petitions and incidents). More importantly, the researchers recorded valuable questions that allow us to measure the behavior changes of township bureaucrats and village cadres after the tax reform.

4.2. Identification Strategy

The gradual rollout of tax reform presents opportunities and challenges in our identification strategy. In our data, no village received any tax reduction in 2000 prior to the agricultural tax reform, but all of them experienced various degrees of tax reduction following the removal of tax collection delegation in 2004. For example, some villages in our sample experienced almost

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complete tax abolition in 2004, resulting in a tax burden of 1.35RMB per capita—a 98% tax burden reduction. The remaining villages received substantial tax reduction in 2004, yielding a tax burden of 51.58RMB per capita—a 58% decline in the tax burden. Finally, all villages experienced complete tax abolition in 2007.

The gradual rollout of tax reform naturally leads to the use of difference-in-differences (DID) strategy to identify the effects of tax reduction. The key treatment is the amount of tax reduction (i.e., intensity of the treatment), which serves as the proxy for the degree of removing delegation of tax collection. It is based on the following: $Tax\_Reduction_{it} = Tax\_Burden_{it} - Tax\_Burden_{i,2000}$. The DID specification follows:

$$Y_{it} = \beta_1 Tax\_Reduction_{it} + \delta X_{it} + v_i + \delta_t + \varepsilon_{it} \quad (1)$$

In Equation (1), Y_{it} is the indicator of local governance for village i at year t. X_{it} is a vector of control variables for village characteristics. To minimize post-treatment biases, we include only three control variables: *(Log) Village Population*, *(Log) Arable-land per capita*, and *(Log) Villager Net Income per capita*. We include both village (v_i) and year (δ_t) fixed effects in the model.

One particular concern in Equation (1) is that the intensity of the treatment (i.e., amount of tax reduction) correlates with village characteristics. Specifically, the *amount* of tax reduction likely correlates with village characteristics prior to reform. In our data, the average prereform tax burden is 103.90RMB with a standard deviation of 75.62RMB. Although the difference in prereform tax burdens partly resulted from the variation in arable land per capita in various villages, it was also a function of local elites' efforts in tax collection; that is, prior low tax burden could result from

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the lack of efforts by village elites in tax collection initially. Figure A2 in Appendix – 1 illustrates

our concern: a strong positive correlation between village cadres' efforts and the size of tax burden

per capita in 2000 prior to the agricultural reform.[2]

Hence, Equation (1) could be biased because the size of the tax reduction is partly shaped by

the level of the prereform tax collection efforts, which is endogenous to a host of observed and

unobserved factors specific to the villages noted above. To address this issue, our preferred model

specification exploits the *timing* of reform implementation instead of the *amount* of tax reform

because the former was exogenous to village characteristics—the gradual rollout of tax reduction

was determined by the central and provincial governments, not by the villages. Once a province

decided to adopt tax reduction or early tax abolition, it often implemented policies across the entire

province or in some prefectures instead of selecting specific villages. The *timing* of reform

implementation—removing tax collection delegation—has little to do with the degree of prior

social discontent in the village. Hence, we use the timing of implementation for tax abolition and

tax reduction to capture the intensity of removing tax collection delegation over time:

$$Y_{it} = \beta_1 Tax\_Abolition_{it} + \beta_2 Tax\_Cut_{it} + \delta X_{it} + v_i + \varepsilon_{it} \qquad (2)$$

In Equation (2), *Tax_Abolition*, an indicator for tax abolition, is coded 1 when a village

experienced complete tax abolition (i.e., 95% or more tax burden reduction), zero otherwise.

Tax_Cut is an indicator of tax reduction, coded 1 for villages experiencing more than 50% tax

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[2] In our data we assess village cadres' efforts in various tasks by asking them to rank the top five of their 34 most time-consuming tasks. Approximately 26.55% of the village cadres did not list tax collection as one of the top five tasks at all in 2000, but 48.67% of the village cadres listed tax collection as the most important tasks in 2000.

burden reduction,[3] zero otherwise. We distinguish *Tax_Abolition* from *Tax_Cut* because they capture different degrees of removing delegation of tax collection: the former is a complete removal; the latter partial removal. The model specified in Equation (2) is superior to that in Equation (1) because we are interested in understanding the impact of removing the delegation of tax collection but not the prereform variation in local elites' efforts. For the remainder of the paper, we rely on Equation (2) for most of the empirical analysis.

Because our key treatment variable is about the timing of reform implementation, *Tax_Abolition* and *Tax_Cut* are highly correlated with the year indicators. Thus, the inclusion of year fixed effects could generate significant multicollinearity leading to an imprecise estimate of our key treatment variables. Hence, we do not include year fixed effect in Equation (2) but consider a number of time-varying factors before and after the tax reform in our robustness checks. Finally, we use clustered standard errors at the village level in this model.

4.3. Empirical Results

We first report the effects of the tax reduction policy on formal tax burden. The prereform average formal tax burden per capita was 103.90RMB in 2000, of which the average agricultural tax per capita was 63.61RMB and associated fees per capita were 32.22RMB. Table 1 reports that both treatments of tax abolition and tax cut sizably reduced the peasants' formal tax burden. Columns 1–2, Table 1 shows that the marginal effects of *Tax_Abolition* on the total formal tax burden are between 40~43 RMB per capita and the marginal effects of *Tax_Cut* are between 54~57 RMB per capita. Given that most villages received some form of tax cut before tax abolition, the estimates of *Tax_Abolition* are smaller than those of *Tax_Cut* in the model specification. Hence, savings from the agricultural tax reform amount to 5% of villagers' personal income in 2000.

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[3] All the villages in our sample experienced more than 50% tax reduction in both 2004 and 2007, but no tax reduction in 2000.

Columns 3–6 evaluate the impact of tax reduction policy on two types of formal tax burden—agricultural tax and associated fees—and the estimates remain negative and statistically significant.

TABLE 1 ABOUT HERE

Next, we evaluate the impact of tax reduction on local governance—tax noncompliance and political unrest. The measure of tax noncompliance is the percentage of households in a village where citizens refused to pay their nonagricultural taxes and fees on time. We use two indicators for social unrest—mass petitions and mass incidents. Mass petitions occur when two or more individuals collectively submit a petition claim. Mass incidents (*quntixing shijan*) are large-scale acts of disobedience that include but are not limited to protests, demonstrations, physical clashes, obstruction of government business, and other forms of gatherings that disrupt social stability.

Table 2 reports regression results, showing that tax abolition and tax cut positively correlate with tax noncompliance and numbers of mass petitions and mass incidents. Substantively, Column 2 suggests that tax abolition increases tax noncompliance by 7.10 percentage points, or a 42% increase from the baseline mean. Meanwhile, Columns 4 and 6 suggests that tax abolition increases mass petitions and mass incidents by 18.1 percentage points and 13.5 percentage points, respectively. The increases are sizable, amounting to 67% and 143% from the baseline mean for mass petitions and mass incidents, respectively. Finally, estimates of the tax cut are positive in all models, but the sizes are smaller and not statistically significant.

TABLE 2 ABOUT HERE

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One concern about the results reported in Table 2 is that in using the timing of the reform, we may overlook heterogeneous treatment effects as well as a common time trend. We report the regression results using the degree of tax reduction based on the DID model with village and year fixed effects specified in Equation (1) in Table A1, Appendix – 2. The results are largely consistent with those in Table 2. The size of the tax burden reduction is endogenous to the variation in the degree of tax compliance prior to 2001 (i.e., village elites' efforts to extract taxes). Hence, we rely on model specification in Equation (2) for the remainder of our analysis.

4.4. Alternative Explanations

The main results reported in Table 2 could be driven by a number of confounders that shape tax noncompliance and social unrest in rural China but not by withdrawing delegation of tax collection. Formally evaluating several alternative explanations, we found that these alternative explanations—although playing important roles in shaping local governance in rural China—do not bias our estimated impact of tax reduction on the rise of tax noncompliance and social unrest.

Changes in the Political Environment. The rise of defiant villagers could be the result of changing domestic political environments following a 2003 change in central leadership. The new Hu–Wen administration appeared more accommodating of petitioners to expose policy failures in the previous administration and emboldened peasants to challenge local governments (Li, Liu, and O'Brien 2012; O'Brien and Li 2006). Mass protests could also serve as a monitoring device to alert higher-level leaders of local power abuses (Lorentzen 2013).

We agree that the policy shift by the central government played an important role in shaping contentious politics in rural China, even though the common policy shock from the central government cannot explain cross-sectional variations among villages observed in our data. We

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address this concern by incorporating villagers' public opinion data in the analysis.[4] Specifically, we generated a village-level aggregated measure on villagers' trust in the Chinese central government for both 2004 and 2007, which ranges between 0 and 1.[5] Figure A3 in Appendix – 1 illustrates that positive correlations between the aggregated trust in the central government and numbers of mass petition and mass incident. In other words, this pattern corroborates with the notion that the central government signals greater accommodation to villagers' demand, leading to higher trust toward the central government and emboldened villagers to stage petitions and protests.

We then replicate our main analysis by including this variable in the model. Table A2 in Appendix – 2 shows that the estimates of tax abolition remain positive and statistically significantly, even when we have to exclude the observations from 2000 due to lack of public opinion survey data. The magnitudes of the estimate have little changes after we include the variable on trust toward the central government. Hence, our main results are not driven by the changes in the overall political environment.

Pre-reform Unstable Villages. Another concern about the main results is that the patterns are largely driven by villages that were unstable prior to the reform. Hence, the observed effects could result from pre-reform factors driving more defiance to government policy implementation from the outset. To evaluate this claim, we divide the sample by village tax noncompliance in 2000 in the analysis (Table A3, Appendix – 2). The higher the tax noncompliance rate in 2000, the more likely that village cadres have weak control over local affairs prior to the tax reform, resulting in more protests and petitions after the tax reduction. Results in Table A3 show that the impact of tax

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[4] The research team conducted public opinion survey from 16~20 randomly selected villagers in 2004 and 2007. Unfortunately, the public opinion survey was not conducted in 2000 prior to the tax reform.
[5] The original survey question on trust in the Chinese central government is in a 5-point scale. We recoded this variable to one if a villager responded that he/she trust or very trust the central government, and zero otherwise.

reform still positively correlates with numbers of mass petitions and mass incidents in the top three quartiles of tax noncompliance prior to reform (Columns 1–6).

Alternatively, we exclude villages experiencing mass petitions and incidents in 2000 in our panel analysis. Our analyses still show strong positive correlations between tax abolition and mass petitions and incidents after excluding previously unstable villages (Table A4, Appendix – 2). Hence, our results indicates that the tax reform led to a decline of local governance in many previously stable villages.

Public Spending. Withdrawing the delegation of tax collection could undermine public spending, which in turn could result in mass discontent. We evaluate the impact of tax reduction on village public spending, and find no significant effect on village public spending (Column 1, Table A5, Appendix – 2). The estimate is negative but far from statistically significant. We then interact our tax reduction variables with the public spending variable, evaluating the impact of public spending on local governance after the tax reduction. As shown in Columns 2–4, estimates of the interaction terms are not statistically significant for tax noncompliance and mass incidents. In the model of mass petitions (Column 3), the estimate of the interaction term with tax abolition is negative and that with tax cut is positive, both statistically significant; however, the interaction effects cancel each other out, suggesting that public spending has little effect on mass petitions after 2006.

Meanwhile, unequal distribution of public spending in villages could be the culprit in rising social unrest. Specifically, those with power and influence could prioritize public goods provision to themselves, given the larger share of public spending earmarked for intergovernmental transfers. Indeed, our survey shows that numbers of mass petitions and protests related to issues concerning

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public spending had risen slightly since 2000.[6] To alleviate this concern, we excluded public spending-related mass petitions and protests in our analysis but still found positive correlations between tax reduction and mass petitions and protests (Table A6, Appendix – 2).

Ad Hoc Fees. Substitutional effects could be another potential explanation for the surprising negative impact of agricultural tax reform: local governments may increase the ad hoc tax burden to meet the shortfall of government revenue. Thus, the *de facto* tax burden remains unchanged. In our data, we find some evidence that the collection of ad hoc taxes and fees had increased after the tax abolition as reported in Column 1, Table A7, Appendix – 2; however, the estimate of tax abolition is small, indicating only a 17.88RMB increase in the informal tax burden, far smaller than the 103RMB formal tax burden prior to tax reduction. Furthermore, models with interaction terms suggest that the rise of ad hoc taxation after tax reform has null effect because estimates of interaction terms are small and not statistically significant in all models. Hence, the magnitude of the ad hoc tax burden is too small to generate mass discontent after the tax reform.

Bureaucratic Infrastructure. In addition to the loss of fiscal revenue, tax reduction may also undermine bureaucratic capacity. For example, tax reduction may weaken the operation of the grassroots Chinese Communist Party (CCP), which facilitates tax collection in rural China (Koss 2018). Table A8, Appendix – 2, however, shows that CCP party membership actually increased after the tax cut; furthermore, party membership has little impact on mass petitions and incidents before and after the tax cut.

Informal Institution. Informal institutions like lineage networks and semiautonomous civic associations play an important role in raising funds to finance rural public goods provision in China

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[6] We define issues concerning public spending as those related to public goods and infrastructure or village finance. No mass petitions or protests related to public spending in 2000, but the number of mass petitions related to public spending rose to 7 in 2004 and 8 in 2007, and the number of mass protests rose to 1 in 2004 and 3 in 2007; however, the share of public spending-related mass petitions and protests did not rise from 2004 to 2007.

(Tsai 2007), but their effects on conflict resolution are mixed. Some scholars argue that informal institutions may help mediate conflicts between the government and citizens (Lu and Tao 2017), others that informal institutions lead to elite capture in rural China, weakening citizen welfare (Mattingly 2016). Informal institutions evolve slowly because accumulating social capital takes time. Hence, the likelihood that the tax reduction policy could have immediate impact on the structure and influence of informal institutions is slim.[7]

Land Expropriation. Land expropriation by local governments has been a primary source of conflict in China (Göbel and Ong 2014). They often seize land from villages in order to promote economic growth and raise fiscal revenues (Chen and Kung 2016). Furthermore, one could argue that the loss of revenue resulting from agricultural reform led to intensified land expropriation, causing greater social conflicts.

Although a key catalyst for rural unrest in China, land expropriation may be only a necessary but not sufficient condition for the rise of social unrest observed in our data for three reasons. First, local governments have primarily enhanced their tax enforcement through VAT taxes instead of land expropriation to compensate for loss of revenue from agricultural tax reform (Chen 2017). Second, many villages experienced land expropriation long before the agricultural reform. In our sampled villages, we found a positive correlation between the tax cut and land expropriation but not tax abolition.[8] Third, village cadres play a critical role in negotiating compensation with local

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[7] Our village survey includes some questions on informal institutions. We use a variable indicating cooperative intermedia association that serves as the ally of the state with the following two conditions: 1) whether at least one of the organizers of these associations is a village cadre; 2) whether these associations have the autonomy to make decisions in infrastructure investment (e.g., building temples or churches). This indicator has also been used in Tao and Liu (2013). In Table A9, Appendix – 2, we include its interaction with tax reform variables in the model. Our analysis shows that estimates of interaction terms have different signs, and they are not statistically significant. Hence, the decline of state capacity in rural China has little to do with the role of informal institutions.
[8] For details on the results, see Table A10, Appendix – 2.

governments and land developers as well as distributing compensation among villagers (Cai 2003; Guo 2011). Hence, the occurrence of land conflict directly results from village elites' effort.

To further show that the overall patterns of social unrest are not driven by land expropriation, we disaggregate our data by land expropriation frequency in these villages. As shown in Column 1–2, Table A11, Appendix – 2, we still find that tax abolition positively correlates with mass incidents in 59 villages experiencing no land expropriation. Columns 3–8 further show that tax abolition positively correlates with a greater number of mass incidents, regardless of how many times the village has experienced land expropriation; however, estimates are less precise because of small sample size.

5. Impact of Tax Reform on Behavior of Township Officials and Village Elites

We have shown that agricultural tax reform, which removed tax collection delegation, had led to rising tax noncompliance and social unrest in rural China. The findings remain robust after we address a number of potential explanations. In this section, we offer direct evidence for the mechanism proposed in our theoretical model—withdrawing tax collection delegation undermined village elites' incentives to assist the state in achieving desirable outcomes—tax collection and local stability. We first evaluate the efforts of village cadres (agents) and township officials (principals). We further show that tax reduction has a negative impact on village cadres' fiscal autonomy and legitimacy, implying that they have a harder time to persuade villagers to comply with state policies.

Efforts through Job Priority. Village cadres' efforts are more critical for maintaining local stability largely because they have the knowledge and social network township officials lack. Given that both village cadres and township officials operate in a multitask environment, one way

to measure their efforts is to evaluate the extent to which they prioritize tasks desired by higher-level governments.

Fortunately, the survey has a battery of questions asking village cadres and township officials to name their top five job priorities from a list of 34 tasks, among them, tax collection, managing petition, and maintaining stability. Based on the survey responses, we created binary variables indicating whether tax collection, social stability, and petitions were among the top five tasks, respectively, for both village cadres and township officials.

We found evidence suggesting that village cadres engaged in efforts to shirk tasks involving local stability; consequently, township officials had to exert greater effort.[9] Figure 2 shows that village cadres were less likely to indicate tax collection and stability maintenance as one of the top five task priorities from 2000 to 2007. Township officials report that they exert much greater effort in maintaining local stability to fill the gap; however, they have neither the knowledge nor the social network of village cadres; hence their efforts yielded little fruitful outcome.

FIGURE 2 ABOUT HERE

Given the importance of maintaining social stability as a "veto policy target" under China's cadre responsibility system,[10] we expect past incidence of social unrest would incentivize village cadres and township officials to exert greater effort. Nonetheless, we found that the social unrest prompted township officials to exert more effort but not village cadres. Specifically, we aggregated

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[9] One could argue that changes in the efforts of village cadres could result from de facto elites no longer running for the village governing body. Evaluating the personal characteristics of village party secretaries and village heads before and after the tax reform, we find little difference (Table A12, Appendix – 2).

[10] In the case of China, higher-level governments often use strategies to incentivize lower-level governments to carry out certain tasks. One of the most important tools is the so-called "veto policy target," which means that failing to fulfill this policy target would immediately hurt the careers of local politicians during the annual cadre evaluation (Edin 2003). This kind of "veto policy target" tends to direct local politicians' time and effort toward tasks like birth control and social stability (Obrien and Li 1999).

the numbers of mass petitions and mass incidents for the three years prior to 2004 and 2007[11] and estimate their effects on village cadres' and township cadres' self-reported job priorities in either petition or social stability. We find consistent evidence that rising social unrest positively correlates with township cadres' job priorities in these two areas (Table 3, Columns 1–4); however, we find little evidence that social unrest has any impact on village cadres' self-reported job priorities in these two areas except for the number of mass incidents during the previous three years (Table 3, Columns 5–8). More importantly, designating petitions or social stability as veto policy targets fails to incentivize village cadres to prioritize achieving these desirable outcomes by the state.

TABLE 3 ABOUT HERE

Fiscal Autonomy. We evaluate the impact of tax reform on village cadres' fiscal autonomy, which plays an important role in incentivizing village elites to assist the state in achieving desirable outcomes. We use several indicators to measure fiscal autonomy. Columns 1–2, Table 5 first report that the wages of village cadres—party secretaries and heads—substantially increased after the tax reform; however, their salary increase primarily derives from intergovernmental transfers after the tax cut (Table 5, Columns 3–4). In other words, village cadres' financial well-being relies on governmental transfers but not rent-seeking opportunities at the local level. Furthermore, we found a strong correlation between tax cut and intergovernmental transfers to village revenues for public spending (Column 5) with the village government receiving a 96.9% increase in intergovernmental transfers. Given intergovernmental transfers are tied to specific public projects, village cadres have little opportunity to exert their influence in the distribution of public spending. Finally, we found a strong negative relationship between tax abolition and the ability of villages to raise revenues by

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[11] The analysis is based only on job priority indicators reported in 2004 and 2007 because we have no data on social conflict prior to 2000.

themselves (Column 6). After tax abolition, the amount of fund raising by village cadres declined by 96.4%. These results provide strong evidence that tax reduction undermines village cadres' fiscal autonomy, in turn undermining their incentives to assist the state.

TABLE 4 ABOUT HERE

Village Cadres' Legitimacy. In our theoretical argument we contend that delegation of tax collection offers village cadres legitimacy in the eyes of villagers and the leverage they need to carry out state policies. To evaluate this claim, we rely on 2008 individual surveys for village cadres and villagers, conducted along with village condition surveys. The village cadre survey included four questions soliciting self-reported assessment of their relationship with villagers following abolition of the agricultural tax and fees in 2006; the questions dealt with job challenge, time spent on the job, relationship with villagers, and difficulty in fulfilling policy targets imposed from above. Meanwhile, the villager survey asked about trust in both village cadres and the central government and whether village cadres had better capacity and served better after the tax abolition.

We use these questions as proxies to measure the legitimacy of village cadres, finding consistent evidence that the greater the tax reduction, the more the village cadres reported that their relationship with villagers deteriorated (Table 5). Specifically, Columns 1 and 3 show that village cadres found their jobs more challenging and their relationship with villagers more difficult as the per capita tax reduction increased. They also reported that they spent more time on the job after the tax abolition, but the estimate is not statistically significant (Columns 2). Because of the challenges in their relationship with villagers, village cadres found fulfilling policy targets from higher-level governments more difficult (Columns 4). Meanwhile, we find no evidence that villagers had higher trust in village cadres after the tax abolition despite the latter's loss of the use of coercion during tax collection and perception that village cadres had worse capacity and did not

serve better. Interestingly, we find the village cadres increased their trust in the central government. The asymmetry in the trust in central and local government is consistent with findings in Lü (2014), who found the same effects for the abolition of school tuition and fees. Taken together, results provide evidence that tax reduction significantly undermined village cadres' legitimacy.

TABLE 5 ABOUT HERE

6. Conclusion

The strength of state capacity hinges on the state's ability to carry out unpopular policies at the grassroots level. In an environment with weak institutions, state capacity relies on cooperation from local elites. We argue that the delegation of tax collection resolves the credible commitment problem in the delegation of discretionary policy implementation and offers fiscal autonomy and legitimacy to local elites. Hence, fiscal capacity with delegation of tax collection enhances state capacity not only through the channel of revenue collection and bureaucratic infrastructure, but it also strengthens the last mile of state capacity by incentivizing local elites to assist the state.

In the case of China, not only did removing the delegation of tax collection undermine incentives for village cadres to assist the state, but it also crippled their capability in dealing with villagers when carrying out unpopular policies. Weakening village cadres inevitably forces local governments to seek alternative assistance to carry out unpopular policies, leading to the rise of outsourcing violence and repression through thugs or other private actors for land expropriation in rural China (Hurst et al. 2014; Ong 2018). Our paper sheds light on this recent development, evidently an unintended by-product of the agricultural tax reform. Although some may view tax reform as an indicator of China's strengthening state capacity through fiscal centralization, the last mile of state capacity is weakened because of the gap between the intent of the state and actual

outcomes. The edifice of state capacity may one day collapse because of corrosion at the very base of the foundation.

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Panel A: The Decline of Local Governance in Rural China
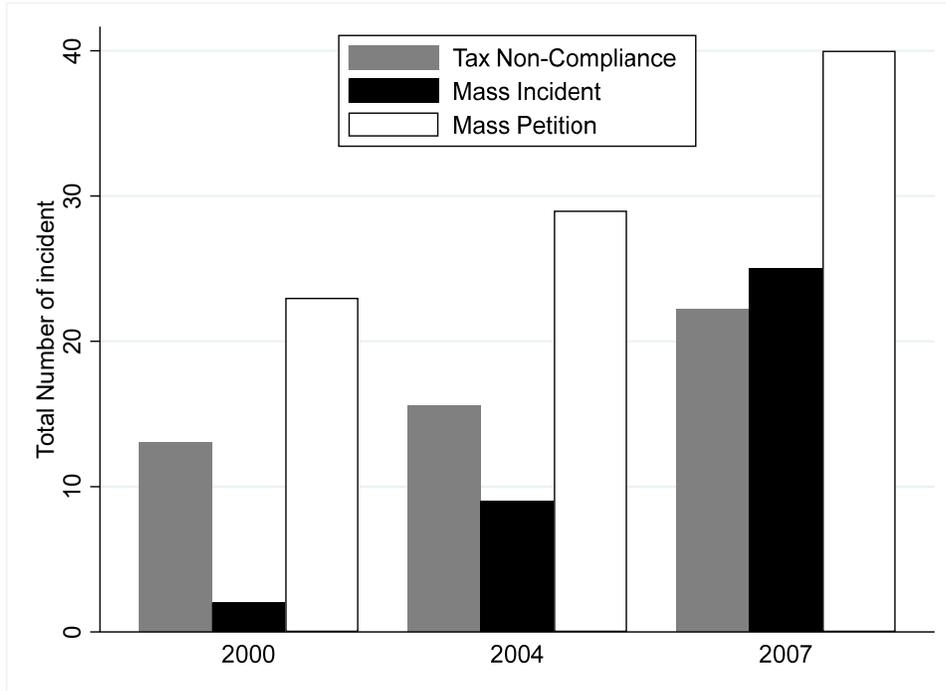
Panel B: Tax Burden and Public Spending
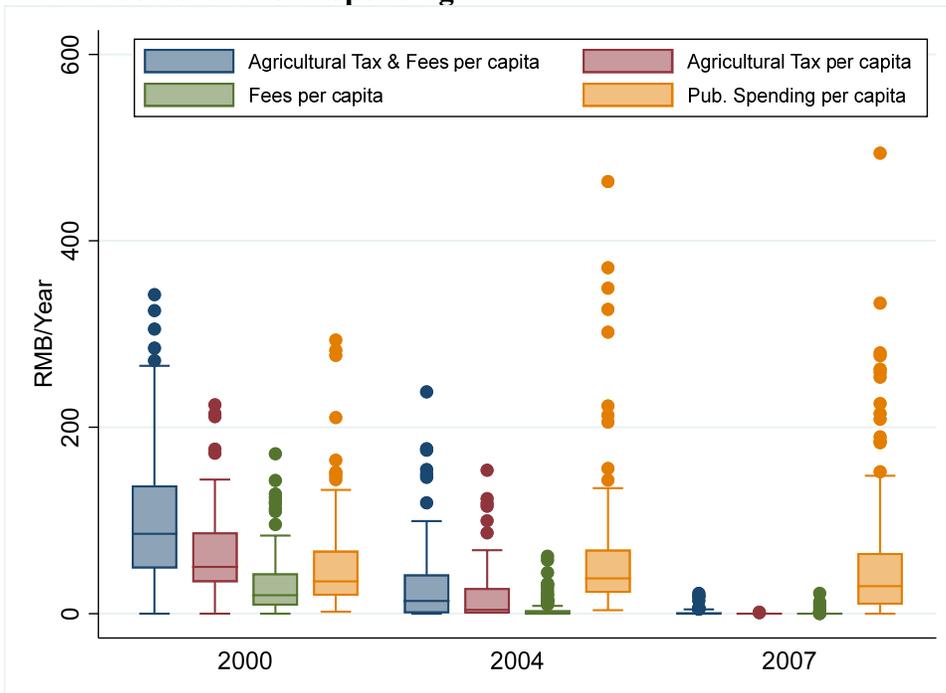
FIGURE 1: LOCAL GOVERNANCE AND TAX BURDEN RURAL CHINA

Note: The figure is based on the data from *Rural Survey of Land, Migration, and Local Governance*.

Panel A: Village Cadre's Job Priority Ranking
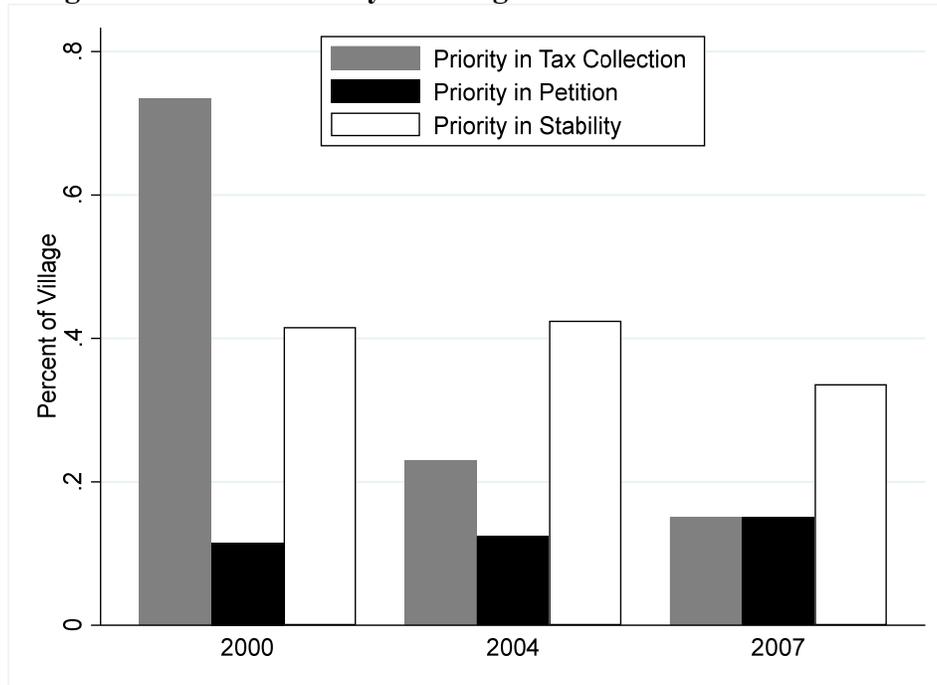
Panel B: Township Official's Job Priority Ranking
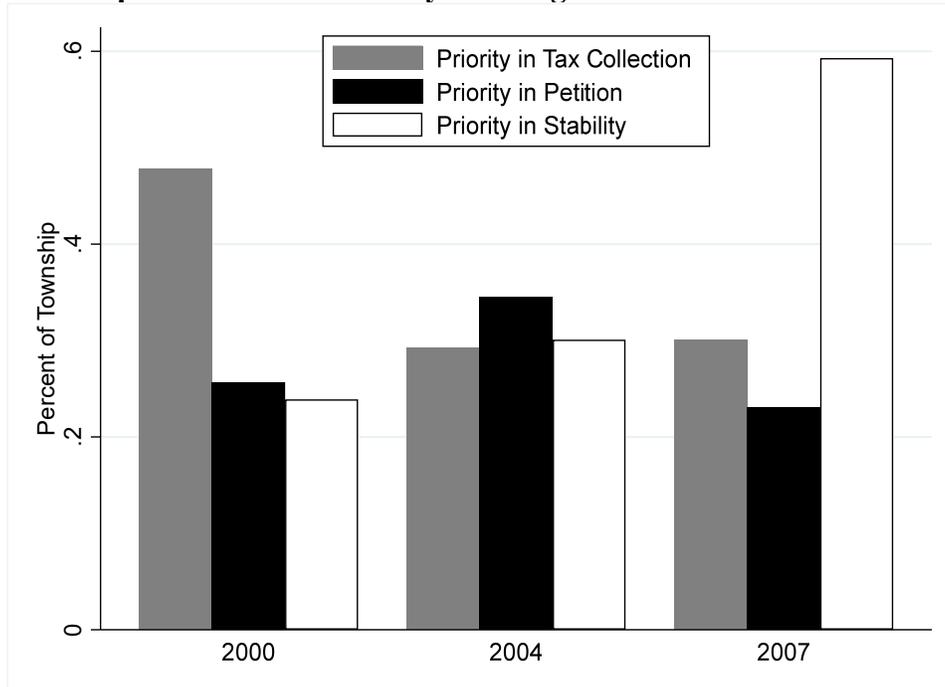
FIGURE 2: BEHAVIORAL CHANGES BY VILLAGE CADRES AND TOWNSHIP OFFICIALS

Note: The figure is based on the data from *Rural Survey of Land, Migration, and Local Governance*. It plots the percentage of villages and townships reported tax collection, managing petition, and managing stability as one of the top-five tasks out of 34 tasks.

TABLE 1 THE IMPACTS OF TAX REDUCTION ON TAX BURDEN

	TOTAL TAX BRUDEN PER CAPITA		AGRICULTURAL TAX BURDEN PER CAPITA		AGRICULTURAL TAX RELATED FEES PER CAPITA	
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	-43.452***	-40.459***	-28.590***	-26.953***	-6.580***	-5.023**
	(5.238)	(5.805)	(3.369)	(3.592)	(1.888)	(2.159)
Tax Cut = 1	-57.125***	-54.137***	-33.599***	-32.187***	-24.934***	-23.293***
	(4.899)	(5.273)	(2.940)	(3.366)	(3.041)	(2.989)
Village Characteristics Control	NO	YES	NO	YES	NO	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	339	339	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE 2 THE IMPACTS OF TAX REDUCTION ON LOCAL GOVERNANCE

	% OF TAX-NONCOMPLIANCE HOUSEHOLD		MASS PETITION (0/1)		MASS INCIDENT (0/1)	
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	4.824	7.098**	0.141**	0.181**	0.131***	0.135***
	(3.242)	(3.426)	(0.068)	(0.074)	(0.048)	(0.049)
Tax Cut = 1	2.390	3.687	0.001	0.063	0.021	0.030
	(1.893)	(2.707)	(0.069)	(0.074)	(0.029)	(0.035)
Mean Dependent Variable	17.082	16.938	0.272	0.271	0.096	0.094
Village Characteristics Control	NO	YES	NO	YES	NO	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	339	339	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE 3 THE IMPACTS OF MASS INCIDENT ON VILLAGE AND TOWNSHIP BEHAVIORS

	TOWNSHIP JOB PRIORITY ON PETITION (0/1)		TOWNSHIP JOB PRIORITY ON STABILITY (0/1)		VILLAGE JOB PRIORITY ON PETITION (0/1)		VILLAGE JOB PRIORITY ON STABILITY (0/1)	
	FE	FE	FE	FE	FE	FE	FE	FE
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
# of Mass Petition (Last 3 years)	0.095* (0.057)				-0.002 (0.024)			
(Log) # of People Participated in Mass Petition (Last 3 years)		0.023 (0.053)				-0.009 (0.020)		
# of Mass incident (Last 3 years)			0.314* (0.180)				0.133* (0.073)	
(Log) # of People Participated in Mass incident (Last 3 years)				0.110* (0.057)				0.040 (0.026)
Designated Veto Policy Target to Village					0.010 (0.103)	0.007 (0.103)	-0.014 (0.100)	-0.023 (0.099)
Township Characteristics Control	YES	YES	YES	YES	NO	NO	NO	NO
Township FE	YES	YES	YES	YES	NO	NO	NO	NO
Village Characteristics Control	NO	NO	NO	NO	YES	YES	YES	YES
Village FE	NO	NO	NO	NO	YES	YES	YES	YES
Year FE	YES	YES	YES	YES	YES	YES	YES	YES
Number of Township/Village	53	53	53	53	113	113	113	113
Number of Observations	106	106	106	106	226	226	226	226

Note: The dependent variable is the indicator of whether a specific task was ranked as one of the top-5 tasks by village cadres or township cadres. Standard errors clustered by village or township are reported in parentheses for village and township analysis, respectively. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Township control variables include *(Log) Township Population, (Log) Net Income per capita,* and *Numbers of Township TVE*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE 4 THE IMPACTS ON VILLAGE FISCAL AUTONOMY

	ANNUAL WAGE (LOG)		% OF INTERGOVERNMENTAL TRANSFERS IN THE WAGE		TRANSFERS RECEIVED IN VILLAGE REVENUE (LOG)	VILLAGE SELF-RASIED REVENUE (LOG)
	V-SEC	V-HEAD	V-SEC	V-HEAD		
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	0.284***	0.307***	-8.635	-8.599	0.273	-0.964***
	(0.055)	(0.056)	(8.030)	(8.169)	(0.176)	(0.186)
Tax Cut = 1	0.125**	0.157***	41.409***	40.910***	0.969***	0.024
	(0.055)	(0.051)	(7.127)	(7.129)	(0.159)	(0.187)
Village Characteristics Control	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	336	333	338	336	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita.* Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE 5 THE IMPACTS ON VILLAGE CADRES' LEGITIMACY

	Village Cadre Survey				Villager Survey			
	JOB IS CHALLENGING	TIME ON THE JOB	DIFFICULT RELATIONSHIPS WITH VILLAGERS	HARDER TO FULFILL POLICY TARGET FROM ABOVE	TRUST IN VILLAGE CADRE	TRUST IN CENTRAL GOV.	VILLAGE CADRE HAD BETTER CAPACITY	VILLAGE CADRE SERVED BETTER
	OPROBIT	OPROBIT	OPROBIT	OPROBIT	PROBIT	OPROBIT	OPROBIT	OPROBIT
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Log Agricultural Tax & Fees per capita Reduction (2000-2007)	0.781***	0.244	0.749***	0.698***	0.112	0.138**	-0.064*	-0.055
	(0.239)	(0.208)	(0.267)	(0.228)	(0.090)	(0.067)	(0.037)	(0.037)
Individual Characteristics	NO	NO	NO	NO	YES	YES	YES	YES
Village Characteristics Control	YES	YES	YES	YES	YES	YES	YES	YES
Province FE	YES	YES	YES	YES	YES	YES	YES	YES
Number of Observations	113	113	113	113	2248	2248	2248	2248

Note: Robust standard errors are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. The individual characteristics control include age, gender, year of schooling, CCP party membership, village cadre status. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

Online Appendix for Taxation, State Capacity, and Local Elites

(8/6/2021)

APPENDIX – 1 FIGURES

APPENDIX – 2 ADDITIONAL TABLES

Figure A1: Geographical Locations of the Sampled Counties

FIGURE A2: TAX BURDEN AND VILLAGE ELITES' EFFORTS PRIOR TO THE AGRICULTURAL TAX REFORM

Note: The figure is based on the data from *Rural Survey of Land, Migration, and Local Governance*. It plots the average tax burden per capita and village cadres' efforts in tax collection in 2000. The Job Priority in Tax Collection is self-reported top-five tasks out of 34 tasks that village cadres spend most of the time during that year. It is coded when tax collection was reported as: 5 for Top 1 Task; 4 for Top 2 Task; 3 for Top 3 Task; 2 for Top 4 Task; 1 for Top 5 Task; and 0 for not named in one of the top 5 task.
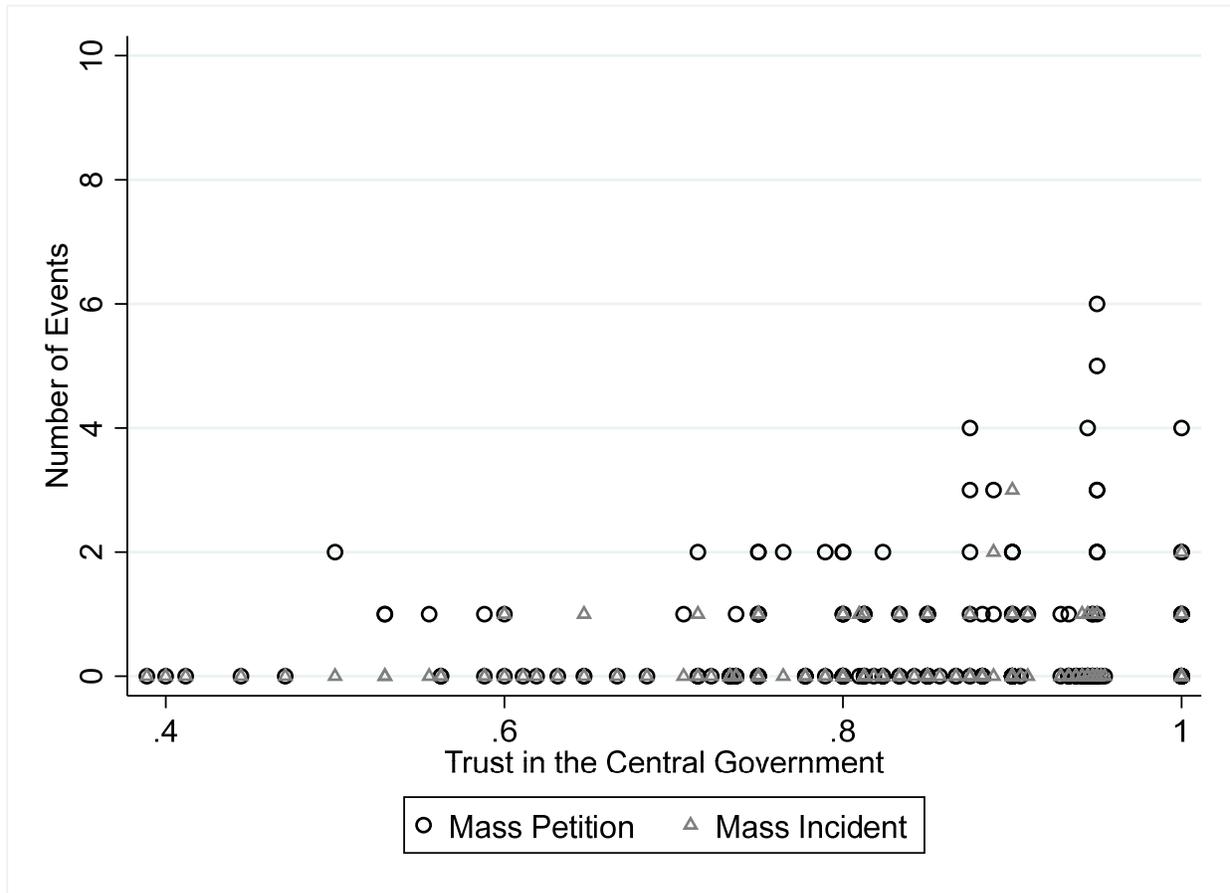
FIGURE A3: TRUST IN CHINESE CENTRAL GOVERNMENT AND MASS PEITTION/INCIDENT

Note: The figure is based on 2004 and 2007 public opinion data of randomly selected villagers in *Rural Survey of Land, Migration, and Local Governance*. Unfortunately, the public opinion survey was not conducted in 2000. This figure plots aggregated village-level trust in the Chinese Central Government and the number of mass petitions and incidents in both 2004 and 2007. The original survey question was in a 5-point scale, and we recoded the variable one if a villager responded that he/she trust or very trust the Chinese central government, and zero otherwise. We then aggregate the village-level measure by averaging the villagers' responses within a village. Hence, the variable *Trust in the Central Government* ranges from 0 to 1, where a higher number indicates greater trust in the central government.

TABLE A1 THE IMPACTS OF SIZE OF TAX REDUCTION WITH VILLAGE AND YEAR FE

	% OF TAX-NONCOMPLIANCE HOUSEHOLD		MASS PETITION (0/1)		MASS INCIDENT (0/1)	
	(1)	(2)	(3)	(4)	(5)	(6)
Total Tax Reduction Per Capita	0.060***	0.063***	0.001	0.001*	0.001	0.001
	(0.022)	(0.022)	(0.001)	(0.001)	(0.001)	(0.000)
Village Characteristics	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES
Year FE	YES	YES	YES	YES	YES	YES
Number of Observations	339	339	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A2 THE IMPACTS OF TAX ABOLITION ON LOCAL GOVERNANCE (CONTROLLING FOR TRUST IN THE CENTRAL GOVERNMENT 2004-2007)

	% OF TAX-NONCOMPLIANCE HOUSEHOLD		MASS PETITION (0/1)		MASS INCIDENT (0/1)	
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	6.842	6.754	0.187**	0.188**	0.148***	0.138**
	(4.233)	(4.357)	(0.079)	(0.081)	(0.059)	(0.063)
Trust in the Central Government		1.717		-0.023		0.198
		(20.853)		(0.421)		(0.271)
Village Characteristics	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	226	226	226	226	226	226

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A3 THE IMPACTS OF TAX REDUCTION ON LOCAL GOVERNANCE (BY TAX NONCOMPLIANCE IN 2000)

	2000 Tax Noncompliance 4th Quartile		2000 Tax Noncompliance 3rd Quartile		2000 Tax Noncompliance 2nd Quartile		2000 Tax Noncompliance 1st Quartile	
	MASS PETITION (0/1)	MASS INCIDENT (0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Tax Abolition = 1	0.375**	0.074	0.035	0.211**	0.315*	0.234**	0.076	0.062
	(0.163)	(0.102)	(0.181)	(0.096)	(0.155)	(0.096)	(0.122)	(0.104)
Tax Cut = 1	-0.004	0.066	0.172	-0.042	-0.134	-0.006	0.261	0.069
	(0.104)	(0.067)	(0.163)	(0.062)	(0.134)	(0.046)	(0.179)	(0.082)
Village Characteristics Control	YES	YES	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES	YES	YES
Number of Observations	84	84	87	87	84	84	84	84

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *(Log) Village Income per capita.* Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A4 THE IMPACTS OF TAX REDUCTION ON LOCAL GOVERNANCE (EXCLUDING UNSTABLE VILLAGES IN 2000)

	% OF TAX-NONCOMPLIANCE HOUSEHOLD		MASS PETITION (0/1)		MASS INCIDENT (0/1)	
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	3.759	7.030*	0.178**	0.203**	0.142***	0.150***
	(3.948)	(4.138)	(0.075)	(0.079)	(0.046)	(0.050)
Tax Cut = 1	3.678	5.238*	0.198***	0.235***	0.022	0.031
	(2.334)	(3.027)	(0.061)	(0.068)	(0.027)	(0.035)
Village Characteristics	NO	YES	NO	YES	NO	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	267	267	267	267	267	267

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A5 THE IMPACTS OF TAX REDUCTION AND VILLAGE SPENDING

	VILLAGE PUBLIC SPENDING PER CAPITA	% OF TAX-NONCOMPLIANCE HOUSEHOLD	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)	(4)
Tax Abolition = 1	-12.352	5.288	0.404***	0.146**
	(20.307)	(5.315)	(0.111)	(0.066)
Tax Cut = 1	-23.205	4.163	-0.102	0.016
	(20.008)	(5.034)	(0.110)	(0.054)
Village Public Spending per capita		-0.023	0.001	-0.000
		(0.032)	(0.001)	(0.000)
Tax Abolition = 1 × Village Public Spending per capita		0.042	-0.006**	-0.000
		(0.099)	(0.002)	(0.001)
Tax Cut = 1 × Village Public Spending per capita		-0.023	0.005**	0.000
		(0.097)	(0.002)	(0.001)
Village Characteristics Control	YES	YES	YES	YES
Village FE	YES	YES	YES	YES
Number of Observations	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A6 THE IMPACTS OF TAX REDUCTION ON LOCAL GOVERNANCE (EXCLUDING PUBLIC SPENDING RELATED SOCUAL UNRESTS)

	% OF TAX-NONCOMPLIANCE HOUSEHOLD		MASS PETITION (0/1)		MASS INCIDENT (0/1)	
	(1)	(2)	(3)	(4)	(5)	(6)
Tax Abolition = 1	2.671	5.956*	0.105	0.140*	0.091*	0.094*
	(3.279)	(3.383)	(0.069)	(0.075)	(0.047)	(0.048)
Tax Cut = 1	2.747	5.190**	-0.014	0.067	0.019	0.033
	(1.911)	(2.586)	(0.069)	(0.073)	(0.028)	(0.034)
Village Characteristics	NO	YES	NO	YES	NO	YES
Village FE	YES	YES	YES	YES	YES	YES
Number of Observations	323	323	323	323	323	323

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A7 THE IMPACTS OF TAX REDUCTION AND AD HOC FEES

	AD HOC FEES PER CAPITA	% OF TAX-NONCOMPLIANCE HOUSEHOLD	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)	(4)
Tax Abolition = 1	17.877*	8.488	0.124	0.113
	(9.265)	(5.787)	(0.120)	(0.082)
Tax Cut = 1	-1.943	-1.073	-0.019	0.018
	(5.673)	(3.947)	(0.116)	(0.060)
Ad Hoc Fees per capita		-0.005	-0.002*	-0.000
		(0.049)	(0.001)	(0.001)
Tax Abolition = 1 × Ad Hoc Fees per capita		-0.062	0.001	0.000
		(0.116)	(0.002)	(0.002)
Tax Cut = 1 × Ad Hoc Fees per capita		0.120	0.002	0.000
		(0.109)	(0.002)	(0.001)
Village Characteristics Control	YES	YES	YES	YES
Village FE	YES	YES	YES	YES
Number of Observations	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita.* Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A8 THE IMPACTS OF TAX REDUCTION AND GRASSROOTS CCP PARTY PENETRATION

	PARTY MEMBERSHIP PER CAPITA	% OF TAX-NONCOMPLIANCE HOUSEHOLD	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)	(4)
Tax Abolition = 1	0.102**	15.011*	0.200	0.165
	(0.044)	(7.626)	(0.162)	(0.112)
Tax Cut = 1	0.230***	-3.706	0.130	-0.013
	(0.064)	(5.681)	(0.165)	(0.092)
Party Membership per capita		5.595*	-0.019	-0.033
		(2.851)	(0.058)	(0.035)
Tax Abolition = 1 × Party Membership per capita		-2.839	-0.007	-0.009
		(2.594)	(0.047)	(0.036)
Tax Cut = 1 × Party Membership per capita		1.940	-0.023	0.017
		(2.148)	(0.051)	(0.030)
Village Characteristics Control	YES	YES	YES	YES
Village FE	YES	YES	YES	YES
Number of Observations	339	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A9 THE IMPACTS OF TAX REDUCTION AND INFORMAL INSTITUTION

	% OF TAX-NONCOMPLIANCE HOUSEHOLD	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)
Tax Abolition = 1	8.267*	0.187**	0.108*
	(4.189)	(0.091)	(0.064)
Tax Cut = 1	3.535	0.055	0.044
	(3.226)	(0.086)	(0.043)
Tax Abolition = 1 × Informal Institution	-3.672	-0.019	0.087
	(6.329)	(0.141)	(0.096)
Tax Cut = 1 × Informal Institution	0.820	0.025	-0.050
	(3.415)	(0.140)	(0.052)
Village Characteristics Control	YES	YES	YES
Village FE	YES	YES	YES
Number of Observations	339	339	339

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A10 THE IMPACTS TAX REDUCTION ON LAND EXPROPRIATION

	LAND EXPROPRIATION (CURRENT YEAR)	LOGGED SIZE OF LAND EXPROPRIATION (CURRENT YEAR)	LAND EXPROPRIATION (LAST 3 YEARS)	LOGGED SIZE OF LAND EXPROPRIATION (LAST 3 YEARS)
	(1)	(2)	(3)	(4)
Tax Abolition = 1	-0.041	0.063	-0.090	-0.035
	(0.051)	(0.191)	(0.065)	(0.244)
Tax Cut = 1	0.159***	0.562***	0.159**	0.581**
	(0.046)	(0.150)	(0.061)	(0.217)
Village Characteristics Control	YES	YES	YES	YES
Village FE	YES	YES	YES	YES
Number of Observations	339	339	339	339

Note: The land expropriation indicator is a binary variable, indicating whether a village had experience land expropriation. Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A11 LAND EXPROPRIATION FREQUENCY AND SOCIAL UNREST

	NEVER LAND EXPROPRIATION		LAND EXPROPRIATION TWICE		LAND EXPROPRIATION TWICE, INCLUDING 2000		LAND EXPROPRIATION TRHEE TIMES	
	MASS PETITION (0/1)	MASS INCIDENT(0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)	MASS PETITION (0/1)	MASS INCIDENT (0/1)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Tax Abolition = 1	0.108	0.122**	-0.139	-0.096	0.082	0.075	0.123	0.046
	(0.091)	(0.049)	(0.244)	(0.178)	(0.255)	(0.096)	(0.152)	(0.098)
Tax Cut = 1	0.029	-0.011	0.358	0.276	-0.236	0.081	-0.631	0.304
	(0.083)	(0.029)	(0.261)	(0.165)	(0.406)	(0.139)	(0.335)	(0.359)
Village Characteristics Control	YES	YES	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES	YES	YES
Number of Observations	177	177	66	66	39	39	15	15

Note: Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land per capita,* and *(Log) Village Income per capita.* Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.

TABLE A12 THE IMPACTS ON VILLAGE CADRE CHARACTERISTICS

	YEAR OF SCHOOLING		VETERAN STATUS		SERVED IN VC		OWNED SMALL BIZ		WORKED IN TVE/TVG	
	V-SEC	V-HEAD	V-SEC	V-HEAD	V-SEC	V-HEAD	V-SEC	V-HEAD	V-SEC	V-HEAD
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Tax Abolition = 1	0.022	0.152	-0.008	0.024	0.010	-0.035	0.029	0.013	-0.036	-0.015
	(0.145)	(0.164)	(0.030)	(0.031)	(0.039)	(0.045)	(0.031)	(0.036)	(0.031)	(0.033)
Tax Cut = 1	0.742***	0.140	-0.006	-0.010	-0.020	-0.011	-0.038	0.020	0.046*	0.030
	(0.251)	(0.197)	(0.021)	(0.052)	(0.045)	(0.045)	(0.053)	(0.033)	(0.026)	(0.018)
Village Characteristics Control	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Village FE	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
Number of Observations	289	284	290	284	295	284	293	284	295	284

Note: All the dependent variables are coded binary, with the exception of year of schooling. Standard errors clustered by village are reported in parentheses. Village control variables include *(Log) Village Population, (Log) Arable-land Per Capita,* and *(Log) Village Income per capita*. Significant at 0.1 level. ** Significant at 0.05 level. *** Significant at 0.01 level.