

**GOVERNMENT REVENUE IN CHINA:
WHY HAS IT RISEN SO RAPIDLY?**

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Executive Summary

1. In the last decade and a half, government revenue in China has consistently outpaced economic growth. Consequently, the ratio of fiscal revenue to GDP doubled between 1996 and 2011. Total government revenue amounted to over 32% of China's GDP in 2010, up from 17% in 1996.
2. This phenomenon is best explained by examining the current institutional arrangement of China's fiscal system. In particular, the 1994 fiscal reform redefines major features of the existing fiscal system in three ways.
3. First, it created a level playing field with a more unified tax schedule. Second, the state capacity to collect taxes has been significantly enhanced by the newly established centralized taxation agency. Third, the new tax assignment and sharing system gives local governments tremendous incentives to maximize local government tax revenue by promoting local economic development.
4. Since then, several minor reforms have been implemented to further overhaul the tax system. As a result, tax revenue grew considerably faster than the overall economy, with its ratio to GDP rising from less than 10% in 1996 to around 19% in 2011.
5. Other components of government's revenue also contributed significantly to the recent surge in government revenue, including especially non-tax budgetary revenues, social security contributions, and land transfers revenues.
6. Government revenue in China is likely to rise further even with relatively slower GDP growth. This is because the tax base is likely to be further broadened and the state capacity in tax collection is to be further improved. In addition, government incentives at central and local levels to raise revenue remain strong.

7. However, total revenue is unlikely to continue to outpace economic growth. With slower economic growth, tax revenue may not grow as quickly as in the past. Moreover, growth potential for various non-tax budgetary revenues, such as that from land transfers may be limited.
8. Meanwhile, growth in other areas seems more promising. Social security contribution will likely continue to outpace economic growth given expanding coverage and welfare benefits of the social security system. New taxes may be introduced, such as inheritance and property tax, and tax rate increase may be implemented for certain taxes, such as resource tax.