

# The Incentive-constraint Cognitive Framework, Basic Thought, Principles and Recommendations for the Optimization of Income Distribution

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**Abstract:** Income distribution is a major and complex issue that directly affects the vital interests of hundreds of millions of people. To deepen the reform of the income distribution system, it is necessary to clarify the accurate connotation of the relationship between “fairness and efficiency” under the framework of “incentive-constraint”, make a correct analysis on the causes of income differences, and lay a foundation for understanding the rationality of the policy. The basic idea of optimizing income distribution in China should be to use the vision of common prosperity as the “goal-orientation” and combine the “problem-orientation” to accelerate the strategic transformation from “getting rich first” to “getting rich together”. The basic principles to be followed are the following: encourages entrepreneurial innovation with reasonable income distribution; recognizes the contribution of each factor and combines the distribution according to work with the distribution according to other factors; and appropriately allows and tolerates the expansion of the income gap in the first half of the “inverted U curve”, that is, actively adjusts and holds “polarization”; builds a system-engineered distribution system with promoting transparency, encouraging enthusiasm, promoting harmony and helping the weak as essentials; promotes the dynamic optimization of the distribution system and policy system with reform, namely effective institutional supply as the leader. On this basis, establish a system of initial distribution of national income with sound rules and fair process; establish a system of national income redistribution with appropriately equalized results; improve the third distribution system of national income; and promotes the reform of the supporting system for national income distribution.

**Keywords:** Income Distribution, Incentive-constraint, Common Prosperity, Prior Prosperity and Common Prosperity

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## 1. Introduction

The problem of income distribution is a major and complex social problem, which is influenced by many factors and is the root of many social problems. Since the reform and opening up, the reform of income distribution system has been gradually promoted in China. The distribution system framework with labor distribution as the main body and multiple distribution methods coexisting has been basically established. The framework of redistribution adjustment mechanism with taxation, social security and transfer payment as the main means has taken shape basically, which coordinated and promoted the establishment of a socialist

market economic system, the development of the national economy and the improvement of the people's living standards. Meanwhile, we must also see that there are still many outstanding problems in the field of income distribution. The urban-rural development gap and the income distribution gap of the residents are still large. The income distribution order is not standardized. The problems of recessive (gray) income and illegal (black) income are prominent. Some of the bottom-level people's lives are very difficult. It is very difficult to carry out a series of rationalization reforms related to the macro-income distribution pattern. The progress of the reforms is slow. These problems are related to the “prominent contradictions” of the economic and social transition and the

overall development of China. It is urgent for us to strengthen the study on deepening the reform of the income distribution system.

The report of the Eighteenth National Congress of the Communist Party of China pointed out that “to ensure that the people share in the fruits of development, we must deepen reform of the income distribution system”. The report of the Nineteenth National Congress of the Communist Party of China further pointed out that “we will work to see that individual incomes grow in step with economic development, and pay rises in tandem with increases in labor productivity.” It can be seen that the issue of income distribution has become a major and fundamental link that can solve the issues of interests that the people care most and improve the material, cultural and living level of the people. It is the spiritual essence of Xi Jinping’s thought on socialism with Chinese characteristics for a new era that adhere to take the people as the center, and take the people’s yearning for a better life as the goal of struggle so as to ensure that all people have more sense of gaining in the development of joint development and sharing, and constantly promote the all-round development of the person and the common prosperity of all people. It is embodied in the basic strategy of adhering to develop socialism with Chinese characteristics in the new era, and it is also the key to crack down on the unbalanced and inadequate development. To solve the problem of income distribution, we need to grasp the policy rationality of optimizing income distribution under the cognitive framework of incentive-constraint, and clarify the basic idea of pursuing the vision of common prosperity and transforming from “prior prosperity” to “common prosperity”. Follow the basic principles of recognizing the contribution of various factors, and combining the distribution according to work with the distribution according to other factors. Take the reform as the lead, namely the effective institutional supply, to promote the dynamic optimization of the primary distribution, redistribution, the third distribution and its supporting policy design and policy system.

## 2. The Incentive-constraint Cognitive Framework for Income Distribution

The “incentive-constraint” related to the income distribution is essentially to deal with the close relationship between “making the cake bigger” and “cutting the cake well”, which is the main and interactive unity of opposites in social reproduction.

### 2.1. The Concept of “Fairness” and the Relationship Between “Fairness and Efficiency” Need to Be Clarified Urgently

The discussion on “fairness and efficiency” has been lasted for long in the academic world, and the practical issues its involved are very important, which have attracted more and more attention in China in recent years. Many researchers have pointed out that the relationship between fairness and

efficiency is not all the opposite, but conditional and mutual. This is very important and needs further detailed analysis. Referring to the issues of fairness, people often translate them according to the context of English. From the perspective of carefulness and rigorousness, we think that the connotation of “fairness” in Chinese should be split to two words, namely fairness and equality, which can express the original meaning more accurately. For example, nowadays, people are becoming more and more aware of the division of fairness in rules, fairness in process and fairness in results. The fairness in rules and in process are the meaning of English “fairness”, which emphasizes the “fairness” of Chinese. These two kinds of fairness have no contradiction with efficiency, and can protect and promote the efficiency. It mainly refers to the fair treatment and handling, so that everyone can play their respective comparative advantages and enjoy a fair environment during the process of development. However, the fairness of the results mainly refers to the meaning of “equity” in English. Actually, it refers to the equalized results. This kind of equality does have a certain opposite relationship with efficiency. If it is too average, the incentive is insufficient and the efficiency is affected. If there is huge gap in the income distribution, then the difficulties and dissatisfaction of the weak and low-income group may bring about prominent contradictions and harm the social harmony and stability. Therefore, the regulators need to make reasonable trade-offs. Regrettably, when people discuss the issue of fairness, they often confuse these two concepts and completely “consider the two concepts as the same”. Following, it comes the problems of “fudge and mudge”, which does not help to clear the problem. It is necessary to clarify the meaning of “fairness” in different scenarios, namely the “fairness” in rules or the appropriate “equality” in the distribution results. This is necessary for the correct and in-depth discussion of the issue so as to avoid “the dialogue of the deaf” and “the comparison of different things”. The contradictions in income distribution have become prominent in recent years. When referring to this, people tend to be impassioned and enthusiastically debated. However, they generally confuse the two propositions that can be clearly distinguished in English, which brings about the confusion in the meaning of the same concept and leads to confusion in “fairness and efficiency” in the context of Chinese [1].

### 2.2. The Responsibility of the Government in “Fairness” and “Equalization” Should Be Clarified and Rationalized in the Environment of Market Economy

From the perspective of fairness in the starting point and fairness in the process (aiming to be fair), the responsibility of the government is to formulate and maintain necessary and reasonable legal systems and rules to protect legal property rights and fair and competitive environment (providing a starting line). From the perspective of the fair results (aiming to be equal), the role of the government should be more reflected in the suppression and mitigation of income gap through redistribution. The “results” of the previous period are the “starting points” of the following period. Thus, another

responsibility of the government is to strive to develop and realize the “equalization” of basic public goods and public services. The essence of this issue is that the government should “guarantee” the minimum level of basic supply, that is, provide public goods and services, such as popularizing compulsory education, implementing social relief and providing basic social security. At the same time, this should not be understood as that the government can and should be offside and reduce the difference formed necessarily during and after fair competition to be flat. It is necessary to clearly form the essentials for the boundary of government responsibilities and “policy rationality”, and promote the rational optimization and adjustment of policies to facilitate the relief of social contradictions and the sustained release of the multi-subjective vitality, and to guarantee and support the sustainable development of modernization.

For example, in terms of the public supply of “housing”, the government should first guarantee the public rental housing instead of “economically affordable housing” (there is no clear distinction between the low-rent housing and the public rental housing, thus both of them are called as public rental housing). The occupants are not entitled to property rights. The government identifies the lowest income class in the society and allows them to “stay and live”. This is a kind of “public goods” that is related with the stability of the whole society. Meanwhile, the government will have a relatively high management cost for doing this. Thus, it is necessary for the government to recognize among the public who is eligible for such public rental housing. After people live in, the government should follow up and observe. If the income of the family staying in the house rises to a certain extent in the future, they should be advised to move out and free up resources to solve the “housing” problem of the real low-income class. This kind of management costs must be paid because this is the thing that the government must do, and it is related to the stability of the whole society. However, if we continue to improve according to this logic, the supply of “economically affordable housing” (which has expanded to more than a dozen specific forms in real life), which is provided in the same way, will be very popular. Thus, a lot of distortions have occurred in reality. Many people with higher incomes take the chance to exploit the “loopholes” of various system and policies. A large number of unqualified higher income earners can buy such houses, which actually squeeze out the corresponding opportunities of the social members at lower levels and unduly occupy the valuable public resources that were originally expected to perform their government functions. Therefore, although we start from the idea of pursuing fairness and justice, yet the results are ridiculous, which make the various “economically affordable houses” become a matter of “being unable to manage and unable to manage well”. The government makes the money that should be provided to those in need turn to “the sweet icing on the cake” and various forms of rent-seeking and speculation. The previous good motivation does not bring good results.

### ***2.3. Grasp the Policy Rationality: It Is Necessary to Use the Correct Analysis on the Causes as the Philosophical Premise of Policy Design***

The fairness of the results (“equalization”) has a certain negative correlation with the efficiency. In the period of “prominent contradiction” in China, properly handling the balance between “equalization” and efficiency is complex and difficult, which is a matter of great concern to all parties and also one of the core issues in grasping the government’s policy rationality in redistribution. Undoubtedly, the government is involved in the redistribution of income with necessary adjustment, regulation and normative means. It is the responsibility of the government to suppress the disparity in the income gap, prevent the solidification of “polarization” and promote its convergence. The government should make an correct analysis on the causes of income gap, and then implement the targeted policies and coordinated, combined and supporting programs. Briefly, encourage the income difference that should be encouraged; tolerate the legitimate income difference as much as possible; regulate and suppress the irregular income difference; and eliminate the improper income difference. Thus, it is beneficial to balance the equalization and efficiency. This kind of understanding comes from the specific analysis on the difference in income of residents.

Specifically, the reasons for the widening income gap of social members since China’s reform and opening up include the following seven levels or seven aspects.

The first is the difference in income that results from the difference in effort and hard work in honest labor. In the traditional system of egalitarianism, there is no difference between doing good or doing bad. It is the mechanism and system for raising lazy people. The income difference is small, but the productivity is not liberated. It is deeply hated by people of insight. After the reform and opening up, the overall degree of “diligence” has improved, but the relative differences between “diligent” people and “lazy people” still exist. The new system and mechanism have significantly widened the income gap between “lazy people” and “diligent people”. This kind of difference in income, which results from different levels of effort and hard work or being an important component of income differences, will inevitably occur in social life.

The second is the difference in income that results from the different endowments and abilities of each individual. There must be certain differences in endowment and ingenuity between members of the society. Under the competitive environment developed after the reform and opening up, the innate talents and the ingenuity developed in the following days based on other reasons combine to form different capabilities and abilities of each person. This kind of objective difference will inevitably lead to differences in the income level of each individual. Some special and scarce abilities and talents, such as entrepreneurial talents, innovative talents of scientific and technical personnel, and special skills of stylistic stars, etc., once they are embodied in competitiveness

in the market, the relevant income difference will be expanded, which will be higher than the income difference brought by “the degree in efforts” for many times.

The third is the income difference that results from the different conditions and level of the possession of the elements [2]. Due to various objective reasons (such as inheritance), each specific member of society must be different in terms of funds, real estate, and even family associations, social connections, etc. (all of which can be attributed to the broad category of “production factors”). The resulting income (such as interest, rent, and important information in business activities, the benefits gained from correct guidance and persuasion, etc.) are different, but also objective, and may form a certain inheritance and “self-superimposition”.

The fourth is the difference in income that results from different opportunities. The typical situation is that the market situation always changes. Different people do the same thing, but they may have different results purely due to different time points (of course, in actual life, there may be other possible differences). “Good luck” may be as good as getting rich overnight, the “bad luck” may be as bad as losing all the capital invested. The factors of opportunity are also undeniable, which may be very obvious in some occasions of the market economy.

The fifth is the difference in income that stems from the “transparent rules” of current system and mechanism. Some monopolistic factors and institutional arrangements caused by the system can strongly influence the income level of social members in real life. For example, the income of employees in general monopoly industries is significantly higher than that of the employees in non-monopoly industries [3]. The income level of public officials has a great relationship with his specific position in organizational arrangements (for example, the income of a certain director in the bureau of finance may increase dozen times when raised by the organization to be the president in local bank and then fall dozen times when transferred back to the original position. “I will be rich when the organization makes me rich, and vice versa, I will be poor when the organization makes me poor”.)

The sixth is the difference in income coming from the “hidden rules” that have actually been formed in the current system and mechanism without being pursued or temporarily being not pursued. This is roughly equivalent to the so-called “gray income”, which is existed in reality, not transparent and assigned according to “implicit” or “inner” manner instead of the normative channels. For example, a large part of the “extra income” of public officials in the past few years, before becoming transparent and standardized through “clearing the under-covered accounts”, can be attributed to this kind of income, which often varies significantly due to different conditions and different departments. In the context of unclear regulations or lax supervision in the enterprise, the difference in the income distribution of employees may be significant due to the difference in “making use of loopholes”.

The seventh is the income difference that stems from illegal behavior and corrupt behavior. This is roughly equivalent to so-called “illegal income”, which is often huge and linked to

illegal tax evasion, power trading, bribery, smuggling and drug trafficking.

The reasons for the difference in income distribution stemming from the above-mentioned multiple angles and different levels cannot be generalized because it is impossible to tell the roles of various factors in a specific case in real life. From the principle of policy rationality, we should first clarify the orientation of different targeted policies corresponding to each income source at the philosophical level.

In rough, it is summarized as follows.

1. For getting rich through diligent work (the first and second reasons mentioned above), the policy should strongly encourage or focus on encouragement.
2. For the difference in income stemming from factors possession and opportunity (the third and fourth reasons mentioned above), the policy should properly regulate, but should not smooth out [4] (otherwise, the factor outflow under open conditions will be very serious, and the pioneering and adventurous spirits objectively required by the market economy will also be greatly suppressed) [5].
3. For the difference in income caused by transparent institutional rules, incomplete hidden rules, and irrationality (the fifth and sixth reasons mentioned above), while clearly regulating and suppressing, the key is to promote the deepening reform and institutional transformation through policy and system construction (including “buying mechanism with money”), seek the rationalization and standardization of the system and take necessary measures to adjust the income redistribution (pure regulation without system construction will inevitably result in the “law not governing the public” or “trying to stop water from boiling by scooping it up and pouring it back”).
4. For the “illegal income” (the seventh reason mentioned above) that violates the law and regulation, the government must resolutely forbid, punish and strike the behavior, punish the income, and focus on strengthening the rule of law and system construction from the source to prevent the occurrence of violations and corruption.

Through the analysis on the policy rationality from the perspective of the above-mentioned philosophy, we obtain relevant ideas and countermeasures, have the correct general direction and targeted essentials, and then make specific policy design (including policy tool selection, policy combination, efficient implementation methods and procedures and grasping of the strength of policies at different stages). Thus, we can implement the policy rationality that the government should have in the redistribution of income, correctly grasp the balance between equalization and efficiency, and play the functions that the policy should have. It should be said that this is a rather complicated and arduous task, and also a systematic project that should be gradually optimized from coarse to fine in the “supply-side structural reform” [6].

### 3. Basic Thought: The Vision and Its Path to Realize “Prior Prosperity and Common Prosperity”

Based on the cognition of the laws governing the development of human society, Marxism proposes that the future society should be a “combination of free people” supported by highly developed productivity. The free development of each individual should be a prerequisite for the free development of all people (*the Announcement of Communist Party*). It goes without saying that the state matching with this pursuit must be the state of distribution of “common wealth” (“Each person does his best and then distribute according to his needs.”). The ideal vision of this common prosperity under scientific socialism has been clearly expressed by Deng Xiaoping as the strategic goal striving for modernization as well as “the essence of socialism” in the great practice of “socialism with Chinese characteristics” after China’s reform and opening up in the primary stage of socialism. Deng Xiaoping highly summarized his understanding of “common prosperity” in a simple way, which was consistent with both the thoughts on “great harmony” in ancient China and the current yearning for the good life of hundreds of millions of people. It is both the general outline representing the development of human civilization and the improvement of social progress and the “target orientation” for optimizing the income distribution in China in the future [7].

#### 3.1. The Distribution Mechanism of “Giving Priority to Efficiency with due Consideration to Fairness” and the Establishment of the Strategy of “Prior Prosperity”

At the beginning of reform and opening up, China’s economic development level is still quite backward, social productivity is extremely low, and basic social contradictions, that is, the contradiction between the people’s growing material and cultural life needs and backward social productivity, is prominent. In order to get rid of poverty and backwardness as soon as possible, China has formulated a development strategy centered on economic growth in a timely manner, and determined the distribution mechanism and principle of “giving priority to efficiency with due consideration to fairness”. The development of the economy is the top priority. Encourage some people get rich first and then lead the others to get rich, achieving common prosperity finally.

At the beginning of reform and opening up, Deng Xiaoping pointed out that under the goal of common prosperity, some regions and some people can be encouraged to get rich first through honest labor and legal management [7]. In 1984, the Third Plenary Session of the 12<sup>th</sup> Central Committee proposed that “common prosperity is by no means equal to or impossible to be completely equal. It does not mean that it is possible for all members of society to become rich at the same speed at the same time... Only part of the area, some enterprises and some people are allowed and encouraged to get rich first through hard work, can they have a strong

attraction and encouragement to most people and drive more and more people to become rich one after another” [8]. In 1992, Deng Xiaoping once again stressed in his talks in the South that “taking the socialist road is to gradually achieve common prosperity” [7]. The Eighteenth National Congress of the Communist Party of China also proposed that “making use of various regulation means including the market to encourage the advanced and promote efficiency so as to reasonably enlarge the income gap, prevent polarization and gradually achieve common prosperity.” In 1987, the Thirteenth National Congress of the Communist Party of China proposed to allow legal non-labor income to reflect social equity and other ideas on the premise of promoting efficiency. In 1993, the Third Plenary Session of the Fourteenth CPC Central Committee proposed that the distribution of personal income should “emphasize the principle of giving priority to efficiency with due consideration to fairness”. In 1997, the Fifteenth National Congress of the Communist Party of China reaffirmed this principle [8].

The allocation mechanism of “giving priority to efficiency with due consideration to fairness” has effectively stimulated economic growth because of its advocacy of efficiency. The country’s economic strength has been significantly enhanced and the people’s living standards have been significantly improved. From 1979 to 2006, the GDP grew from 362.41 billion yuan to 20,940.7 billion yuan, with an average annual growth rate of 9.66%, while the world average GDP growth rate was only between 3% and 4%. In recent years, due to the impact of the international financial crisis, although China’s economic growth rate has declined somewhat, it is still far above the world average. At the same time, with the rapid development of the national economy, the issue of social equity with the imbalance of income distribution as the core is also intensifying. The contradiction between economic growth and social equity has become increasingly fierce and has become a major issue and prominent contradiction that cannot be ignored in the economic and social development currently [9]. In 2002, the World Bank pointed out: “The large-scale poverty reduction is one of the greatest achievements of China after the 1979 reform.... The deepening reforms since then have not benefited the poor as before. Without solving the distortions in other domestic markets, carrying out these forms has widen the income gap in China.”

#### 3.2. Accelerate the Strategic Shift from “Prior Prosperity” to “Common Prosperity” in the Next Stage

In the early stage of reform and opening up, in response to the characteristics of national conditions with low social productivity and relatively backward economic and social development level, China has formulated a strategy of “priority prosperity” with economic growth as the core and encouraging some people to get rich first. Facts have proved that this decision is the right choice. Thus, China got rid of poverty and backwardness as soon as possible. Of course, this unbalanced development strategy also has a price. With the development of the economy and society, the negative consequences represented by the expansion of the income gap

have become increasingly prominent. Different levels of harm have already occurred. The phased transition of the economic development strategy from “prior prosperity” to “common prosperity” is becoming more and more urgent, and the timing and conditions for transition have matured. On one hand, the economic achievements since the reform and opening up have created necessary material basis for regulating income distribution and building a harmonious society. The basic economic system in which public ownership is the main body and diverse forms of ownership economy develops side by side provides a strong institutional foundation for this. On the other hand, it is urgent to narrow the gap between the rich and the poor and avoid the objective requirements of the middle income trap. This indicates that the time for China’s development strategy to shift from “prior prosperity” to “community prosperity” has matured, with both necessary material conditions and strong practical urgency [10].

Choosing the right time to shift the focus of economic work from “prior prosperity” to “community prosperity” is an established development strategy established at the beginning of the reform, and an inevitable requirement for socialist common prosperity. According to the enlightenment of the laws and experiences of economic development in various countries in the world, and in view of the increasing negative impacts and various hazards brought by the excessive income gap, under the direction of “problem-orientation”, China has now ushered in an overall opportunity to transit from “prior prosperity” to “community prosperity”, especially based on the achievements of the western development strategy, the rural tax and fee reform, the revitalization of the Northeast and the rise of the central region since the end of the last century. The gap between the living and income levels of urban and rural residents has gradually narrowed in recent years, laying a solid foundation for the implementation of the common prosperity development strategy. In the next stage, China should be guided by the spirits of the Nineteenth National Congress of the Communist Party of China, target at the main social contradictions between the growing needs of the people for a better life and the development of unbalanced development, combine the “problem-orientation” with “target-orientation”, and formally establish the develop strategy of “those getting rich first to lead the others to finally achieve common prosperity” as one of the priorities in the future economic development, and continue to promote the reform of the income distribution system. Thus, the whole society will be more concentrated in the realization of the fundamental goal of socialism, namely, common prosperity.

#### **4. Basic Principle for Pursing the Vision and Realization of “Prior Prosperity and Common Prosperity”**

Some people and some regions get rich first, although there are demonstration effects and radiation effects that may drive

other people and other regions to seek wealth, but they will inevitably result in the uneasiness and dissatisfaction of social members of lower incomes with the widening income gap and accumulated social contradictions in a certain stage. If this contradiction is not properly handled, it will inevitably restrict the healthy development of the economy and society, and even result in adverse consequences of social and political events brought by economic problems in the field of income distribution. In his discourse on “prior prosperity and common prosperity”, Deng Xiaoping has keenly and forward-lookingly emphasized to prevent and overcome the “inevitable occurrence” of the polarization problem [7]. The framework of “prior prosperity and common prosperity” contains and relates to a lot of basic principles that we should correctly grasp in the field of national income distribution [11-23].

##### ***4.1. Encouraging Entrepreneurial Innovation with Reasonable Income Distribution***

The vitality of economic development triggered by entrepreneurial innovation is the social productivity that fundamentally determines the development and upgrading of social development and production relations. “Development is the last word.” which requires income distribution to handle from the perspective of facilitating the development of productive forces the institutional functions of encouraging to “make a big cake” and “innovative development”. This principle deals with the fundamental developmental dynamics from the historical materialism principle of “production deciding distribution”. In general, the people’s income can only achieve simultaneous growth on the basis of economic growth, and workers’ compensation can only be achieved on the basis of improved labor productivity. Otherwise, the beautiful distribution vision will also become water without a source and a tree without a root.

##### ***4.2. Recognizing the Contribution of Each Factor and Combining the Distribution According to Labor with the Distribution According to Other Factors***

During the operation of the socialist market economy in the primary stage of socialism, it is necessary to deal with the construction of the mechanism of “distribution according to labor”. Meanwhile, it is also necessary to deal with the construction of the mechanism of distribution according to contributing factors such as capital, land and technological achievements, etc. so as to facilitate the liberation of productive forces and sustainable development. This principle mainly deals with the problem of “dividing a cake well” in the initial distribution process so as to continuously encourage to “make a big cake” [14]. For the initial distribution, more emphasis should be placed on the fairness of the rules in the market competition and the fairness of the process.

##### ***4.3. While Allow and Tolerate the Widening of Income Gap in the First Half of the “Inverted U Curve”, Necessary to Actively Impose Regulations to Curb “Polarization”***

The process shown in the inverted U-curve is that the

income gap is widened to the top and then begin to shrink, which should not be considered as and may not be a purely natural process [15]. The social welfare policies, taxation and social security systems formed by developed economies all reflect the plasticity space and active space of institutional mechanism design. In the socialist China, which clearly pursues common prosperity, this plasticity is worthy of being actively referenced and further emphasized and strengthened [16]. This principle is mainly dealt with in the field of redistribution and third distribution, and has formed a corrective effect on the long-term strength of capital revealed by the Piketty Institute to further “divide the cake well” to serve the problems of continuously “making a big cake” and harmonious development [12]. In the field of redistribution and third distribution, more emphasis should be placed on the appropriate leveling adjustment of the outcome of market competition, and the “fairness of the starting point” for related subjects in the next round.

#### ***4.4. Building a Distribution System with Promoting Transparency, Encouraging Enthusiasm, Promoting Harmony and Helping the Weak as Essentials***

Different levels and different links of the distribution system may focus on different distribution functions, but the general principle is to systematically coordinate and supplement all the distribution functions to form a virtuous cycle between “making a big cake” and “cutting the cake well”.

#### ***4.5. Promotes the Dynamic Optimization of the Distribution System and Policy System with Reform, Namely Effective Institutional Supply as the Leader***

Development must be characterized as staged. Institutional arrangements and policy design need to adapt to the objective phased transitions and make dynamic optimization. This principle mainly deals with the difficulties encountered in the reform of the establishment of long-term mechanism framework and the phased dynamic optimization during the process of interactive cycle development between making the cake and cutting the cake. In China, which is now in the deep water zone of the reform, this principle will inevitably need to deal with a series of tough problems such as optimizing the direct taxation, improving the social security and intergovernmental transfer payment system.

## **5. Main Suggestions for Optimizing Income Distribution Based on Thoughts and Principles**

### ***5.1. Establishing a System of Initial Distribution of National Income with Fair Rules and Process Equity***

The initial distribution is the distribution of national income, which is directly related to the factors of production. It is based on the efficiency of each production factor in production, that is, the “efficiency principle”. Under the relevant

institutional framework, the wealth is distributed in the form of labor compensation and production tax to the residential sector and government departments. Therefore, the government department can adjust and regulate through tax leverage and laws and regulations so as to play the central role of the market mechanism at this stage. Since the initial distribution is the primary link of national income distribution, the outstanding problems it needs to solve are mainly the distribution of the interests of the owners of money capital and the owners of human capital. The amount is large and involves a wide range. If there is any major social injustice in this link, it is difficult to reverse in the redistribution of the government; if the source of the income of the residents is fully motivated and the income gap is properly controlled in this link, then the income gap will be controlled better and the redistribution will reduce the regulation pressure of the government. Thus, it will enable the government to better improve the income distribution system of the residents through fiscal and taxation means. Therefore, how to establish a distribution system with fair rules and processes in the initial distribution is crucial. The so-called fair rules and processes mainly means that the initial provisions of the rights structure of the whole society are just and reasonable, and various resources have as much liquidity as possible between regions, departments, enterprises, groups and individuals rather than being highly concentrated in certain regions, departments, businesses, groups or individuals. Opportunities are generally open to all regions, sectors, companies, groups and individuals, rather than open to certain competitors, but blocking to some competitors.

#### ***5.1.1. Give Full Play to the Role of the Factor Market in Resource Allocation***

Since the market mechanism should be the core in the initial distribution, establishing a market that is fair, open, transparent and orderly is the key to determine whether the income distribution mechanism can be operated in a healthy manner at this stage. This requires the provision of a legalized market operating environment to stabilize market expectations, clear up the obstacles of hidden rules, establish reasonable market access standards, prohibit the establishment of unreasonable and discriminatory access and exit conditions, and rationally determine the contribution of various factors. Establish a market-based fair employment system and a flexible and orderly wage growth mechanism; improve the planning and allocation level and efficiency of real estate and resources in land development; promote the enterprises to achieve effective capital accumulation and improve labor productivity; rationalize the relationship between labor income and property income; give full play to the basic role of factor market resource allocation in income distribution.

#### ***5.1.2. Enable the Market Play a Decisive Role in Resource Allocation and Better Play the Role of the Government***

In the initial stage of income distribution, it is necessary to clarify the role boundary between the government and the market, reduce the government’s intervention in the basic resource allocation mechanism, and reduce and strive to eliminate rent-seeking income opportunities. The government

mainly establishes a unified and clear-cut factor market in accordance with the law, allows the market to play a decisive role in resource allocation, eliminates institutional barriers, reduces the institutional transaction costs of the market participants, and effectively conducts market supervision to ensure the fair and orderly operation of the market. Guide all entities and departments to reasonably expect the growth of traffic revenue and stock assets. Meanwhile, the government should actively encourage and guide the enterprises to form harmonious labor-management relations and improve their competitiveness and operational efficiency.

### ***5.1.3. Promote Fairness and Equal Opportunity in Distribution Rules***

In the initial distribution, China has problems such as unfair distribution rules and unequal opportunities. To this end, we should increase the intensity of the reform of the urban and rural household registration system, improve the labor market system, reduce the barriers to income distribution between urban and rural areas and also industries and regions, promote the realization of “equal pay for equal work”, and gradually eliminate the institutional barriers to urban and rural labor market and labor transfer. We will improve the regulatory role of the labor market, appropriately intervene in the labor force with appropriate minimum wage system, and rationally guide labor negotiations to provide a good competitive platform for urban and rural labor [17]. At the same time, vigorously develop and improve various factor markets, promote free flow and fair competition of the capital, technology and other production factors, and improve the efficiency of market allocation. Break the restrictions on the free flow of factors in departments and regions, and alleviate the unfair distribution of income.

### ***5.1.4. Strengthen the Reform of the Income in Monopoly Industry***

First of all, it is necessary to promote the realization of equilibrium market prices, suppress or eliminate monopoly prices, so that individual departments, individual industries and individual enterprises can not obtain monopoly profits, and cannot obtain the abnormally high income generated by high monopoly profits. Secondly, it is necessary to promote the construction of a society ruled by law, prevent illegal income and unreasonable income of market entities, greatly reduce illegal income and gray income, and eliminate the income generated by monopoly of power. Finally, eliminate artificial entry barriers, reduce market entry barriers, provide fair market competition opportunities for market players, and create necessary prerequisites for achieving fair income distribution. The state should adopt anti-monopoly measures to eliminate monopolistic factors, so that all industries participate in the process of profit averaging, making the industry's profit rate approaching the social average profit rate.

### ***5.1.5. Enhance the Ability of Members of Society to Participate in Social Competition Through Equalization of Basic Public Services***

Members of society have equal rights in the cultivation and acquisition of abilities, which will have a

pre-rationalized adjustment effect on the income distribution of the whole society. “The efforts to promote the fair conduct of economic - political competitions are much more important in advance than afterwards.” [11] To be specific, the government is required to further strengthen the universality and fairness of the system and policies, actively promote the equalization of basic public services such as employment, education, medical care and social security, etc., and generally promote the social members, especially the vulnerable group, to participate in social competition by popularizing basic public services. In particular, vigorously developing education is the most important and effective way to equally stimulate individual potential and promote substantive equity. By equally and generally providing education to all social classes, members of the general public can acquire the basic ability and quality of equal access to society and competition. Ensuring the fairness of sharing the educational resources by the whole society can open up channels for all sectors of society, especially the vulnerable groups, to change their own destiny and obtain the opportunities for a fair, rational and open upward mobility. In this sense, creating equal opportunities for education and conditions for every member of society is one of the inherent requirements of the fairness in starting point.

### ***5.2. Establishing and Improving a National Income Redistribution System with Appropriately Equalized Results***

It is generally believed that in the two distribution levels of national income, initial distribution tends to be efficient, and income distribution difference is both the source and motivation of market efficiency and the results of market efficiency. However, if the results of income distribution are too large, it will be against social equity and social and long-term interests. Therefore, the government should effectively adjust the national income redistribution through taxation and fiscal expenditures, etc. to promote the vision of common prosperity. The initial distribution focuses on the fairness and justice of the rules and processes, while the redistribution focuses on the results and the fairness and equalization of the next round of starting points.

#### ***5.2.1. Implement the Statutory Principle of Taxation, Give Play to Its Income Distribution Adjustment Function and Achieve “Good Law and Good Governance”***

- 1) Develop good law in statute taxation and promote good governance to ensure the effectiveness of income regulation

Income distribution is linked through production and consumption economically and connected with the subject and interests legally. It is undeniable that the fiscal and taxation issue is first and foremost an economic issue, which cannot avoid the most basic need as human beings, namely the acquisition and use of wealth. Only by establishing the standards of justice to guarantee the order of distribution, can we ensure the stability and harmony of a community. The Third Plenary Session of the Eighteenth CPC Central



Committee clearly put forward to “implement the statutory principle of taxation”, which is an important strategic arrangement for promoting the modernization of the national governance system and governance capacity and comprehensively promoting the rule by law.

Developing good law is not only a legislative technical issue, but more importantly, is to clarify the overall thought of the taxation system reform. It requires systematic thinking. It cannot be divided into individual taxes or substantive laws and procedural laws for consideration. It is necessary to prevent the fragmentation of tax legislation and establish a taxation system that is conducive to scientific development, social equity and market unification. First of all, we must consider the reform of the taxation system in the context of the new normal of economic society, and give better play to the role of the taxation function and serve the economic and social development. Secondly, the taxation system should have a holistic and long-term vision, clarify the overall framework of the taxation system, do a good job of top-level design, coordinate the tax collection of income, regulate economic operations and regulate income distribution. On this basis, it is also necessary to clarify how the various taxes and tax items are matched, how the elements of the tax system are combined and matched, and how to implement them. Thirdly, establish a scientific and rational incentive assessment mechanism to guide the tax authorities to change the thinking of taxation according to indicators or tasks, and use taxation law as the sole basis for taxation. Meanwhile, it is necessary to establish and improve the supervision and accountability mechanism for tax enforcement, and effectively protect taxpayers’ access to relief, especially the right to judicial relief.

## 2) Gradually increase the proportion of direct taxation and form a taxation system that is conducive to structural optimization and social equity

The taxation system required by the modern market economy is generally a compound taxation system of “multiple tax categories, multiple links and multiple tax collection”. It is impossible to solve the taxation problem simply by relying on one or two kinds of taxes. The government must focus on the construction of the whole taxation system and regulates the income of the high-income class from consumption expenditure, income flow and income stock in order to alleviate and narrow the income gap through multiple channels. These taxes complement and coordinate each other in terms of adjustment scope, adjustment intensity and breadth, thus forming a continuous and overall coordination of taxation adjustment mechanisms. In the compound taxation system, the role of direct tax is more reflected in regulating income distribution and regulating economic and social life while raising government revenue. The regulation of direct tax is based on the principle of ability to pay, that is, “taking from those who have much and give to those who have little”. In the case of inevitably high and low incomes of members of society, direct taxes enable the wealthy members of society with higher ability to pay to make more contributions to public treasury. The resources that enter the public treasury are then transferred to the expenditures of

the vulnerable groups through standardized budgetary arrangements and financial allocations to enhance the welfare of low-income social members. The direct tax is based on the ability to pay to curb the polarization trend, making it an indispensable position in the whole process of social distribution.

## 3) Further improve the personal income tax system

First of all, it is necessary to change the mode of the collection of personal income tax, and implement a personal tax collection mode combining the comprehensive and classified personal income tax collection. The combination is based on household and annual collection at an excessive progressive tax rate, and a more reasonable tax rate and fee deduction standard is formulated. On the basis of the deduction standard for local fees in the unified market framework, we will adhere to the national unified personal income tax deduction standard. At the same time, due consideration shall be given to the deduction of fees for taxpayers and dependent family members. Secondly, it is necessary to reform the personal income tax collection and management system and assign the jurisdictional authority for personal income tax to the central government. As a direct tax to narrow the income gap, the personal income tax is classified into the central government not only to enhance the state’s ability to regulate and distribute, but also to meet the needs of the central government’s transfer payment. It is also necessary to prevent the deduction of the bases, the lack of strict collection and management, and the loss of taxes. Third, we must strengthen and improve the means of collecting personal income tax. Strengthen and establish a declaration system based on individual self-declaration, build a national tax network collection and management system, unify individual tax codes, and share personal tax information across the country to block collection loopholes. Increase the supervision and punishment of illegal activities such as tax evasion, and increase the cost and risk of taxpayers evading taxes.

## 4) Promote the reform of consumption tax

For the consumption tax, the taxation scope should be adjusted in time according to the changes in the economic situation. In expanding the collection scope of consumption tax, we should not only add some luxury consumer goods items, such as high-end fashion, high-end entertainment facilities, etc., but also include some high-end consumer behaviors, such as bathing saunas, night clubs, entertainment, and so on. Second, we must adjust the taxation link of consumption tax. At present, China’s consumption tax is mainly imposed in the production link, which is easy to evade taxes. For example, some enterprises have set up sales companies with independent accounting and then sell the products to sales companies at low prices, which will sell the products at normal prices to avoid consumption tax, which weakens the income adjustment effect of consumption tax.

## 5) Accelerate the legislation of real estate tax and promote the reform in a timely manner

For real estate tax, we must first expand the scope of taxation, which should include not only the operating real estate and rental properties, but also the self-occupied property.

Secondly, the tax base and the tax rate should be determined according to the value of the property and actual use. A zero tax rate or a low tax rate is applied to the housing that meets the basic needs of life, and a high tax rate is imposed on the housing exceeding the housing standard, so that high-income groups bear more tax burden while enjoying large-scale housing. The resistance should be ruled out and the guiding opinions of the Third Plenary Session of the Eighteenth Central Committee on “accelerating the legislation of real estate tax” should be implemented as soon as possible. Once the legislation is completed, it can be levied first in the first-tier and second-tier cities where house prices are rising.

#### 6) Research on inheritance and gift tax

Both inheritance and gift tax are direct taxes. The taxpayer and the tax bearer are unified, and the target of taxation is precise. It is one of the main means of social wealth redistribution. This tax directly faces the high-income class and can prevent the residents from gaining wealth through the inheritance of wealth through non-individual efforts, which is conducive to narrowing the income gap between generations. China should study how to introduce such taxes early, in order to actively play its role in regulating income distribution to curb the further expansion of the income distribution gap, and objectively encourage public welfare foundations and charities to receive more financial support. China is in a period of economic system transformation, some of the income is in a gray or illegal state, but personal income tax can only be applied to transparent income, and it is difficult to regulate the opaque income. According to the experience of various countries around the world, combined with the characteristics of various taxes, the introduction of inheritance tax can incorporate the opaque income before inheritance into tax regulation, thus effectively making up for the deficiency of personal income tax.

### 5.2.2. *Improve the “Full-covered” Government Budget System and Improve the Revenue Sharing System*

#### 1) Improve the “full-covered” government budget system to regulate government revenue

A wide variety of non-tax revenues are messed and scattered in reality, which has caused enterprises and nationals to bear the heavy pressure from this. The management and supervision of this part of the funds has huge hidden risks. In fact, it is necessary to use non-tax revenues to assist in raising financial funds and alleviating the shortage of funds in the administrative department. However, if there is disorder, weak management and weak supervision in the system, it will inevitably cause the negative effects of confusion in fee collection, and it will easily evolve into the breeding ground for rent-seeking and corruption, thus exacerbating social injustice and worsening income distribution. Therefore, it is necessary to strengthen the regulation of non-tax revenues, and prevent the excessive and disorderly expansion of non-tax revenues by inclusion of them in full-covered budgets, strict examination and approval, tracking control, and clearing powers and responsibilities. Establishing a unified and comprehensive budget is conducive to keeping the

government’s power in the cage and preventing resource mismatch and unfair income distribution caused by government actions.

#### 2) Expanding the scope of collection of state-owned capital income and increasing the proportion of profits paid

The report of the Eighteenth National Congress of the Communist Party of China clearly stated that in order to alleviate the unfair distribution of income, a reasonable sharing mechanism for the transfer of public resources will be established. As an important part of public resources, the state-owned capital has the legitimacy and inevitability of sharing its operating results by the whole people. The state-owned capital operation budget, as a fiscal system arrangement that regulates the management of state-owned capital operating income, should play its specific role of regulation and distribution. Reasonable determination of the proportion of state-owned capital income distribution should be based on the principle of “coordinating and balancing with moderate concentration”, taking into account the needs of enterprises’ own accumulation and development, state-owned economic restructuring, and macroeconomic regulation and control of the national economy. At the same time, according to the actual situation of the enterprise, the proportion of pure profits turned over to the treasury will be gradually increased, which will gradually reach the international level.

#### 3) Constructing a national sharing mechanism for state-owned enterprises to pay profits

At present, the profits turned over by state-owned enterprises in China have not yet been shared by the whole people, and more than 90% of the profits paid are cycled within the state-owned enterprises. In order to change this tendency, we should establish a complete profit-sharing mechanism, adjust the use direction of state-owned capital budget expenditures, and substantially increase the proportion of state-owned capital gains for social security and people’s livelihood, and truly realize “all assets owned by the whole people and the benefits shared by the whole people”. To this end, it is necessary to revise and improve the relevant laws and regulations, clearly stipulate the scope, method and proportion of the state-owned capital income for the people’s livelihood expenditure, so as to lay the cornerstone of the system for the national profit to invest in the people’s livelihood. Considering that China’s long-term social security funding gap is huge, when the income of state-owned assets is invested in the people’s livelihood, we should focus on the requirements of social security, and set a minimum expenditure ratio to ensure that a certain amount of funds are used for social security every year. Thus gradually solve the problem of historical debts in this field.

### 5.2.3. *Increase the Proportion of Expenditure Directly Used for People’s Livelihood and Balance the Supply of Public Goods Between Urban and Rural Areas*

#### 1) Improve the expenditure structure and increase the proportion of people’s livelihood expenditure

With the focus on safeguarding and improving people’s livelihood, we will further optimize the structure of public

finance expenditures, effectively “use good steel in the blade of the knife”, strengthen financial input, tax support and social construction in the field of people’s livelihood, and provide an increasingly complete, rich and precise social security system for the national. At the same time, in the position of equality and unbiasedness, we must also consider the special needs of different groups of people to design targeted and operational institutional content, and give special care to vulnerable groups such as migrant workers and rural five-guarantee households.

- 2) Clarify the division of powers and expenditures and balance the supply of public goods between urban and rural areas

The fiscal and taxation relationship between the central and local governments should be improved in accordance with the principle of “power of affairs corresponding with the expenditure responsibilities”, and the power of affairs and expenditure responsibilities of the central government and local governments at all levels should be reasonably defined, and gradually clarified through legal forms. Under the premise of clarifying the boundary between the government and the market, according to the thought of clear power of affairs - expenditure responsibility - dividing income - matching financial resources, we should coordinate, adjust and regulate the relationship of income and expenditure and financial allocation between the central and local governments, establish and improve the fiscal and taxation system with financial powers corresponding with power of affairs and financial resources matching with power of affairs, balances the supply of basic public goods in urban and rural areas and creates a large environment for deepening reform and harmonious development.

#### **5.2.4. Reform and Improve the Transfer Payment System to Promote the Equalization of Basic Public Services**

On the basis of rationalizing the relationship between government affairs and financial power, the transfer payment system, as a regulation mechanism for intergovernmental fiscal funds, has the special effect of balancing financial resources and is an important tool for achieving equalization of basic public services. Currently, it has become an important measure to promote the equalization of basic public services.

- 1) Optimize the transfer payment structure, increase the general transfer payments and standardize the special transfer payments

First, increase the size and proportion of general transfer payments in order to control and narrow the financial gap between local governments. Financial transfer payments, such as current wage transfer payments with specific policy objectives, should be merged into the system, and the projects that have not changed much between the years will be included in the system subsidy permanently, and the local solution will be offset. Secondly, strictly regulate the setting of special transfer payments, and clean up and integrate various subsidized projects that are provided by the central government to local government. For special transfer payments, focus on key issues, set up only on important issues

involving the national economy and people’s livelihood, cancel odd special transfer payments, and completely change the current diverse and scattered special transfer payments. Integrate and compress the existing local special transfer payments, and integrate the projects that have the same direction of use and can be integrated, and cancel or compress the expired projects, one-time projects, and projects that need not to be established according to the needs of macro regulation. Thirdly, the existing local special transfer payments shall be classified according to the classification of government revenue and expenditure, and coordinated with the preparation of departmental budgets so as to make the classification of local special transfer payments more reasonable, standardized and orderly, which is beneficial for the supervision of the people’s congress and the audit. During the implementation, the classification can be further refined to the item, and according to the needs of the project, the project funds are managed separately according to the expenditure purposes, such as the expenditure for the reform of the rural compulsory education funding guarantee mechanism. Fourth, it is not allowed to make financial support for special transfer payments for local requirements.

- 2) Improve the calculation formula and method of transfer payments

Improve the calculation formula and model of the normative general transfer payment, improve the transparency of transfer payments, and eliminate the room for bargaining. In terms of factor selection, combined with China’s current regional development conditions and balanced goals, we should focus on the main objective factors such as the sparseness of the population and the differences in the natural environment of each region, highlight ethnic areas, border areas and revolutionary old areas to maintain social stability and ethnic unity, and emphasize including the “three rural” factors and key regional assistance into the distribution formula, making it scientific and rationalized through repeated calculations. In addition, the management of transfer payments funds and special grants shall be strengthened. For the special funds suitable to be allocated by the factor method, adopt the factor method to avoid the phenomenon of sharing money according to relationship, “distributing equally the limited resources without regard to relative importance” and “obtaining funds by making use of the relationship with the department”. For those suitable for project management, strengthen the system construction, standardize the operation and form a scientific and reasonable allocation basis and system norms. For the allocation of special transfer payment funds, set clear performance targets for fund use, track and supervise the use of funds.

- 3) Exploring the establishment of a horizontal transfer payment mechanism in the form of “counter-support” with Chinese characteristics

Horizontal transfer payment is to arrange the transfer of financial funds between local governments under the established fiscal system, so as to achieve the purpose of strengthening regional support, narrowing regional gaps and balancing financial resources. Most countries in the world

implement a single vertical transfer model, that is, the fiscal transfer payment model from the central government to local governments and from higher-level governments to lower-level governments. Only a few countries such as Germany, Sweden, and Belgium, etc. implement a transfer model with both vertical and horizontal transfer payments. As far as historical path dependence is concerned, although there is no standardized transfer, formulation and legalized horizontal transfer payment system between local governments in China, “counter-support” of this nature already exists. Supporting the underdeveloped areas in the central and western regions by the developed regions in the eastern is conducive to accelerate the coordinated development between regions and improve the overall economic development level of the country, which in turn is conducive to the economic development of the eastern region. Therefore, it is possible to try and develop horizontal transfer payments such as “count-support” and “ecological compensation”, etc. while focusing on the vertical transfer payment mode.

### ***5.2.5. Improve the Social Security System and Rationally Increase the Transfer Income of the Residents***

#### ***1) Improve the social insurance system***

Adhere to universal coverage, appropriate protection, clear powers and responsibilities and efficient operation, steadily improve the social security coordination level, and establish more fair and more sustainable social security system. First, improve the social insurance system. Implement the universal participation in social insurance plan to basically cover the statutory personnel. Adhere to the actuarial balance, improve the financing mechanism, distinguish the responsibilities of the government, enterprises and individuals, etc., and appropriately reduce the social insurance premium rate. Secondly, improve the basic endowment insurance system for urban employees, which is combined with unified accounts, build a multi-level pension insurance system including occupational annuities, enterprise annuities and commercial insurance, and continue to expand the coverage. Actively realize the national pooling of basic pensions for employees, improve the personal account system for employee pension insurance, improve the incentive and constraint mechanism for participating insurance contributions, and establish a reasonable adjustment mechanism for basic pensions. Actively develop enterprise annuities, occupational annuities and commercial life insurance, and coordinately introduce tax deferred pension insurance. Better play the role of unemployment and work injury insurance, enhance the flexibility of determining the rate, and optimize the applicable scope. Third, establish a more convenient social insurance transfer and connection mechanism. Transfer some state-owned capital to enrich the social security fund, broaden the investment channels of social insurance funds, strengthen risk management, and improve the return on investment. Significantly increase the proportion of flexible employment and migrant workers to participate in social insurance.

#### ***2) Improve the social assistance system***

The social assistance system is an important part of the social security system. In the overall planning of the urban and rural social assistance system, we should improve the minimum living security system, strengthen policy linkages, promote institutional integration, and ensure the basic livelihood of the people in need. Strengthen the coordination of the social assistance system with other social security systems, special assistance and subsistence relief, etc.. Build a comprehensive rescue work pattern, enrich the contents of rescue services, rationally raise the standard of assistance, and realize “one-in-one acceptance and collaborative management” for social assistance. Establish and improve a social check-up mechanism for the family’s economic situation, and strive to help those in need and retreat those out of need. Carry out a comprehensive pilot of “helping those in emergency and in difficulty” and strengthen the construction of rescue facilities for vagrants and beggars at the grassroots level.

### ***5.3. Improve the Third Distribution System of National Income***

The third distribution system mainly refers to the charity and social assistance activities from various domestic and international social donations. Therefore, the third distribution is based on charitable donations. The source of charitable donation funds in China includes enterprises, individuals and social organizations, and the main problem in the structure of the mechanism is that the public welfare foundation is significantly underdeveloped, and the management problem is that the use and management of charitable funds are not standardized. Thus, in order to effectively make up for the shortcomings of initial distribution and redistribution in narrowing the income gap of the residents, it is necessary to further improve the mechanism of the third distribution system in the existing distribution system.

#### ***5.3.1. Strengthen the Management of the Existing Charitable Fund Management Institutions***

In recent years, negative news about improper disposal of charitable donations by staff of public organizations such as the Red Cross has raised concerns about the future of charity. Charitable donations are different from other funds. They are completely voluntary behaviors of the public. The public hopes that their love can help more people with difficulties. They hate those who misappropriate and squander charitable donations. They think it is a kind of embarrassment for their love. Therefore, the willingness to donate will be significantly reduced, and the third income distribution system will not be able to play a better role in narrowing the income gap of the residents. Therefore, it is necessary to strengthen the management of charity management institutions. First of all, in the appointment of personnel, set a standard stricter than the general appointment standard to ensure the excellent thought and quality of the staff. Second, improve the transparency of the entire process of capital revenue and expenditure, support credibility with sunshine, and ensure the supervision of the use of charitable funds. A

tracking mechanism for the use of charitable donations should be established to monitor the use of donations throughout the process, and at the same time, the use of donated funds should be publicly disclosed to the public and social supervision should be accepted. Third, strengthen the building of social charity and the construction of public welfare foundations to promote the development of charity in China. From the current situation of charitable donations in China, the scale of social donation and assistance is still relatively small. Therefore, through publicity, the public should be made aware of the significance of donations and create a harmonious society with sincerity, nobleness, love and mutual help. In addition, it is necessary to publicize the public to understand how the charitable donations are used and what projects are used for the funds, so that the donors can fully understand the use of their donations, be transparent to the public, and accept full supervision from the society. Thus, the public can be assured and they would like to voluntarily, happily and constantly donate with ease.

### **5.3.2. Improve the Taxation Policies to Encourage Enterprises, Social Organizations and Individuals to Make Active Donations**

The tax policy should consider the pre-tax deduction standard for corporate donations. It is recommended to use the progressive deduction standard, that is, the greater the amount of corporate donations, the higher the pre-tax deduction ratio, which can effectively mobilize the enthusiasm of corporate donations. For the individual donation, the deduction ratio should not be set, and the full deduction method should be adopted.

### **5.3.3. Encourage and Guide the Development of Charitable Foundations and Volunteer Organizations**

Make the charitable donations institutional, standardized and normal to avoid emergency, suddenness and transience so as to provide sustainable financial support for the third distribution. Drawing on international experience, public welfare foundations and volunteer organizations that have certain development foundations and strong willingness to develop in China should be actively developed to encourage and guide them to conduct charitable activities in a standardized and sustainable manner for a long time.

## **5.4. Promote the Reform of the Supporting System of National Income Distribution**

The reasons for the widening income gap of residents are various. Therefore, in addition to regulating the initial distribution, redistribution and the third distribution of income, it is necessary to promote the reform of the income distribution system in a targeted manner, which mainly includes the following aspects.

### **5.4.1. Actively Promote the Construction of the Income Distribution Legal System**

The problem of income distribution is largely caused by institutional defects and institutional loopholes. We should establish a relatively complete and mutually compatible

system of income distribution laws and regulations as soon as possible, and severely crack down on all kinds of illegally behaviors of seeking personal income. Strengthen law enforcement and reverse the situation of violation of the laws and slack law enforcement. At present, according to the outstanding problems in the distribution of personal income, some temporary regulations and management measures should be established first, and then the law should be gradually formed through continuous improvement. We should vigorously establish and improve the supervision mechanism of the personnel in relevant fields, make full use of the supervision power of all aspects in society, and control and restrain the spread of illegal income of society.

### **5.4.2. Reform the Current Trade Union Organization**

Trade union organizations are important defenders of the interests of employees. To narrow the income gap of residents, we can consider reforming the current trade union organizations and giving play to the functions of trade unions to truly protect the interests of employees.

- 1) Provide the trade union organization with independent status

At present, the trade union organizations of the enterprises and institutions in China do not have independent status in the unit. Their main functions are to sympathize with the employees of the unit during the holidays, organize the cultural activities of the employees to enrich the life of the employees, etc., which is far from the functions of the trade union in the modern sense. According to the new *Trade Union Law*, when enterprises and institutions violate the relevant provisions of the *Labor Law* and infringe on the rights and interests of employees, the unit trade union organization can negotiate on behalf of employees with the enterprises and institutions, thereby protecting the legitimate rights and interests of employees from infringement. However, in fact, it is still impossible to implement in China because the trade union organization is a department attached to the unit, which does not have independent power. Thus, it is impossible for them to represent the employees to negotiate with their own units. In order for the trade union to truly assume the responsibility of safeguarding the rights of workers, it is necessary to give the trade unions an independent status and give them the right to negotiate on an equal footing with the employers.

- 2) Effectively play the role of the “regulator” of trade union organizations

An important role of trade union organizations is the “regulators” of both employers and employees. The main function is to coordinate the disharmony between employers and employees. First, carry out early warning service activities, timely understand and master the employees’ ideological dynamics, psychological worries and difficulties, and give early warning information to all parties. The second is to improve the level of life assistance. After mastering the basic conditions of the employees in difficulty, it is necessary to increase the assistance to the workers who have difficulties in life, including condolences and assistance, and provide

assistance to employees who are suffering from serious illness or long-term illness, and help the children of the disabled to complete their studies, and so on. The third is to help the disabled workers to re-employ, such as the staff re-employment skills training, job introduction, self-employment guidance, and so on. The fourth is to establish a system of trade union visits, provide solutions for workers and staff who reflect problems, consult policies and seek help, resolve the difficulties and confusion of employees, and resolve conflicts between labor and capital.

#### **5.4.3. Accelerate the Reform of Investment and Financing System, Establish and Improve the Diversified Supply Mode of Basic Public Services**

##### **1) Promote the public-private partnership (PPP)**

Establish a PPP project guidance fund, standardize the PPP project operation procedures, establish and improve a reasonable investment return mechanism, encourage and guide social capital to participate in the investment and operation management of public goods and public service projects. Promote PPP model in important fields, such as rail transit, waste water treatment, energy, water conservancy, affordable housing, medical care, pension, education, culture, parking facilities, etc., and improve the supply capacity and efficiency of public goods and public services.

##### **2) Further promote and improve the government's purchase of public services**

Continue to expand the scope and scale of government procurement services. The government will not directly undertake those that can be provided by the government through purchase services. For those that can be provided by the cooperation of the government and social capital, widely attract social capital to participate. Improve relevant policies, develop and issue guidance catalogue for government purchase services, and gradually expand the scope and scale of government procurement services. Formulate government procurement service implementation plans for key public service areas, and gradually increase government procurement services in key areas such as education, social security, environmental protection, culture, municipal management and city appearance, and promote the selection of demonstration projects with large social influence, demonstration and driving, and mature market mechanism, which shall be undertaken by social forces through the purchase of services and followed up during the process of implementation. Strengthen the fund management of government procurement services, improve the efficiency of fund use and the level of public service supply. Increase the support for the cultivation of social organizations, attach importance to the development of the service industry market, and stimulate and mobilize the enthusiasm of the social forces to participate in the government's purchase of services.

#### **5.4.4. Deepen the Reform of Education and Scientific Research Management System**

Under the guidance of the problem, we must resolutely implement the guiding principles of the central government on optimizing the scientific research environment and

strengthening the incentives for intellectual factors, so as to substantially deepen the reform of education and scientific research, and cultivate innovative talents in line with the law of talent growth. Follow the law of scientific research to create institutional environment and social atmosphere for sustainable development of scientific and innovative activities. Correctly handle the relationship between human care, material encouragement, the use of funds and the restriction of academic norms.

#### **5.4.5. Explore the Establishment of an Early Warning System for Income Distribution**

First, establish a harmonious goal of income distribution, build proper measurement scale for measuring the degree of income gap, and lay the foundation for establishing an early warning mechanism for income gap. Secondly, explore the establishment of an early warning model for urban and rural income distribution, an early warning model for inter-regional income distribution, an early warning model for inter-group income distribution, and an early warning model for inter-industry income distribution. These early warning models are not completely independent. We can determine the public risk of income distribution by making use of various early warning models to evaluate the risks of the income gap so that the work department can development and implement the policies accordingly and control the risks within acceptable limits. Third, support the income distribution and regulation mechanism. The establishment of an early warning mechanism for income distribution gap can help the government to dynamically grasp the changes in various income gaps and total income gap in a timely manner. In the primary distribution, we will strengthen the top-level design of the mechanism in reforming and improving the income distribution system, and focus on establishing and improving the basic growth of employee wages and economic growth as well as effective adjustment mechanism of income distribution in different industries. In the redistribution, we will establish and improve wealth adjustment and regulation mechanism, taking from those who have much and give to those who have little. In the third distribution, the charity and public welfare undertakings are fully developed to promote the sustained and healthy development of China's economy and society.

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