

# **How a Local Growth Coalition Collapsed: A Case Study of Anti-Confiscation Movement of Private Oil Investors in a Northwestern Chinese County**

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## **Introduction**

In the last three decades, the commonly assumed 'close relationship' between China's local governments and local economic elites, particularly private entrepreneurs, has been considered the key driver of China's economic miracle (Pearson 1997; Oi 1999; Dickson 2000; 2003; 2008; Goodman 2008; Fu & Lin 2013). Most published research on government policies has been more concerned with the so-called 'collusion' or alliance between local governments and business investors (Oi 1992; Lin 1995; Walder 1995; Wank 1998; Chen & Dickson 2008). This close alliance was believed to be built upon the pursuit of a common goal – economic growth. Hence, the alliance is often called the 'local growth coalition', the thesis being particularly popular among urban development specialists (Molotch 1993; Zhu 1999; Zhang 2002; He & Wu 2005; Domhoff 2006; Hsing 2006). On the other hand, a burgeoning literature detailing conflicts between local governments and social groups, such as workers and peasants, as the local governments relentlessly pursued local economic development, has cast doubt on the 'local growth coalition' thesis. Even more questions are raised about it in the light of a growing number of conflicts between local governments and private entrepreneurs.

To most analysts, the close relationship between the local governments and the local businesses seem to be unbreakable and most entrepreneurs prefer to maintain the status quo (Dickson 2003; Tsai 2007; Walder 2009). In recent years, however, conflicts between local governments and private enterprises seem to be on the rise. In most cases, such conflicts do not turn into public political events; they are more like competitive games between political and economic elites on the economic front (Nathan 2003; Gilley 2004; Kennedy 2008; Lu 2012). But there are disputes which have turned into public events or even take on considerable political significance (Han & Lu 2011). The growing number of such conflicts indicates that the 'local growth coalitions' or 'local growth alliances' that analysts speak of may have existed only at particular times or in particular places and therefore cannot be regarded as a lasting, general feature of China's economic development. It is not just a theoretical possibility but also a fact that relationships of 'lovers' become relationships of 'enemies'. The purpose of this chapter, however, is not simply to question the 'local growth coalition' thesis but to explore the ways in which groups of dominant local elites work together and compete with each other in economic development. Of particular interest are questions about why conflicts emerge, who benefit and suffer at various

stages of conflicts, and how conflicts are eventually resolved. The focus of the chapter is placed on the entrepreneurs' strategies for protecting their rights vis-à-vis local political elites as well as the processes and mechanisms of their right protection.

The chapter centres on the case of the 'Northern Shaanxi Oilfield Event', which took place in 2003, to illustrate the critical stages and analyze mechanisms in place that turned a close collaborative relationship between the government and local business elites into one of conflict. In 2003, under the instruction of the Shaanxi provincial government, county governments in northern Shaanxi confiscated vast oil well assets run by private investors. In order to protect their rights or seek higher compensation, some of the investors engaged in a three-year legal battle with government agencies at different levels of Shaanxi Province, which attracted national and international attention. The Chinese media called it the 'Northern Shaanxi Oilfield Event'; it will be simply referred to as 'the event' in the chapter.

The chapter will be divided into three parts. The first part is descriptive and will provide a general overview of the event. The second will analyze the critical stages of the event, especially the advantages and disadvantages of major strategies implemented by the various parties. In the third and final section, some resolutions will be proposed for similar conflicts in the future.

### **Three Stages: From Alliance to Conflict, and the Current 'Compromise'**

The changing relationship between local governments and private oil investors in Shaanxi in the past two decades can be divided into three phases. The first phase (early 1990s to 2003) saw local governments in Yan'an and Yulin, two prefecture-level cities, engaged in various campaigns to attract private investments, foreign and domestic, to drill for oil. They were in a honeymoon during this period, while conflicts frequently erupted between the Changqing and Yanchang because of a 'turf war' on controlling more oil wells.<sup>1</sup> The former is a subsidiary of the China National Petroleum Corporation (CNPC) based in Northwestern China, and the latter is a state-owned enterprise (P-SOEs) under provincial government control and based in Shaanxi Province. During the second phase (2003-2006), local government agencies started to 'confiscate' the private-run oil wells. The relationship between the government and the private sector, which used to be compared to 'fish and water', became one like 'oil and water'. The private investors attempted but failed to protect their rights. The third phase (2006-2011) was characterised by the co-existence of two strong competitors, the restructured, province-run Yanchang Group and the re-organised CNPC-run Changqing Group, with a much smaller private sector struggling to survive by cooperating with the two big players. The second phase is the focal point of this chapter's analysis. The first is the background of the 'Northern Shaanxi Oilfield Event'; it traces how the 'local growth coalition' came into being and reveals the root cause of the breakup of this coalition. The third is a 'postmortem' analysis of the event that deals with the repairs of the damaged collations and the emergence of new local growth alliances.

### ***Prologue of the Event: A 'Fish-Water' Relationship***

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<sup>1</sup> The full name of Changqing and Yanchang were then Changqing Petroleum Exploration Bureau and Yanchang Oilfield Management and Administration Bureau, respectively. Both of the two names kept changing during restructuring. I use shorter names as Changqing and Yanchang in respective to refer each of them in most cases unless it is necessary to point out a certain full name.

In most provinces, only state-owned enterprises (C-SOEs) under the central government, including the CNPC, are allowed to explore crude oil. However, for complicated historical reasons in northern Shaanxi, both Changqing and Yanchang, which represent the interests of the central and the provincial governments, are allowed to do so. This peculiar system for dividing exploration of crude oil is known as ‘ownership by one state and exploration by dual governments’. The natural resources, including oil and gas, are owned by the state, but the rights to explore and extract oil are shared by Changqing and Yanchang, respectively. Starting from the mid-1980s, credited to an effort to encourage development in the ‘old revolutionary’ districts in northern Shaanxi, local governments were allowed to establish county-level companies to engage in oil exploration and extraction in local areas.

However, the extraction of oil carried high costs and high risks due to the lower quality of the oil reserve in northern Shaanxi. The local governments which owned these county-level drilling companies used incentives, such as lower taxes and sale of oil wells, to encourage private investors to bring in capital and technology in response to capital shortages and technical difficulties. Starting from the early 1990s, private capital from Hong Kong, Macau, Guangzhou, Tianjin, Wenzhou and other places poured into the oil drilling industry in these counties through ‘contracts’ or ‘joint ventures’. As a result, three types of oil enterprises emerged in northern Shaanxi: (1) Changqing and Yanchang, both with the capital and technical qualifications for oil exploration and drilling; (2) fourteen drilling companies established by fourteen county governments in northern Shaanxi; and (3) over eight hundred joint ventures or consortiums formed by private investors. In the counties of Jingbian and Dingyuan, over 95 per cent of the oil wells were drilled by these joint ventures.

It was during this period that Changqing’s interests were infringed upon by the CNPC, a monopolistic explorer in all Chinese provinces. The private investors and the various local governments, which stood to benefit directly from the local ‘oil money’, formed a local growth coalition, or in the words of the media, a ‘fish and water’ relationship. Though the CNPC and the Shaanxi provincial government signed an agreement in 1994,<sup>2</sup> conflicts among those vital players occurred frequently due to disputes over boundaries arising from poor demarcation.

During this period, especially after 1998, the CNPC hoped to acquire all of the local oil enterprises in Shaanxi Province. On the other hand, the provincial government sought to ‘reform within the province’ in a bid to protect local interests. The result was a paradoxical situation where the provincial government continued to implement ‘reform within the province’ while the sub-provincial governments continued to maintain a ‘loose relationship with private enterprises’. The central government turned up the pressure after 2002 for the CNPC to absorb all the local oil enterprises in Shaanxi Province. Various levels of the provincial government took a ‘pre-emptive’ strike and launched the campaign of involuntary recovery of private oil assets so that the CNPC would not be able to take over the entire provincial oil industry.

### ***Unfolding of the Event: A Relationship of ‘Oil and Water’***

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<sup>2</sup> The full name of this agreement is ‘An Agreement on the Development of Oil Resources in Northern Shaanxi’, which was signed on 14 March. I will use a shorter name, i.e., the ‘3.14 Agreement’, to represent it in this article.

Following the instruction of the Shaanxi provincial state, county governments where oilfields were located started in March 2003 mandatory confiscation of the 'Three Rights' previously awarded to the private investors (the right to manage, the right to operate and the right to receive profit). The confiscation was conducted like a campaign with a specific deadline and with the support from a large number of government leaders. Even the police were on hand to assist. The mandate was to 'adhere to the policy of consolidation and full access' and to take 'tough measures to enforce recovery' so that full state control of the wells would be achieved. The government's actions aroused widespread indignation among the investors, many of whom saw these actions as nothing less than unexpected and complete betrayal. Several mass petitions took place after June, with some groups including as many as over 3,000 people. There were even incidents of violence during these petitions during which several key members of the petitioning groups were arrested.

While organizing these large-scale petitions, key activists also started to work on public opinion and sought political support in Beijing. A number of well-known scholars and activists showed support to the private investors through publishing articles which addressed the question of 'how to protect the legitimate interests of private enterprise'. They even signed letters addressed to the Standing Committee of the National People's Congress, calling upon the Congress to better supervise the local governments in law enforcement. The private investors also set up their own websites. There were official media, such as CCTV, which reported the incidents in favor of the investors. Interviewees mentioned written comments on the incidents by central leaders.

The Shaanxi provincial government relented in the execution of their strategy under pressure from the central government and as a result of public opinion. They abandoned the original policy of 'uncompensated confiscation', agreeing instead to provide 'an appropriate level of compensation' to 'small oil investors approved by local county governments'. However, the compensation offered by the various local governments was not satisfactory to any of the private investors, particularly the local farmers who had just taken over the oil wells, many of whom had invested everything they had.

The organised mass petitions had basically come to an end in 2004, but initiatives frequently used in 2003, such as organizing discussions and seminars and contacting the media, were still being employed on a regular basis. However, vital members among the private investors had begun to pursue justice through legal proceedings. While the rationale of their tactics with the goal of protecting their 'three rights' was subject to debate, their law suit against the three levels of the Shaanxi government – county, municipal and provincial – ultimately resulted in extreme internal and external pressure against the local governments and prompted the provincial government to resort to extreme measures. In July 2005, the representatives of the private investors were arrested. The defendants in the original lawsuit (i.e., the government) arrested the plaintiffs (i.e., oil investors) and became plaintiffs themselves. In January 2006, three prominent members of the activist group were charged with the crime of 'illegal gathering to incite social unrest' and sentenced to jail. Thus ended the rights-protection activities of the 'Northern Shaanxi Oilfield Event'.

***The Follow-up: The Restructuring of the Yanchang Group***

The heavy-handed confiscation of oil wells and the harsh treatment of the private investors led to three major consequences in northern Shaanxi with regard to the market configuration of oil resources. First, the unique situation of ‘ownership by one state and exploration by dual governments’ in Shaanxi Province remained intact. After taking over fourteen county level drilling companies, the ‘Shaanxi Yanchang Petroleum (Group) Co., Ltd.’ was restructured by the Shaanxi government. In the Northern Shaanxi petroleum industry, the newly-emerged Yanchang could now go toe-to-toe with Changqing, quashing any lingering ambition of Changqing to acquire Yanchang and forcing Changqing to accept the co-existence of two big oil companies in Shaanxi Province, thus safeguarding the latter’s economic interests.

Second, the state’s confiscation of the oil wells severely damaged the economic interests of the private oil investors, especially the small investors who were mostly deep in debt when the fieldwork for this chapter was conducted in 2012. Additionally, any proposed financial compensation to these investors became a thorny political rather than economic issue in the mind of local officials due to the political sensitivity of the law-suit. Third, the county and municipal governments lost control of the oil-drilling companies. The Yanchang Petroleum Group has been a provincial government-run enterprise under the supervision of the provincial branch of the State-Owned Assets Supervision and Administration Commission (SASAC), which gained full control of the enterprise’s finances and personnel. The oil companies previously under county-level governments had severed nearly all personnel and financial relationships with county governments after the restructuring. The oil-producing municipalities and counties became shareholders as part of the SASAC and retained the right to receive their share of the profit but did not interfere with the operating activities of the oil companies.

### **The Collapse of the Coalition: Crucial Mechanisms**

The preceding summary provides some background of the three stages of the ‘Northern Shaanxi Oilfield Event’. This section will focus on the ‘second stage’ of the event. The first and third stages of the event will be dealt with elsewhere. The focus of the analysis in this section falls on three questions: How did a local economic dispute escalate into a political event under national spotlight? What resources and strategies did the major players, including the Shaanxi provincial government, local county and municipal governments and the private investors mobilise and deploy as the dispute escalated? How did other third parties such as pro-market intellectuals, the professional human-rights activists, human-rights lawyers, the media, both domestic and international, get involved? What strategic and tactical missteps did they commit?

#### ***From a ‘Restructuring Project’ to a ‘Political Event’***

The restructuring and management of the oil market in northern Shaanxi Province could have been a relatively simple economic event. The various stakeholders could have taken advantage of this opportunity to clean up the mess left behind due to various historical factors and to establish a modern enterprise system whereby property rights, responsibilities and accountabilities are clearly defined. That would have helped achieve a win-win situation for all stakeholders, including the central government, the private investor, the local governments and local residents. So what are the reasons that the restructuring failed to achieve such an outcome but evolved into

a ‘political event’ where the provincial government enforced a mandatory nationalisation of the oil wells? The following explanations are offered in this chapter.

- A. The state-owned enterprise of the Changqing Oilfield and the Shaanxi Provincial Government, which represented local interests, failed to find a ‘win-win’ solution under the guidance of the central government. Instead, both sides approached the conflict as a zero-sum game. Consequently, the restructuring project was severely constrained and could not be accomplished through normal market forces and channels.

Due to historical grievances and practical circumstances, both the CNPC and the Shaanxi provincial government had only their own interests in mind and lacked good faith for cooperation. The restructuring project became a zero-sum game where the players seemed to be saying to each other: ‘You want to swallow me, so I will do anything to prevent you from succeeding’. The merging of local oil companies into the CNPC was equivalent to the total reversal of the ‘ownership by one state and exploration by dual governments’, a situation that the Shaanxi government had fought hard to maintain. On 26 July 2002, the CNPC submitted a report to the State Economic and Trade Commission entitled ‘On the Reorganisation and Restructuring of Local Oil Companies in Shaanxi Province’ (CNPC Research (2002) File No 302). In the report, the CNPC claimed that

The amalgamation of the entire Shaanxi local oil industry into the China National Petroleum Corporation Group (CNPC Group) is not only the key to rationalizing the oil management system, but also the only way of resolving the chaos in the exploration and extraction of crude oil by local oil companies. We propose that as part of the restructuring and reorganisation, the Yanchang Petro Group and the fifteen county-level drilling companies located in Yan’an city and Yulin city should be completely decoupled with the local governments, and the personnel, assets and operations of these companies should be absorbed into the CNPC Group as soon as possible. After the amalgamation, their crude oil production, processing and distribution should be managed by the CNPC Group. The CNPC Group will commission its subsidiaries to manage their day-to-day operation. The assets, liabilities and shareholder equities of other state-owned companies such as the Yanchang Oilfield, the Yan’an Refinery, and the Yulin Additives Plant, which currently form the Yanchang Petroleum Group, should be audited by an intermediary agency and appropriated into the CNPC Group with no compensation.

The proposal was completely unacceptable to the Shaanxi provincial government, especially to those officials who grew up locally. As a result, the Shaanxi provincial government submitted, on 11 August 2002, their own report entitled ‘On Restructuring Northern Shaanxi Local Oil Enterprises under the Auspice of Yanchang Oilfield and Other Issues’ (government letter (2000) No. 18) to the State Economic and Trade Commission. The report asked the central government to allow local governments to have the ‘autonomy to make adjustments and restructuring’ and proposed a restructuring of the northern Shaanxi oil enterprises with the establishment of Shaanxi Yanchang Petroleum Industrial Co., Ltd. The provincial government also intended to establish a petroleum group with regional shares. In other words, the provincial government argued for maintaining the status quo and therefore holding on to a major source of revenue for

the local government which, they argued, was in line with the overall ‘tax sharing’ principle of the central government.

The point here is not to judge the economic rationality of the two proposals. What is worth noting is that, from a policy perspective, the central government had only three options: to support the CNPC, support Shaanxi Province, and act as an ‘arbiter’ who will help the two sides find an acceptable ‘win-win’ solution. For various reasons, however, the central government did not express its intention clearly, nor did it provide any mechanism or a platform for the two sides to negotiate. Both Shaanxi Province and the CNPC submitted their own petition, but they never sat down at a negotiating table to seek an agreement. They never even bothered to develop a roadmap or timetable for cooperation. Both sides stuck to their own arguments and lined up their own supporters in the belief that they could race against time and accomplish a *fait accompli* that would be advantageous to them and then force the other party to accept the *fait accompli*.

It would have been helpful to establish a formal and effective system where large state-owned enterprises and local governments can resolve economic disputes. The ‘petitioning’ system, similar to the system of ‘financial contributions to the ministries’, is a seemingly formal but actually informal system through which cases of self-interests can be expressed and made. The final outcome often depended upon the personal likes and dislikes, as well as the political clout of the individual supporters that the two sides could line up. In this case, both sides pinned all their hope on the maximum support of their political guardians in this zero-sum game of life and death, making it impossible for any communication between the two parties even on the technical level (such as establishing road maps and time tables). In the end, the weaker party felt forced to take desperate and unconventional measures to break the deadlock, thus triggering a chain of reactions.

- B. The provincially mandated restructuring project lacked substance, leading the county-level government officials to erroneous judgment and missing an opportunity to establish a modern enterprise system in the country. Therefore, the ‘autonomous restructuring’ program, while sounding logical and reasonable on the surface, lacked a local economic base.

Unlike the CNPC, the Shaanxi provincial government advocated a ‘self-rectification’ process to be executed by the provincial government-controlled agencies alone. In the process, the Yanchang Petroleum Industry Group will become the main entity, corporate cover will be extended to the fifteen drilling companies located in Yan’an and Yulin cities on the basis of their legal qualifications and capital, and a new corporate identity will be formed with subsidiaries directly owned and managed by the Yanchang Group. Accordingly, the provincial government requested that county governments correct any potential policy or legal violations within their own jurisdictions first, so that the drilling companies within their counties would have legal standing. After obtaining their legal standing, the drilling companies could attempt to recover the assets of their joint-venture partners who were private investors – in accordance with the instructions specified in ‘File No. 1239’. Cooperation with the Shaanxi Yanchang Petroleum Industry Group could take many different forms, such as asset transfer, acquisition, merger or share investment, depending on the circumstances of the drilling companies and the nature of their joint ventures.

Economically, this top-down approach made good sense. The program was also reasonable politically. The provincial government clearly understood that to achieve its goal, the first step was to ‘rectify any violations committed by the government agencies’. However, even after the three levels of government started the mandatory recovery of the oil wells, the proposal was still not fully implemented. The absurd situation was that those county drilling companies that tried to merge with joint venture companies did not have the legal standing approved by the central government either. Worse still, the legitimacy of country state drilling companies was weaker to some extent than those joint venture companies, because those private investors claimed that they had legal property rights over their assets according to their contract with local governments. How did these incidents occur?

The primary reason was that the municipal governments of Yan’an and Yulin had vastly different views about the impending merger of the county drilling companies into the Yanchang Oilfield and had conflicts of interest that were hard to reconcile. Even after the ‘recovery movement’ had started, some county governments were ‘not resolute in their approach, taking an overall negative wait-and-see approach’ and ‘very ill-prepared for the merger into the provincial industrial group’, according to a government document (Yulin Political Documents 2003, No. 55). There was clearly a lack of well-defined allocation of benefits between the provincial and municipal governments in this case, a similar situation to what happened between the large state-owned enterprise and the provincial government.

Second and perhaps more important, ‘restructuring and reorganisation’ has long become a cycle of tokenism. Many county government officials were primarily concerned about how to look good when the central government or provincial inspection groups came to check their progress. Issues such as clarifying property rights, defining economic interest of all parties, collecting real and reliable economic data and establishing institutionalised channels of communication between government and businesses, were put on the back burner. What was even worse, such superficial management of the restructuring program was condoned by some provincial government officials. It was also this restructuring program that gave the CNPC legitimacy for taking a more direct and radical approach in the amalgamation of the Shaanxi local oil industry, as they felt they could no longer count on the cooperation of the Shaanxi provincial government. Feeling the pressure from the CNPC, the latter decided to make a pre-emptive strike. On the other hand, they also realised that it was impossible to implement their originally proposed reasonable plan as ‘self-rectification’. In fact, they did not even have the time to develop the details of the restructuring plan. In order to manufacture a *fait accompli* of a ‘successful reorganisation’ of the Yanchang Petroleum Group, the provincial government could only resort to confiscation, by force if necessary. Thus, an event which started as an economic dispute eventually evolved into a political event.

Clearly, there is a need for fundamental institutional guarantee in place for any large-scale economic restructuring program. This is not dissimilar to any war campaign in that food and supplies must move ahead any movement of the forces. In the case here, the essential preparation included the following:

- (1) Empowering the enterprises with well-defined responsibilities and accountabilities and allow them implement the restructuring plan and the government to be an independent arbiter. More often than not, the government is the one who proposes 'restructuring and reorganisation', usually with a goal of resolving a specific problem. Rarely does any government agency consider the issue of establishing a modern enterprise system and therefore resolving the fundamental institutional issues that cause confusion in the market place. In fact, even after the start of 'self-rectification', many county-level drilling companies still had no legal qualifications and some were even 'ghost companies' that were in no position to act as an independent party in the reorganisation. As a result, the government was forced to directly tackle the potential conflicts with private joint ventures. The solution, therefore, was to establish enterprises with clearly defined responsibilities and accountability so that they could implement the market restructuring programs, while the government acts as an intermediary only.
  
- (2) Relying on real and reliable economic data and introduce independent auditing and valuation by third-parties. There was a general lack of understanding of private investors among the local government officials. Government officials did not even grasp the most basic economic data (such as oil production) and even if they did, some of the data were inflated numbers from years ago. The danger of falsified data was that if the numbers were inflated to highlight achievement of the local officials, then the price of the oil wells became too high for the government to pay; on the other hand, if the numbers were shrunk in the past for tax evasion or avoidance, then the investors refused to accept lower compensation. In fact, during the negotiation process between the government and the investors later, it became obvious that the two sides were worlds apart on what constituted fair compensation. It was ironic that both sides were drinking their own bitter brew. Without reliable data, discussions of enterprise restructure and of reasonable compensation ran into great difficulty or a deadlock. Compensation settlements became a case by case negotiation determined to a large extent by personal feelings of the negotiating officials. This process in turn prompted further accusations of corruption. Considering the fact that statistics departments within the governments are liable to manufacture data according to the will of their superiors, it would be advisable to use independent third-party auditing and valuation agencies.
  
- (3) Preparing adequate funds. Market consolidation is an economic affair and as such would need funding. Fair compensation to the private investors should have been the policy from the beginning regardless of whether such compensation was for the purpose of consolidating the market or weakening the political willpower of the private investors for collective action. But when the Shaanxi provincial government was ready to reclaim the billions worth of private capital assets, the municipal and county governments realised that they had no corresponding funds to pay for such assets. The only option available to them was 'uncompensated confiscation'. This option would undoubtedly spur large-scale resistance and protests. On 10 July 2003, one hundred and nineteen days after the 'mandatory confiscation' program was launched, the provincial government was facing tremendous pressure from the central government and condemnation from the media across the nation due to massive resistance by private oil investors. It was only then that the Shaanxi government woke up to announce an alternative project with 'partial compensation'. Over-confidence in their own ability to implement their strategies and underestimation of the

capacity of the private investors might be the reasons why the Shaanxi provincial government did not propose a ‘compensatory restructuring’ policy from the very start. In addition, the lack of funds at county governments and county state drilling companies must also have played an important role in their decision. Even after the ‘partial compensation’ policy was announced, the payment of these ‘compensations’ had to be made in installments, a process that was not conducive to the resolution of resistance.

- (4) Establishing contingency plans. The lack of contingency plans makes it impossible for the government to retreat when a program meets with serious resistance. The government is forced to crack down on the resistance. But this may result in a deadlock, and sometimes the conflict may evolve into a political event. Any issue, once elevated to the political level or to the level where social stability is threatened, would put a local government in a dilemma where they could either retreat or push forward.

C. The private oil investors had unrealistic expectations about their profit and security due to earlier protective actions and verbal commitments from the provincial, municipal and county governments. It stimulated a complicated network of investors, that is, a massive number of local villagers, along with wealthy entrepreneurial investors from outward areas, invested in the oil wells even with huge debts, which constitutes the social basis for massive collective actions against the confiscation in the future.

In fact, right before the ‘self-rectification’ campaign by the provincial government, some county governments were still trying to convince the private investors of the advantages of preferential treatment of subcontracting oil wells and joint-venture agreements with investors. The county governments’ verbal commitments to protect the interests of private investors gave them a misleading signal: they concluded erroneously that they could ‘maintain the status quo’ in their oil production despite the ‘self-rectification’. This signal was a time bomb in the ensuing outbreak of rights disputes. What made it even worse was that many small investors (particularly the local villagers) continued to pour money into their oil wells, even using borrowed usury. The pressure of paying the interests of usurious loans was another reason that the uncompensated confiscation quickly led to the large-scale sit-down petition by those desperate villagers.

In the meantime, the provincial government was also facing strong pressure from the CNPC, which wanted to absorb all of Shaanxi’s oil industry. Provincial leaders believed that their only option was a pre-emptive restructuring campaign to control those assets before the CNPC’s move. However, lacking the basic economic might to resolve the issue by compensation, they could only resort to mandatory means reminiscent of a political movement. When the government seeks a political instead of economic solution for economic issues, it inevitably finds itself in an awkward position: a buying-out will be escalated into political action. As the resistance swelled, the provincial government was forced to compromise and to offer ‘partial compensation’. But even this concession was designed as two-step process: mandatory confiscation first, appropriate compensation later. This design, however, did not ameliorate the situation for a couple of reasons.

First, the design was not a result of consensus between the government and the private investors. Rather, it was the government’s one-sided concession. The private investors had no idea prior to

the government announcement, but even if they knew in advance, they would not find such terms acceptable. They believed that the idea of mandatory confiscation followed by appropriate compensation violated the principle of fairness, according to my interviews with those activists of resistance. Second, there was no effective communication between the government and the private investors. Some big investors obtained promises of compensation through personal connections with government officials, but most medium and small investors had no idea at all about when and how they could be compensated. The government's political measures could only quell the dissatisfaction of the big investors but underestimated the will and capacity of the medium and small investors to take collective action. If the government had been more proactive and democratic or had taken effective measures prior to the confiscation, it would have been in a better position to concentrate the private oil assets in the hands of fewer big investors through asset transfer, acquisition and share repurchase while at the same time reducing the number of small investors, especially those with usurious loans, and therefore to avoid the large-scale resistance. The 'self-rectification' could then have been completed through economic means as the economic disputes should have been.

There is therefore a clear need for local governments to establish effective channels of communication with private investors, particularly medium and small private businesses. While numerous large private investors have entered political representative bodies, such as the local People's Congress and Chinese People's Political Consultative Conference (CPPCC), most small investors do not have institutionalised channels of communication with the government. The authorities of Jiangbian County, which witnessed the most stiff resistance during the event, had a chance to establish a chamber of commerce for the private oil investors, but the idea was never followed up. Thus, when the medium and small business investors realised that they did not have representatives to negotiate with the government, they would most likely select those who they believed would best represent their interest at the time. Ironically, those representatives selected under such circumstances were mostly people who had more radical ideas and were inclined towards radical actions.

In summary, the Shaanxi provincial government set about resolving an economic issue by means of a political campaign in the absence of reliable economic data, adequate funds, a contingency plan and an effective communication system. It is thus unsurprising that during the confiscation that the government became the target of mass protests in a situation where the government had no financial means to appease the protestors and lost the flexibility in terms of actions and moral high ground. The government policy of 'mandatory confiscation first, appropriate compensation later' led to the eventual breakout of conflicts. In other words, the evolution of the disputes on the oil wells from an economic matter into a political event was caused by tactical errors committed by the Shaanxi provincial government in their attempt to create a 'fait accompli' through their own confiscation to stop the CNPC from 'annexing' Shaanxi's oil industry.

### ***From a 'Political Event' to 'Judicial Activism'***

The private investors had three major complaints about the Shaanxi provincial government. First, they felt betrayed by the government, because the latter had previously promised them they could continue to operate through asset transfers, purchases, acquisitions, mergers or joint-ventures with provincial the state-owned company of Yanchang. However, the government

began to confiscate their assets instead of keeping its promise. It was a serious breach of trust in the government. Second, even though some private investors accepted the government's compensation proposal and agreed to withdraw from Shaanxi, they felt the compensation was so low that it bordered on outright usurpation. Third, the government's use of police and other paramilitary force during the confiscation infuriated many investors as they felt their rights and dignity were violated.

On the other hand, the escalation of the event was also due to a series of actions taken by the private oil investors. Without the enormous capacity for activism of the private investors and their representatives, the confiscation would have undoubtedly had the same outcome as 'forced land seizures', 'forced evictions' or countless other 'forced measures' implemented by the government in Shaanxi and elsewhere, and ended with a simple incident of mass protest or total victory by the government. In fact, the Shaanxi provincial government had probably never expected this level of activism on the part of the private investors, nor were they prepared for their strategies of rights-protection. The private investors used five principal tactics:

- A. A number of private investors of medium-sized assets with ample financial resources and partially motivated by a sense of justice played a key role in steering the activities away from being a simple incident of 'protests for economic compensation'.

Private investors were the direct victims of government's confiscation campaign. They can be grouped into 'big', 'medium' and 'small' categories according to the size of their assets. For the government, the 'big' investors were the easiest to deal with. Some of them liquidated their assets through various means in the early stages of 'self-rectification' program. Some of them had received considerable compensation from the local governments. However, appeasing the 'big' investors as a top priority was not the correct approach because the 'big' investors typically had enough liquidity of money to last for a while. They are usually more inclined than small businesses to cooperate with governments at various levels, and it is easier for the latter to communicate with them. Having used the limited funds to satisfy a small number of 'big' investors, the government was unable to financially appease the larger number of medium and small investors, thus making themselves the targets of mass discontent.

Although there were a few 'big' investors who funded the resistance or participated in the organisation of protests, the core members of the activists were medium and small investors. The medium investors included local residents and business people from other provinces. Most of the small investors were local peasants who borrowed heavily to invest in the oil wells. If the oil wells were confiscated by the government without compensation, their families would have lost everything. That meant they had the most to gain and were the least hesitant to participate in assistance against the confiscation. At the peak of the protests, the number of petitioners who sat in silent protest in front of the government buildings exceeded 4,000. However, if the protestors had been small investors exclusively, the event would probably not have stood out from other mass protests in China, such as peasants' petitions and protests over land seizure. What made the incident unique was the involvement of the medium investors, or what the Shaanxi government called the 'ring leaders'. These investors suffered great financial losses, but unlike the big investors, they did not have strong formal or informal connections with local governments and were therefore more determined to protect their rights and recover their losses through resistance.

However, not all the medium investors became core members of the activist group. The core typically had one of the two following characteristics: (1) like the traditional 'literati', they were well educated people who believed in the pursuit of freedom and equality; or (2) like the 'gentry' class in the past, they enjoyed high social prestige and had a reputation of being fair and reasonable. Their rights-protection activities are not simply motivated by economic considerations but buy a sense of fairness as well. Therefore, their demands could not be met by economic compensation alone.

- B. The key members of the private oil investors, the pro-market intellectuals, the professional rights activists and the human rights lawyers established the foundation for the resistance that escalated from a local conflict into one of national significance.

In the beginning, the key members of the rights-protection activists included mostly medium and small investors who organised meetings and solicited opinions. They did not have a well-thought-out plan to escalate their campaign to a national level. Their initial idea was simply to plead with the central government, make a case with the provincial government and seek the assistance and support of senior government officials. But their plan soon proved to be unrealistic. The turning point was when the activists invited pro-market intellectuals to discussions and seminars with a view to garnering support from the media and the public. But these discussions and seminars brought the investor-activists into special circles in Beijing which comprised well-known pro-market scholars, rights lawyers and rights activists. These three groups of people have different positions in relation to the establishment. Some were officials or scholars who worked inside the system while others were dissidents not tolerated by the system, although they had much in common in terms of economic interests and ideological orientation.

- C. The characterisation of the resistance as a specific case in the wider political discourse of 'protection of private property rights' and 'constitutional rights' provided moral support to the private investors and justification for their resistance.

Taking note of the advice of the pro-market scholars, rights lawyers and rights activists, the representatives of private investors finally decided to take a 'judicial approach' and to characterise the petition as a case in the broader political discussion of 'protection of private property rights', 'administration according to the law' and 'constitutional rights', despite considerable differences in motives and objectives among the four groups of core players.

What drew the pro-market scholars into the resistance, aside from the usual economic considerations, was their desire to bring this local event into the national spotlight and to shift the focus of the discussion towards broad, controversial topics in China's ideological contestation, such as constitutional amendments and property law.

The rights activists and lawyers saw it as their moral obligation and duty to defend private property rights. In one of the public statements during the confiscation, the Shaanxi provincial government claimed that these lawyers were not only keen to participate in the event but also to take advantage of the investors by encouraging them to resort to litigation so that they could charge legal fees, and that, when the investors were disappointed with the outcome of the

litigation, these lawyers would redirect the investors' anger and resentment towards the government. In the government's original words in the statement, 'they sow the seeds of social instability'. There can be no doubt that, in the eyes of the provincial government, the activists and lawyers were dangerous agents of social instability and instigators who added fuel to the fire. But as they are held in high regard both domestically and internationally, the government has to be more cautious with heavy-handed measures when dealing with rights activists and lawyers.

- D. The well-funded and experienced rights activists and lawyers launched a successful public relations campaign, while the propaganda department of the state acted clumsily.

The major players in the four resistance groups achieved surprising results in influencing the media and shaping public opinion. Their lawsuit against three levels of government eventually generated tremendous pressure both internally and externally on the government officials. This was indisputable evidence of the private investors' clever use of the mass media. Stories about the 'Northern Shaanxi Oilfield Event' appeared in the overwhelming majority of non-official Chinese media with a focus on financial and economic matters, and there was hardly a single story which was unsympathetic towards the private investors. In addition, the latter set up their own website. Government authorities shut down the website repeatedly, only to see more sympathy with and support for the investors from the public. The private investors even published their own academic and investigative reports, which included verifiable data, put forward unique perspectives and demonstrated good writing techniques, and appeared objective and convincing. In contrast, the capabilities and skills of the propaganda departments of the Shaanxi provincial government proved to be inadequate even though it had the official provincial media under its command.

- E. The private investors' unwillingness to compromise on the issue of property rights led directly to the failure of resistance, although some issues were deemed insolvable because of political restrictions more than anything else.

At the beginning of the resistance, the Shaanxi provincial government tried to initiate dialogues with the activists. However, these dialogues ended with the arrest of the key representatives of the private investors. The government only started to soften its stance when the investors decided to bring lawsuits against it. It became eager to bring the situation under control as soon as possible due to pressure generated by overwhelming media coverage. According to a local media report, for example, the Party Secretary of Jinbian County, Ma Lebin, said in an interview, 'Let's leave the legal issues and what is right and wrong to the higher authorities. We want to do what we can within our authority to help people and solve some practical problems.' The 'practical solutions' he referred to meant additional compensation for the private investors. But the investors' representatives rejected the proposal, insisting instead on the government's abandonment of assets confiscation. A successful outcome proved impossible because the negotiating parties took irreconcilable positions. It was only a matter of time for the government to resort to violence. On 5 January 2006, three rights key activists, Feng Bingxian, Feng Xiaoyuan and Wang Shijun, were arrested and sentenced to prison. The arrests marked the end of the rights-protection activities in the 'Northern Shaanxi Oilfield Event'.

*From 'Judicial Activism' to 'Economic Disputes'*

Nevertheless, the litigation related to the Northern Shaanxi Oilfield did not stop immediately. By March 2007, the key government officials at every level of jurisdiction who were involved in the event had been retired, removed or replaced. The change of the guard opened a window for a compromise. But the key to a resolution of the event was the rights activists' strategic shift from 'regaining control of the oil wells' to 'requesting increased compensation' without completely ruling out the possibility of further legal actions, which transformed a lawsuit against the government into a non-litigious negotiation. The Shaanxi provincial government's response to the shift was positive. The government proposed a case-by-case solution to individual investors under the overall premise that the government action was not wrong. However, the fact that the investors' 'recovery of the three rights' evolved from an economic dispute to a political campaign involving the use of police called into question the competence of many government officials. As a result, the implementation of the case-by-case solution became very difficult due to lingering resentment against individual government officials. In addition, the county governments had frequent disputes with the group over who should be responsible for the liabilities as a result of the confiscation.

The resistance seemed to have quietened down following the imprisonment of key investor representatives, at least on the surface. Still, most of the private investors still harbored grievances over the governments' heavy-handed measures for recovering the oil wells. Many ended up with huge debt and were destitute to the extent of not being able to maintain their livelihood. The event also tarnished the Chinese government's image overseas. The most critical questions arising from the event were whether the confiscation was necessary and justifiable and, if so, what could have been done to ensure that the private investors received fair and acceptable compensation. When the imprisoned investors are released, it will be a test of the wisdom and flexibility of the Party and governments at various levels whether the event will be redefined and treated as an economic dispute as it was to begin with.

### **Concluding Remarks and Policy Implications**

Although the 'Northern Shaanxi Oilfield Event' was just one case, the case study can be extended (Burawoy 1998; Eliasoph & Lichterman 1999; Small 2009). It is illustrative in revealing how an event evolved (Mitchell 1983). In fact, the case is not isolated in China; conflicts triggered by disputes over mining rights, for instance, have been one of the major causes of local petitions or even mass riots. Most of the published policy research has focused on the coalition between the local governments and mine investors, while peasants and miners are the subjects of cracking down by the government-business coalition. Therefore, relevant policies were more concerned about establishing mechanisms and systems for the profit-sharing between the government and labour.

Today, with rapid economic development and the expansion of governments' rectification actions, conflicts between local governments and private investors have increased in frequency. The even under discussion is not the only major incident that was played out on the national stage; there have been actually many conflicts that were similar or even identical to the Northern Shaanxi Event. Judging from later coal mining rectification campaigns in Shanxi, Shaanxi and Henan, one cannot fail to notice that the government officials in these provinces did not learn

any lessons from the event. Many of the policies are still made in a vacuum without the support of relevant research.

Although this chapter does not attempt to analyze any other cases, what can be gleaned from reports published by the media is that some of the reasons for the frequent conflicts between local governments and private investors over 'mining reorganisations' include defects in the governments' policy designs similar to those implemented in the Northern Shaanxi Oilfield. For example, in addition to the old problem of poorly-defined property rights, the lack of transparency of financial data was another fatal flaw in these reorganisation programs. Some local governments support and help the private investors with report of lower production volumes so that they can less tax or do not have to pay taxes at all. It is a win-win situation for pro-development local government and private entrepreneurs. But when it came to compensating the private investors according to their production volumes, the data that the government received was problematic to go by. Another typical government practice in the re-organisation programs is to instinctively resort to means reserved for dealing with mass unrest and incidents. Governments frequently ignore or contravene their own policies and procedures due to the non-existence of a system of procedural monitoring or safeguards.

Like many of the reported conflicts between the government and the private sector, economic disputes triggered the event in Northern Shaanxi. The key to conflict resolution lay in a good understanding and skillful management of the competing interests and complex relationships among the large state-owned enterprises, the local state-owned enterprises, the provincial and county governments, the private investors and local residents. However, due in part to the lack of established institutional mechanisms for handling such conflicts, the conflict of interest between the large state-owned enterprise and local government turned into a zero-sum game which, in turn, prompted the Shaanxi provincial government to embark on the mandatory confiscation program in a bid to address the issues of market disorder. As it turned out, conflicts between state organs not only prevented the original disputants from finding a solution but exacerbated the conflicts. In the end, it was the private businesses which suffered the most as a consequence.

A series of mismanagement on the part of the Shaanxi government resulted in the implementation failure of a quite clear economic restructuring program. The government became the target of mass protests due to the failure to establish a modern enterprise system with clearly-defined rights and accountabilities, to grasp real and reliable economic data, to have sufficient funding, to plan for contingencies and to establish a system of effective communication channels between the government and the private sector. This was compounded by the lack of a benefit-sharing system between the provincial and county governments, which led to the latter's loss of motivation for implementing 'self-rectification'. In effect, the county government added fuel to the fire when they gave private investors false expectations that the confiscation would be no more than tokenism.

As local elites, while the private oil investors shared many similarities with ordinary citizens in rights protection, they stand out in several ways. For one thing, the majority of the small investors were local villagers, and they constituted the social basis for the large-scale resistance. It was the medium investors who acted like the 'literati' and 'gentry' class of the past, became the core group of activism, and pushed the local rights-protection movement onto the national

stage. Because of their economic and cultural capital, this group of investors formed a rights-protection alliance with the pro-market intellectuals, rights activists and rights lawyers. They were able to successfully set their own agenda in the media, thus putting enormous pressure on the government. Public opinion forced the Shaanxi provincial government to meet at least some of the investors' demands for compensation on a case-by-case basis. However, a compromise between the government and the private investors became impossible due to the uncompromising position that the representative investors took on the issue of property rights.

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