



The Status Quo and Problems of the Building of China's Social Credit System and Suggestions

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Abstract

In the Third Plenary Session of the 18th Central Committee of the Chinese Communist Party, the proposal that we should modernize the country's governance capacity and governance system was put forward, which means that social credit system, as a new way of social management in the critical period of deepening reform, deserves substantial development. In this paper, based on the experience from the developed countries in terms of their social credit system building, the writers make an attempt to analyze the status quo and problems of the building of China's credit system in details, and also give corresponding suggestions, in the hope that these suggestions will be of great assistance for the improvement of China's social credit system in the new era.

Key words: Social credit; Social credit system; Credit investigation system

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INTRODUCTION

As a tool to evaluate credit, credit investigation means to measure, analyze, and investigate the credit history of enterprises and public institutions such as legal person, unincorporated and natural persons, as well as the overall information that compose their qualifications, status quo, and behaviors, so as to determine their current credit status and judge whether they have the ability to fulfill the credit obligations¹. The building of credit investigation system is a key component of the establishment of social credit system, which is now in its infancy in China. Therefore, if we carry out the work of credit investigation smoothly, this will exert immense significant impact on the overall building of China's social credit system.

1. THE STATUS QUO OF THE BUILDING OF CHINA'S SOCIAL CREDIT INVESTIGATION SYSTEM

According to the common understanding of the academia, the development of China's credit investigation system has gone through three stages. The first stage is the initial stage of the development of the credit investigation system, which began in the early 1990s when some credit intermediaries mainly in charge of giving an evaluation on one's credit status appeared in China due to the demand of foreign enterprises for credit investigation, but the size and business of such credit intermediaries were relatively small. The second phase, beginning in the late 1990s, witnesses a rapid development of the credit investigation system. At that time, with China's sustained economic development, especially with the expansion of foreign trade, the market began to set higher

¹ Wang, X. Y. (1999). *Strategic Management and Marketing Management of Modern Commercial Banks*. Beijing: China Financial Publishing House.

requirements for enterprises' credit, thus the single credit investigation mode in the previous stage was unable to meet this trend, which gave birth to a new intermediary that ran the business of giving credit guarantee. Besides, a number of foreign credit companies entered into China's market such as Dun & Bradstreet credit company. All these have jointly promoted the development of China's credit industry. The third stage began from the early 21st century when the development of the credit industry drew governments' attention. In the report of CPC's 16th National Congress, the strategic task of building the social credit system was proposed for the first time. Furthermore, the work of collecting enterprises' credit information on the part of the banking sector achieved good success, and the personal credit industry has entered into its pilot phase. In addition, the credit information system with the government as the main part developed in parallel with the joint credit investigation system which regarded social credit intermediaries as the main part.

1.1 The Working Mechanism of Social Credit Investigation System Gradually Improves

The building of China's credit investigation system is led by the People's Bank of China. In November 2008, it took the lead to hold an inter-ministerial joint conference centering on the theme of building social credit investigation system. In October 2011, the State Council changed the leading department from the People's Bank of China alone to the National Development and Reform Commission and the People's Bank of China together, and the number of the departments that should take part in the inter-ministerial joint conference expanded to 39. At the same time, the building of social credit investigation system continued to expand its scope and connotation, including not only financial credit investigation but also economic credit investigation. In 2011, the Sixth Plenary Session of the 17th Central Committee of CPC expanded the scope of social credit system building by further including government credit, commercial credit, social credit, and judicial credit, and so on. This shows that the scope ranges from economic sector to ethical field. In terms of the legal in situation building, in 2007, the State Council issued the "Opinions on Social Credit System Building" to accelerate the construction of social credit system. In 2011, the joint conference of the People's Bank of China formulated the "Plan for Building Social Credit System (2011-2015)" and submitted it to the State Council.

1.2 The Building of Credit System in Industries is Carried out Effectively

Under the lead of the People's Bank of China, China's credit building in industries has developed steadily. In the meantime, directed by the People's Bank of China and by the "Opinions on Social Credit System Building" formulated by the State Council, various regions in the whole country have actively carried out the work

of building credit system in relevant industries and departments. Through years, remarkable results have been achieved. In specific, the competent departments of most industries developed a system for credit information collection and usage aimed at their own industries, effectively evaluated the credit status of their management objects, and implemented different management measures according to different categories. For instance, commerce and industry, tax industry, banking sector, public security, and other units have collected, processed, and stored the credit information of their objects within the scope of their jurisdiction, so that it becomes more convenient to take targeted measures to deal with their objects. Besides, national network was employed in the credit counseling system of banking sector, and all the commercial banks collected and processed the credit information of enterprises, public institutions as well as various economic organizations that are relevant to bank credit in accordance with the unified standards of the People's Bank of China, then sent the credit information to the credit database of the People's Bank of China, so that commercial banks can check their customer's credit information in the database to determine whether they give loans or not. In this way, credit risks were reduced and the stability of financial market was ensured.

1.3 The Building of Credit Investigation System Proceeds Smoothly in Small and Medium-Sized Enterprises (SMEs)

With the further development of the market economy, SMEs plays an increasingly important role in China's economic development. In this sense, building credit investigation system in small and medium-sized enterprises can not only guarantee fair competition in market, but also can facilitate SMEs to obtain loans from banks, which in turn will reduce banks' credit risks and promote the development of SMEs. In 2010, the People's Bank of China issued the "Guidelines for Building Pilot Areas for Small and Medium-sized Enterprises in Building of Credit Investigation System", which marks that the building of credit system in SMEs went on a standardized, scientific, and systematic track. In addition, the People's Bank of China has coordinated relevant departments. Through building pilot areas for SMEs to establish credit investigation system, it also set up a unified system for managing SMEs' credit files, promoted SMEs to share credit information, and carried out the work of credit rating for SMEs. It aimed to penetrate the credit awareness throughout SMEs' daily business activities and promoted SMEs to create a favorable credit environment.

1.4 The Building of Rural and Personal Credit Investigation System Makes Progress

In 2009, the People's Bank of China issued the "Opinions on Promoting the Work of Building Rural Credit Investigation System", which marks that the

building of rural credit system has embarked on a road of standardized development. Following the road of SMEs' building of credit investigation system as well as under the coordination of the People's Bank of China, relevant departments set up pilot areas for building rural credit investigation system, established credit files, and gave evaluation on the credit status. They also chose some villages as credit models and elected new users. All these activities have significantly promoted the building of rural credit system.

After October 28, 2013, the number of pilot areas for inquiring personal credit information online further increased to nine provinces including Beijing, Shandong, Liaoning, Hunan, Guangxi, Guangdong, in addition to the former Sichuan, Chongqing, and Jiangsu province. Individuals can inquire three aspects of credit information on the internet which are personal credit information tips, personal credit information summary and personal credit report. According to the plan, if the pilot work goes well, the online inquiry system is expected to be promoted across the whole country in 2014.

2. PROBLEMS IN THE BUILDING OF CHINA'S SOCIAL CREDIT (INVESTIGATION) SYSTEM

As can be seen from the above situation, the building of China's social credit investigation system got a late start, but the basic idea of the building itself has taken shape. However, we should notice that some government departments administer in their own way at present. Moreover, the degree of disclosure and sharing of information is rather low, and there is a lack of unified standards to guide the various regions. Apart from this, the standards for collecting credit information are uneven, and the internet platforms used to inquire the credit information are not open to each other. All these have seriously hindered the building of a unified social credit system. Therefore, we have good reasons to analyze the existing problems, with the aim to pave the way for the building of a more comprehensive and sound social credit system.

2.1 The Standards for Collecting Credit Information are not Unified and the Credit Information is not Open to Public

The basic work of building social credit system is to collect credit information. Due to the uniqueness of credit information, it is decentralized and abstract. Therefore, it is highly important to ensure that the collected credit information can be used interchangeably without any obstacle. At present, the credit information is basically concentrated in banks, commerce and industry, tax industry, public security, customs, quality inspection sector and other regulation and law enforcement sectors.

However, the collected credit information of these units and individuals intending to facilitate the performance of their functions tend to have some characteristics of their own, which results in the fact that each unit does not collect credit information in accordance with unified standards, so the final established credit system can only be used for each unit, which makes it impossible to exchange credit information among all the units.

It is also true for social credit intermediaries. Each credit intermediary organization has his own set of credit evaluation system, which leads to the fact that the credit evaluation results of the same enterprise obtained from different credit intermediaries are not the same, or even are totally different. Since unified standards are the benchmark of market development, the credit market will be in chaos and there will be no significance for the credit evaluation without unified standards. For example, when enterprises or individuals are applying for loans from banks, the confusion of the credit evaluation standards often makes some enterprises or individuals who previously have good credit unable to get loans, while others who do not have good credit finally get the loans successfully. This not only damages the market order, but also increases the chances of bad debts, and increases the probability of the occurrence of financial crisis.

2.2 The Legal System for the Building of Credit Investigation System is not Sound

The building of credit investigation system is a systematic project, which includes such stages as the collection, processing, transmission, storage, extraction, and usage of credit information. Any failure in each stage will lead to problems in the operation of the whole system. Although the credit system exchanges credit information all around the country through the use of Internet, it still needs people's participation and needs specialized talent to design and operate the system. Nevertheless, due to various reasons, people often make mistakes; in this sense, it is rather crucial to formulate scientific legal systems during the process of building credit investigation system to regulate human behaviors and monitor work procedures. The old saying that nothing can be accomplished without rules or standards exactly hit the point. Thus it is clear that such a complex, lengthy, and systematic project needs good legal systems to guarantee smooth progress. However, The current development of legal system in China is still lagging behind in this regard. The non-unified standards for collecting credit information that have been mentioned above is a good example for this. According to the actual situation in China, the government should take the lead to start a joint conference mechanism for the building of social credit investigation system. And based on the unified standards devised through scientific study and assessment, the government should try to ensure normal operation of the market.

2.3 There is a Lack of Punishment Mechanism for Acts of Losing Credit

Lack of credit has always been an important problem in the various aspects of Chinese economy and society. In recent years, it even becomes increasingly serious. The reason behind it is the lack of a clear punishment mechanism for acts of dishonesty. From an economic point of view, when the cost of losing credit is less than the benefit of losing credit, the person who lacks credit tend to breach regulations and laws in order to pursue the benefits. So, developing a clear and operable punishment mechanism for acts of dishonesty and ensuring that the cost of losing credit is not less than the benefit will help us to curb the occurrence of dishonest behaviors to a great extent. Meanwhile, it is also recommended to establish an incentive mechanism for honoring honest behaviors, so as to form a stark contrast. With the implementation of these two mechanisms, we will finally build a complete and compulsory credit system. In recent years, such events related to food security, drug safety, manufacturing safety and other events occur frequently in China, and mass media have done a lot to expose and report these events; however, such events still repeatedly happen, and some enterprises and individuals who have been reported already even go back to their road of breaching the laws again, which has seriously affected the healthy development of Chinese market economy.

We may note the fact that at present there is no severe penalty imposed on any enterprise who loses credit. If there is no death, punishment is often given through charging fines and requesting rectification, and the reports from news media are only released in a certain period of time when people show great attention on the events. In fact, the two methods including charging fines and requesting rectification are only taken to punish the party concerned "at the very moment" instead of giving sustained attention. In addition to this, the cost and benefit of breaching laws are out of balance. Therefore, we should establish a system for registering the enterprises lacking credit, build credit files of enterprises and update them without delay. Besides, we should also expose these information on the network to facilitate the access to people, effectively monitor the dishonest behaviors all around the society, and substantially increase the cost of breaching laws.

3. SUGGESTIONS FOR IMPROVING THE BUILDING OF CHINA'S SOCIAL CREDIT INVESTIGATION SYSTEM

Improving the building of China's social credit investigation system is the cornerstone of establishing a unified social credit system. The development of credit industry is not only the business of the industry itself; instead, in the face of the status quo of China's credit

industry, its future development also needs the concerted efforts of the government, legal laws, market and other parties. In the Third Plenary Session of the 18th Central Committee of CPC, a requirement was given that we should establish a sound social credit investigation system, praise acts of honesty and credit, and punish those of dishonesty. Under the background of deepening reform, the writers put forward four suggestions for the development of China's credit industry. They are from the perspective of legal laws, government, market, and network platform.

3.1 Improving the Legal System of China's Credit Industry

When market develops to a certain size, a variety of interest disputes and industry regulations will appear. Then legal laws are needed to uniformly standardize the market. The United States attached importance to the role of laws in the credit market at the stage of standardizing the building of social credit system. In 1970, the United States issued the "Fair Credit Reporting Act", marking that America's social credit system embarked on a road of standardized development. Some other laws were also formulated on this basis and enjoyed rapid growth. In 1996 and 2003 respectively, the United States made major changes on the "Fair Credit Reporting Act". Until then the framework for American social credit system took shape. And the United States formed a complete legal system which regards the "Fair Credit Reporting Act" and "Financial Services Modernization Act" as the core complemented by some relevant laws such as the "Equal Credit Opportunity Act", "Fair Debt Collection Practices Act", "Truth in Lending Act", "Fair Credit Billing Act", "Credit Card Issuance Act", "Fair Credit and Charge Card Disclosure Act", and "Electronic Fund Transfer Act". As for China, although the building of its credit investigation system has achieved initial progress, no specialized law was released aimed at the building of social credit system according to the "Report on the Development of China's Credit Industry (2003-2013)" published by the People's Bank of China. Nevertheless, there were only relevant regulations and guidance given by the People's Bank of China or the State Council. Hence we can see that legal system for the building of China's social credit investigation system is in dire need.

3.2 Establishing Industry Regulation Department

The development of China's credit industry is still in its infancy, and the regulations of industries are not mature, so industry regulation department is needed to coordinate and supervise the behaviors of various market participants to ensure the healthy operation of the credit market. At present, taking various practical factors into account, the People's Bank of China is in a best position to bear the responsibility of monitoring credit industry. This is because it has the absolute ownership of the credit information of enterprises and individuals, and it also has

good technical conditions to regulate the credit industry. The central bank of China should give clear guidance to the problems appearing in the process of building credit investigation system in all regions, put forward suggestions, and guide the behaviors of market players to establish industry regulations as well as standardize the market order.

3.3 Giving the Leading Position to the Government, Letting the Market Play a Decisive Role, and Promoting the Development of the Credit Company

Due to the special nature of the credit industry, it sets relatively higher requirements for coordinating information resources, technology of building the network platforms, capital investment and others. So in the early stage of market development, it is unrealistic to let enterprises bear the responsibility alone. In this sense, in this period, government is needed to participate in the credit market. First, it should give support to market players in terms of training, technology, information resources, and funding. Besides, it should also support some large credit companies by means of buying state-owned shares, thus promoting the rapid development of credit business in a short term. Since the Third Plenary Session of the 18th Central Committee of CPC determined the decisive role of market in the allocation of resources, when market develops to a certain extent, we should guide state capital to take initiative to exit market orderly as well as return enterprises to the market to let the market play a decisive role in the allocation of resources, so that all the market players will spontaneously merge and reorganize themselves under the influence of the market itself, thus accelerating the mature growth of the credit industry.

3.4 Setting up a Unified Credit Information Platform

The foundation of credit investigation system is the collection of credit information. However, at the moment, standards of collecting credit information used by local governments in China are not the same, which results in the fact that the credit information in various places cannot be shared. Therefore, it is highly urgent to establish

a unified credit information platform. In this way, the platform can realize its value in two ways: First, the platform can ensure that the standards used to collect and process the credit information uploaded on the platform are unified, which will lay a good foundation for the building of a comprehensive credit system; Second, the platform can guarantee the sharing of credit information in all regions, and the platform is open to management. In the early phase of developing credit industry, individuals and enterprises can have a free access to the needed credit information from the platform so that the sharing of credit information will not be confined. When the credit industry becomes more mature, the usage of the platform can charge certain fines. Since the building of such credit information platform sets higher requirements for the integration of technology and resources, it is generally under the lead of the central government or the People's Bank of China.

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