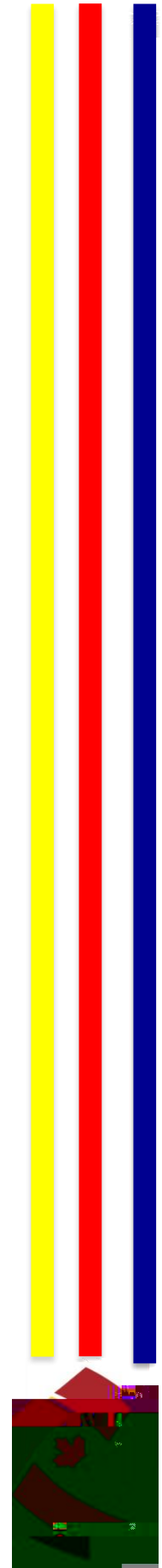


Measuring Fiscal Federalism and Decentralization in Latin America: Argentina and Brazil in Comparative Perspective

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ABSTRACT¹

Argentina and Brazil are two traditional federations in Latin America. Both countries have a formal

therefore to consider the size and character of these transfers (conditional or unconditional, discretionary or non-discretionary) in order to measure the extent of dependency in administration of their competences and delivery of public services. Fifthly, the (5) total expenditure of each level of government combined is another useful index to measure the size of subnational administration of competences and public services. It is also complementary to the former (federal transfers) to measure the degree of dependency or autonomy with which levels of governments perform their responsibilities. In this respect, it is necessary to distinguish to what extent subnational units cover their expenses with their own resources or with 10(s a)-7(nd p9 0 0 1 262.3 20912 0 612 792 reW*28)is cover their expenses wi00000912 0 5(he)-10(i)5(r)-7()23(e)-

Table 1: Seven variables to measure decentralization

1.	Constitutional competences	Measures the size of subnational governments within a federation.
2.	Constitutional revenue-raising capacity	Measures the formal or institutional decentralization of autonomy's fiscal aspect and the scope of subnational taxation power.

Subnational units (“states” in Brazil and “provinces” in Argentina) are endowed with a wealth of authority, making both federations highly decentralized politically. Both constitutions reserve residual power upon the subnational units (Art. 25, par 1. CFR: art. 121 CAN). In order to simplify this complex matter, it is useful to classify the competencies as federal, state/provincial, shared and concurrent. Federal competences are those competences assigned exclusively to the federal government, whereas state/provincial competencies refer to authorities assigned exclusively to state governments. Shared competencies are those that require the consent of the two level of governments to be implemented. Finally, concurrent competencies are those that may be exercised independently and simultaneously by any level of government – but not necessarily in a coordinated manner.

The system of distribution of competences used by the Brazilian constitution consists in an enumeration of the Union’s competences (Art. 21) and of concurrent competences with the states (Articles 23 and 24 – legislative competences). Brazilian federalism can be classified as a devolutive federalism, in the sense that it was the central government – through a constitution – which recognized autonomy and therefore a set of competencies and authorities to the federated states (similar to Belgium, Australia and Canada). Conversely, Argentine federalism is an integrative one (See Hernández 2011), because provinces created – through a constitution – a central government and delegated to it a set of competencies and authorities (similar to the cases of USA, Switzerland and Germany). Normally, a devolutive federalism entails an allocation of residual power to central governments. Nonetheless, Brazilian constitution attributes most powers to the states when it establishes that ‘all powers that this Constitution does not prohibit the states from exercising shall be conferred upon them’ (Art. 25, par 1, CFR). According to this principle, the constitution endows to the central government with enumerated and limited competences (the same is true for municipalities).

Argentine federation has the same method of distribution of power: ‘The provinces reserve to themselves all the powers not delegated to the Federal Government by this Constitution, as well as those powers expressly reserved to themselves by special pacts at the m c] v (

Subnational entities are constitutionally authorized to implement programs in health, education, welfare, housing, sanitation policies, and environment (Arretche 2003, 2004; Almeida 1995; Samuels and Mainwaring 2004; Ter-Minassian 1997; Souza 2001, 2005). In fact, most of the consolidated public spending in these areas corresponds to subnational levels. However, the evolution of the decentralization processes that occurred in both countries resulted in subnational governments being in charge of implementation, whereas the federal governments reserved the role of coordinators and setting the general guidelines in those policies. Both constitutions reserve to the federal level traditional functions: defense, foreign affairs, army, economy (control of the money supply and of the financial system), etc.

The 1988 Brazilian constitution “assigns relatively few functions exclusively to each level of government for the vast majority of public expenditures, however, the constitution envisages concurrent responsibilities, to be further specified by a federal law – which so far has not been proposed” (Ter-Minassian 1997:441-2). Argentine federal design allocates to both levels of government most of the competences as concurrent (Art. 75, 18 and Art. 125)¹⁰.

This federal design is similar to the German, Australian and Swiss federations, where “concurrent powers are used extensively” (Thorlakson 2003:9). Those federations have as a common feature that they have relatively few policy fields falling under exclusive state competence. In this respect, all these countries are institutionally more decentralized than other developed federations such as the United States of America or Austria, where constitutions provide fewer concurrent competencies (Thorlakson 2003 and Watts 1999).

TABLE 2: Constitutional Allocation of Competences

	Brazil		Argentina	
Federal	11	61%	8	14%
Concurrent	7	39%	10	56%
	18	100%	18	100%

Source: Own elaboration

Table 2 intends to show the degree of policy decentralization constitutionally provided, taking into account 18 significant and traditional competences. Although this information involves a fair amount of discretion, since “constitutional allocation may mask the underlying reality of power allocation in the state” (Thorlakson 2003:11), it is still useful to highlight the degree of institutional decentralization. This sample shows that the Argentine constitution provides an institutionally more decentralized federation from that envisaged by the Brazilian constitution: 56 percent of 18 competences are concurrent in Argentine federation, compared to 39 percent in Brazil.

Both constitutions also provide another type of competences, those that I have called “shared” competences. In both countries, constitutions provide, as a shared competence, the merge, subdivision or dismember of states, requiring the consent of subnational units involved. Argentina also provides two

¹⁰ The Argentine Supreme Court has stated that, in principle, all competences are concurrent.

number of competencies and authorities to local levels, however if the(n L)6(at)3(in)3(A)11(m)-2(e)0 pper 20

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renationalized the social security system. These percentages align Argentina with other decentralized federations, such as Germany (38) and Switzerland (39) (Swenden 2006:109).

In Brazil, fiscal federalism shows two phases: from 1980 to 1994, where a decentralization process occurred and a second phase from 1994 on, where intergovernmental relations experienced a recentralization process (Soares and Pereira Neiva 2011:97). The first period is characterized by an increase in the share of tax resources and a decentralization of public expenditures in favour of the state and local governments. This process, however, was carried out in an uncoordinated way, characterized by a lack of constitutional and/or institutional mechanisms for cooperation and fiscal accountability (Soares and Pereira Neiva 2011).

The share of public expenditure of states governments began to increase sharply. While in the beginning of the 1980s, state public expenditure share represented 22 percent of the total consolidated public expenditure (considering federal and local levels of government) in 1988 the share began to systematically increase from 27 percent (Soares and Pereira Neiva 2011) to 45 percent in 2003 and 59 percent in 2012, with an average of 47 percent between 1997 and 2012 and 46 percent in the period 2002-2012²⁴. These values place Brazil among the most decentralized federations in the world.

TABLE 12: Subnational Expenditure as percent of Total Country Expenditure

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	AVG
Argentina												
a	40%											

The Brazilian experience was quite similar. In the 1970s, state borrowing increased sharply and in the next decade, with a deepening recession, states experienced a widespread default in 1989 and 1993. The federal government rescheduled states' public debt on a twenty-year period, after lengthy negotiations. In the mid-1990s, states expenditure began to rise again, especially in 1995 when states increased the salary of public employees. Brazilian state behaviour was similar to Argentine provinces. To finance themselves, Brazilian states resorted to payment of suppliers and employees, in arrears short-term borrowing from commercial banks and guarantees for bank borrowing by contractors for state infrastructure projects. States' public debt increased from 2.5 percent of GDP in 1991 to 5.4 percent in 1996. The federal government had to intervene once again, shifting most of the states' debt into federal bonds (Ter-Minassian 1997:451-2).

Rodden (2002) develops two hypotheses that could explain subnational fiscally unruly behaviour. First, if subnational units have access to credit, higher levels of dependence on intergovernmental grants will be associated with larger subnational deficits. Second, this commitment problem should be most pronounced in federal systems, especially when the states are directly and disproportionately represented in the upper legislative chamber (2002:671). Both hypotheses are present in the Argentine and Brazilian cases.

CONCLUDING REMARKS

Based on the analysis of these seven variables it is possible to have a broad idea on the degree of fiscal decentralization in these two traditional Latin-American federations.

Regarding variable 1, both federations constitutionally recognize a large number of competences as concurrent among both levels (or three levels, if we consider municipalities in the analysis), and the bulk of those policies are social in nature. This reveals two things: constituent convention desired a cooperative – rather than a dual – federalism and they wanted to create a subnational-based welfare state. Regarding variable 2, the Argentine constitution is vaguer in defining the fiscal powers of both levels and ultimately, that gap was filled by intergovernmental agreements that result in a centralization of fiscal resources. The Brazilian constitution is more precise and delegates a significant number of taxes to subnational units: 26 percent of Brazilian taxes are subnational, compared to 11 percent in Argentina (Table 3).

When it comes to own resources, Brazil is again more decentralized. Both federations have maintained a regular percentage over the decade, Argentina between 19 percent and 20 percent in the period 2002-2012 and Brazil between 25 percent and 26 percent in the same years (Table 4). As a consequence of that, federal transfers play a more important role in Argentina than in Brazil. Federal transfers have increased in size and importance during the last decade.

Argentine provinces rely more on federal transfers, which cover 59 percent of provincial budgets (Table 7). Brazilian states cover 39 percent of their budgets with central transfers (Table 13). When we add federal transfers, both federations increase the total amount of resources at the subnational units' disposal.

With respect to power the most important variable in measuring subnational autonomy, it is clearly observable that state levels of government have increased their participation in public spending due to the increased allocation of constitutionally recognized powers. In Braziln s15(s. I)17(n B)8(r)-7(a)01 474.-10(r)-7(e)12(a)-10(s

