



RE1-05-007

Economic and Social Study Series

**WHO DECIDES ON
PUBLIC EXPENDITURES?
A POLITICAL ECONOMY ANALYSIS
OF THE BUDGET PROCESS:
THE CASE OF ARGENTINA**



**ARGENTINA
BOLIVIA
BRAZIL
CHILE
PARAGUAY
URUGUAY**

**Emmanuel Abuelafia
Sergio Berenztein
Miguel Braun
Luciano di Gresia**

September 2005

REGION 1

Inter-American Development Bank

This document is not an official publication of the Inter-American Development Bank. The purpose of the Economic and Social Study Series is to provide a mechanism for discussion of selected analytical works related to the development of the country members of the Regional Operations Department I. The opinions and conclusions contained in this document are exclusively those of their authors and do not necessarily reflect the policies and opinions of the Bank's management, the member countries, or the institutions with which the authors are affiliated.

**WHO DECIDES ON PUBLIC EXPENDITURES?
A POLITICAL ECONOMY
ANALYSIS OF THE BUDGET PROCESS:
THE CASE OF ARGENTINA**

Emmanuel Abuelafia
CIPPEC

Sergio Berenztein
Universidad Di Tella

Miguel Braun
CIPPEC

Luciano di Gresia
Universidad Nacional de la Plata

This paper is part of the IDB project “Who decides on public expenditures? A political economy analysis of the budget process”. The authors wish to thank without implicating Carlos Scartascini, Ernesto Stein, Damián Bonari, Gabriel Filc, Pablo Guidotti, Jesús Rodríguez, Alejandro Bonvecchi, Gerardo Uña, Luis Tonelli, Andrés Borensztein and Luis Babino for very helpful comments and discussions. We also thank all the interviewees, who gave generously of their time and knowledge.

Abstract

The budget process is increasingly considered key for reform efforts to improve fiscal outcomes. In this paper we embark on a political economy analysis of the budget process in Argentina, in the spirit of the IDB project “Political Institutions, Policymaking Processes and Policy Outcomes” in order to understand who determines budget outcomes in Argentina. In particular, we seek to characterize the institutional framework that regulates the budget preparation, approval, implementation and control. Furthermore, we identify which actors are involved both formally and informally in the process at each stage, and seek to understand their incentives and interactions.

We find that the President has a *de facto* role that is much more powerful than what the laws and institutions of the budget process stipulate. However, the rigidity of the budget process, together with other constraints such as macroeconomic shocks, fiscal rules, agreements with International Financial Institutions (IFIs) and the influence of other actors such as governors, legislators and lobbies - have limited the ability of the Executive to substantially modify the budget process. Furthermore, compared with the period of high inflation of 1983-1991, in the past decade we have witnessed dramatic improvements in the institutionalization of the budget process, both in political and administrative terms. These reforms have accompanied a strong improvement in fiscal outcomes in the 1990s compared with the 1980s, and provided some of the tools necessary to limit the depth of the recent crisis and regain macroeconomic stability.

Table of Contents

I. Introduction	4
II. The Analytical Framework.....	5
III. Fiscal policy in Argentina: the role of the budget process	9
IV. The formal budget process in Argentina.....	17
V. The actual workings of the budget process	18
Formulation	19
Approval.....	24
Implementation.....	29
Evaluation and control.....	42
VI. The contribution of the budget process to solvency, efficiency and representativeness.....	44
VII. Conclusions and policy recommendations	47
Appendix A: A detailed description of the formal budget process	50
Stage 1: The budget formulation	50
Stage 2: Congressional approval	51
Stage 3: Implementation.....	52
Stage 4: Evaluation and control.....	53
The legal framework behind the Budget process	54
The budget process prior to the LAF	54
References.....	59

Figures

Figure 1: The National Budget 2004.	10
Figure 2: Primary and overall budget surplus (% of GDP), 1961-2003.....	12
Figure 3: Changes over time in the degree of discretionality of spending.....	15
Figure 4: Relationship between discretionally and GDP growth.....	16
Figure 5: A simple presentation of the Argentine Budget Process.....	17
Figure 6: Forecasted and collected revenues. 1995-2003.	19
Figure 7: Changes introduced by Congress to the Executive budget proposal.....	26

Figure 8: Changes in the composition of spending by stage (1995-2003	29
Figure 9: Changes in the composition of spending by stage (1995-2001)	29
Figure 10: Changes between budget law and actual budget, 1995-2003.....	30
Figure 11: Degree of underexecution of the budget in the implementation phase	31
Figure 12: Changes in total spending, budget law and executed budget	31
Figure 13: Changes between the Bill and the Budget Law. Weighted by discretionality index.....	32
Figure 14: Changes between the Budget Law and the executed budget. Weighted by discretionality index.	32
Figure 15: Net Fiscal Benefit by provinces, 2002 (pesos per capita).....	45
Figure 16: Population per representative (underrepresentation) as an explanation for the distribution of the Net Fiscal Benefit per province.	46

Tables

Table 1: 2004 Budget. Expenditure classified by its rigidity	21
Table 2: The legislative approval process, 1995-2003.....	26
Table 3: Degree of budget execution by type of expenditure, 1995-2003.....	33
Table 4: Regression results for bureaucratic learning	36
Table 5: Legal Instruments that created the fiduciary funds and entities	39
Table 6: Fiduciary Funds dates of creation and 2005 budget.....	39
Table 7: Robust OLS regression of NFB as Dependent Variable.....	46

I. INTRODUCTION

The recent crisis of 2001-2002 has left Argentina with a fragile fiscal outlook over the medium run, with a debt expected to be significantly above its pre-crisis level of 56% of GDP even after a successful renegotiation with holders of defaulted bonds. Given Argentina's history of fiscal profligacy – including two hyperinflations in 1989 and 1991 –, achieving the primary surpluses necessary to service this debt without compromising key aspects of government spending such as social policy will be a significant challenge. Furthermore, there is increasing awareness of inefficiency and inequality in budget allocations¹. Overall, the sustainability, representativeness and efficiency² of Argentine fiscal outcomes are clearly in question.

Fiscal rules, and in particular, the procedural rules regulating the budget process, are increasingly considered as a relevant part of reform efforts to improve fiscal outcomes³. However, it is not clear precisely which rules have to be changed, how, and to what effect. To contribute to the understanding of the role of budget institutions, in this paper we embark on a political economy analysis of the budget process in Argentina, in the spirit of the IDB project “Political Institutions, Policymaking Processes and Policy Outcomes”⁴ in order to understand who determines budget outcomes in Argentina. In particular, we seek to characterize the institutional framework that regulates the budget preparation, approval, implementation and control. Furthermore, we identify which actors are involved both formally and informally in the process at each stage, and seek to understand their incentives and interactions. This understanding should help to determine the extent to which the current institutions of the budget process contribute to or mitigate the country's fiscal policy problems, and thus serve as a valuable input in the effort to improve fiscal institutions and outcomes in Argentina. We focus our analysis mainly on the period 1995-2003 due to data availability, but also contrast this period with previous experiences.

Our main finding is that the Executive power, and in particular the President, has a de facto role that is much more powerful than what the laws and institutions of the budget process stipulate. However, it is important noticing that the budget is not the main arena for political bargaining. During the last decade, the negotiations – particularly with the provinces– had taken place outside the budget process, i.e. by the creation of fiduciary funds that are not included in the budget. The rigidity of the budget, together with other constraints such as the strength of some recent macroeconomic shocks - and to a lesser degree, fiscal rules, agreements with International Financial Institutions (IFIs) and the influence of the federal system and other actors such as governors, legislators and lobbies - have limited the ability of the Executive to substantially modify the budget and to use it for political bargaining. Furthermore, compared with the period of high inflation of 1983-1991, in the past decade we have witnessed dramatic improvements in the institutionalization of the budget process, both in political and administrative terms. These reforms have accompanied a strong improvement in fiscal outcomes in the 1990s compared with the 1980s, and provided some of the tools necessary to limit the depth of the recent crisis and regain macroeconomic stability.

¹ For example, recent news articles in major newspapers (eg: cover store in *La Nación*, 24/04/2004) reflected doubts regarding the extent to which social spending actually reached beneficiaries.

² Sustainability refers to intertemporal fiscal solvency, efficiency refers to the traditional measure of equating the marginal social benefit of public spending across state activities, and representativeness refers to the extent to which budgetary outcomes satisfy overall social preferences rather than particular group preferences.

³ See for instance, *Kopits (2004)*.

⁴ See *Spiller, Stein and Tommasi (2003)* and *Scartascini and Olivera (2003)*.

The paper is organized as follows: in Section II we present the analytical framework with which we study the budget, and also discuss some relevant literature on the Argentine budget process. In Section III we outline the political and economic environment in which the budget process has evolved, with particular attention to fiscal policy reforms and outcomes. In Section IV we present an outline of the formal rules of the budget process. In Section V, we present an analysis of the actual workings of the budget process, and in Section VI we relate our results on the workings of the budget process to fiscal policy outcomes. Finally, Section VII concludes.

II. THE ANALYTICAL FRAMEWORK

Fiscal discipline is a key element of macroeconomic stability. Therefore, it is difficult to explain why fiscal outcomes across countries and over time vary so much relying on the explanatory power of purely economic causes. Increasingly, economists have turned to political causes as explanatory variables. A “first generation” of political economy explanations, illustrated for instance by Alesina and Perotti (1995), argue that conventional economic arguments are unsatisfactory to explain the growing disparity observed in fiscal performance in OECD countries in the 1970s and 1980s. These countries basically share a similar economic structure and face similar economic shocks. However, some countries such as the US and the UK followed a stable debt path, whereas others such as Italy and Belgium saw skyrocketing debt/GDP ratios and high fiscal deficits during this period. They show that differences in fiscal institutions such as budget procedures can help explain the differences in fiscal outcomes.

The political problems identified in this literature as underlying poor macroeconomic and fiscal behavior could be summarized in two categories: principal-agent problems and cooperation problems⁵. By principal-agent we refer to the relation between the citizens and their elected representatives. Imprudent fiscal behavior is often the result of actions taken by public officers who are not maximizing the welfare of their constituencies. These problems are compounded by excessive discretion by officials, and by lack of adequate transparency and accountability. If it were possible to limit policymakers’ discretion by “contracting” clear rules, then principal-agent problems would be limited. Furthermore, adequate transparency and accountability would allow voters to monitor and control their representatives more effectively.

By cooperation problems we refer to the game played by multiple sub-national and national political actors that maximize objectives that, to some extent, include the welfare of their electors. A classic example of cooperation problems is the well-known common pool problem. Weingast, Shepsle and Johnsen (1981) for example, show how public expenditure can increase due to the common pool problem inherent in the political interaction between regions represented in Congress. Congressmen have an incentive to propose spending increases that accrue to their region, because resources are collected from the entire country, and thus the marginal benefit of an extra dollar of local spending is positive. Velasco (1999) illustrates how the common pool problem operates in a dynamic setting, resulting not only in higher spending, but also in higher deficits and debt accumulation.

Common pool and principal-agent problems with fiscal policy can vary across countries and over time due to variations in the underlying incentives faced by key players in the fiscal game. For example, Alesina and Perotti (1996) argue that more hierarchical budget processes, that give

⁵ See, for instance, Tommasi (1998) and Von Hagen (2002) for surveys.

more power to the finance minister vis a vis the spending ministers in the budget design phase, tend to reduce the common pool problem, because the finance minister internalizes the government's intertemporal budget constraint more than other ministers. In the Argentine case, several authors have identified federal fiscal arrangements, budget procedures and fiscal rules as among the most important fiscal institutions that contribute to fiscal policy problems⁶. These problems go beyond fiscal sustainability, and extend to issues of efficiency and representativeness of public spending. . A serious principal-agent problem will result in policymakers extracting rents, and allocating funds to inefficient and particularistic projects. Common pool problems result in resources being allocated according to the capacity of different groups to extract rents, rather than maximizing social welfare.

This literature then recommends analyzing the extent to which different budget procedures enhance or mitigate principal-agent and common pool problems so as to improve sustainability, efficiency and representativeness of fiscal policy. However, it is often difficult to find convincing empirical evidence on the effect of fiscal rules on fiscal policy outcomes. Braun and Tommasi (2004) argue that changes in fiscal rules are not common at the national level, and when they occur, they are often accompanied by other reforms (financial liberalization, privatization, etc) that affect fiscal outcomes. This limits the explanatory potential of within-country time-series regressions and of cross-country regressions, because a study that finds a correlation between fiscal rules and prudent fiscal outcomes without controlling for other reforms would be biased. A related limitation on studies on the effectiveness of budget institutions is given by the question of origin of rules. If these rules reflect voters' preference for fiscal rules, and at the same time, voters desire fiscal austerity, then any study finding a correlation between rules and outcomes would be contaminated by omitted variable bias. The academic literature on the effectiveness of fiscal rules has attempted to deal with these complex identification issues, but the results are as yet inconclusive.

A more recent literature, which we call "second generation" political economy, places more emphasis on explanations related to the features of the policymaking process that determine policy outcomes. Spiller, Stein and Tommasi (2003) state that the capacity to sustain intertemporal commitments, the quality of implementation and the stability and credibility of policies are all influenced by the characteristics of the policymaking process and those of the political process in each country. The political process is conditioned by the incentives and constraints facing the key political actors. These, in turn, are shaped by the country's political institutions. This new literature proposes a deeper, more country-specific approach to analyze the effects of the budget process on fiscal outcomes.

The authors propose a framework to analyze the impact of political institutions on public policy. They present a theory that links the features of public policies to the institutional capacity to enforce cooperative intertemporal political exchange. Under this framework, public policies are considered as the outcome of the intertemporal transactions among political actors. Additionally, the transactions are conditioned by the rules of the game and by political institutions. Therefore outcomes depend to some degree on some basic institutional features of the country such as its constitution, its governmental organization and its history.

⁶ See Braun (2003) for a recent survey.

The main idea of this theory is that important features of public policies will depend on the ability of political actors to achieve cooperative outcomes. The negotiation among actors can be analyzed as a repeated oligopoly game. Then, the likelihood of existence of a cooperative equilibrium increases if: i) the number of key political actors is small, ii) those actors have strong intertemporal linkages, iii) policy and political moves are widely observable, iv) good enforcement technologies are available, v) key political exchange takes place in well behaved arenas and vi) the short run payoff from non cooperation are not too high.

As Spiller and Tommasi (2003) point out, the Argentine political negotiation environment is far from ideal. Legislators have a high rotation and low tenure rates, which generates few incentives to specialize, or to acquire specific policy or legislative expertise. Governors and local party bosses are highly influential on legislative careers. Therefore, many key political transactions are made at the level of provincial party leaders. Furthermore, there is a lack of an independent bureaucracy that could serve as an enforcement mechanism of intertemporal political agreements. Finally, the Argentine Supreme Court has not been an important enforcer of political agreements. This environment leads to deficient policies in Argentina, in terms of instability, lack of coordination – between different levels of government and across ministries – and lack of cooperation among key actors. In turn, these aspects of policies are central in explaining Argentina's poor outcomes in terms of development, since policy instability leads to lack of credibility and economic volatility, which in turn lead to low investment and growth.

The authors argue that the difficulty to strike long-term political deals is caused by the institutional legacy of political and economic instability suffered between 1930 and 1983 – a period in which 12 presidents were removed by force -, and the institutional characteristics defined by the country's constitutional structure and its electoral rules.

Political instability has led to short planning horizons and myopic behavior by policymakers and interest groups. Furthermore, the short horizons of upper political leaders has led to a high rotation in the bureaucracy, which has left the country with weak cooperation and coordination mechanisms across agencies and levels of government, together with a lack of a stable and professional civil service. In addition, presidents have tended to replace Supreme Court justices, leading to a weak judiciary, with low capability of limiting political decisions.

In turn, the specific nature of electoral rules, federalism and the constitutional structure have conspired to weaken the arenas for intertemporal political transactions. In particular, Congress has been rendered practically ineffective by the combination of the electoral system and strong presidential powers. The electoral system gives provincial party elites – mainly provincial governors - ample powers to appoint and remove candidates for Congress. This leads to a high rotation of legislators, giving them low incentives to invest in the legislative career, and thus low incentives to develop congressional capacity for policy analysis and oversight. Furthermore, the President has ample legislative initiative – as reflected for example by the regular use of decrees (Decretos de Necesidad y Urgencia) to make policy. The bottom line is that Congress is not the arena in which political deals are made. Rather, these are made in informal arenas by the President, provincial governors and interest groups. However, these deals are short-lived and

unstable, because they lack the enforcement provided by formal political agreements⁷, by an independent bureaucracy capable of implementing them, or a judiciary able to enforce them.

Regarding the budget process, the main hypotheses that emerge from the work of Spiller and Tommasi are that

- we should expect the President to have strong capabilities to implement his desired budget decisions vis a vis Congress;
- provincial governors are powerful informal actors, despite not having a formal role in the budget process;
- The bureaucracy that implements the budget suffers from high rotation, low capacity, and therefore lacks the ability to effectively implement political agreements;
- As in other areas of policy in Argentina, we should expect to observe instability in budget outcomes, in terms of fiscal results and budget allocations across programs.

Not much work has been done on the political economy of the budget process in Argentina. Two exceptions are Jones (2001) and Rodriguez and Bonvecchi (2004), who study the role of Congress in the budget process, and arrive at radically different conclusions. On one hand, Jones claims that Congress has an important role in the budget process. He argues that the smooth passage of the budget proposal sent by the Executive branch to Congress is not evidence of Congress' lack of power in the process. Rather, he argues that the Peronist party is a disciplined party that had a congressional majority during most of the 1990s, that negotiations between legislators and the Executive take place in the formulation stage of the budget, and that the Peronist majority allows these deals to be enforced in Congress with a swift passage. He shows that during the Menem government, the percentage of federal transfers that goes to a province is positively correlated with the percentage of the president's party legislative bloc that comes from that province. Jones claims that this is evidence of the power that (peronist) legislators wield in the budget process.

On the other hand, Rodriguez and Bonvecchi (2004) study the role of Congress in the budget process, and they find that it has been systematically weak over the past 20 years. They divide the period into three stages, defined by differences in the macroeconomic context and in the cohesiveness of the party system, and find that in periods of high macroeconomic instability (1984-1991 and 1996-2004) Congress plays a merely validating role of the Executive's decisions. In periods of economic expansion (1991-1995), Congress plays a marginally expansive role, adding some items of pork to the Executive proposal.

In the analysis presented below, we reconcile these two points of view. We argue that the evaluation of the role of Congress in the budget process depends on the universe of public expenditure that one analyzes. If we look strictly at the federal budget process – the universe studied in this paper –, without including coparticipation and other transfers to provinces that are earmarked and therefore not voted on in each year's budget, then we would have to agree with Rodriguez and Bonvecchi. The role of Congress is very limited, and in fact, most changes to the

⁷ For instance, Aninat, Longregan, Navia and Vial (2004) argue that in the case of Chile, the ability of veto players to block reforms in congress imply that once a law is passed, it is unlikely that it will be reversed, providing stability to political decisions that pass through congress.

budget are made during the implementation phase controlled by the Executive, so agreements made in Congress are not necessarily sustainable. However, when we analyze the sum of all transfers to provinces, we indeed find that provinces with fewer inhabitants per legislator – i.e. provinces that are over-represented in Congress – receive more transfers per capita. This reflects the political power of local party bosses – especially governors – who are capable of trading their votes in Congress in exchange for a larger share in the allocation of funds to provinces⁸. These negotiations do not occur in the arena of the federal budget process. In fact, most interviewees argued that governors were not significant actors in the federal budget process, despite being key actors in policymaking in general.

An important corollary is that the budget process is really the arena where society reflects and implements its decisions to allocate the resources collected each year through the tax system. We emphasize the term “reflects”, as opposed to “decides”, because many of the expenditures present in national budgets arise from past decisions and agreements by policymakers. For example, social security payments and debt payments reflect past decisions regarding the pension system and the accumulation of past fiscal deficits. Although in theory these and other previous decisions can be modified during the budget process, in practice many budget items are rigid. In the next section we analyze this issue in more depth.

III. FISCAL POLICY IN ARGENTINA: THE ROLE OF THE BUDGET PROCESS

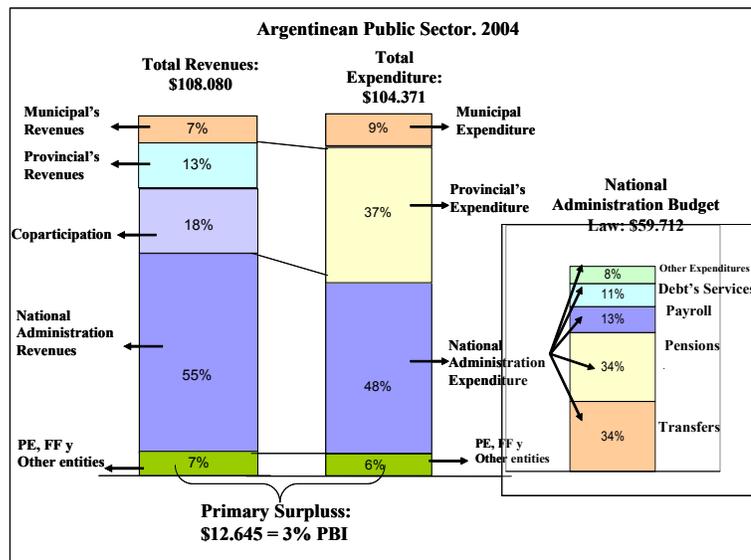
Before describing how the budget process actually works in Argentina and therefore who decides on public expenditures, we discuss *what* is actually decided in the budget process. We first show that the federal budget process is only a fraction – although an important one at that – of total public spending in Argentina. Then we briefly describe some of the highlights regarding fiscal policy reforms and outcomes in the last 15 years, and show that many of these reforms were decisions outside the formal budget process.⁹

First, it is important to understand that the national budget process accounts for only a fraction of overall public resources. Argentina is a federal country, with a very centralized tax structure and a very decentralized allocation of spending responsibilities. In 2003, the federal government collected 81% of total tax revenues, but spent only 53% of total expenditures. \$25,335 bn, or 5.85% of GDP was transferred automatically by the federal government to the provinces by a tax-sharing system called “coparticipación”, and other automatic transfers. The result is that of the total public spending done in Argentina by the Federal Government the provinces and the municipalities, the federal budget process only accounts for 48%. In Figure 1 we show the percentage of total aggregate revenues and spending that actually passed through the federal budget process in 2004.

⁸ Tommasi and Spiller (2004) and Jones, Saieg, Spiller and Tommasi (2001) show that the electoral system for Congress gives large power over who gets nominated to local party bosses, and thus imposes loyalty and discipline on legislators, whose votes can be exchanged in negotiations between the provinces and the executive.

⁹ For a complete description of fiscal policy during the 1990s, see Cetrángolo and Jimenez (2003). Here we only mention reforms related to the main fiscal policy aggregates that help us put into context the role of the budget process.

Figure 1: The National Budget 2004.



Source: Informe de Presupuesto 2004., CIPPEC.

As we argued in the previous section, this distinction helps reconcile the different positions regarding the power of Congress in the budget process held by Jones (2001) on one hand and Rodriguez and Bonvecchi (2004) on the other. Jones is really talking about the transfers between the federal government and the provinces, whereas Bonvecchi and Rodriguez are talking about the funds allocated in the national budget process. Since coparticipation funds – the bulk of transfers to provinces – are decided by a law outside of the budget process that has to be approved by all 24 provinces, clearly provincial governors are able to extract more rents the more legislators their province has. This explains the results found by Jones (2001). At the same time, when we restrict attention to the federal budget process, we will show that Congress is less important, since the Executive has several mechanisms to bypass legislative interference with the budget.

We now turn to a brief description of the main fiscal policy reforms and outcomes in the recent past. Following the hyperinflation in 1989, Carlos Menem was elected president in 1989, and the first part of his administration was characterized by various attempts to control inflation. The depth of the economic crisis had created an unusual opportunity for audacious, orthodox reforms in line with the international recommendations crystallized in the “Washington Consensus”. Indeed, an ambitious program of structural reforms was implemented during the first part of the 1990s that was supported by a large, ambiguous and plural coalition (both political and electoral), and that brought about a remarkable performance in terms of growth, increased productivity, and direct foreign investment. After a couple of unsuccessful stabilization attempts, Domingo Cavallo was appointed Finance Minister in 1991, and implemented a strict currency board arrangement known as the Convertibility Law. This law pegged the value of one Argentine peso to one dollar, and called for 100% reserve backing for the monetary base. This arrangement implied that fiscal discipline was a necessary ingredient of the macroeconomic program, since the traditional resort to inflationary finance of deficits was no longer a policy option. This led to several efforts to improve fiscal outcomes, such as a tax reform focused on increasing VAT and

income tax collection, a massive privatization program, a reform of the pension system to improve long-term fiscal solvency, several fiscal pacts with the provinces, and the implementation of an ambitious reform in the federal budget process known as the Ley de Administración Financiera (LAF) (see next section, Box 1 , and Appendix A for more details on this reform).

Box 1: The reform of the federal budget process as a tool of fiscal discipline

Although we will discuss the budget process at length in the next sections, it is pertinent here to discuss the reform of the budget process that was implemented in the early 1990s as part of the reform process. The economic context in 1991 was alarming. In the midst of depression and hyperinflation, the 1990 and 1991 budgets had not yet been approved by Congress. Years of three-digit inflation had left the budget process in a shambles. The last budget that was submitted to Congress within the dates established by law was in 1966, and the last approved by Congress before the beginning of the fiscal year was in 1954 (Makon, (1998)). The budget was not used as a tool for public policy formulation and the accounting system was not integrated with other governmental activities. It was not regulated by a unique norm. Rather, the Ley de Contabilidad (Accounting Law) – from the 50s – was complemented in some important areas by the Ley Complementaria Permanente de Presupuesto (Complementary Budget law). Additionally, the lack of institutional capacity in the key areas of the budget was a characteristic of the system, with the President lacking a clear picture of actual spending and revenues, and thus the ability to control fiscal policy.

As mentioned above, one of the key features of the economic reforms of the early 1990s was the need for fiscal discipline. Thus, the Executive embarked on a program of reform of the administrative processes of the state, including the reformulation of the budget process, so as to increase control over public expenditures. This reform was welcomed and supported financially by the IFIs. Makon (1998) highlights that this reform was a necessary condition for the success of the new economic policy.

The first activity of the process was to formulate the reform's objectives and to explain them to the Executive's members involved with the aim of reestablishing the budget culture within the bureaucracy. Secondly, the Ministry of Economy prepared the financial administration law proposal because the legal framework represented an important constraint to the reform process and some areas did not have any regulatory norm at all. After the proposal was approved, the first stage of the process was to develop a financial information system centralized in the Secretaria de Hacienda. The objective of this system was to obtain accurate information for policy and resource allocation decisions. The second stage was the reformulation of the human resource management, and the instauration of the Sistema Nacional de Profesión Administrativa scheme. The third and the fourth were related to the payments and public credit systems.

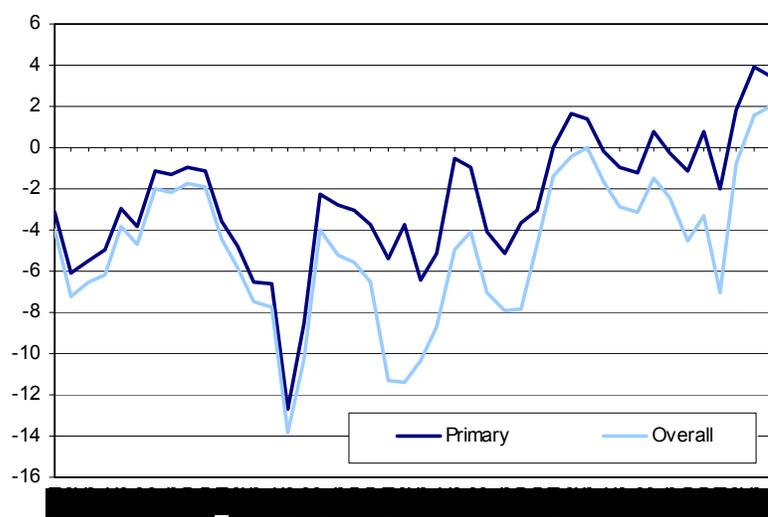
The strategy adopted by the reformers was to guarantee the political support necessary for a successful reform. The early instauration of the financial information system was the main activity to maintain political support. This system provided the Executive with the information required for the fiscal adjustment process, and was therefore instrumental in increasing the credibility of the Convertibility plan.

The nature of the process by which the LAF was created calls into question the arguments of the political economy literature presented in the previous section, by which more hierarchical budget procedures contribute to fiscal solvency. In the case of Argentina, the government was

committed to fiscal solvency, and therefore decided to reform the budget process, together with other reforms. The correlation between improved fiscal outcomes and a better budget process is really due in this case to fiscal solvency being a government priority.

As a matter of fact, fiscal outcomes improved substantially during the 1990s, compared with Argentina's history of fiscal profligacy (see Figure 2). Thanks to strong economic growth, stable prices (which reverted the loss of revenues produced by the Olivera-Tanzi effect under high inflation) and revenues from a massive privatization program, the country ran a primary budget surplus for the first time in at least 30 years in 1992. Throughout the decade, the primary balance averaged 0.29% of GDP, compared with - 3.08% in the 1980s. The overall budget balance was -2.34, against -7.83% in the 1980s.

Figure 2: Primary and overall budget surplus (% of GDP), 1961-2003.



Source: Ministry of Economy (2004)

Despite this dramatic improvement in the long run fiscal performance, fiscal outcomes worsened starting in 1994. The main culprits were the rapid growth of interest payments, the costly privatization of the pension system and the increase in provincial spending (see Cetrángolo and Jimenez (2003) for a detailed account of fiscal policy in the 1990s). Growing interest payments account for the widening gap between the primary and overall budget balance observed in Figure 2 after 1995. The reform of the pension system generated a deficit that grew from about 1% of GDP in 1993 to an average of well over 3% of GDP in 1996-2001. This deficit arose because of the well-known transition cost involved in converting a pay-as-you-go pension system into a system of private accounts: the public system lost revenues to the newly created private pension administrators, but still had to pay for current pensioners who did not have retirement accounts. Provincial spending grew at a rate of over 5% per year in real terms between 1991 and 1999.

Starting in 1995 with the Mexican crisis, Argentina suffered the consequences of a series of international financial crises, which undermined investor confidence in emerging markets, and particularly in those with fixed exchange rate regimes. The “sudden stop” (Calvo et al , 2002) of capital inflows contributed to a recession starting in 1998. Moreover, the Brazilian devaluation in

1999 further deteriorated the economic environment and expectations, as the Argentine currency overvalued vis a vis the country's principal trading partner. Furthermore, Argentina lost competitiveness elsewhere as a direct consequence of the US dollar appreciation. This combination of factors made the fixed exchange rate unsustainable. As credibility in the peso eroded, a bank run forced the government to forbid the withdrawal of money from the banks in late 2001, causing violent protests in the streets of Buenos Aires, and ultimately ending with the resignation of President De la Rúa from the Alianza government that had succeeded Carlos Menem, the collapse of the Convertibility regime and the largest default of sovereign debt in history.

In the aftermath of the crisis, there has been a significant improvement in the short-term government budget balance, together with a significant increase in the debt/GDP ratio, despite the significant reduction in the dollar value of the debt following the default and renegotiation. The short-term budget balance increased significantly due to the sharp increase in revenues from export duties following the devaluation of the peso, and due to the increase in nominal revenues due to inflation and growth, together with lower increases in nominal expenditures. (in fact, a reduction in real government wages and pensions). As shown in Figure 2, there was a record primary surplus of almost 4% of GDP in 2003. However, the debt burden is higher than before the crisis, due to an increase in debt resulting from the bailout of the financial system, and because of a reduction in the dollar value of GDP following the devaluation.

Some analysts¹⁰ argue that strong fiscal surpluses during the years of high growth in the 1990s could have averted the crisis, and that therefore, the fiscal stance was incompatible with a currency board in a small open economy subject to a volatile international context. Others answer that the magnitude of the shocks suffered by Argentina could not have been averted even with more prudent fiscal policy, and that fiscal policy was not that bad¹¹.

Although the goal of this paper is not to resolve this dispute, we do believe that a relevant question that arises from this discussion is the extent to which the budget process enhanced or mitigated fiscal problems in Argentina. First a caveat. We showed that the federal budget process accounts for only a fraction of total public spending in Argentina. Furthermore, it is worth noting that the three items of spending identified by Cetrángolo and Jimenez (2003) as the culprits that account for a significant proportion of the fiscal imbalances that occurred starting in 1994 are actually outside the federal budget process. Interest payments are exogenous to the present year budget – they are partially determined in the bond and debt contracts and reflect previous years' deficits and reforms introduced. The pension reform was passed by law, and the annual budget simply reflects the revenues and expenditures of the pension system as it stands. Finally, provincial spending is decided by provincial governments. This observation is consistent with the idea that the federal budget simply reflects the monetary implications of decisions made in other arenas, and could lead one to argue that the budget process is of limited importance to understanding fiscal outcomes in Argentina.

This line of reasoning would lead us to argue that the budget process is not very relevant as a determinant of fiscal outcomes in Argentina, and therefore reforms to budget institutions are not important to achieve sustainability, efficiency and representativeness in fiscal policy. Although

¹⁰ *Mussa(2002) and Fanelli and Heymann (2002)*

¹¹ *Hausman and Velasco (2002) and Cabro, Izquierdo and Tabi (2002).*

we find some merit with this point of view (see for instance Braun and Tommasi (2004) for a skeptical look at fiscal rules in Latin America), we will show that there are still important decisions regarding the allocation of resources that are made in the federal budget process, and that political actors and lobbies aim to exert influence regarding these decisions. To explore this question more formally, we now turn to an econometric analysis of the degree of exogeneity of spending decisions in the federal budget process in Argentina.

The degree of exogeneity of public spending in Argentina

The discussion presented above can be framed as a more general question. To what extent do governments actually decide on public expenditures? Are changes in spending simply exogenous or automatic responses to shocks? To study this issue formally, we develop a simple methodology¹². For each finality and function of spending, we estimate the following model using OLS:

$$[1] \quad dS_{it} = \beta_0 + \beta_1 dS_{i(t-1)} + \beta_2 dGDP_t + \beta_3 dPOP_t + \beta_4 dPRI_t + \beta_5 dEMP_t \\ + \beta_6 dDEB_t + w_t (1 + \beta_7 dGDP_t + \beta_8 dPRI_t) + u_{it}$$

Where

- dS_{it} is the change in spending on item i in year t with respect to year $t-1$. Spending is measured in real terms, and each item is determined by the government's classification of expenditure by objective and function¹³. The only excluded item is debt payments, which we consider exogenous to the present year budget process. (source: Dirección de Gastos Sociales Consolidados - Secretaría de Política Económica).
- $dGDP_t$ is the real change in GDP in year t vs $t-1$.
- $dPOP_t$ is the change in population. The data is constructed by interpolation of census data.
- $dPRI_t$ are the wholesale and retail inflation rates.
- $dEMP_t$ is the change in the unemployment rate. (source: Encuesta Permanente de Hogares).
- $dDEB_t$ is the real change in debt service payments.
- w_t is a dummy variable that takes the value of 1 for the period 1980-1991, and zero for the period 1992-2003. It is included to allow for the possibility of structural break in the model after the implementation of the convertibility regime.

The specification is in first differences to confront the presence of non stationary in the dependent variable. The same information set was used for the independent variables in each regression.

¹² See Blanchard (1990) and Alesina and Ardagna (1998) for a discussion of problems with determining the exogeneity of fiscal policy changes and a proposed methodology.

¹³ The Objective and Function Classification is presented according to the nature of the services that public agencies offer to the community. It allow to determine the general objective and the action through which they are projected to be accomplished.

The vector of fitted values of \hat{dS}_{it} that we obtain for each spending item can be considered as the “exogenous” change in spending that occurs in response to changes in the independent variables. We consider observed deviations from these fitted values as a proxy for the level of discretionality in that item of spending.

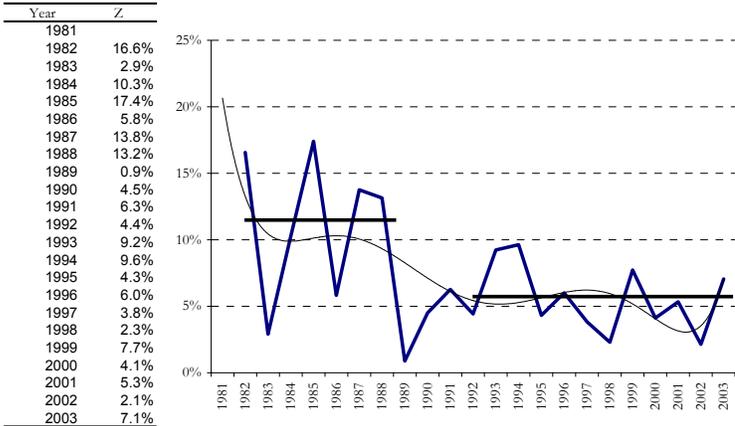
If we define Z_{it} as the absolute value of the residuals from regression [1], normalized by the level of spending in each item, i.e.

$$[2] \quad Z_{it} = \text{Abs}(u_{it}) / S_{it}$$

Then the average of the Z s for an item of spending gives us an idea of the magnitude of deviations with respect to its exogenous trend. We can then compare the average Z for different spending items, and thus compare the level of political discretionality that governments actually exercise in different spending items. We can also average the Z s for a specific year, and compare the evolution of average discretionality over time.

We apply this model to data for the 1980-2003 period. Our main finding, illustrated in Figure 3, is that there was a significant reduction in the discretionality of spending following the implementation of the Convertibility regime and the Ley de Administración Financiera. Whereas the pre-1991 average was above 10% of spending, the post-1992 average was closer to 5%.

Figure 3: Changes over time in the degree of discretionality of spending.



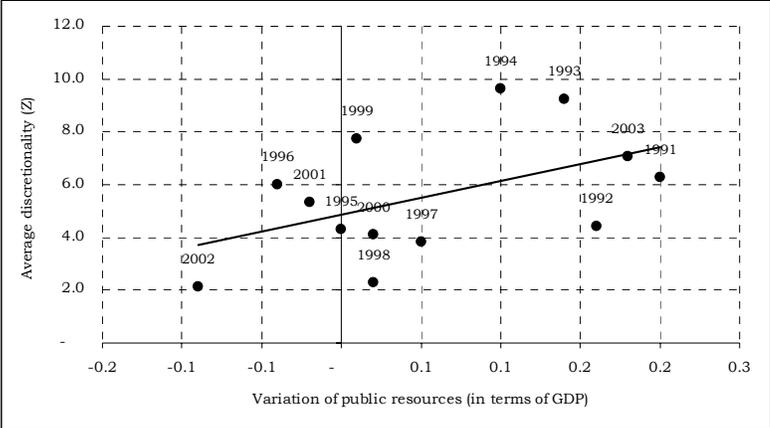
Source: authors' elaboration

The observed reduction in discretionality is probably related to the privatization process and the reduction of inflation, which hardened the government budget constraint, and thus limited the degree of changes in spending that could be implemented¹⁴. We also hypothesize that the reform of the federal budget process with the implementation of the Ley de Administración Financiera contributed to reducing discretionality by improving the organization of public spending.

¹⁴Also, during these years, the secondary education service and few remaining national hospitals were transferred to the province. The decentralization process implied a decrease in the expenditure allocated to basic education from 3% to 0,5% of total expenditure between 1991 and 1995. It is relatively low in comparison with the budgetary impact of the privatization of the public enterprise. In this case, the expenditure decreased from 14% to 7% of the total expenditure.

Another aspect of interest is to test the hypothesis that discretionality increases when tax revenues increase. The idea is that spending is rigid and incremental, and therefore last year's budget is a good proxy for what this year's budget will look like. Therefore, when tax revenues increase, the government has the possibility to allocate the additional funds at will, thus increasing the observed discretionality. We do in fact find a positive correlation between discretionality and increases in tax revenues (as a % of GDP). A 1% increase in tax revenues in terms of GDP is associated with a 1.8% increase in discretionality. (Figure 4)

Figure 4: Relationship between discretionally and GDP growth



Source: authors' elaboration

Recent public discussions regarding the 2003 and 2004 budgets have focused on the excessive power of the President, and the discretionary nature of spending. Since these years have witnessed large increases in tax revenues, our results show that an increase in discretionality should not be surprising.

Regarding the discretionality observed across spending items, we find that spending in justice, defense, education, health, social services and social security tends to have a low degree of discretionality, averaging close to 5% for the whole period. On the other hand, we find a large degree of discretionality – above 20%, and up to 100% for the case of housing - of spending in housing, water and sewers and investment spending (energy, fuel, mining, industry and services).

The point of this discussion is to show that federal public spending has a high degree of rigidity and exogeneity¹⁵, and that therefore, when we talk about “who decides on public expenditures” in the context of the federal budget process, we are talking about who decides on the allocation of the discretionary fraction of public spending that passes through the budget process. Those items outside the budget process such as transfers to provinces via coparticipation, those items determined by other laws such as the pension system, and those items that are rigid or respond to exogenous changes in the economic environment are not part of what is decided. This is the precise meaning of what we mentioned in Section II: to a large degree, the budget is a reflection of past decisions and agreements, rather than the arena where these decisions are made.

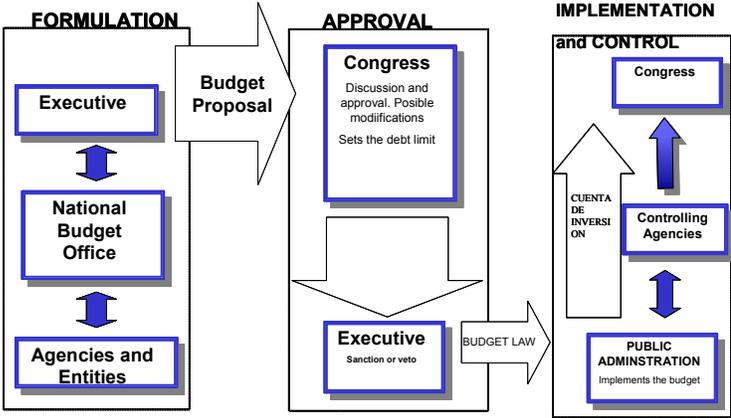
¹⁵ Other authors, such as Schick (2003) and DNGSC (2000) have studied the rigidity of the budget, using an ex-ante criterion. That is, they focus on the degree to which different spending items are predetermined by law. We argue that in an unstable macroeconomic context such as Argentina, in which the real value of legally mandated items such as wages can change drastically, our ex-post analysis adds valuable information. In Section V we present some information on ex-ante rigidity.

Having made this point, we now turn to an analysis of the federal budget process itself, and will come back to the discussion regarding the relevance of budget institutions for fiscal outcomes in our conclusions.

IV. THE FORMAL BUDGET PROCESS IN ARGENTINA

The budget process in Argentina consists of four stages that involve several activities, negotiations and actors. The first stage is the formulation of the Executive power’s budget proposal, the second is congressional discussion of the proposal and approval of the budget law, the third its implementation and the fourth its evaluation and control. In this section, we present a brief description of these stages, focusing on the formal aspects of the process. The dimensions to be considered are the different components, the actors and the negotiations involved and the important dates of the process. In Figure 5, we show a simple outline of the different stages mentioned above.

Figure 5: A simple presentation of the Argentine Budget Process.



Source: authors’ elaboration

The main actors contemplated by the rules that guide the formal budget process are the Executive branch – especially the President, the Chief of Cabinet and the Ministry of Economy - and Congress. Let us now analyze their role in the different stages of the process

In a nutshell, the Executive, at the formulation stage, decides the aggregate budgetary policy and distributes the expenditure ceilings among the agencies. It submits to Congress the main guidelines of the budget in June and the budget proposal in September. The line ministries allocate the resources they receive among programs and formulate the *anteproyectos* (preliminary budget proposals). At the approval stage, it submits the proposal, replies to enquiries (oral or written) formulated by the Comisión de Presupuesto y Hacienda (budget committee) in Congress. After Congress approves the budget, it can introduce line item vetoes to the budget. At the implementation stage, the Executive distributes the expenditure authorizations among agencies, and introduces modifications to the project. It cannot introduce modifications that alter the total expenditure and the debt level. The agencies’ heads distribute the quotas among the programs and they are responsible to keep record of the physical execution. The Chief of Cabinet is responsible of providing information regarding budget execution to Congress. At the control stage, the SIGEN (that depends on the Executive) coordinates the internal auditing activities and

procedures, and the internal auditing units (that depend on the line ministries) perform the internal audits.

At the formulation stage, the Ministry of Economy sets the budget priorities and defines the investment programs, prepares macroeconomic forecasts, and provides support in the definition of expenditure ceiling setting. The National Budget Office (ONP), the ruling authority of the process, evaluates the anteproyectos prepared by the agencies and puts together the aggregate proposal. At the implementation stage, it administrates the quota system (that regulates the pace of execution of the budget) and prepares the execution reports that are submitted by the Executive to Congress.

At the formulation stage, Congress only receives information about the general guidelines of the budget proposal. At the approval stage, it evaluates, through the Comisión de Presupuesto y Hacienda of both chambers, the budget proposal. It can summon members of the Executive to discuss the issues it finds relevant. It is empowered to approve or reject the budget proposal, to introduce modifications and to remove articles. If the Executive uses its veto power, Congress can overrule the vetoes with a 2/3 majority. At the implementation stage, Congress is the only institution that can modify total expenditure, the debt level and the purpose and objective of expenditures. It receives quarterly execution reports submitted by the Executive. At the evaluation and control stage Congress, through the AGN, performs ex-post controls regarding budget implementation. Additionally, it has to evaluate and approve the Cuenta de Inversión (the annual budget execution report elaborated by the Executive). In Appendix A we present a more detailed description of the formal budget process.

V. THE ACTUAL WORKINGS OF THE BUDGET PROCESS

The Budget process, as every political process, is composed of a formal and an informal part. The previous section analyzed the formal workings of the budget process. It sets the stage for our analysis of the actual workings of the budget process. We find that there are several differences between the formal and actual budget process. In terms of actors, clearly the Executive plays a much more important role in practice vis a vis Congress than the formal rules define. For instance, the Executive has unilaterally modified the budget via decree in several instances, even after Congress had approved the budget. Furthermore, several actors that are not mentioned in the formal process play a role. These include provincial governors, lobbies – both inside and outside the government – and International Financial Institutions.

In terms of arenas for decision-making, the formal rules call for the approval stage in Congress to be the arena in which budgetary bargains are discussed and sealed. In practice, most changes in the budget are made at different stages, rendering agreements made in Congress difficult to sustain.

In this section, we replicate the description of each stage of the budget process presented in the previous section. However, instead of focusing on the formal rules, we discuss the salient features of the actual workings of the budget process in the period 1995-2003. The analysis draws on actual budget information, on interviews conducted with civil servants and politicians¹⁶ and on secondary sources.

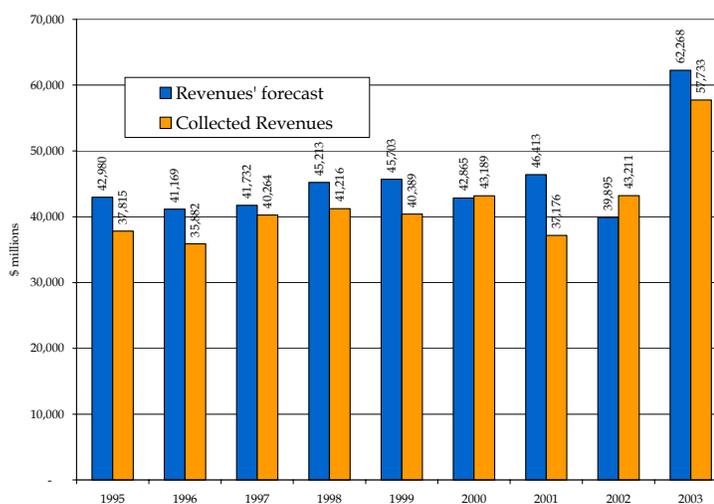
¹⁶ Several interviewees chose to remain anonymous. Those who did not are listed in Appendix B.

Formulation

The formulation stage of the budget is conducted within the Executive, following the formal steps outlined in the previous section. The key actor is of course the President, but he is constrained in his actions by a combination of macroeconomic conditions, internal negotiations in his government coalition, the rigidity of the budget, legal constraints imposed by fiscal rules, agreements with IFIs and the influence of powerful actors such as provincial governors and other lobbies.

The first stage of the process involves the development of macroeconomic and revenue forecasts. These are theoretically designed to act as a limit on spending, and to contribute to fiscal sustainability. However, we find that in practice, there is a systematic strategic use of macroeconomic forecasts which are developed by the Secretaría de Política Económica and the Secretaría de Hacienda. As we show in Figure 6, between 1995 and 2001, the forecasts significantly overestimated the total revenues of the national government. This trend was reversed in 2002, when the total resources were underestimated by 8%. In 2003, revenues were again overestimated, but in this case it was not provoked by an error in GDP growth forecast. Instead, the inflation rate was lower than the expected. In 2004 (not shown in the figure), revenues were once again significantly underestimated.

Figure 6: Forecasted and collected revenues. 1995-2003.



Sources: Ministry of Economics and Budget Laws.

These forecasts are not presented with sensitivity or risk analysis, they are not subject to public validation, and they usually differ from market expectations, which tend to be closer to actual outcomes. This suggests that the government uses forecasts strategically. Besides being used for budget projections, macroeconomic forecasts by the government affect the expectations of economic agents. Therefore, a plausible explanation for this behavior would take into account the differing goals of the government regarding both budgetary goals and the influence of forecasts on private expectations.

In the period 1995-2001, and especially once the recession started in 1998, the government had incentives to try to influence expectations by announcing high growth forecasts. In years in

which the macroeconomic models at the Secretaría de Política Económica predicted negative growth, political authorities insisted on presenting positive growth forecasts. Furthermore, given the growing debt burden in these years, the Executive required high growth and revenue forecasts so as to be able to present a budget without proposing spending cuts to Congress. These required cuts could easily be implemented later in the budget implementation stage. Hence, both political convenience and economic incentives promoted a systematic overestimation of growth and revenue forecasts in these years.

Following the crisis however, this pattern was reversed, with the Executive significantly underestimating revenues in 2004. In this case, the Executive faced a high growth environment, and therefore had less incentive to bolster growth via higher expectations. At the same time, given the extent of the real adjustment in spending following the devaluation – inflation caused an increase in nominal revenues, without a corresponding increase in the most relevant spending categories such as wages and pensions – the government had no problem presenting a politically appealing budget to Congress, at least in nominal terms. Finally, being in the middle of a process of debt renegotiation, the Executive faced further incentives to be prudent in the extent of its macroeconomic estimates. For all these reasons, the strategy of systematic overestimation seems to have been replaced with one of underestimation of revenues. However, there is a constant: the strategic use of macroeconomic forecasts by the Executive.

Once the Executive has its revenue forecasts, the President, together with the National Cabinet, establishes the expenditure ceilings for each agency. In years of high revenue growth such as 2003 or 2004, the President has more flexibility to push his agenda by allocating resources to preferred programs and provinces. In years of low growth, given that resources are probably overestimated, adjustments to the budget occur in the implementation phase.

While the budget is being prepared, the heads of each ministry, secretary and even program try to obtain the maximum amount of resources possible for their jurisdictions. The Chief of Cabinet is a relevant actor because he is in charge of solving the divergences that may arise among ministries regarding resource allocation. There are no formal rules about this issue but the common solution is that the disputes among line ministries are resolved by satisfying demands at least partially. In case an agreement cannot be reached, the President is the one that allocates the resources. The results of these negotiations are influenced by the relative strength of the ministries.

Apart from macroeconomic conditions and internal negotiations, the President faces another limit to his ability to implement his policy priorities via the budget process: the rigidity of expenditure in Argentina. As shown in Table 1, around 78% of spending included in the 2004 budget can be considered as ex-ante rigid. This figure includes wages, pension payments, specific transfers to provinces, debt payments and other payments that theoretically cannot be changed without affecting acquired rights of individuals,, renegotiating federal agreements and debt contracts or generating contingent liabilities.

Table 1: 2004 Budget. Expenditure classified by its rigidity

In total amount and in share of the primary and total expenditure.

Concept	\$ Millions	% Primary Expenditure	% Accumulated	% Total Expenditure	% Accumulated
Payroll	7,528	14%	14%	13%	13%
Transfers related to Salaries	3,519	7%	21%	6%	19%
Pensions	20,445	39%	59%	34%	53%
Funds and trusts	4,172	8%	67%	7%	60%
Non-transferred pension system deficit	1,116	2%	69%	2%	62%
Transfers to provinces	2,984	6%	75%	5%	67%
Debt interest	6,661		75%	11%	78%
Total Rigid	46,425			78%	
Plan Jefas y Jefes de Hogar Desocupados	3,407	6%	81%	6%	83%
Goods and Services	3,056	6%	87%	5%	89%
Real Direct Investment	1,472	3%	90%	2%	91%
Other Expenditure	5,442	10%	100%	9%	100%
Total Flexible	13,377			22%	
Primary Expenditure	53,051	100%		89%	
Total Expenditure	59,712			100%	

Source: 2004 Budget Law and its modifications

At this stage, the President is also constrained by legislation designed to secure fiscal discipline, and by agreements with the IMF that stipulate deficit limits. However, these constraints are often violated at the budget implementation stage. For instance, faced with a deteriorating budget balance and growing debt payments, the Argentine Congress approved a Fiscal Solvency Law in September 1999. This law aimed to achieve budget balance at the national level of government by 2003. Apart from establishing numeric limits for the central government's fiscal deficit, it also limited the growth of expenditures. Furthermore, the law stipulated the adoption of pluriannual budgeting, the creation of a countercyclical fiscal fund and the implementation of transparency measures. The Law established that fiscal balance had to be reached no later than 2003, and it set nominal targets for the non-financial public sector deficits between 1999 and 2002. In its very first year, the Law was broken, as the observed deficit was significantly higher than the target (3,1 vs 1,9% of GDP). The 2001 Budget Law modified the targets and extended the date at which the balanced budget should be achieved to 2005. Again, the target was unfulfilled in 2001.

Finally, the Executive must deal with the influence of lobbies and pressure groups, both from inside and outside the government. Spiller and Tommasi (2003) highlight the important role that provincial political leaders have on national policy. The governors and local party bosses are highly influential on legislative careers. They conclude that key political transactions are made at the level of provincial party leaders. The budget process is part of a larger policymaking process that involves several other dimensions and it requires negotiations between the national government and the provinces. The budget might be used as a vote-buying mechanism by means of pork barrel investments in some provinces to guarantee the legislators' support to some other issue or even in the budget approval stage.

However, it is not clear that governors exert their influence in the budget formulation stage. Rather, agreements between the President and provincial governors appear at this stage as done deals, and contribute to the rigidity of the budget process. For example, the decision by the national government to take over the deficit of provincial pension systems in 1997 became part of the budget, but was not strictly a decision taken at the formulation phase. There is a continual negotiation between the President and provincial governors in informal arenas, and the budget process simply reflects some of the agreements reached.

As was shown in Table 1, around 78% of the budget can be considered rigid. That constrains the President to implement her desired policies because she can only modify the remaining 22% of the federal expenditure. Nevertheless, there were some cases where the Executive itself introduced new rigidities to the budget. An interesting case to analyze is the financing scheme of the provincial pension systems' deficits.

In 1999, the national government committed to finance an increasing percentage of the provincial pension system deficit. This policy was a result of the negotiation that took place during the sanction of the 1999 Fiscal Pact. The main commitments in this agreement were i) the Federal Government fixed a monthly transfer of \$1350 millions to the provinces, ii) both the Federal and the provincials' governments committed to sanction a new Tax Sharing Law during 2000, iii) the provincial governments committed to pass both Solvency and Fiscal Responsibility Laws in their provinces reflecting the aim of the FRL of 1999 and iv) the federal government committed to finance pension systems' deficits gradually if the provinces permitted a federal audit and standardized the benefits.

The incentives faced by the different actors are relatively clear. The first commitment fixed the resources to be transferred to the provinces. On the one hand, the provinces would receive a fixed amount that provided the provinces with predictability in income, avoiding the cyclical component of the federal transfers. On the other hand, the national government kept a larger share of incremental revenues expected both from an economic recovery and an increase in federal tax pressure (Rosenblath and Webb 2001) as a retribution for the absorption of the risk involved in the fixed amount. In order to make this agreement more attractive for the provinces, the national government committed to finance an increasing percentage of the deficits of the provincial pension systems. This commitment has a double objective. In first place, as was mentioned above, the objective was to make the agreement more attractive. In second place, the national government was trying to impulse the reform of the provincial pension systems that were unsustainable in the long run¹⁷. These systems were characterized by higher benefits and weaker conditions for retirement than the national pension system.

The national government's commitment to finance the pension systems' deficits was also endorsed by the 2001 and 2002 fiscal pacts. The total resources allocated to this scheme increased from \$222,8 millions in 2003 to \$1.243 millions in 2005. The provinces that received extra resources are Buenos Aires (only in 2004), Córdoba, La Pampa, Santa Cruz, Santa Fe and Entre Rios (only in 2005). In the last two budgets, an important portion of the transfers

¹⁷ Some provinces transferred their pension systems in 1994. See Nicolini et al for further details about the 1994 transfers.

were not geographically classified and they account for 27% and 42% of the total for 2004 and 2005, respectively.

Furthermore, several agreements involve payments that are not even included in the budget. For example, during the Menem administration, the funds and trusts that were outside the budget such as the Fondo de Desequilibrio Provincial (provincial disequilibria fund) and the Aportes del Tesoro Nacional (ATN – National Treasury funds) were the main tools used to buy political support for the economic reforms¹⁸. During the Duhalde administration, and in the first part of Kirchner's, the main tools to buy political support were the renegotiation of provincial debts, and the deficits of the non-transferred pension systems. The national government offered to roll over provincial debts that in some cases accounted for almost 500% of their revenues. In the pension system case, the national government offered to cover up to 100% of the pension system deficits of certain provinces that agreed to introduce minimal reforms to their pension systems. In 2004, these funds were part of the negotiation with different provinces, such as Buenos Aires and Cordoba, for the approval of the Fiscal Responsibility Law.

There are other pressure groups that influence the formulation stage. They included the unions and other pressure groups such as “piqueteros” and pensioners. There are several occasions where these pressure groups influenced the budget formulation. The teachers' unions are a good example. Towards the end of Menem's presidential period, teachers established a permanent protest known as the *carpa blanca* (white tent) in front of the Congress, demanding an increase in their salaries. As a result of this protest, a special fund was introduced in the budget – the fondo de incentivo docente – that constituted an additional payment to the teachers' salary. At the beginning it was financed by an earmarked tax on motor vehicles but later this tax was eliminated and the national treasury provided the funding. Due to resource shortages, the government incurred in delays in the payment of this fund, accumulating several periods of debt. The union lobbied and finally managed to introduce in the 2003 and 2004 budgets extra resources to pay some of the owed payments during the budget execution.

A minor issue worth mentioning regarding the documentation prepared at this stage is that the 1999 Solvency Law established that the national government has to submit to Congress, together with the annual budget proposals, a pluriannual budget encompassing at least 3 years. These documents have to include the revenue forecast, the expected expenditures, and the investment program for the period, the IFIs credit programs and a description of the macroeconomic and fiscal framework used. These pluriannual budgets are useful to improve the availability of information in issues related to the pension system, debt payments, etc. Unfortunately, they are developed only to fulfill with the formal obligations, they are only descriptive and not a long run planning activity. They do not constitute any legal obligation for the coming years. A reflection of their lack of relevance is that they are not used as inputs in the formulation of the following year's budget.

Finally, we present some evidence on the discretionary use of funds by Presidents, by showing the allocation of investment funds for routes by province. La Rioja was the most favored province during the Menem presidency. Buenos Aires province gained \$64 million (13% of the total budget) during Duhalde's brief presidency, and Santa Cruz is receiving \$236 million (15% of the total budget, despite representing close to 1% of the total population) under Kirchner. Each

¹⁸ See Tommasi (2002) for further details about this topic.

president was governor of his home province before becoming president. This is suggestive of presidents having as one of their political goals the provision of resources to their home provinces, and having the power to achieve this goal through the budget process.

Approval

The Constitution and the laws described in the previous section provide Congress with a key role in the budget process. However, in practice Congress has played a weak role, limited to marginal changes in budget decisions associated with pork barrel spending items tagged on by eager legislators, rather than the role of discussing the Executive proposal in depth, and monitoring and evaluating budget implementation.

Rodriguez and Bonvecchi (2004) study the role of Congress in the budget process, and they find that it has been systematically weak over the past 20 years. They divide the period into three stages, defined by differences in the macroeconomic context and in the cohesiveness of the party system. In the first stage, 1984-1991, Argentina suffered from high inflation – including two hyperinflations –, and at the same time, the party system was highly cohesive, especially the government coalition until 1989. In this context, Congress played a merely formal role in the budget process, approving the Executive proposal well into the fiscal year.

In the second stage, 1991-1995, the authors claim that macroeconomic stability and growth followed after the implementation of the Convertibility regime. At the same time, the Peronist party controlled both the Executive and the Legislative branches. This set the stage for Congress to play a marginally expansive role, in the sense of adding limited amounts of pork to the Executive proposal, in particular by increasing proposed spending on infrastructure projects.

In the third stage, 1996-2004, Congress seems to have returned to its role of validating the Executive budget decisions. The period saw the return of macroeconomic instability – although still with low inflation – following the impact of the Mexican crisis in 1995, and the Asian, Russian and Brazilian crises between 1997 and 1999. Instability led the Executive to request special powers for budget reallocations in 1996. These have been sustained in recent years, leading to significant differences between the approved and implemented budgets, which we document below.

In Table 2 we present some characteristics of the approval process in the period under study. In the first place, and contrary to previous practice, in almost every year the budget proposal was submitted within the legal dates (the only exceptions were in 1995 and 1997 that were submitted six and two days after the established date, respectively). Secondly, all budgets except the one in 2002 (the year of the default and devaluation, which forced a sharp revision in the budget proposal in the first quarter) were approved by both chambers of Congress before the beginning of the corresponding fiscal year.

The average time elapsed in budget approval is 87 days. The minimal time corresponds to the 2002 budget – with 29 days - and the maximum to the 2000 budget with 104 days. The Lower Chamber used, on average, 84% of the total time to analyze, modify and approve the corresponding budget. The Senate approved the budgets within 14 of receiving them.

The Budget Committee evaluates the proposal and prepares a single or a double report (one from the majority and one from the minority). In the period 1995-2003, the reports from the majority recommended approving the budget considering some modifications. It is worth

noticing that there have been several partial and a small number of total dissidences within the majority reports. There were also reports from the minority in the approval process of the 1996, 1997 and 1998 budgets.

Regarding the vetoes introduced by the Executive, in all proposals approved by Congress, the President vetoed some articles. The lowest number of vetoes introduced was in the 1997 budget, where only one partial veto was introduced. The President used his veto power 18 times in the 2003 budget proposal – 16 articles were vetoed totally and 4 articles partially -. Given the presidential vetoes, Congress can override them by two-thirds of the total votes. Congress overrode the Executive's vetoes in only three occasions, in the 1998, 1999 and 2003 budget laws.

In 1998, Congress overrode two line-item vetoes. The first one was related to the economic promotion scheme (tax breaks for investment in some provinces). It dealt with the incorporation of new provinces into the scheme. The second article was related to public works in Buenos Aires and to the Ministry of Defense. The total resources involved in this article were \$8 million. In 1999, Congress overrode all the vetoes introduced by the government. The articles were related to the financing of a institution depending on the Ministry of Defense, an increase of resources transferred to the political parties in relation to each vote received in the previous election, the extension of the economic promotion scheme and the transfer of non executed resources of the Secretaria de Pequeña y Mediana Empresa to the 1999 budget. Additionally, one of the articles overrode increased the budget of some health programs by \$19 million. The others were related to the creation of branches of public services regulating authorities. In the 2003 budget, the article for which Congress overrode the presidential veto dealt with a reallocation of resources from the non-personal services to the Secretaria de Obras Publicas and the Direccion Nacional de Vialidad to increase resources allocated to public works.

Rodriguez and Bonvecchi (2004) argue that the veto of the economic promotion scheme was a regular political maneuver. The Executive would include the proposed extension of the scheme, the legislators from those provinces could show to their constituents that they had succeeded in obtaining more pork, and then blame the Executive for vetoing it. The veto overrides of 1998 and 1999 were exceptions, caused by the need of legislators to sustain cooperation among themselves, and by the pressure of provinces not involved in the Peronist internal struggle to extract the maximum possible revenues. The small size and relevance of veto overriding during the period is consistent with Congress having a marginal role in the budget process.

Table 2: The legislative approval process, 1995-2003

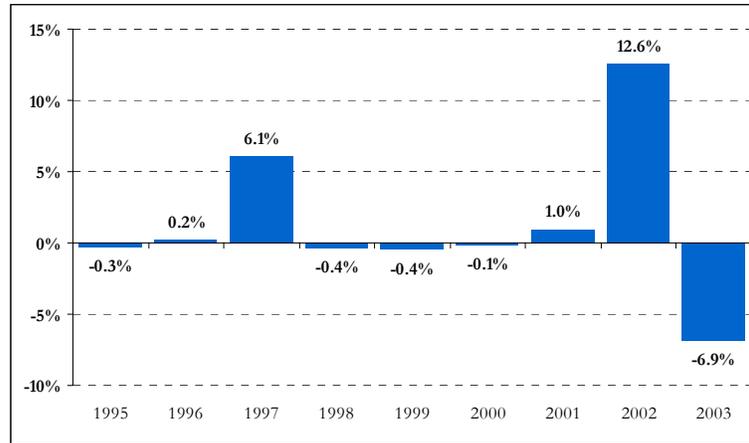
Fiscal Year	1995	1996	1997	1998	1999
Presentation Date	21-Sep-1994	15-Sep-1995	13-Sep-1996	15-Sep-1997	14-Sep-1998
Report from Majority	yes w/mod				
Partial Dissidences	11	5	7	1	13
Total Dissidences	0	0	8	5	0
Report from Minority	no	yes	yes	no	yes
Date of treatment (Lower Chamber)	29-Nov-1994	7-Dec-1995	6-Nov-1996	26-Nov-1997	2-Dec-1998
Date of Lower Chamber's approval	1-Dec-1994	8-Dec-1995	21-Nov-1996	28-Nov-1997	2-Dec-1998
Date of Senate's approval	23-Dec-1994	28-Dec-1995	18-Dec-1996	18-Dec-1997	7-Dec-1998
Date of Promulgation	30-Dec-1994	29-Dec-1995	2-Jan-1997	30-Dec-1997	30-Dec-1998
Vetoes introduced by the Executive	yes	yes	yes	yes	yes
Total Vetoes	9 articles	5 articles	0 articles	9 articles	6 articles
Partial Vetos	2 articles	5 articles	1 article	3 articles	6 articles
Insistences (override)	no	no	no	yes, 2	yes, 1
Approved Insistences				04-May-1998	29-May-1998 25-May-1999

Fiscal Year	2000	2001	2002	2002	2003
Presentation Date	14-Sep-1999	15-Sep-2000	17-Sep-2001	6-Feb-2002	13-Sep-2002
Report from Majority	yes w/mod	yes w/mod		yes w/mod	yes w/mod
Partial Dissidences	16	6		7	
Total Dissidences	1	5		2	
Report from Minority	no	no		no	
Date of treatment (Lower Chamber)	15-Dec-1999	30-Nov-2000		28-Feb-2002	18-Dec-2002
Date of Lower Chamber's approval	16-Dec-1999	30-Nov-2000		28-Feb-2002	18-Dec-2002
Date of Senate's approval	28-Dec-1999	7-Dec-2000		5-Mar-2002	26-Dec-2002
Date of Promulgation	6-Jan-2000	29-Dec-2000		19-Mar-2002	10-Jan-2003
Vetoes introduced by the Executive	yes	yes		yes	yes
Total Vetoes	2 articles	9 articles		11 articles	16 articles
Partial Vetos	2 articles	5 articles		4 articles	4 articles
Insistences (override)	no	no		no	yes
Approved Insistences					12-Mar-2003

Source: Honorable Cámara de Diputados and Infoleg

We now analyze the extent to which Congress actually modifies the budget. We show in Figure 7 the changes introduced by Congress to the Executive budget proposal. In four out of the nine years studied, these changes were lower than 0,5% of the budget in absolute value, and in two more, they were below 2%.

Figure 7: Changes introduced by Congress to the Executive budget proposal



Source: authors' elaboration

An apparent exception occurred in 1997, when Congress made relatively large changes in total spending. This change was concentrated in an increase in Social Security, and in fact responded to an agreement between the Executive and some provincial governors for the national government to take over the funding of the deficits of provincial pension schemes. This agreement was signed after the Executive proposal entered Congress, and therefore had to be included in the approval stage. Clearly, it is consistent with the weak role of Congress, and is not really an exception.

During the post-crisis years of 2002-2003, changes have also been high. In 2002, the budget proposal was very inadequate because the macroeconomic situation changed very fast. For the first time in a decade, the budget was not approved within the time-frame stipulated by the Ley de Administración Financiera. The budget proposal was presented in early 2002, and approved in March 2002. Between these dates, the exchange rate depreciated significantly, and prices increased. For this reason, we do not consider the changes introduced by Congress in 2002 as a reflection of stronger influence, but rather as an inevitable adaptation to the crisis. In 2003, the budget proposal included an item of spending of \$3.700 million, under the “Fiscal Administration” denomination, with the explanation that the Executive needed flexibility due to the volatile economic context. Congress rejected this item of spending following a public outcry from the opposition and independent analysts, who argued that the Executive could not simply present a spending item without explaining the expected uses of those resources. Although this is the only case in which Congress significantly changed the budget, it is not sufficient to revert the claim that Congress has a weak role in the budget process.¹⁹

We also show that Congress has a limited role in budget reallocations. To estimate the relative magnitude of changes in spending composition introduced in different stages of the budget process, we calculate the following coefficients:

$$[1] \quad \text{Stage 1: } C_{BL} = \frac{\sum_{i=1}^N |B_i - L_i|}{2}, \text{ for each year}$$

¹⁹ The fact that Congress introduces only marginal changes to the budget is also consistent with a model in which Congress is powerful, and the Executive simply adapts its proposal to the expected preferences of Congress. However, the ample deviations in budget implementation vis a vis the budget law make this hypothesis untenable.

$$[2] \quad \text{Stage 2: } C_{LV} = \frac{\sum_{i=1}^N |L_i - V_i|}{2}, \text{ for each year}$$

$$[3] \quad \text{Stage 3: } C_{VD} = \frac{\sum_{i=1}^N |V_i - D_i|}{2}, \text{ for each year}$$

Where:

B_i : is the participation of item i in total spending presented in the Executive budget proposal.

L_i : is the participation of item i in total spending approved in the budget law.

V_i : is the participation of item i in the total of effective credit.

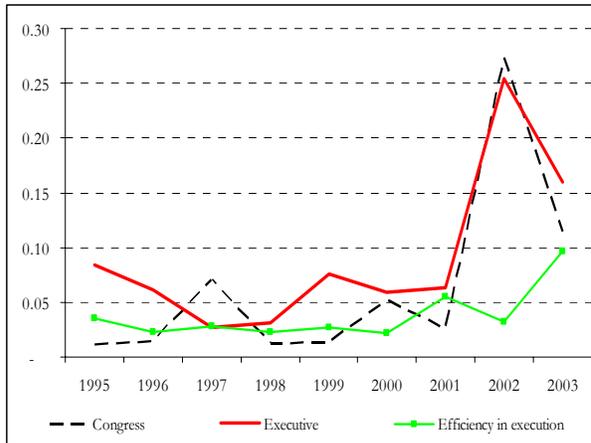
D_i : is the participation of item i in the total of executed expenditure.

The coefficients C_{BL} and C_{LV} represent the yearly changes in the composition of spending in the approval and execution phases respectively.

C_{VD} on the other hand is a crude indicator of budget efficiency, since it measures the extent to which planned expenditures are actually executed.

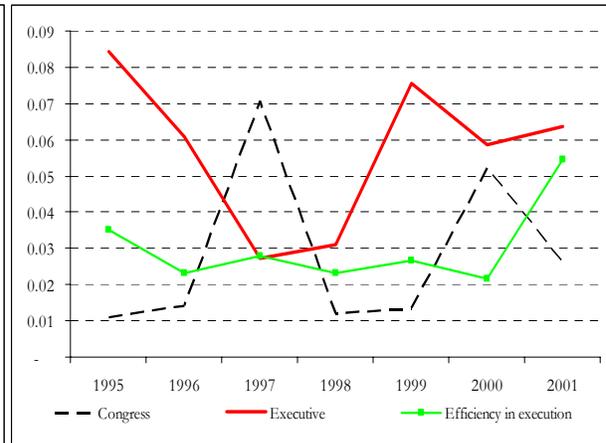
We present the results for the coefficients in Figure 8 and in Figure 9. Only in 1997 and 2002 does Congress play a more important role than the Executive in defining budget outcomes, and the coefficients in these years are influenced by the special circumstances discussed above. This is once again consistent with the limited role played by Congress in the actual workings of the budget process.

Figure 8: Changes in the composition of spending by stage (1995-2003)



Source: authors' elaboration

Figure 9: Changes in the composition of spending by stage (1995-2001)



Source: authors' elaboration

However, as argued by Rodriguez and Bonvecchi (2004) and shown by our quantitative analysis, some negotiation does go on in Congress, even if most of the action occurs at the Executive level. Provincial governors, ministers and public managers who failed to include their budget needs in the planning phase and private interests attempt to exert influence on legislators to modify the budget. Furthermore, legislators attempt to increase pork for their districts.

Consistent with its weak role in the budget process, Congress lacks the technical capabilities to analyze macroeconomic and fiscal issues. Furthermore, the time allocated to analyzing, discussing and approving the budget is clearly insufficient for an in-depth analysis.

It could be argued, following Jones (2001), that the fact that Congress does not make significant changes in the budget is not sufficient evidence of its weak role. It could be that legislators negotiate with the Executive in the implementation phase, or that the Executive tailors its proposal to fit the preferences of Congress so as to ensure its approval. However, most interviewees rejected this claim, arguing that the preparation phase of the budget was mainly an internal matter in the Executive, and that legislators did not have much say at that stage. Furthermore, in the next subsection we show that significant changes in the budget occur at the implementation phase. Therefore, agreements in Congress do not appear to be credible or sustainable. The Executive has the power to unravel these agreements. This power is enhanced by the weakness of the oversight and control institutions.

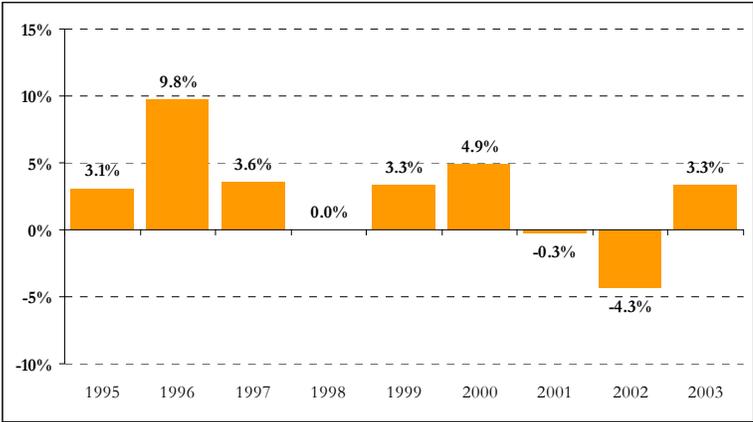
Implementation

The formal budget process envisages the implementation stage of the budget process as one in which the Executive simply implements the allocations approved by Congress in the most efficient manner possible. If any significant change has to be made to the size or allocation of the budget, Congress must approve it. However, the Executive has clearly exerted its political power at this stage, and increasingly put Congress in the back seat of the budget process.

There are two main ways in which the Executive changes the budget. The first is by changing the approved budget (crédito vigente) by using decrees (Decretos de Necesidad y Urgencia). In this case the Executive uses – or rather, abuses - the power conceded by the Ley de Administración Financiera, by which it is entitled to increase the total amount of the budget in case of an emergency. In theory, these decrees are subject to Congressional revision. Whenever the Executive promulgates this kind of decree it has to submit them, jointly with a justification, to Congress. A bi-cameral committee is empowered to overrule these decrees. However, the committee has not been constituted yet and therefore the Executive can modify the budget unchecked. An interesting example of this abuse of executive power is the method used by the Executive to modify the 2004 budget, that was increased by close to 9%. As was mentioned before, the Budget Law exempted the government from the regulation of the LAF but the major modifications were introduced using decrees, instead of invoking the powers delegated to the Jefe de Gabinete.

In Figure 10 we show the changes introduced in this manner by the Executive. During the 1995-2003 period, the Executive systematically modified the corresponding budget law, increasing the total amount in almost all years. In 2001, the decrease in the budget was due to the zero deficit rule adopted by the government. In an attempt to stem the upcoming crisis, the Executive imposed a 13% reduction in nominal wages, retirement and other payments, keeping the debt payments constant. The total effect of the policy was relatively small, but the budget reductions were around 10% in all the agencies excluding debt services and the legislative and judicial branches²⁰. The 2002 reduction was due mainly to a reduction in the budget for debt interest payments, which were reduced from \$12.328 to \$ 7.209 million.

Figure 10: Changes between budget law and actual budget, 1995-2003



Source: authors' elaboration

The second way in which the Executive changes the budget allocation is by the discretionary administration of the quota system described in the previous section. In theory, the quota system is simply an administrative tool by which the budget is implemented. In practice, it was used in years of overestimation of resources as a de facto way for the Executive to decide on budget allocations. By choosing which agencies and ministries received their full quota and which

²⁰ Both the Judicial and the Legislative powers have an independent budget that, even if included in the national budget, cannot be modified by the Executive.

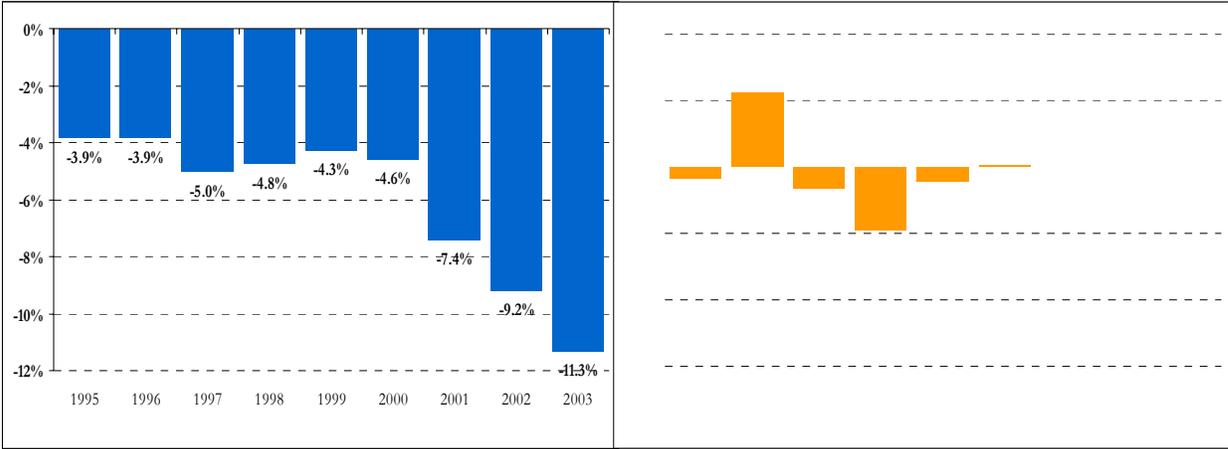
received less, the Secretaría de Hacienda could decide the actual allocation of the budget. This allocation often differed substantially from the allocation approved by Congress.

As mentioned in the analysis of the formulation stage, revenue forecasts were in general too optimistic in the period 1995-2001. This led to the Executive having insufficient revenues to cover planned expenditures, making an adjustment necessary. An across-the-board adjustment is out of the question, because of the rigidity of several budget items²¹. Therefore, the Executive was left with the option of implementing selective cuts, related to minimizing political costs. In a paper that studies this strategy, former Budget Secretary Jorge Baldrich (2003) argues that "...expenditure management emerges as one of the few instruments of fiscal policy and, certainly, as the only instrument in hand of the fiscal authorities in most cases..."

The Ley de Administración Financiera establishes that Congress is the only branch of government entitled to modify total expenditures and the total authorized debt level. Additionally, only Congress can modify the economic classification of expenditures and its objective and function. In practice, the combination of overestimation of revenues in the formulation stage, together with the discretionary use of the quota system, have led to the erosion of the actual influence of Congress on budgetary decisions, and left the Executive with the ability to unilaterally decide changes in budget allocations. In Figure 11 we present data on the degree of underexecution of expenditure in different years. It is clear that, as argued by Baldrich (2003), with the crisis in 2001 this became a strategy to limit spending and try to avoid the economic collapse that ensued.

Figure 11: Degree of underexecution of the budget in the implementation phase

Figure 12: Changes in total spending, budget law and executed budget



Source: authors' elaboration

Source: authors' elaboration

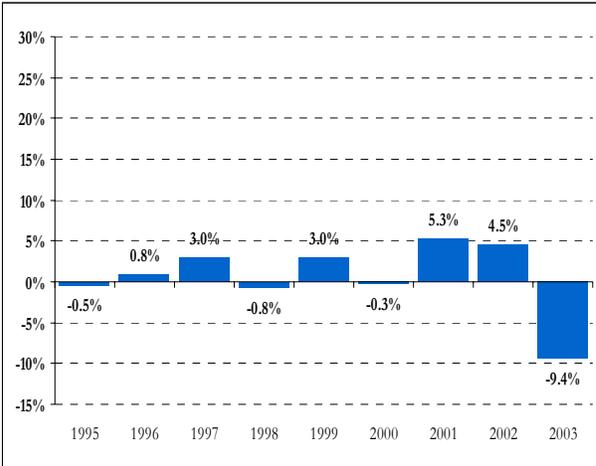
The combination of these mechanisms has led to significant changes in the budget being implemented by the Executive over the years vis a vis the budget law approved by Congress. We have already shown that the Executive dominates in terms of changes in composition. We now show in Figure 12 the combined effect of changes implemented by the Executive via decrees and

²¹ The Zero-Deficit Law, that called for across the board cuts so as to spend less than revenues on a monthly basis, was of course impossible to implement, and was immediately violated.

underexecution. In normal times, the Executive has a more relevant role than Congress. This disparity becomes even stronger in times of crisis, such as in 2001.

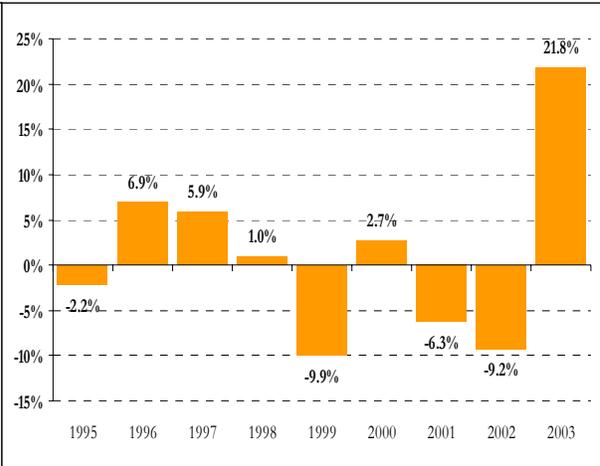
It is interesting to analyze the role of the Executive and Congress regarding changes in discretionary spending. In the following tables, we present evidence on changes in different stages of the budget, weighted by their degree of discretionality – measured by the index Z calculated in Section III for each budget item).

Figure 13: Changes between the Bill and the Budget Law. Weighted by discretionality index.



Source: authors' elaboration

Figure 14: Changes between the Budget Law and the executed budget. Weighted by discretionality index.



Source: authors' elaboration

This exercise shows that when we take into account the actual possibility of making changes, the relative power of the Executive is even more evident. The changes in absolute value at the implementation stage are systematically larger than in the approval stage. The bottom line is that when we analyze who decides on public expenditures that are actually decided upon in the federal budget process, the answer is that clearly the Executive has a preponderant role.

An interesting case of Executive discretion is the implementation of the 2004 budget. Since revenues had been significantly underestimated, the Executive found itself with excess resources. Instead of asking Congress to approve any change in the budget, it unilaterally implemented a series of decrees (DNU) that increased spending by \$8.650 million, almost 15% of the original spending approved by Congress.

A first decree approved in May increased spending by approximately \$755 million. The second important modification was introduced by the decree 917/2004 in July, which increased the budget by \$4.200 million. The third important modification was introduced by the decree 1687/2004, which raised the budget by approximately \$2.383 million. The main modifications were an increase in the pension payments that implied an increase in the budget of \$1.155 million. The Ministerio de Planificación saw its budget increased by 33%, with the goal of averting a potential energy shortage by importing gas from Bolivia and Venezuela. Also, the teachers' union managed to introduce an additional payment of the Fondo de Incentivo Docente in the 2004 budget. Additional increases were introduced to the Obligaciones del Tesoro for investment

related to the energy crisis and to transfers to provinces to improve the regional economic development.

Clearly, the increases are related to the need to provide national public goods for which the electorate makes the President responsible – such as energy -, to the desire to increase popularity by increasing pension payments and public sector wages, and to the influence of provincial governors and powerful lobbies, such as teachers’ unions. An interesting question is why the Executive used DNU instead of invoking the delegated powers – see box 3 for more details about this issue -. It can be related to the lack of oversight of the DNU. As was mentioned before, the Constitution establishes that a bi-cameral committee to control the DNU issued by the Executive but it has not been constituted yet. **NO ACLARA MUCHO PERO NO TENGO MUY CLARO X Q LO HACE; EN PRIMER LUGAR!**

The point of this example is that consistent with our results so far, significant decisions on public expenditure in the budget process are actually taken in years in which revenues increase substantially. 2004 was such a year, and the President decided on the allocation of these extra resources, influenced in some cases by other political actors and lobbies.

Returning to the issue of the rigidity of spending discussed in regard to the formulation stage, it is important to note that the rigidity of certain budget items is also related to the ease of execution. In Table 3 we show that the degree of underexecution is not homogeneously distributed among the different components of the budget. Rather, the degree of execution of consumption and use goods is systematically lower than other components of the budget, and higher for payroll expenses, transfers and debt services (at least before default).

Table 3: Degree of budget execution by type of expenditure, 1995-2003

Purpose of Expenditure	1995	1996	1997	1998	1999	2000	2001	2002	2003
Financial assets	78.8%	92.6%	91.0%	95.9%	98.4%	89.7%	90.0%	79.8%	79.0%
Consumption goods	90.2%	90.7%	93.5%	92.6%	86.0%	86.3%	94.2%	84.7%	88.4%
Use goods	64.9%	71.0%	76.7%	87.1%	101.8%	75.1%	79.6%	64.3%	78.0%
Payroll	97.9%	98.5%	98.1%	98.7%	99.4%	98.5%	97.3%	95.6%	98.4%
Public Debt Services	93.7%	93.9%	97.9%	96.8%	99.0%	99.3%	95.4%	92.3%	72.8%
Non personal services	90.8%	89.6%	90.1%	90.2%	90.2%	85.2%	92.4%	80.9%	82.8%
Transfers	97.8%	97.2%	94.6%	94.8%	94.3%	94.8%	90.7%	90.7%	91.2%
Total	96.1%	96.1%	95.0%	95.2%	95.7%	95.4%	92.6%	90.8%	88.7%

Source: SIDIF. Ministry of Economy.

Thus, expenditures that are classified as rigid also appear to be those more likely to be executed²². This probably reflects in part the rigidity itself – it is legally difficult to pay less salaries and pensions, for instance – and in part the relative technical difficulty of executing some items of expenditure, such as investment projects and consumption goods that require complex purchasing processes such as auctions.

In terms of the relevant actors at the implementation stage, the Secretaría de Hacienda, via the National Budget Office (ONP), is in charge of setting expenditure quotas for the line

²² This result holds if we use the ex post definition of rigidity as well.

ministries and agencies. As was mentioned above, the government in case of fiscal tightening uses this system strategically. The budget offices of the agencies receive the expenditure limits each quarter and have to distribute them, following the guidelines given by the head of the agency, among the different programs and activities. Baldrich (2003) highlights that the fiscal tightening process in Argentina is highly decentralized, although the Secretaria de Hacienda is the one that sets the expenditure limits via quotas. The final decision of what expenditures to cut is taken at the agency level by its head.

The role of the ministries and other heads of agency is also very important in this stage. They manage the quotas within their agencies; they protect their budget from cuts and exert pressure to obtain resources for their jurisdictions. A classic question regarding bureaucracy is its capacity to influence policy vis a vis elected officials²³. Tommasi and Spiller (2003) argue that the high rotation of the bureaucracy in Argentina limits its power, and therefore its capacity to act as enforcer of intertemporal political agreements. This lack of bureaucratic power leads to more unstable and lower quality policies. We find evidence consistent with this hypothesis. We show in Box 2, that more experienced ministers can protect and increase their budget more efficiently, and can execute a higher percentage of their budgets.

Box 2: Testing for bureaucratic learning in the Argentine public sector

A salient characteristic of the policy making process in Argentina is the high volatility of ministers and secretaries. In the period 1995-2003, a minister remained in his post for an average of 2.36 years. The maximum is 6.42 years (Dr. Alberto Mazza, Minister of Health under President Menem) and the minimum less than two weeks (Dr. Ricardo Lopez Murphy, Minister of Economy under President de la Rúa). These changes erode the institutional capabilities of the ministries, as each new minister appoints her own staff, a sort of parallel bureaucracy, so as to overcome the lack of collaboration – due to low-powered incentives and low capability - of the permanent staff.

This bureaucratic volatility leads to low capacity in budget execution. The problem is that, together with the budget quota system, the purchasing mechanism requires a high institutional capacity in order to execute expenditures satisfactorily. There are several activities to be done and there are no written manuals of how to prepare the documents that are mandatory for the majority of public acquisitions. The institutional capacity in Argentina is undermined not only by the lack of incentives faced by permanent bureaucrats to collaborate with the political appointed executives but also by the lack of experience of the temporarily hired employees.

We therefore hypothesize that the degree of execution of the budget, especially in the case of programs that require complex purchasing procedures instead of automatic transfers or payroll payments, will be lower the less experienced the minister is. Furthermore, as bureaucratic work may involve a learning process, the degree of underexecution may decrease over time for teams which remain in office.

The observational units in this analysis are the budgetary programs (classification of expenditure that summarizes information about the activities developed by the agencies and the source of funding of these activities). We construct an unbalanced panel, composed by the different programs in the 1995-2003 period. The budgetary information available for the programs are their degree of execution, their composition (payroll, automatic transfers,

²³ For a classic study, see Niskanen (1971)

consumption goods, use goods, non personal services and others), and their source of funding (internal or external sources, general revenues, earmarked taxes, transfers and credits). Each program is associated with its corresponding line ministry²⁴.

We measure the experience of bureaucrats as the average number of months of experience that a minister has in a given year. So for example a minister that is appointed on January 1st of 2000, and lasts for 1 year will have a value of 6,5 months average experience for that year. This definition is consistent with the fact that the learning process is considered a side product of the regular activities, and therefore grows over time. The maximum value for this variable is observed for the Ministry of Health in 1999 with an average number of months in charge of 68.83.

Our dependent variables then are 1) the degree of execution of the program, 2) the degree of execution of the program relative to the agency's degree of execution, and 3) the degree of execution of items classified as consumption or use goods.

Our independent variables included are the agency's degree of execution and the experience of the ministry. The first variable is expected to be positively related with our dependent variables because one may expect that higher degree of overall execution would imply a higher level of program execution, after controlling for its composition. The experience of the ministry is expected to be beneficial for budgetary execution because of the above mentioned learning process. The squared value of the ministry's experience is included to capture possible non-linearities in the model.

Regarding the program related variables, the control variables included are the percentage of the total expenditure devoted to payroll, automatic transfers and consumption and use goods

Our results, shown in Table 4, confirm that bureaucratic experience has a positive but decreasing effect on the degree of execution.

²⁴ In the case of the Secretariat of Social Development and the Ministry of Social Development and Environment, there were identified during all the period (even it was a Secretariat until 1999) because their composition was easily matched and relatively stable over the whole period.

Table 4: Regression results for bureaucratic learning

Dependent Variable	Program's degree of execution		Program's degree of execution relative to agency's execution		Consumption and usage goods execution	
	Coefficient	Standard Error	Coefficient	Standard Error	Coefficient	Standard Error
Agency's Degree of Execution	0.591	0.043			0.733	0.127
% of Consumption and Usage goods	-0.098	0.014	-0.086	0.015	0.234	0.035
% of Payroll	0.058	0.006	0.071	0.006	0.234	0.023
% of earmarked taxes	0.028	0.008	0.038	0.009	0.141	0.026
% of external transfers	-0.564	0.048	-0.601	0.053	-0.268	0.066
% of external credit	-0.280	0.019	-0.306	0.019	-0.249	0.054
% execution external transfers	0.054	0.025	0.076	0.027	0.115	0.054
% execution external credits	0.128	0.005	0.133	0.007	0.057	0.019
Ministry's experience	0.003	0.001	0.003	0.001	0.010	0.002
Ministry's experience squared	-0.00004	0.00001	-0.00004	0.00001	-0.0001	0.00003
1996	-0.015	0.006	-0.015	0.007	-0.055	0.021
1997	0.011	0.007	0.013	0.008	-0.004	0.023
1998	0.031	0.007	0.033	0.007	-0.025	0.021
1999	0.008	0.008	0.013	0.008	-0.076	0.023
2000	-0.002	0.008	-0.001	0.009	-0.070	0.026
2001	0.014	0.009	0.015	0.009	0.062	0.025
2002	-0.024	0.010	-0.024	0.010	-0.104	0.027
2003	0.023	0.008	0.018	0.009	-0.035	0.025
Constant	0.275	0.040	0.891	0.011	-0.214	0.117

Source: authors' elaboration

The high rotation of the bureaucracy leads to problems in the execution and efficiency of the budget. An interesting exception to this problem however is the fact that the bureaucracy that is responsible for most of the budget process – the Secretaría de Hacienda – has shown a remarkable stability relative to other areas of government, and furthermore is considered to have a high degree of professionalism.

The bureaucracy at the Ministry of Economy has the distinguishable feature that it is more professional and competent and with lower rotation than the other ministries' bureaucracy. Illustrative examples are the figures for the employees included in the Sistema Nacional de

Profesión Administrativa (SINAPA). The SINAPA is a human resource management scheme that includes around 40% of the national civil servants. It has a merit based promotion system and has six hierarchical levels, much simpler than the previous system. 28% of the total employees included in the scheme work for the Ministry of Economy.

- a) The average seniority of the Ministry of Economy employees is around 23 years, 15% higher than the average seniority of all the SINAPA's employees (20 years). Compared with the other agencies, the Ministry is in the top of the employees' seniority distribution.
- b) The educational level of the Ministry of Economy's bureaucracy is above the average. 38% of the total Ministry's employees have tertiary education, two times more than the Ministry of Internal Affairs and 20% more than the SINAPA's average.
- c) The Ministry of Economy has a higher proportion of upper echelons. 44% of its employees are in the top 3 categories, compared with the system average of 38%.

Interviewees both within and outside the Ministry argued that this is because of the complexity of managing the budget system. As opposed to other line ministries, where political appointees can bring in their loyal followers and allocate jobs and funds to them, if this were done at the Secretaría de Hacienda, the budget system would grind to a halt. Furthermore, political appointees to the Secretaría tend to be highly qualified, and therefore value the expertise of the established bureaucracy.

Congress clearly has a weak role during the implementation stage. The modifications introduced by Congress are almost minimal. It delegates – in the budget law itself in some cases – or the Executive entitled itself the powers that the LAF stipulates for Congress to modify the budget law. The Chief of Cabinet has to submit to the Congress the quarterly execution report. In that occasion, the Congress can ask for explanations about changes and underexecutions. They are just questions that do not have any legal consequences.

In fact, despite the key role given to Congress by the LAF, since 1996 different mechanisms have been used to undermine this role, recognizing in law what was happening de facto, i.e. the preponderance of the Executive in the budget process. (see Box 3).

Box 3: The legal delegation of budgetary decisions of Congress to the Executive

The LAF stipulates that the National Congress is the only institution entitled to modify the total expenditure and the total authorized debt level. Additionally, it is the only one that can modify the economic classification of the expenditure (for example, from capital to current expenditure) and its objective and function (e.g. from social expenditure or debt services). These restrictions were almost never fulfilled. The Congress (in the budget law or in a particular law) or the Executive (by decrees of necessity and urgency) authorized the Jefe de Gabinete to modify the budget without the above restrictions. In 2000, 2001 and 2004 the authorizations were conceded in the Budget Law. In 1998, 1999, 2002 and 2003 the authorizations were established by decrees. In 2002 and 2003, the decrees were based on the Economic Emergency Law.

The 1997 budget law included the restrictions but another law, sanctioned separately in December 1997, authorized the Jefe de Gabinete to introduce the changes without the constraints imposed by the LAF. In 1996, the budget law included similar restrictions than the LAF but did not quote this law. Again, Congress passed another law to authorize the modifications. In both cases, Congress established that the Executive should inform whenever they used the delegated powers.

In addition to legal delegation of powers, the Executive has also increased its power by creating special funds to implement its policy goals while avoiding the obligation of automatically transferring extra tax resources to provinces via the coparticipation scheme. (see **Box 4**).

Box 4: The creation of special extra budgetary funds

From the budgetary point of view the National public sector is composed of the national administration - that includes the Central Administration, some decentralized entities and social security institutions -, national public enterprises and national fiduciary funds. Congress only approves the budget of the first part of the national public sector. The other two parts are excluded from the formal budget process described in the previous sections. The funds, trusts and entities that are actually excluded from the National Administration budget (NAB) were generally were created outside the NAB but some of them were excluded from the NAB.

Fiduciary Funds are regulated by the Law N°24.441 that establishes that these funds have to follow the guidelines set by the Ministry of Economy, their budgets have to be approved by the Ministry and that they cannot directly hire any employee. The funds, even though they belong to the public sector, do not have the same controls and regulations than any other entity of the national administration.

The entities that do not belong to the National Administration are any State organization – excluding companies – with financial autarky, legal entity and own assets, where the State is the majority owner of the assets or has control over key decisions. These entities can formulate their own budgets and have to submit them to the ONP for evaluation. The ONP evaluates the budget and elaborates a report concerning about the consistency of the budget with the policies, plans and strategies of the government. The Executive is entitled to approve the entity's budgets without Congress' intervention.

In 2005 there are 15 fiduciary funds and 6 agencies that are included in the national public sector budget but not included in the National Administration budget. Additionally, there are 13 agencies (plus the national universities²⁵) that are not included in the national public sector budget. The consolidated expenditure projected for the fiduciary funds in 2005 is \$3.705 million, the one of the six agencies is \$5.564 million and the aggregated budget of the agencies that are not included in the national budget is above \$1.000 millions (excluding national universities). This represents 9% of the total federal budget.

The funds and entities were created by different legal instruments (decrees, laws and resolutions) according with the legal and political context of their moment of creation. Almost 50% of the funds and 75% of the agencies that consolidate in the public sector budget, but not in the NAB, were created by Executive decree and the majority was created between 2001 and 2003

²⁵ The resources transferred from the national government to the national universities are included in the budget but their budgets are not subject to the same regulations than the national budget.

Table 5: Legal Instruments that created the fiduciary funds and entities

	FFSPN	ESPN	ENSPN
Decree	7	4	3
Ministry's Decision	1		
Law	7	2	5
	15	6	8

Source: Ministry of Economy and Infoleg²⁶

The first fiduciary fund, *Fondo Fiduciario de la Secretaria de Hacienda – BICE*, was created by a Ministry of Economy's *resolution* in 1994. The total expenditure of this fund, for 2005, is around \$7 million. The funds with the largest budget in 2005 are the *Fondo Fiduciario para el Sistema de Infraestructura de Transporte –FFSIT-* (\$1746 million), the *Fondo Fiduciario para el Desarrollo Provincial – FFDP-* (\$ 732 million) and the *Fondo Fiduciario de Infraestructura Hídrica –FIH-* (\$ 586 million). These three funds represent 82% of the total expenditure of fiduciary funds.

Table 6: Fiduciary Funds dates of creation and 2005 budget

	Number of Funds created	2005's Budget
1994	1	7.2
1995	1	732.1
1996	1	12.0
1997	2	20.6
2000	2	23.3
2001	4	2,643.7
2002	1	126.8
2003	2	138.6
2004	1	0.6
	15	3,705

Source: Ministry of Economy and Infoleg

The FFDP was created by decree in 1995 to help in the privatization process of the publicly owned provincial banks. The fund was endowed with equities from YPF and sponsored by the IFIs. The provincial banks used to perform poorly and were considered a source of fiscal indiscipline. They suffered a hit following the massive withdrawal of deposits in the wake of the Mexican crisis. The only provinces eligible to receive loans from the fund were those that privatized their banks. Later, this fund was entitled to renegotiate the provincial debts and the quasi-monies issued in 2001. The fund then, was created to smooth the implementation of an economic reform. It provided the incentives for the provinces to privatize the provincial banks than otherwise the national government would not be able to supply.

²⁶ FFSPN are Fiduciary funds that consolidates in the national public sector; ESPN are entities that consolidate their budget in the national public sector budget and ENSPN are entities that do not consolidate in the public sector budget.

In 2001 the major fund formed was the FFSIT, financed by a specific levy on gas oil (created specifically for this purpose). Its resources are devoted to public infrastructure investment such as highways and bridges and to reduce or eliminate tolls. The geographical distribution of resources is independent of the tax sharing agreement and follows a different distributional pattern. This fund was created without Congress' intervention by an Executive decree because of the special power delegated by the Congress that allowed the Executive to create new levies, subject to the condition that they were exclusively devoted to finance infrastructure investment. The second most important fund, also created by an Executive decree, is the FIH. Its objective was to develop hydric projects to recover productive land. The source of funding of this fund is a levy on fuel. As the previous fund, the distribution of resources is independent of the coparticipation law and was created by a Decree, invoking the same delegated power than in the FFSIT case.

These funds were created during the economic recession as part of Minister Cavallo's strategy to jump-start economic growth and avoid the 2001 crisis. During his second term as minister, Cavallo introduced so-called "competitiveness plans" that included tax exemptions and other policies to promote industrial production. Cavallo's strategy also included an increase in public expenditure on infrastructure. The challenge that he faced was how to deviate the scarce resources to public investment avoiding the coparticipation system that would transfer the funds automatically to provinces. To do so, Cavallo established the specific levies and created these two fiduciary funds. Using these instruments he managed to avoid the coparticipation labyrinth because the levies did not have to be shared with the provinces and the fiduciary funds had their own distributional patterns.

The agencies that consolidate in the national budget but are excluded from the national administration budget are the AFIP (revenue collection agency), the INSSJyP (retired persons' health system), the INCAA (national cinema institute), SAFJP (Superintendence of the private pension system), the Instituto Nacional de la Yerba Mate and the Unidad Especial de Yacyretá. The latter three agencies were directly created outside the CAB and the former three were excluded from the CAB by Executive decrees.

The AFIP was excluded from the budget in 2001 by President De la Rúa. It obtained the same status than a public enterprise in which case the Executive (not the Congress) is empowered to approve its budget. The source of funding of the institution was established as a fixed percentage of the total revenues collected. This norm also instrumented an incentive scheme for AFIP's employees. They now receive a bonus related to the increase in tax collection. In this case, the objective was to provide more flexibility and autonomy to the AFIP, simulating the workings of an independent Central Bank. The entity was granted with its own decision-making process, independent human resource management, etc.

The public entities and funds that do not consolidate in the national budget are the Fondo Especial de Tabaco (Special Tobacco Fund), the National Universities, the Fondo Solidario de Redistribución (Social Security Fund), among others. The Fondo Especial de Tabaco was excluded from the budget by Law in 2001. This fund is financed by a special tax on cigarettes and it is automatically transferred to the provinces. The exclusion of this fund from the budget was the result of the economic crisis of 2001. The national government kept delaying the transfers to the provinces because of the shortfall in resources. The tobacco producers complained hardly about the delays and their governors pressured to the Congress to pass a law to secure this fund from further cuts and delays.

Thus, the main thrust for the creation of extra-budgetary items has been the initiative of the Executive branch, seeking to implement policies while avoiding the mandatory and automatic nature of transfers to provinces. There have also been instances of removal of programs from the budget by initiative of bureaucrats (AFIP) or provinces and lobbies (Fondo del Tabaco). These instances demonstrate the advantages for specific programs to escape the budget process and obtain earmarked funding, so as to avoid oversight and Executive discretion.

According to some interviewees, the IMF is another relevant actor in this stage of the budget process in some periods. The agreements signed by the government with the IMF usually establish quarterly fiscal deficit targets. Consequently, they affected the rhythm of execution of the budget as the government sometimes postponed some spending from a quarter to another to fulfill with the commitment.

Box 5:: The impact of Fiscal Federalism on tax collection

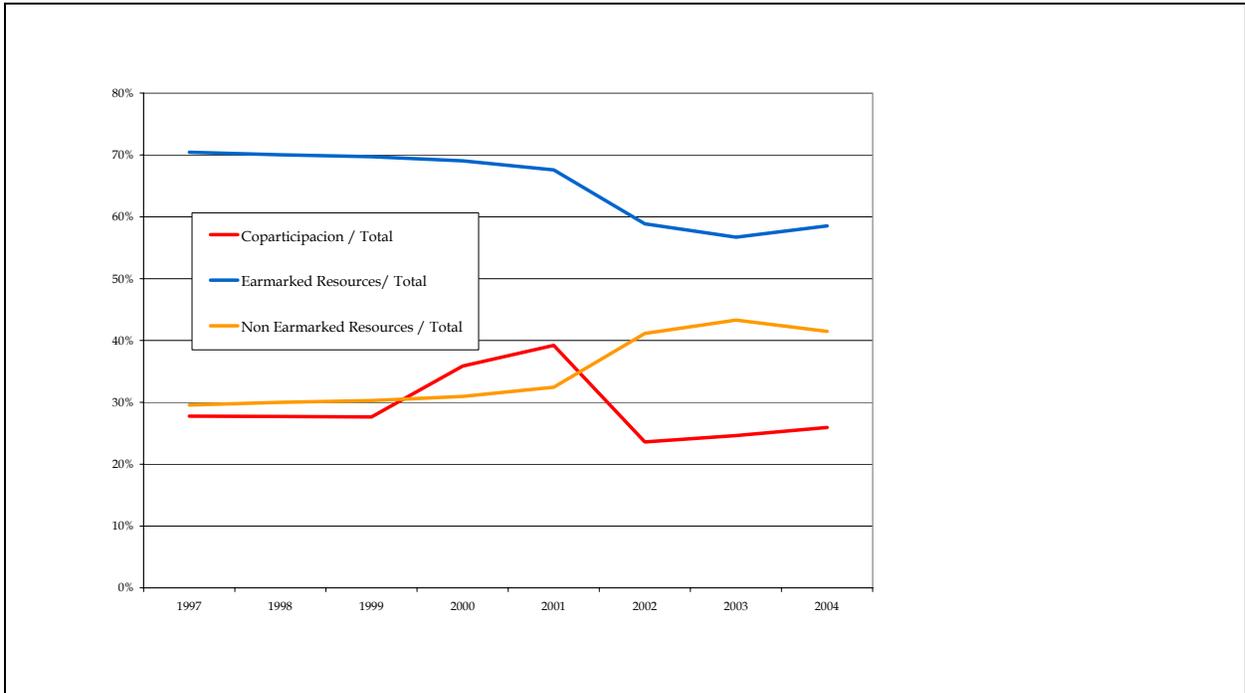
An important constraint that the national government faces, in its intent to expand public expenditure, is the Argentinean fiscal federalism. For each peso of national government's tax collection, it receives 41 cents on average as the rest is distributed to the provinces or earmarked to different funds and the pension system²⁷. The fiscal policy's strategies adopted by the federal government to obtain extra resources to overcome shortfalls or to increase expenditure had changed during the last years. In the late 90s, the Executive signed Fiscal Pacts with the provinces, as was explained above, which guaranteed a certain level of transfers to the provinces. The amount set in these agreements were similar to the average of the last two or three years (Rosenblath and Webb 2001). In a context of economic growth, the national government would keep all the resource beyond the floor established. Unfortunately for the National Government, in 2001 the floor established was above the actual revenue collection.

The second strategy adopted in 2000 and 2001 was the introduction of new taxes or levy earmarked to new expenditure. It is interesting to analyze three cases: the Fondo de Incentivo Docente, the Fondo Fiduciario para el Sistema de Infraestructura de Transporte and the Fondo Fiduciario de Infraestructura Hidrica. In the first case, as was mentioned, a new tax on motor vehicles was introduced to finance the additional payment to the teachers' salaries. It did not last for more than a year and FONID is now financed by general revenues. In the other two cases, as it is explained in depth in BOX 4, specific levies were introduced to finance public infrastructure investment. These two funds were created by Executive's decree and as they are financed by levy instead of taxes the Executive managed to avoid the federal labyrinth.

The third strategy, adopted during the economic crises, was the introduction of new taxes – ITF and export taxes – that were not initially shared with the provinces. These two newly introduced taxes were used to overcome the resources shortfall in the midst of the crisis - the income tax collection decreased from \$10,091 millions to \$8,919 millions and the VAT collection decreased by around \$ 800 millions between 2001 and 2002-. After the crisis, the taxes were not removed and they provide fresh resources to the national government to implement its desired policies. As it is shown, the percentage of revenues collected by the national government that is earmarked decreased after the crisis from 70% in 1997 to 58% in 2004.

²⁷ *Figures for 2004*

Figure 15:



Evaluation and control

A corollary of the weakness of Congress is that budget transparency and accountability, in particular, oversight by congressional audit and control institutions, is weak. In this section, we analyze the role of the Sindicatura General de la Nacion and the Auditoria General de la Nacion (AGN), the two public entities charged by the LAF with oversight and control responsibilities in the budget process. The SIGEN is the internal control institution of the Executive, and responds to the president. The AGN is the external auditor, and formally responds to Congress. Berensztein et al (2000) argue that audits by the AGN are sparse, usually not timely, do not go above and beyond legal compliance, and have not been used as an effective tool to improve budget efficiency or punish corrupt practices.

The conventional wisdom claims that existing evaluation and control mechanisms regarding the budgetary process are ineffective, thus requiring further reforms to enhance their capabilities. However, there is not a clear understanding of what exactly is wrong with it; what particular issues need to be improved; the scope, depth, and therefore resources those reforms may entail; and last, but not least, the eventual ability that political and bureaucratic actors involved in the process may have to resist and eventually dodge any attempt to revamp the prevailing system.

Our take on this matter is that even though additional efforts to improve the current evaluation and control mechanisms are indeed desirable, what is crucial is the political will and incentives to thoroughly employ whichever mechanism is in place. Moreover, the current system would work remarkably better by meeting that condition –the existence of political will as well as of lasting incentives to comply with the law.

Political and social actors develop specific strategies to take advantage of the opportunities that given institutional settings present, including the limitation or mishandling of the control

mechanisms theoretically in force. Thus, in the absence of strict and effective transparency procedures and eventual sanctions to prevent such behaviors, formal changes involving program design, implementation, as well as policy priorities may lack any substantial impact. In sum, what really matters in the underlying set of preferences and opportunities that formal and informal institutions generate. In the absence of constituencies with strong incentives to enforce existing administrative procedures and norms, it could not make much of a difference to implement reforms that would theoretically improve evaluation and control mechanisms.

As we have previously argued, law 24.156 is the main formal and administrative resource designed to organize and regulate Argentina's budgetary, Treasury, and accounting systems. It prescribes that two organisms, SIGEN and AGN (subordinated to the Executive and Legislative branches, respectively) are in charge of controlling all government agencies. We now turn to the main features of the way the system works in practice.

The main problem affecting the way control mechanisms work relates to their being highly politicized; that is, they are subject to political interference and manipulation by powerful actors who are able to limit and/or distort the functioning of the agencies and personnel involved in the process. Both the AGN and the SIGEN are influenced by those behaviors, yet the former is somewhat more politicized than the latter. This has to do with their respective institutional setting.

According to Section No. 85 of the Constitution, the AGN chair should belong to the main opponent political party holding the majority number of seats in Congress. The assumption is that this clause would secure transparency and independence from the Executive Branch. However, due to the weakness and fragmentation of the party system, and contrary to the original purpose, that requirement has made no impact whatsoever. The President is the most important political actor and has the ability to strongly influence both the political and the policy agendas, while Congress and the Judiciary are residual institutions. The AGN is indeed chaired by a representative of the opposition, thus meeting the existing formal requirement. Yet rather than providing for an independent and fair evaluation and control of public expenditures, it is used as an additional resource in the bargaining table. Thus, only certain events, agencies or officers are subject to auditing procedures. Also, their severity depends on politically driven strategies and may fade away according to unclear reasons. In sum, if a particular agency, program or officer is audited and irregularities are identified, the AGN report may be used as a bargaining chip before it becomes public.

The SIGEN is arguably better organized and staffed than the AGN. Its main advantage stems from the UAIs capacity to constantly control each jurisdiction of the State, thus permitting internal auditors to have a better grasp and knowledge of the respective operations. According to an interviewee that ran several public institutions in the late 1990s, "the SIGEN generates behavior, at least in the formal sense, since they pressure you to comply with the formal requirements of public administration law." However, the agencies being audited are often reluctant to provide the requested information in due time and manner. Also, there is a trend not to audit certain issues depending on their political significance and/or according to the electoral cycle. Finally, according to section No. 104 of law 24.156, the Auditing Committee must report to the President, who is supposed to inform to the Fiscalía Nacional de Investigaciones Administrativas (the Prosecutors Office for Administrative Affairs). That is, the President has discretionary powers to manage a specific case.

Another important issue to be considered is the fact that controls are carried out ex-post, while no preventive device exists to provide for more rigorous, random inspections of areas suspected of corruption and/or discretionary, politically driven behaviors. It could be argued that this type of procedure would further slow down an already heavy public administration system. But preventive measures are to be used selectively, focusing on particular policy areas, and for a limited period. In any case, it is true that the current public administration system is highly ineffective and slow, with the exception of specific, and scarce, “pockets of efficiency”. Thus, an overall effort to improve information systems, public employees’ skills, and other transparency devices is highly recommended. If such policies are indeed implemented, preventive devices which may indeed decelerate the pace of particular agencies is a price worth paying for the sake of transparency and accountability.

Furthermore, an additional topic refers to the moment in time when auditing reports are presented. There is broad evidence that both the SIGEN and the AGN run behind schedule, sometimes postponing deadlines even for years. Also, considering the habitual high turnover in public administration, individuals eventually responsible for potential wrongdoing or questionable decisions may no longer hold office. Moreover, this creates serious inconveniences to officials actually in charge of those agencies, who are forced to respond for resolutions they did not take. For example, the AGN presented the 1994 auditing report of PAMI (the Social Program for Retired and Pensioners) in August, 1999.

The bottom line is that oversight and control mechanisms are very weak in Argentina, generating only some formality in the compliance with regulations, but not acting as enforcers of efficiency and honesty in public administration. Furthermore, although Congress has the formal responsibility for controlling the role of the Executive in budget implementation, de facto it does not enforce this formal power, and lacks both the technical capacity and political power to do so.

VI. THE CONTRIBUTION OF THE BUDGET PROCESS TO SOLVENCY, EFFICIENCY AND REPRESENTATIVENESS

It is not straightforward to link the institutions of the budget process to fiscal policy outcomes, since there are many factors that influence these outcomes, and as we saw above, the federal budget process accounts for only a part of fiscal policy in Argentina. However, we have seen that the reform of the budget process in the early 90s was probably a contributing factor to the improvement witnessed in fiscal solvency. At the same time, the fact that the process is de facto very hierarchical – the President is clearly the key player in the budget process -, and that he has more incentives for overall fiscal discipline than Congress and other political actors, the process contributes to fiscal solvency.

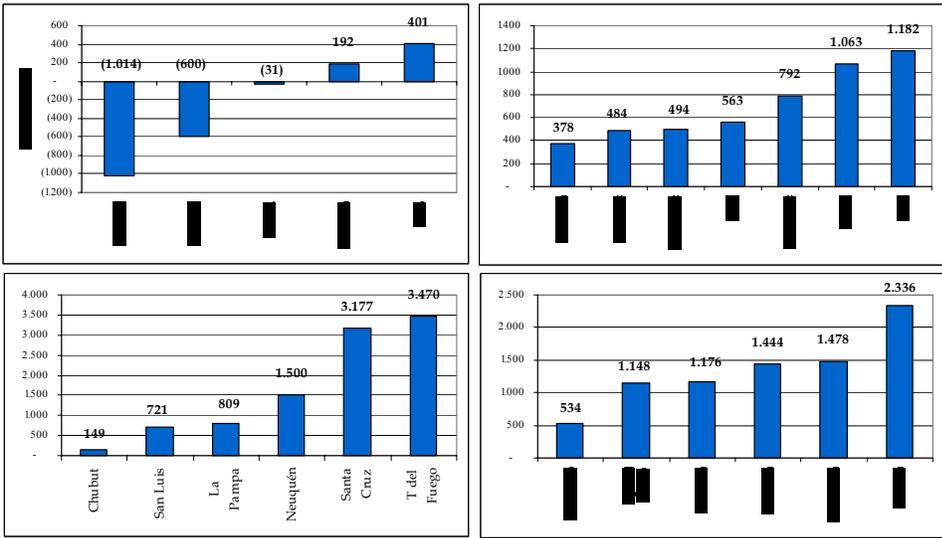
Regarding efficiency, although it is hard to obtain evidence, we have seen that the high level of rotation in the bureaucracy is a contributing factor to underexecution of the budget, which we take as a proxy of inefficiency. The current political economy of the budget process, by which there are no incentives in the line ministries to generate a professional bureaucracy to increase the efficiency of spending, and in which Congress has low incentives to monitor and control spending, is not conducive to efficiency in public spending. Furthermore, the fact that the Executive has so much unchecked power in the process leads to political abuse of public resources, in which political gain is a more important criterion than efficiency and representativeness.

The evidence presented on the distribution of funds to the President's province is suggestive of this problem. Another issue with representativeness is the level of overrepresentation in Congress. This means that public resources are not necessarily allocated to the poorest regions, or those most in need of investment, but rather, to those with the possibility of extracting resources from the common pool. This is consistent with the hypothesis of Spiller and Tommasi (2003) regarding the importance of governors as key actors in the political process, and with Jones (2001), regarding the relevance of Congress as an instrument of governors in the allocation of public funds.

To show this, we construct an index of Net Fiscal Benefit per province. This index measures, for an average citizen of each province, the difference between her tax payments and the resources allocated to finance public goods, both from national and local sources, and compare the results for provinces with similar socioeconomic characteristics.

We would expect that individuals belonging to similar provinces, grouping them by their development and population density, would receive a similar NFB. To analyze the Argentinean's situation, the provinces were classified in four categories: high density and development, low density and high development, high density and low development and low density and development. Figure 16 shows that there exist big differences in the NFB that an average citizen receives depending on their provinces of residency, even among provinces with similar socioeconomic characteristics. Among the low developed and densely populated provinces, a citizen from Jujuy receives 2.12 times more fiscal benefit than a citizen from Tucumán. The inequality is even larger for the less developed and less populated provinces. Citizens from La Rioja receive 3.13 times more than the residents of Rio Negro and 0.5 times more than the residents of Catamarca and Formosa.

Figure 16: Net Fiscal Benefit by provinces, 2002 (pesos per capita)



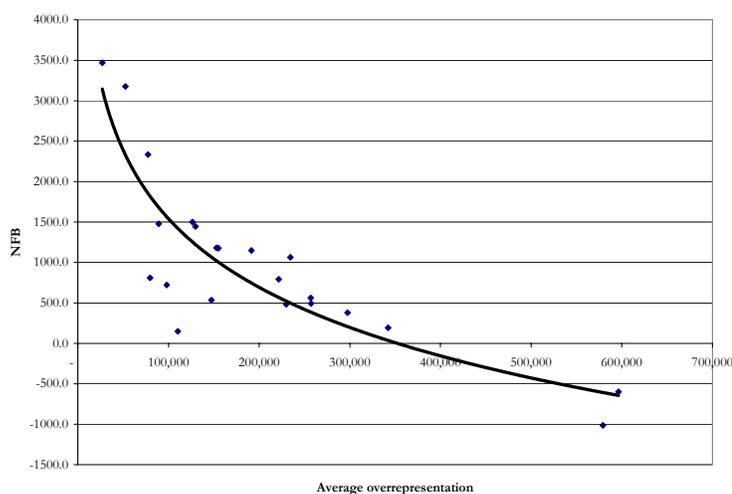
Source: Abuelafia, Braun and Diaz Frers (2005).

This result is explained in part by the fact that small provinces are highly overrepresented in Congress. For instance, the province of Buenos Aires has one deputy every 197,531 persons and one senator every 4,609,068 habitants whereas Tierra del Fuego has a deputy and one senator every 20,216 and 33,693 habitants, respectively. Porto and Sanguinetti (1993) have argued that this

explains in part the inequality in the distribution of coparticipation funds across provinces. We show in Figure 17 that there is a negative correlation between the number of population per representative and the NFB. This implies that provinces that are overrepresented (have less population per representative) receive a larger fiscal benefit.

A simple regression model (Table 7) confirms the results from the graphical analysis. After controlling for GDP per capita and the percentage of the population with unsatisfied basic needs per province, the relation between the NFB and the underrepresentation of each province is still negative and significant.

Figure 17: Population per representative (underrepresentation) as an explanation for the distribution of the Net Fiscal Benefit per province.



Source: authors' elaboration

Table 7: Robust OLS regression of NFB as Dependent Variable

N° of Observations 22.

		Robust		Robust		Robust	
		Coef.	Std. Err.	Coef.	Std. Err.	Coef.	Std. Err.
% population with NBI		6,950	1,666	4,605	2,098	4,745	2,022
GDP per capita		0.08	0.03	0.12	0.04	0.12	0.035
under representation	Lower Chamber	-0.02	0.003				
	Senate			-0.002	0.0005		
	Averga					-0.004	0.001
Constant		901	841	-323	866	-118	873
Adjusted R²		0.78		0.71		0.72	

VII. CONCLUSIONS AND POLICY RECOMMENDATIONS

We have analyzed the actual workings of the budget process in Argentina. Overall, the picture that emerges is that the President is the leading actor in the budget process. He seeks to maximize his objectives, which include obtaining reelection, maintaining high support from public opinion, and helping his home province. To achieve these objectives, in terms of the budget process, the President needs to sustain a sufficient degree of fiscal solvency -probably below the optimal level, but above that desired by other actors such as provincial governors -, to provide a set of national public goods, and to provide pork for his province and for his political coalition.

The President seeks to maximize his goals subject to a series of constraints, which include the rigidity of the budget, fiscal rules, and agreements with IFIs. He has to deal with macroeconomic shocks, which require changes in the level and composition of spending, and he has to deal with pressure from other actors, such as provincial governors, legislators and lobbies. Budgetary outcomes are a result of this game.

For example, this game helps understand why Argentina was unable to accumulate systematic fiscal surpluses during its years of high growth, which could have averted the crisis of 2001/2002. According to the political economy literature, such as Alesina and Perotti (1996), the relative strength of the Executive vis a vis Congress in the budget process should contribute to fiscal discipline. However, the relevant negotiations do not take place in Congress. In fact, the relevant negotiations take place between the President and provincial governors, in informal arenas, and are later incorporated into the budget, contributing to its rigidity. This rigidity, combined with other decisions that reduced fiscal solvency, such as the pension reform, led in the period analyzed to the impossibility of accumulating sufficient budget surpluses to avert the crisis. Although the Executive managed to cut spending in 2001, it was already too late.

Rigidity, high ministerial rotation and Executive discretionality also help explain why budget allocations are inefficient and in many cases particularistic – as opposed to representative. Social conditions across provinces can change, but the rigidity in budget allocations make it difficult to respond. Furthermore, high ministerial rotation makes it difficult to execute public spending efficiently, especially infrastructure and complex purchases.

Another set of problems underlying the actual workings of the budget process stems from the lack of a consensual and strong political commitment to enforce the existing procedures and regulations. For instance, many of the problems regarding Executive discretion could be limited if revenue forecasts were not used strategically. However, there are no political actors with the incentive and strength to make this outcome an equilibrium. Hence, the Executive makes use of this tool whenever necessary.

In fact, budget politics is not the only, and probably neither the most important, policy area in which the rule of law is not in fact applied. As described by Spiller and Tommasi (2003), other major policy issues are also characterized by the constant manipulation, modification, and erosion of legal procedures according to the short term preferences of influential political and social actors.

Thus, in the context of such an ambiguous environment, there is a high probability that even the most important rules and regulations can be changed, limited, or even ignored. Non-

cooperative behaviors prevail, as actors develop strategies that assume short time horizons and which discount the eventual consequences of an ex post facto regulatory change. As the literature on collective action suggests, this kind of strategic interaction entails the creation of intricate vicious circles that are very difficult to remove.

There is however a natural temptation to suggest possible changes in the existing budget process in order to make it more transparent, effective, and accountable. Indeed, any institutional mechanism can be improved after elaborating proper diagnosis and reasonable proposals. Moreover, converging towards international standards in terms of capacity building and institutional strengthening seems to be the most logical strategy. Yet in the absence of a previous, vast effort to promote a democratic compromise on the need to enforce the rule of law and to revert the negative incentives for institutional development documented by Spiller and Tommasi (2003), almost any policy recommendation may seem futile.

Despite this pessimism, we note that Argentina has improved its budget process and fiscal outcomes significantly, and that this has limited the damage suffered in the wake of the recent crisis. We therefore believe that some observations regarding possible avenues of reform are in order.

- ***Coordination mechanisms between the federal and provincial governments.*** The Ley de Responsabilidad Fiscal calls for the creation of a Federal fiscal organization in which representatives from the Federal and provincial governments should get together to discuss budget issues such as macroeconomic forecasts and aggregate revenue forecasts. This could become a formal arena in which budget negotiations take place, bringing key informal actors such as provincial governors into the formal process.
- ***Focus reform on “points of discretionality”:*** Any attempt to implement numerical rules such as structural budget balance rules, countercyclical funds, etc should focus on the items of spending that are flexible, and pay special attention to years of high revenue growth, since these are the points in the budget process in which more decisions on budget allocations are made.
- ***Capacity building in Congress.*** Although Congress as a whole lacks the incentives to invest in capacity to analyze and control the budget, certain actors within Congress, such as legislators from minority parties in large districts, do. This provides an opportunity to improve capacity in Congress – for instance, with the creation of a Congressional Budget Office -, which would reduce the cost for legislators to understand and participate in budget discussions, possibly contributing to improving the process and strengthening the role of Congress.
- ***Improvement of expenditure evaluation.*** State agencies and Congress lack the incentives and capacity to seriously evaluate the impact of government programs. This limits the capacity of the budget process to act as a strategic guide for spending allocation.
- ***Use of private forecasts for budgeting.*** Following the example set by the Central Bank, who conducts a weekly survey of private consultants’ macroeconomic forecasts, these could be used to estimate growth and revenues by the government. This would limit the ability to use forecasts strategically.

- ***Improve bureaucratic capacity:*** although we do not have specific proposals regarding administrative reform, clearly reducing the level of rotation of the bureaucracy would contribute to increase spending efficiency.

APPENDIX A: A DETAILED DESCRIPTION OF THE FORMAL BUDGET PROCESS

Stage 1: The budget formulation

The beginning of the process is in early March of the previous year when the *Oficina Nacional de Presupuesto* (National Budget Office) – ONP - sets the schedule of activities involved in the budget formulation. At this moment, the *Grupo de Apoyo para la Elaboración del Presupuesto* (Budget's Elaboration Support Group) –GAEP - is constituted. This group is formed by the heads of the Ministry of Economy's offices involved in the budget formulation and its chairman is the Budget Undersecretary. Its objective is to support the entire budgetary process. For example, macroeconomic forecasts and the budgetary ceilings for each line ministry are discussed within this group.

In May, the *Secretaría de Política Económica* (Economic Policy Secretariat) and the *Secretaría de Hacienda* (Treasury Secretariat) produce short run macroeconomic forecasts. Using this information, the *Secretaría de Hacienda* sets the budget priorities and generates the public investment programs and plans. Simultaneously, the ONP elaborates the first document of the process that stipulates the next activities of the process, the responsible officers and their deadlines.

The President, the Jefe de Gabinete and the Ministries (supported by the GAEP) discuss and decide the aggregate budgetary policy and set the expenditure ceiling to each line ministry. These decisions are based on the macroeconomic forecasts developed by the Ministry of Economy, the fiscal needs and preexistent commitments of each agency (i.e. pension payments, debt services, etc.). The interaction between the line ministries, the Jefe de Gabinete and the Ministry of Economy begins in at this point. This stage of the budget formulation can be understood as a two way process where information and guidelines go from the highest to the lowest level of bureaucracy within the ministries and vice versa.

The *Ley de Reforma del Estado* (State Reform Law, 1996) stipulates that the Executive has to inform Congress, before June 30th of the previous fiscal year, of the general guidelines regarding the upcoming budget proposal.

The Jefe de Gabinete defines the expenditure ceilings for each agency and then communicates this information to each one. Within each agency, the expected resources are allocated to specific budgetary programs and activities. The descending process involves the interaction between the political and technical components of the agencies. The final outcomes are the *anteproyectos de presupuesto*, developed by the budget offices in each agency. These offices have to compile and consolidate the information provided by the programs and to generate the *anteproyectos*. The *anteproyectos* summarize the activities that the agency plans to implement during the next fiscal year, and the financial needs involved.

As a part of the ascending process these new documents are submitted to the Secretaría de Hacienda for their evaluation. The sector specialists of the National Budget Office evaluate these proposals and, in case of divergence between the *anteproyecto* and the stipulated ceiling, interact with the agency to settle the differences. After consolidating all the *anteproyectos*, the budget proposal is prepared and presented to the President, the Jefe de Gabinete and the Ministers for its

discussion and approval. Finally, the Jefe de Gabinete sends the Budget proposal to Congress, ending the budget formulation stage.

Stage 2: Congressional approval

The Constitution empowers Congress to approve the National Budget each year. The Ley de Administración Financiera stipulates that the proposal has to be submitted to the Lower Chamber before September 15th of the previous fiscal year²⁸. The President attaches a message to the budget proposal. This message includes the main objectives of economic policy for the next year and how they are reflected in the budget. It highlights the main programs and activities that the Executive plans to carry out.

As soon as the proposal is submitted to the Lower Chamber, it is sent to the *Comisión de Presupuesto y Hacienda* (Budget Committee). This committee is composed of 45 deputies belonging to all parties, and it has the power to require explanations from the Executive power regarding different aspects of the budget proposal. The inquiries can be either oral or written. In the former, the committee summons members of the Executive branch to meetings, following a previously set schedule, in which they are asked to make a presentation and then answer questions. In the latter case, the written questions are sent to the Jefatura de Gabinete. After studying the entire budget proposal and considering all the explanations, the committee prepares either a single or a double report - one made by the majority and another by the minority in the case of disagreements. The report includes recommendations regarding the proposed bill (i.e.: to pass or reject the entire law, to modify some articles, etc). The *Comision de Labor Parlamentaria* (the agenda setting committee composed by the chairman of each party at the Chamber and the president of the Lower Chamber) decides when the bill will be considered in a plenary session.

At the Chamber of Deputies' plenary sessions there is no formal procedure to discuss the budget, and every congressman has the right to make his statement. However, the custom is that the chairman of the *Comision de Presupuesto y Hacienda*, or some other deputy that supports the majority report, is the first speaker. The second one is a congressman who supports the minority report (if there is one). After these speeches the other members can express their opinion about the proposed budget.

The proposal can be either rejected or passed in general. If it is rejected in general it returns to the *Comision de Presupuesto y Hacienda* for a new report. If it is approved in general, the next step is to consider each article individually.

The individual articles, if there are no objections, are approved by a simple majority. In case of objections, the interested deputies can suggest either changing the article or removing it. When the individual approval procedure is finished, the members of the Lower Chamber can suggest the inclusion of new articles. These new articles are subject to the same approval procedure than the original bill proposal's articles. The budget proposal, after its approval article by article at the Lower Chamber, is sent to the Senate for its consideration.

The Executive can either ratify the bill without modifications or use its veto power. In the latter case, the Executive can veto one or more articles, as long as this does not alter the main objectives of the bill. A typical case is when new articles are introduced by the Congress. The Executive can veto these articles if they contradict the political and economic objectives of the

²⁸ It is worth mentioning that the fiscal year in Argentina runs from January 1st to December 31st.

government or if they violate the *Ley de Administracion Financiera* (Financial Administration Law) – LAF -. This law stipulates that the sources of funding of any new expenditure have to be clearly specified in advance. The bill is returned to the Lower Chamber and it can overrule the vetoes introduced by the Executive by a special majority rule (two-thirds of the total votes). In this case, it is sent to the Senate. If it is approved (by the same majority rule) by the Senate, it becomes the new budget law. In the case that the budget proposal is not approved by January 1st, the previous year budget will be extended until its approval²⁹.

Stage 3: Implementation

The LAF stipulates that the Oficina Nacional de Presupuesto is the ruling authority at this stage. It is empowered to set the rules and procedures of the budget execution and to prepare the execution reports.

After Congress approves and enacts the budget law, Article 30 of the LAF stipulates that the Executive has to distribute the expenditure authorizations among the different agencies. It is worth noting that there is a quota system that controls the budgetary execution. The quotas are established on a quarterly basis and they mainly reflect the availability of resources and the rigidity of expenditure. The quota formulation process is also a two way process, from bottom to top of the agencies and vice versa. The ascending process takes place when the bureaucrats in charge of specific programs ask for the resources that they need to fulfill the programs' objectives. These requests are consolidated by agency and remitted to the National Budget Office. The descending part occurs when the *Secretaria de Hacienda* sets the agency expenditure quotas. These quotas are assigned to programs within each agency by the ministries. No agency can spend more resources than the set quota in each quarter and they cannot change the purpose of the authorized expenditure. Each agency has to keep a record of the physical execution of the budget and has to submit them to the *Oficina Nacional de Presupuesto*.

Regarding the evaluation of the budget's execution, the ONP has to inform the degree of budget execution both during and at the end of the fiscal year. A quarterly execution report and the annual report, *Cuenta de Inversión*, have to be presented to the National Congress. These reports are prepared using the information provided by the agencies and collected by the accounting system. The reports include an analysis of the financial and physical execution, its variations with respect to the budget and plausible explanations of these variations. Additionally, the ONP prepares recommendations for the authorities regarding how to solve the problems found during the implementation.

The budget is not a rigid law; it varies according to the changes of the economic and social environment. In the Argentinean case, the LAF stipulates who can introduce modifications, regarding their relevance and impact.

The National Congress is the only institution entitled to modify the total expenditure and the total authorized debt level. Additionally, it is the only one that can modify the economic classification of the expenditure (for example, from capital to current expenditure) and its objective and function (e.g. from social expenditure or debt services).

²⁹ The LAF gives the instruction of how to extend the budget from one year fiscal year to the other.

Classification of Expenditure:

By purpose of Expenditure: it is a systematic and homogeneous order of goods and services, transfers and the variation of assets and liabilities which the public sector applies in the development of its activity (e.g. payroll, consumer goods, non personal services, etc.).

By Objective and Function: the classification is presented according to the nature of the services that public agencies offer to the community. It allow to determine the general objectives and the action through which they are projected to be accomplished.

By Economic Classification: allows to identify the nature of the transactions performed by the public sector (i.e. current and capital expenditure)

The Executive can increase the total expenditure only in case of an emergency (flooding, earthquake, etc.). These increases have to be notified to the Congress immediately jointly with its justification. However, the Executive can reallocate the budget both within and across agencies during the implementation phase. Some examples of the authorities involved in the modifications of the budget are:

1. Modifications that require an Executive decree: changes within each expenditure purpose.
2. Modifications that require a *Jefe de Gabinete's* administrative decision: expenditure reallocation among different agencies.
3. Modifications that require a Ministry or State Secretary's administrative decision: reallocations among different budgetary programs within the same agency.
4. Modifications that require a *Secretario de Hacienda's* resolution: changes in the source of funding, changes in the expenditure purpose (i.e. increase on payroll and decrease in goods and services).
5. Modifications that require an involved secretary's resolution: compensation among different expenditure objectives in the same program, reallocations among subprograms of the same program and all other modifications excepting the related to payroll expenditure.
6. Modifications that require an ONP's resolution: changes in the programmatic structure of the agencies.

Stage 4: Evaluation and control

The budget control system is composed by internal and external auditing bodies. The internal auditing entities are the Internal Auditing Units (IAU) of each agency. They report to each ministry and to the *Sindicatura General de la Nación* (SIGEN), which in turn reports to the President. The external auditing authority is constituted by the *Auditoria General de la Nación* (AGN) that reports to the Senate.

The internal control is focused on an ex-post control of the financial and administrative activities of the agencies. The internal auditing system is coordinated by the SIGEN, which stipulates the rules and supervises the activities of the IAU. The main functions of SIGEN are i)

developing internal control rules and supervising their implementation, ii) coordinating or producing audit reports on financial, legal and management issues, and iii) informing any irregularity to the President.

The external controller, the AGN, is an autarkic body whose rules and functions are set by the *Comisión de Presupuesto y Hacienda* and the *Comisión mixta revisora de cuentas* of both chambers. Its main function is to perform ex post controls on the budget management, the economic and financial and balance sheet statements. The AGN is constituted by seven members, three appointed by the Senate, three by the Lower Chamber and the remaining member – who must belong to the opposition - by the presidents of both chambers.

The legal framework behind the Budget process

The Budget process is mainly regulated by the Ley de Administración Financiera (LAF) that was sanctioned in 1992. The previous legal framework was constituted by several rules that dated from the 50's and 60's that were changed every year by the new budget law. The new law systematizes and regulates the major governmental activities, particularly the ones related to the budgetary system. It is not the unique Law that regulates the budget process; other laws, and even the National Constitution, refer to this issue. In this section, the legal framework will be summarized and analyzed.

The budget process prior to the LAF

The state of the governmental administration system at the end of the 90's can be summarized as:

- a) The budget was not used as a tool for public policy formulation.
- b) The accounting system was not integrated to the other governmental activities and it just provided information for controlling.
- c) Not all the public agencies and entities were regulated by the financial administration and control norms.
- d) There was not a unique regulatory norm. The Ley de Contabilidad (Accounting Law) was out of date. It did not reflect the needs and requirements of an efficient accounting system. The Ley Complementaria Permanente de Presupuesto complemented this law in some important areas.
- e) The lack of institutional capacity in the key areas of the budget was a characteristic of the system.
- f) The congress did not have an important role in the budget process.

The main reforms introduced by the LAF were:

- a) The consideration of the administrative system as an integrated and interrelated system.
- b) The incorporation of all the agencies and entities under the LAF.

- c) The increase the Congress role in the budget process. It was disposed that it is exclusive power of the Congress to increase the expenditure and to modify the debt limit.
- d) The creation of the Auditoria General de la Nación.
- e) The consolidation of the information of expenditure of all levels of government.

National Constitution (1994)

The National Constitution, established in 1853 and most recently reformed in 1994, has several articles regarding the budget process.

- Article 4° stipulates that the Federal Government has to prepare a budget that includes both the planned expenditure and its sources of funding.
- Article 75° states that the National Congress is entitled, among other faculties, to approve the federal budget.
- Article 85° creates the Auditoria General de la Nación that is the external auditing body. It determines the AGN's duties and powers.
- Article 100° stipulates that the Jefe de Gabinete is the officer in charge of submitting the budget proposal to the Congress for its consideration and approval. Additionally, this article gives responsibility to the Jefe de Gabinete of collecting the national resources and executing the national budget.

Ley de Administración Financiera (1992)

The LAF is a nonspecific law in the sense that it does not include procedural details. It stipulates the basic and general guidelines of the budget process. The specific procedures are regulated by other rules³⁰. The main points of the Law are:

- It sets which agencies should be included in the budget law³¹ and integrates the different governmental systems (budgeting, public credit, treasury, accounting and control).
- It separates, from the budgetary point of view, the national government in different agencies (Legislative Power, Judicial power and Executive power, composed by the President, the ministries and the secretaries).
- It stipulates that the fiscal year runs from January 1st to December 31st and no new expenditure can be authorized a posteriori of the closing date.
- Until 1989 the budgets were usually extended from one fiscal year to the other because the new budget laws were not sanctioned on time or even not submitted for their consideration to Congress³². The LAF stipulates that the budget proposal has to be

³⁰ The other norms related to the budget process are Decree N° 2.666/92, Reglamento Parcial N°1, Decree N° 253/93, Reglamento Parcial N°2 and Decree N°1.361/94, Reglamento Parcial N°3.

³¹ The LAF stipulates that the National Public Sector is composed by the National Administration (Central Administration, Decentralized entities) and public enterprises. The Law N° 25.565 introduced the Fiduciary Funds and the public enterprises.

³² As we mention in section 3, in a context of high inflation – X% average between 1975 and 1991 – ex-ante budgeting becomes a futile exercise.

submitted to Congress before September 15th of the previous fiscal year. Also it regulates the budgetary extension in case that the new budget proposals were not approved until January 1st.

- The LAF and its modifications also stipulates the level of detail and classification required of budgetary information.
- The LAF stipulates that the National Budget Office has to annually prepare a consolidated budget of the public sector. The Congress has to be informed about it before March 31st of the fiscal year.

Ley Complementaria Permanente de Presupuesto

Another law that regulates the budget process is the Law N°11.672, Complementaria Permanente de Presupuesto. It is an old law that consolidates the legal usages from the period previous to the reforms, as it was changed by each new budget law. The main points of this law are not closely related to the core of the budget process but are influential in the final outcome of the policymaking process.

- It creates the *fondos reservados* (secret funds that are administrated by the Executive).
- It stipulates that the Legislative and Judicial power are budgetary independent in the sense that they can modify their own budget without Executive's interventions.
- It authorizes the Federal Government to transfer in advance resources of the coparticipation to the provinces.

Ley de Reforma del Estado (1996)

The Ley de Reforma del Estado (State Reform Law, N° 24.629) is basically related to privatization and deregulation issues but includes rules related with the budget formulation and implementation process.

- The budget proposals have to include information about the geographical distribution – by province - of the national expenditure.
- The Executive has to submit to Congress, before June 30th, a report that summarizes the main points of next year's budget.
- It stipulates that the Executive must present to Congress a quarterly execution report within 30 days of the end of the quarter.

The recent changes in the legal framework.

The poor fiscal discipline and the procyclicality of the public expenditure in all levels of government have been an issue for at least twenty years in Argentina. Aiming to solve these problems, the Executive promoted a new Fiscal Responsibility Law – LRF -. This Law not only establishes hard budget constraints and expenditure' growth limits but also modifies some features of the budget process. The main modifications related to the budget process are:

- i) All the governmental agencies (central administration, decentralized entities, fiduciary funds and special trust) have to consolidate in the general budget. Every

new entity created has to be included in the general budget or be ruled by the LAF.

- ii) The future budget laws have to include an estimate of the fiscal cost of tax exemptions.
- iii) The degree of execution does not only depend on the budget but also on the availability of resources.

The power of the Congress in the budget process has been undermined by Executive interventions. Since 1999, the Executive found a way to bypass the restrictions imposed by the LAF and the LRF with regards to the modifications of the budget. In 2000, 2001 and 2004, the budget law itself allowed to the Executive to modify the total expenditure and to change the objective of expenditure without congressional approval. In 1999, 2002 and 2003, the same power was given to the Executive by decretos de necesidad y urgencia.

APPENDIX B: INTERVIEWS

G. Martirene. Former Budget Undersecretary. Secretaria de Hacienda. Ministerio de Economía.

D. Bonari. Director. Dirección Nacional de Gasto Consolidado. Secretaria de Política Económica. Ministerio de Economía.

H. Rodríguez Larreta. Former INSSJP Director.

Legislators and other public officers that prefer to remain anonymous.

Acronyms

AGN	Auditoria General de la Nación.	National Auditing Agency
GAEP	Grupo de Apoyo para la Elaboración del Presupuesto.	Budget's Elaboration Support Group
LAF	Ley de Administración Financiera N° 24.156	Governmental Administration Law
LRF	Ley de Responsabilidad Fiscal N° 25.975	Fiscal Responsibility Law
ONP	Oficina Nacional de Presupuesto	National Budget Office
SIGEN	Sindicatura General de la Nación.	

REFERENCES

- Abuelafia, E., Braun, M. and Díaz Frers, L. 2005. "Coparticipación Federal: una mirada más allá del debate de corto plazo". Documento de Políticas Públicas N°3, CIPPEC, Buenos Aires, Argentina. Mimeographed document.
- Alesina, A. and Perotti, R. 1995. "The Political Economy of Budget Deficits". IMF Staff Paper 42 (1):1-31.
- .1996. 'Fiscal Discipline and the Budget Process', American Economic Review, 86 (2): 401-407.
- Alesina, A. and Ardagna, S.1998. "Tales of Fiscal Adjustment". Economic Policy N° 27: 489-545. Great Britain.
- Alesina, A., Hausmann, R., Hommes, R. et.al. 1999. "Budget Institutions and Fiscal Performance in Latin America". Journal of Development Economics, 59 (2): 253-273.
- Alt J. and Lowry R. 1994. "Divided Government, Fiscal Institutions, and Budget Deficits: Evidence from the States". American Political Science Review 88: 811-28.
- Aninat, C., Londregan, J., Navia, P. et al. 2004. "Political Institutions, Policymaking Processes, and Policy Outcomes in Chile". Interamerican Development Bank, Washington,DC. Mimeographed document.
- Baldrich, J. 2003. "The Political Economy of Short Run Fiscal Policy under Fund Supported Agreements: Some Evidences from Argentina". Buenos Aires. Argentina. Mimeographed document.
- Blanchard, O. 1990. "Suggestions for a new Set of fiscal indicators". Economics and Statistics Department Working Paper No.79. Paris, France, OECD.
- Bercoff, J., Meloni,O. and Nouges, J. 2003. "La Influencia del Congreso en la Distribución de Fondos Federales". Anales 28va Reunión Asociación Argentina de Economía Política.

- Berensztein, S., Ortiz, L. and Peña, M. 2000. "Transparencia, Instituciones y Reforma: la Economía Política del Proceso de Ejecución y Ajuste Presupuestario". *Revista Internacional de Presupuesto Público* Año XXVII N°44 - noviembre diciembre 2000: 61-94
- Bohn, H. and Inman, R. 1996. "Balanced-Budget Rules and Public Deficits: Evidence from US States" *Carnegie-Rochester Conference Series of Public Policy* 45:13-76.
- Bonari, D., and Bertranou, E. 2003. *El Gasto Público Social en la Argentina: diagnóstico y perspectivas*. Córdoba, Argentina: Fundación Arcor.
- Braun, M. 2003. "Institutional Proposals for Fiscal Solvency in Argentina". CIPPEC, Buenos Aires, Argentina. Mimeographed document.
- Braun, M. and Tommasi, M. 2002. "Fiscal Rules for Subnational Governments. Some organizing principles and Latin American experiences". Paper presented at IMF/World Bank Conference on Fiscal Rules and Institutions, Oaxaca, Mexico.
- Braun, M. and Tommasi, M. 2004. "Subnational Fiscal Rules: A Game Theoretic Approach". In: G. Kopits, editor. *Rules-Based Fiscal Policy in Emerging Markets: Background, Analysis and Prospects*, Washington, DC, United States: Macmillan.
- Calvo, G., Izquierdo, G. and Talvi, E. 2002. "Sudden stops, the real exchange rate and fiscal sustainability: Argentina's lessons". Interamerican Development Bank, Washington, DC, United States. Mimeographed document.
- Cetrángolo, O. and Jiménez, J.P. 2002. "Política fiscal en Argentina durante el régimen de Convertibilidad," CEPAL. Santiago, Chile. Mimeographed document.
- Dirección Nacional de Gastos Sociales Consolidados. 2000. "Caracterización y Evolución del Gasto Público Social". Ministerio de Economía. Buenos Aires, Argentina.
- Eaton, K 2003. "Politicians and Bureaucrats in Argentina: Applying Theories of Political Control to a New Democracy". *Latin American Politics and Society* 45 (4): 32-62 United States.
- Fanelli, J. and Heymann, D. 2002. "Monetary dilemmas: Argentina in MERCOSUR" *Serie Estudios y Perspectivas* No7. Oficina de la CEPAL en Buenos Aires, Argentina.
- Gibson, E and Calvo, E. 1997. "Electoral Coalitions and Market Reforms: Evidence from Argentina". Paper presented at the XX International Congress, Latin American Studies Association. Guadalajara, Mexico. April 1997.
- Hausman R. and Velasco, A. 2002. "Hard Money's Soft Underbelly: Understanding the Argentine Crisis" Kennedy School of Government, Harvard University. Boston, United States. Mimeographed document.
- Iacovello, M., Zuvanic, L. and Tommasi, M. 2002. "El Servicio Civil en Argentina. Disfuncionalidades y Nucleos Centrales de Abordaje". Interamerican Development Bank. Washington, DC, United States.
- Jones, M. 2001. "Political Institutions and Public Policy in Argentina. An Overview of the Formation and Execution of the National Budget". In: S. Haggard and M.D. McCubbins editors. *Presidents, Parliaments, and Policy*. Cambridge, Great Britain: Cambridge University Press.
- Jones, M., Saiegh, S., Spiller, P. et al. 2001. "Amateur Legislators – Professional Politicians: The Consequences of Party-Centered Electoral Rules in a Federal System" *American Journal of Political Science*. 46 (3): 656-669.
- Jones, M., Sanguinetti, P. and Tommasi, M. 2000. "Politics, institutions, and fiscal performance in a federal system: an analysis of the Argentine provinces," *Journal of Development Economics*. 61 (2): 305-333.

- Kopits, G. (2004). *Rules-Based Fiscal Policy in Emerging Markets: Background, Analysis and Prospects*, Washington, DC, United States: Macmillan.
- Makon, M. 1998. "La Experiencia de la Reforma de la Administración Financiera Gubernamental en la Argentina". *Revista ASAP* 39: 39-50 Buenos Aires, Argentina.
- 1999. "El rol del poder legislativo ante el proceso presupuestario," Buenos Aires, Argentina. Mimeographed document.
- Mussa, C. 2002. "Argentina and the Fund: From triumph to Tragedy". Washington, DC, United States. Institute for International Economics. Mimeographed document.
- Nicolini, J. P., Posadas, J., Sanguinetti, J. et al. 2002. "Decentralization, Fiscal Discipline in Sub-National Governments, and the Bail Out Problem: The Case of Argentina". Documento de Trabajo 68, Fundación Gobierno y Sociedad. Buenos Aires, Argentina.
- Niskanen, W. 1971. *Bureaucracy and Representative Government*, Chicago, Aldine-Atherton
- Porto, A, and Sanguinetti, P. 1993. "Descentralización Fiscal en América Latina: El Caso Argentino" Serie Política Fiscal No 45. CEPAL/GTZ Chile.
- Poterba, J. 1994. "State Responses to Fiscal Crises: The Effects of Budgetary Institutions and Politics," *Journal of Political Economy*. 102 (4): 799-821
- Rodriguez, J., and Bonvecchi, A. 2004. "El Papel del Poder Legislativo en el Proceso Presupuestario: La Experiencia Argentina". Serie macroeconomía para el desarrollo N°32, CEPAL. Santiago, Chile.
- Saiegh, S. and Tommasi, M. 1999. "Why is Argentina's Fiscal Federalism so Inefficient? Entering the Labyrinth". *Journal of Applied Economics*. 0: 169-209.
- Sanguinetti, P. and Tommasi, M. 2004. "Intergovernmental transfers and fiscal behavior insurance versus aggregate discipline". *Journal of International Economics*. 62(1): 149-170.
- Scartasini, C and Olivera, M. 2004. "Political Institutions, Policymaking Process and Political Outcomes. A Guide to Theoretical Models and Possible Empirics". Design Paper 2. Interamerican Development Bank. Washington, DC, United States.
- Schick, A., and LoStracco, F. 2000. *The Federal Budget: Politics, Policy, Process*. Brookings Institution Press, New York, United States.
- Schick, A. 2003. "The alternative budget system in Argentina". World Bank. Washington, DC, United States. Mimeographed document.
- Spiller, P., and Tommasi, M. 2003. "The Institutional Foundations of Public Policy: A Transactions Approach with Application to Argentina". *Journal of Law, Economics and Organization*. 19 (2): 281-306. Oxford University Press
- Spiller, P., Stein, E., and Tommasi, M. 2003. "Political Institutions, Policymaking Processes and Policy Outcomes: An Intertemporal Transactions Framework". Design Paper 1. IDB, Washington, DC, United States.
- Stein, E., Talvi, E. and Grisanti, A. 1997. "Institutional Arrangements and Fiscal Performance: The Latin American Experience" Interamerican Development Bank. Washington, DC, United States. Mimeographed document.
- Tommasi, M 1998 "Instituciones y Resultados Fiscales" en *Desarrollo Economico* Vol 38 No149.
- 2002. "Fiscal Federalism and the reform of the 1990's". Working Paper N°72. Fundación Gobierno y Sociedad. Buenos Aires, Argentina.

Velasco, A. 1999. "A Model of Endogenous Fiscal Deficits and Delayed Fiscal Reforms". In: J. Poterba and J. Von Hagen editors. *Fiscal Institutions and Fiscal Performance*, NBER, Illinois, United States:University of Chicago Press.

Von Hagen, J. 2002 "Fiscal Federalism and Political Decision Structures" in Conference Reader of the International Conference on Federalism 2002, St. Gallen (CH).

Von Hagen, J. and Harden, I. 1996. "Budget Processes and Commitment to Fiscal Discipline". Working Paper 96/78. IMF. Washington, DC, United States.

Weingast, B., Shepsle, K. and Johnsen, C. 1981. "The Political Economy of Benefits and Costs: A Neoclassical Approach to Distributive Politics". *Journal of Political Economy*. 89: 642-64