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Developing a Congressional Caucus to Promote Fiscal Reforms in Argentina

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The federal fiscal system in Argentina is in a state of disrepair. Rather than providing equality, transparency, and stability for Argentina's federal and provincial governments, the system exacerbates the country's pervasive inequalities, corrupt practices, and instability. One of the reasons for the failures of the fiscal system is lack of civil society participation in the policymaking process.

To strengthen the legislature's ability to examine and debate FCS reforms, the Argentine Center for the Implementation of Public Policies Promoting Equity and Growth (CIPPEC), with support from CIPE, helped to create a congressional co-participation caucus consisting of reform-oriented legislators from across party lines, civil society leaders, and academics. The caucus has had a strong impact on the policymaking process in the country, and in the coming years it will continue to serve as the only vehicle in Argentina for organizing a reform-minded coalition of legislators, civil society leaders, and academics to discuss issues, find solutions, and implement change, thereby strengthening Argentine democracy.



Introduction

Argentina has a long history of fiscal mismanagement. Over the past 20 years, the country has undergone two debt crises and two periods of hyperinflation. Public expenditures have been systematically higher than tax revenues. As a consequence, successive governments have resorted either to printing money or issuing debt to finance the gap. The abuse of these instruments in Argentina has led to recurring crises. An inability to achieve prudent fiscal management became a systematic feature of the Argentine political system.

Although the latest figures seem to indicate a more responsible fiscal management, few structural changes to the system have been implemented. The reality today is that fiscal institutions need to be strengthened (or created in some instances) in order to ensure prudent fiscal policies in the long run.

The poorest Argentines have been hurt the most from these policy failures. Inflation and devaluation have affected the purchasing power of peso incomes, but left wealthy citizens with dollar-denominated assets better off. Furthermore, when a recession hit and credit dried out, the government was forced to reduce spending on social services, which are mainly targeted to the poor. This practice is contrary to countercyclical fiscal management policies typically implemented in developed countries.

The result of these and other misguided policies was that between 1975 and 1990, real GDP per capita in Argentina fell by over 30% (with a bubble in the late 1970s due to the unsustainable overvaluation of the peso promoted by the military dictatorship). Growth in the 1990s resumed following market reforms, deregulation, and financial stability measures, but given the existing imbalances, it did not prove to be sustainable. Furthermore, income distribution became substantially more unequal. The richest 20% of the population earned 26 times more than the poorest 20% in 2001, whereas this ratio was considerably lower at 14 in 1991. All these indicators worsened severely after the last crisis, which drove more than half of the population under the poverty line and a quarter under indigence levels in 2002.

Consequences of Weak Fiscal Institutions

The weakness of fiscal institutions and the subsequent recurrent crises have had a significant negative impact on general economic performance, on the business environment, and on the incentives of the private sector for long-term investment.

Moreover, fiscal instability has had negative consequences in the provision of public goods, thus limiting the outcomes of Argentine democracy and its public legitimacy. Argentina's Congress, as others in Latin America, lacks adequate technical staff and institutions to analyze, debate, and control fiscal matters in an appropriate manner. There is no institution comparable to the U.S. Congressional Budget Office, for example, and few legislative aides have professional proficiency in tax and federal issues. In that sense, the quality of the debate on fiscal issues in the legislative branch of government through in-depth analyses, advice on implementation, and targeted advocacy strategies is lacking.

The negative consequences of this state of affairs in Argentina are both economic and, more importantly, political. There is popular support for democracy in Argentina, yet very low levels of satisfaction with its performance. The 2003 Latinobarómetro poll, for example, showed that in Argentina a democratic government is preferred over an authoritarian one by 69% of the population, compared to the average of 53% for the rest of Latin America. But only 29% of those polled in Argentina showed satisfaction with the day-to-day functioning of its democracy, compared to 34% in other Latin American countries. The disparity is evident.

Failures of the fiscal system and the subsequent socioeconomic failures are one of the reasons for this frustration with democracy in Argentina. Further, the functioning of the fiscal system, which lacks true civil society participation in the process, is a testament to the lack of participatory democratic institutions in the country. Such institutions are integral to the success of any democracy. This emphasis on participation in policymaking is key, because democracy is about much more than simply electing officials to the public office.

The Real Problem

Clearly, the federal fiscal system in Argentina is in a state of disrepair. Rather than providing equality, transparency, and stability for Argentina's federal and provincial governments, the system exacerbates the country's pervasive inequalities, corrupt practices, and instability. But what are the underlying reasons for this problem? Although the factors behind this mismanagement are many, three in particular must be emphasized.

The first major problem is the existence of discretionary, non-transparent fiscal expenditures. In Argentina, expenditures have been consistently higher than taxes. Lacking transparency and subject to political pressures, successive governments have resorted either to printing money or issuing debt to finance this gap.

The second major problem is the complex, unstable, and inefficient tax system. Although Argentina's tax rates are similar to those of other countries with comparable levels of economic development, its tax receipts are relatively small - a clear indication of low tax administration efficiency and high levels of tax evasion. Furthermore, this makes the tax load excessive for those who cannot or will not evade, creating multiple distortions and feelings of injustice and general discontent. The 2001 fiscal crisis exacerbated the situation through new, highly distorting taxes such as the levies on financial transactions and exports.

Finally, Argentina also has a very complex and arbitrary federal co-participation system. Established in the 1930s, the Argentine Federal Co-participation System (FCS) transfers a portion of the revenues collected from certain federal taxes, including personal and corporate income taxes and the value added tax, to the 24 provincial governments. In 1997, for example, the federal government collected 79% of total tax receipts, while the provinces and municipalities collected 16.5% and 4.5%, respectively.¹ In addition to the tax revenue sharing, there are several other mechanisms by which the federal government transfers revenues to the provinces, despite the constitutionally granted power of local governments to institute their own direct

taxes. The FCS has been severely criticized for 1) a high degree of vertical disequilibria; 2) extreme complexity and lack of transparency; 3) arbitrary distributions; 4) absence of debt limits; 5) federal bail-outs through ad-hoc agreements; 6) repeated breaking of commitments by the federal government and the provinces; and 7) the absence of a federal fiscal or judicial institution to solve these conflicts. Overall, the FCS has produced funding difficulties among the different levels of government as well as abundant opportunities for corruption via the discretion used to distribute resources among the provinces.

Addressing the Problem: FCS Reform

The weak, inefficient federal fiscal system has had a significant negative impact on economic performance, the business environment, and private-sector incentives for long-term investment. There is no doubt in anyone's mind that the system must change.

One of the benefits of implementing FCS reform is that if done right, it would lead to more predictable fiscal outcomes, thus facilitating better public policy planning and better quality and/or quantity of public goods provision in the federal, provincial, and municipal governments. Such improved planning and public goods provision, in turn, can lead to increased equality of opportunity for Argentine citizens. For example, the provinces of La Rioja and Cajamarca have similar characteristics in terms of population density and per capita income, but La Rioja receives \$900/month more per capita from the federal government, the apparent result of political bargaining. Improved planning and public goods provision will also help stimulate long-term investment.

Another benefit is a major improvement in the Argentine government's transparency via the improved transparency of fiscal institutions and reduced tax evasion. Higher transparency standards and less evasion and corruption are especially important for a democracy like Argentina's, in which corruption ranks as the most important issue second only to unemployment (Latinobarómetro 2003 poll), and would create a more level playing field for private activity.

FCS reform would also lead to more transparent and efficient tax and revenue allocation systems, which may help diminish existing citizenship contradictions in Argentina, in which citizens' rights and obligations have been excessively dissociated.

A reform of Argentina's fiscal federal system can only come about with the commitment and support of the executive and legislative branches of government at the national and provincial levels. These two branches, however, have severely undermined efforts for reform. The legislature usually exercises its power to stop reforms or introduces unnecessary complexities to legislation, leading the executive to approve reforms by decree, without input from the public or civil society groups. While the legislature is more suited for this type of discussion, it is constrained by a shortage of technical staff that can evaluate all the implications of fiscal policies. As noted earlier, few legislative aides have professional proficiency in tax and federal issues, and there is no regular mechanism for training members of Congress on tax issues. Consequently, there is a serious lack of understanding, which hampers the objectivity of debates and the ability of Congress, the media, and citizens for meaningful participation in these issues.

A Novel Approach to Reform: The Caucus

To strengthen the legislature's ability to examine and debate FCS reforms, the Argentine Center for the Implementation of Public Policies Promoting Equity and Growth (CIPPEC) helped to create a congressional co-participation caucus consisting of reform-oriented legislators from across party lines, civil society leaders, and academics. The caucus was launched on December 16th, 2004 by Senator Celso Jaque, President of the Senate Co-participation Commission, and Vice-President Daniel Scioli, who also serves as President of the Senate.

The caucus represents a ground-breaking approach to addressing fiscal imbalances some seventy years in the making by providing a transparent forum for analyzing and debating reform-related issues as well as reform proposals. It has raised awareness among members, the legislature, and the public of the need for and benefits of a responsible, stable fiscal policy. It

has also provided sound information and analyses to foster a better understanding and strengthen debate of tax and co-participation policies. A website (<http://forofederalismo.senado.gov.ar>) was developed to register the events of the caucus and link its participants.

A key element of CIPPEC's approach to developing the caucus centered on identifying legislators with an interest in and influence on fiscal-policy decision-making, inviting them to meetings, introducing policy briefs to them, and soliciting their cooperation as disseminators of these briefs within committees and Congress. By building a closer relationship with legislative offices, CIPPEC was able to enhance the effectiveness of our efforts and thereby strengthen the links between research and policymaking.

Initially, CIPPEC developed three policy briefs on co-participation. An analysis of the negative consequences of co-participation on the education system struck a cord with and was well-received by the politicians and academics, since the impacts of the FCS on everyday life are generally either not addressed at all or are treated in a very abstract manner. A detailed analysis of the evolution of provincial finances, featuring a comparison before and after the 2001 crisis, with emphasis on the role of co-participation, generated significant interest among the media.

CIPPEC sent copies of policy briefs to the offices of all representatives (257) and senators (72) and followed up by telephone. Thirty one-on-one meetings with legislators and advisors were held to discuss the best way to advance discussion on co-participation in Congress, including personal and partisan incentives to support change and challenges of implementation. Additionally, CIPPEC organized and participated in 8 presentations and seminars attended by 45 legislators and advisors to discuss fiscal issues. A very successful seminar in May 2004 was attended by well-known politicians, legislators, and aides, including the governor of the province of Buenos Aires, Felipe Solá and it received extensive coverage through 13 newspaper articles.

CIPPEC worked closely with the Senate Co-participation Commission, which is charged with overseeing legislative proposals concerning the FCS.

The Commission also examines the provision of transfers and other services to the provinces by the federal government. As such, it takes the lead in all caucus events, but many other institutions participate in the forum. Together with other organizations, CIPPEC has organized several workshops to encourage policymakers, business, and other civil society leaders to discuss how to shape specific policy reforms. Specialized journalists were also invited to help disseminate the ideas discussed during these events. Interaction among these sectors plays a pivotal role in building consensus, increasing advocacy opportunities for different groups, and strengthening civil society's participation in the policymaking process.

CIPPEC has focused on supporting the caucus by providing technical advice on tax bills in the form of policy briefs and complementary communication strategies. CIPPEC has published 10 policy briefs on tax bills, covering topics ranging from the Fiscal Responsibility Law to the taxes implicitly approved in the national budget to very specific tax bills.

Impact

CIPPEC's biggest achievement has been the formation of the caucus and the commitment from the Senate Commission on Co-participation to lead its events. Given that caucuses are not a common strategy to advance reform in Argentine politics, the fact that CIPPEC achieved institutional support from Congress to set up a caucus to address reforms in such a sensitive legislative area is a clear signal of success.

The activities carried out within the caucus have had several impacts. Clearly, there is an increasing awareness in Congress and civil society regarding the importance of sound fiscal policy, thanks to the influence in Congress and the media of CIPPEC's policy briefs and presentations. The research, website, and workshops are providing Congress, civil society, and the public with sound information and analysis on tax and co-participation issues.

From CIPPEC's own small survey of legislators conducted in March 2005, 25 out of 26 respondents (96%) said that they had read at least some of the

organization's policy briefs. Of these, 21 (84%) said the topics discussed were very relevant, 19 (76%) stated that the documents were interesting, and 17 (68%) found the policy briefs useful for their decision-making process. Furthermore, CIPPEC estimates that around 30 legislators are active participants in the caucus, while 75 legislators and 60 advisors have participated in nearly 100 meetings.

Another way to assess the impact is to analyze the results on the bills CIPPEC evaluated. Although it must be recognized that other factors have contributed to their implementation, recommendations from several of CIPPEC's policy briefs that dealt specifically with tax bills were included in the approved legislation. For example, recommendations from Policy Brief #3, which focused on the analysis of the 2005 budget, on stronger anti-evasion measures, a reduction in the financial transactions tax, and a stronger analytical capability on budget issues, were included in legislation.

Through its program, CIPPEC received media coverage in 81 newspaper articles, 64 radio/TV interviews, and 45 online website articles. Some policy briefs, like the one on education and co-participation or the one on the social security system, have received significant popular and media attention, with numerous requests for further information from other NGOs and academics, as well as legislators and their aides. Media plays a crucial role in allowing civil society to introduce new topics into the public agenda as well as enhance the quality and depth of discussion around significant public issues such as tax reform and co-participation. CIPPEC has become a reference source for journalists and opinion leaders, who, in turn, influence policymakers through news coverage. Several legislators indicated in the survey that they use newspapers and CIPPEC's policy briefs as their sole sources of information, aside from some research carried out by their aides.

Much work, however, remains to be done. CIPPEC's experience thus far indicates that tax bills are generally not significantly modified in Congress and are either approved or discarded in their original version. Nonetheless, there has been a significant improvement in how the system functions, in that

an outside party like CIPPEC has been given the opportunity to contribute to the policymaking process. The inroads that the organization has made into the legislative process provide ample opportunity for future achievements.

CIPPEC's next steps include implementing programs to strengthen the analytical capability of the Argentine legislature on fiscal policy. CIPPEC has observed that one of the main reasons behind the pass/fail approach to passing laws seems to be the lack of technical capabilities to thoroughly evaluate the effects of pending legislation. Through its capacity-building efforts, the caucus can help advance the cause of fiscal reform in Argentina and stimulate progress toward the other important benefits described above. In addition, the caucus will continue to serve as the only vehicle in Argentina for organizing a reform-minded coalition of legislators, civil society leaders, and academics to discuss issues, find solutions, and implement change, thereby strengthening Argentine democracy.

¹In the same year, however, provinces and municipalities accounted for 47.3% of total spending, versus 52.7% for the federal government.

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Miguel Braun received his Ph.D. and MA in economics from Harvard University and a BA in Economics, summa cum laude, from Universidad de San Andrés in Buenos Aires, Argentina. In 2000, he cofounded CIPPEC, a think tank dedicated to policy research and implementation in Argentina, and became director of the Fiscal Policy Area. He teaches at Universidad de San Andrés, where he also served on the Advisory Council, and has worked as a consultant for the Inter-American Development Bank, the Economic Commission for Latin America and

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