Budgeting in Brazil

by

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**Introduction**

During his September 2002 visit to OECD Headquarters in Paris, Mr. Guilherme DIAS, the Minister of Planning, Budget and Management, requested the OECD to carry out a review of the Brazilian budgeting system in a similar fashion as it does for its member countries.

The OECD responded positively to this request, recognising that Brazil is an established observer of the OECD Working Party of Senior Budget Officials and a key partner in the OECD’s overall programme of co-operation with non-members.

In view of the short timeframe available for conducting the review, it was agreed that the report would not discuss Brazil’s system of fiscal federalism.

A mission visited Brasilia in October 2002 to carry out the review. During this visit, the mission met with senior officials from the Ministry of Planning, Budget and Management; the Ministry of Finance; the central bank; the Ministry of Internal Control; and line ministries, including the Ministry of Education and the Ministry of the Environment. The mission also met with senior officials from the Brazilian Congress and the Court of Audit.

The mission would like to express its gratitude and appreciation for the warm and cordial reception by the Brazilian authorities and the uniformly frank and useful discussions with Brazilian officials. In particular, the mission would like to express its thanks to Minister DIAS for the generous time he shared with the mission during its stay in Brasilia.

Finally, the mission would like to thank Mr. Joaquim LEVY, Chief Economist and Ms. Giulia PUTTOMATTI, Ministerial Advisor, Ministry of Planning, Budget and Management, for organising the mission’s visit and for their excellent and invaluable assistance throughout this review.

The views expressed in this report are those of the OECD Secretariat and should not be attributed to governments of OECD member countries, or to any organisation or individuals consulted for this review.

The review was completed in December 2002.
1. Budget formulation process

1.1. Introduction

The macro-economic environment for budgeting in Brazil has undergone profound change in the past eight years with the introduction of the Real Plan in 1994. Its cornerstone was to bring down inflation and nurture macro-economic stability. Inflation went down from 5,014% in the 12 months preceding the Real Plan to 22% in the next 12 months (1995), then to 9% in 1996, 4% in 1997, and 2.5% in 1998. It rose again to 8.4% in 1999, the year of devaluation and the introduction of a floating exchange rate (brought on by the Russian crisis), before dropping back to 5.3% in 2001.

After decades of inflation, the country’s budget had come to rely on the “inflation tax” as a significant source of revenue. The government in effect indexed the revenue side of the budget, while a significant portion of the expenditure side of the budget was non-indexed. This price differential was an artificial means of maintaining expenditures. With the sharp drop in inflation achieved by the Real Plan, it was no longer possible to finance the same level of government expenditure.

At the state level, the impact of the loss of the “inflation tax” was exacerbated by the fact that the states had accumulated large debt as a result of previously enjoying easy access to the financial markets. This created a crisis for the states as they would no longer be able to service/repay their debts. As a result, the federal government embarked on a large debt-restructuring programme for the states in 1997. The federal government assumed the states’ debt to banks and the bond markets, issuing Treasury bonds to the states’ creditors and entered into contractual agreements with the states for their eventual repayment of the debt that had been assumed. These contracts were on much more favourable terms than those offered by the market, but they were conditional on a set of states’ commitments to fiscal adjustment. These conditions were also enshrined in the Fiscal Responsibility Law of 2000, along with other provisions.

The net result for the federal government is, however, that its level of debt increased significantly by this assumption of debt. The debt profile of the federal government is also characterised by a short maturity and the fact that a significant part of it is indexed either to short-term interest rates or the exchange rate.

For the federal government, it is essential to bear these two factors in mind: first, the funding constraint brought by the loss of the “inflation tax” and the volatile debt profile.

Budgeting is generally viewed as having three functions. First, the maintenance of the aggregates. Second, the allocation (and reallocation) of
resources to sectors where they are most needed. Third, the efficient use of resources in each sector. There are generally tensions between these three functions, with countries forced to choose which one they place more emphasis on. It is evident that Brazil’s budget formulation process puts a large emphasis on the maintenance of the aggregates. This is well justified as stabilisation of the aggregates is a prerequisite for overall economic stability which is essential for all other activity in the economy. In addition, several institutional constraints limit the scope for discretionary changes in allocations across programmes or sectors.

Box 1. **Fiscal Responsibility Law**

The Fiscal Responsibility Law enacted in 2000 evolved from the “hands on” experience of the renegotiation of state debts. As such, it is a practical and pragmatic law that consolidates previous directives and introduces a comprehensive set of provisions to foster fiscal responsibility. Among the key features of the law are maximum limits on the level of personnel expenditure and the level of debt, as a proportion of net current revenues, and the principle that any new medium-term expenditure has to be “affordable.”

The limits on personnel expenditure are identified for each branch of government in the three levels of the federation (union, states and municipalities) and include both active and retired public servants. Ceilings on the debt are also set by level of government.

“Affordability” is demonstrated in several ways. In some cases, it is sufficient to show that new expenditure will fit within the established budget expansion baseline (i.e. room created by GDP growth keeping constant policies).

For the case of new mandatory expenditure, the requirement is strengthened by the rule that the room has to be created by replacing other expenditure or introducing new taxes. (This is similar to the PAYGO rules applied in the United States.) Similar rules also bind any new tax expenditure and subsidies to the private sector.

The law also contains extensive provisions for increased budget transparency and the monitoring of budget implementation. The law also provides for extensive corrective measures to be taken in case of any breaches, including both institutional and personal sanctions. The latter includes fines and incarceration for the officials responsible.
This section is divided into two parts. Section 1.2 presents several distinctive features of the Brazilian budget formulation system. Section 1.3 builds on these and discusses the main steps in the annual budget process.

1.2. Distinctive features

This section reviews three distinctive features of the Brazilian budget formulation process compared to those generally found in OECD member countries. They are the high degree of rigidity in the system, the operation of a separate planning function and the lack of rolling multi-year expenditure frameworks.

1.2.1. High degree of rigidity

The Brazilian budget is very rigid. This is due to the large amount of expenditures that are mandated by the Constitution, the earmarking of tax revenues to specific uses and the designation of certain expenditures as “mandatory”. The effect is to insulate a very large proportion of the budget from effective scrutiny each year. It is estimated that over 90% of the budget is subject to these rigidities.

1.2.1.1. Constitutionally mandated expenditures

The Brazilian Constitution contains provisions that guarantee the funding of three types of government expenditure:

- revenue-sharing with states and municipalities;
- salaries (and pensions) for government employees;
- interest on, and repayment of, the public debt.

From a budgetary point of view, the first two items pose challenges. The protection of government employees’ salaries has the effect of largely insulating them from fiscal adjustments and from critical scrutiny during the budget formulation process. Once an individual is in a certain position, it is “for life”. This is discussed further in Section 3 – Management. A constitutional amendment has been approved to change this provision, but it is currently being challenged in the courts and has not become operational.

Revenue-sharing with municipalities and states is not detailed in the Constitution itself but elaborated in a “complementary” law. Such laws require a super-majority (two-thirds) in Congress in order to amend them, which is generally an insurmountable hurdle. Furthermore, the interpretation of the Constitution is that virtually all existing or new non-earmarked taxes have to be shared with states and municipalities.
1.2.1.2. Earmarking of tax revenue

Earmarking of tax revenue to finance certain categories of expenditure is widespread in Brazil. It is estimated that about one-half of total revenues is earmarked. In terms of amounts, it is focused mainly in the social sectors (education, health care, housing, social benefits) but is prevalent in all sectors. In order to avoid double-counting, it is important to note that part of the expenditure for education, salaries for example, is counted as a constitutionally mandated expenditure as well. This double binding serves to further illustrate the rigidity in the Brazilian budget formulation process.

There would appear to be several major reasons for the widespread use of earmarking – both historical and contemporary.

First, during Brazil’s high inflation years, earmarking was essentially meaningless to have a specific appropriation in the budget in nominal terms. By linking expenditures with a revenue source, it was possible to “insure” the expenditures against the effects of inflation, as the revenues would rise in line with inflation.

Second, with the end of high-inflation, it was a reaction against the system of presidential budget implementation decrees, which are discussed later in this section. The Brazilian budget is “authoritative”, i.e. it sets the “maximum” level of expenditure for each appropriation, but the government is not obligated to spend the full amount appropriated. It can reduce certain appropriations made by the Congress (impoundment). Appropriations linked to earmarked taxes are less susceptible to such actions.

Third, because of the revenue-sharing imposed on most non-earmarked taxes due to the legal interpretation of the Constitution, the federal government is sometimes compelled to introduce an earmarked tax, despite their lower efficiency.

The effect of earmarking varies greatly according to how specific it is. Earmarking in bulk to large sectors such as education – which most objective analysis would agree is an area in need of additional resources – is the equivalent of setting expenditure ceilings, or rather “floors”, for those sectors. Budgeting then consists of allocating that aggregate amount among the various programmes within the sector. This type of earmarking appears to be largely harmless in individual cases. However, taken together they impose serious rigidities on the budget formulation process.

Earmarking for very specific purposes imposes rigidities of a different order. For example, royalty taxes for the exploitation of a certain natural resource were earmarked to conducting environmental impact studies. When the world market price for this natural resource rose significantly, the revenue made available to conduct environmental impact studies multiplied. This type
of very specific earmarking undermines effective budgeting and measures should be taken to avoid them.

The overall effect of earmarking is to insulate a large proportion of the budget from scrutiny each year. In fact, seeking earmarked status has become the major budgeting battle in recent years. For example, health care has recently been linked to an earmarked tax and therefore escapes potential cuts during the annual budget cycle.

A unique measure was introduced in 1993 to overcome the rigidities. A "tax" was introduced on all earmarked taxes at the rate of 20% (except revenue-sharing arrangements with the states and municipalities). The proceeds of this tax are made available for general purposes as decided in the annual budget each year. This arrangement expires at the end of 2003. While alleviating some of the symptoms of the rigidities in budgeting, this tax does not address its underlying causes.

1.2.1.3. “Mandatory expenditures”

A third level of rigidity is introduced in the budgeting system by the existence of expenditures established by law as “mandatory,” (e.g. entitlements). The major effect of being so designated is to insulate the appropriation from cuts in the presidential budget implementation decrees. Mandatory expenditures can be divided into two groups: those deriving their status from constitutional mandates, as discussed above, and those deriving their status from ordinary law (notably the Budget Guidance Law – see Section 1.3.1). The latter are reviewed annually and are therefore of a different nature than the former ones.

Mandatory expenditures are largely funded by earmarked revenues, but the link may not be direct or comprehensive. A recent constitutional amendment establishes that a minimum percentage of GDP should be spent on health activities (circa 1.7% of GDP). However, only relatively little specific revenue is formally earmarked to health expenditure (circa 0.4% of GDP). Moreover, Congress has in recent years designated several other expenditure programmes as “mandatory” in the Budget Guidance Law, in order to protect them from cuts in the presidential budget implementation decrees.

Efforts should be made to reduce the level of rigidities in the budget process. This will likely be a slow process as the rigidities have built up over many years. The annual budget process needs to show that it can resolve competing claims for resources. It should simply not be necessary to have such rigidities in a well-functioning budgeting process, especially if previously agreed priorities established within a multi-year framework are established between Congress and the government, including its different ministries.
1.2.2. Central planning function

In recent years, Brazil has developed an elaborate central planning function in addition to the budget. In relation to the budget process, the plan can be seen in at least three lights.

First, it can be seen as an attempt at results-oriented budgeting, to complement the regular input-based budget. The plan comprehensively covers all government expenditures – current, capital and transfers – in several hundred outcome- or output-based programmes.

Second, it explicitly highlights the political priorities of the government. About one-fourth of the total number of programmes are designated as priority programmes. This has two major effects. First, priority programmes are automatically designated as “mandatory” programmes and protected from cuts in the presidential budget implementation decrees. Second, their designation as priorities in the plan should be viewed as an attempt to improve the management of those resources that would in any case be spent. In contrast to ordinary programmes, which are subject to the discretion of individual ministries, spending on “priority” programmes is aided by the Ministry of Planning, Budget and Management, which can optimise the allocation of scarce resources over the whole portfolio of such programmes.

Third, it serves as a marketing device for attracting private sector investment in various capital projects (public-private partnerships) by officially listing desired projects and showing how private sector investment may be leveraged by public investment in related areas.

The Brazilian planning system is therefore not the classic “central planning” model.

The plan and the budget should complement each other. In reality, however, they operate in parallel and largely disconnected ways. Both the budget and the plan are the responsibility of the Ministry of Planning, Budgeting and Management, although they are located in two very distinct secretariats within the ministry. These are both impressive organisations; but in their separateness they detract from each other.

It is difficult to rationalise one system for deciding the outcomes/outputs of government and a separate system for deciding the inputs of government. The two are dependent on each other, both conceptually and practically. The practice in Brazil is for decisions to be made in the budget and in the accompanying budget implementation decrees, and only subjected to perfunctory consistency with the plan. One reason for this disconnection is that the plan is for a fixed period in time, rather than for a rolling multi-year horizon (see Box 2).
Brazil has a unique opportunity to unify its budget and plan, and integrate its budgeting and planning apparatus. This would create a truly results-oriented budget process that would provide important advantages over the present system. It would strengthen policy co-ordination. It would assist in resource allocation by having clear linkages between inputs/results. Over time, this would serve to lessen the reliance on the rigid measures detailed above. It would also avoid the duplication of effort – both at the centre and in the spending ministries – and end the non-clarity of the dual budgeting/planning system.

Box 2. Preparing the plan

The plan is a fixed four-year instrument. Each President must present a plan to Congress during the first year in office. The plan thus covers three years of each presidency plus the first year of the subsequent presidency.

Prior to elections, meetings are held with representatives from all presidential candidates to inform them of the process of preparing the plan and to get indications of the possible directions of the plan, given the election of each candidate. Line ministries are then informed about the likely priorities of the different candidates in regard to the plan.

In parallel with these consultations, policy studies are undertaken, primarily by hired external consultants. In addition, civil servants are trained in how to contribute to the making of the plan. Finally, a number of more general projects as regards planning techniques are typically initiated. As part of the preparation for the 2003-2007 plan, for example, a unit has been established to investigate how a new approach to public-private partnerships can be applied in the plan.

Attempts to strengthen the results-oriented aspects of the plan have already resulted in the setting of quantitative targets for each programme, typically measured by changes in social indicators computed by independent agencies.

The actual drafting of the plan is undertaken in an iterative dialogue between line ministries, the Ministry of Planning, Budget and Management and the President’s Office. The Ministry of Planning, Budget and Management is responsible for ensuring consistency between programmes.
1.2.3. Lack of rolling multi-year expenditure framework

There is no rolling multi-year expenditure framework in place in Brazil.³

In OECD member countries, medium-term budget frameworks form the basis for achieving fiscal consolidation. They need to clearly state the government’s medium-term fiscal objectives in terms of high-level targets such as the level of aggregate revenue, expenditure, deficit/surplus and debt. They then need to operationalise these high-level targets by establishing hard budget constraints for individual ministries and programmes over a number of years. This lends stability and credibility to the government’s fiscal objectives.

By their very nature, high-level fiscal targets are set in a medium-term context. They aim to achieve a certain fiscal outcome over a number of years. However, budgets are enacted for a time period of one year and are notorious for their short-term focus. This short-term time horizon is often criticised for impeding effective expenditure management; decisions on resource allocation are said to be made on an ad hoc or piecemeal basis with the implications of past and present decisions beyond the next year being neglected. This is not a new criticism. Medium-term budget frameworks aim to bridge this gap. Their successful implementation has been nothing short of a “cultural revolution” in public expenditure.

Although the level of detail of such frameworks varies from country to country, they generally mirror the format of the budget, i.e. the medium-term frameworks are at the same level of detail as the annual budget. This means that a formal framework (or hard budget constraint) exists for each and every appropriation, most often for three years beyond the current fiscal year. These are rolling frameworks that are presented with the budget each year; year-1 in the previous year’s framework becomes the basis for the budget and a new year-3 is added. This has greatly increased the effectiveness of planning and eased the annual budget process.⁴ These frameworks are not, however, enacted into legislation; they are planning documents that reflect the political commitment to fiscal discipline.

It should also be emphasised that these are living documents. The fact that a three-year budget framework is in place does not mean that no changes can be made to the document. In fact, shifting appropriations within ministries has been key to their success in member countries. However, it is imperative that all such changes be clearly depicted and explained, e.g. whether the changes are the results of changed economic circumstances or new policy decisions. Most countries publish detailed reconciliation between year-1 in the previous year’s framework and the current budget proposal.
There is every reason to believe that such a framework would be effective in Brazil. In fact, to the extent to which the budgetary process has moved in this direction – i.e. the imposition of high-level fiscal targets and aggregate revenue and expenditure estimates – results have been positive. The framework, as already implemented, has helped to introduce greater transparency to the conduct of fiscal policy and facilitate the discussion of the annual budget, despite localised resistance and scepticism.

1.3. Annual budget process

The annual budget process is divided into three phases. The first phase concerns the setting of aggregate multi-year fiscal targets in the draft Budget Guidance Law that is presented to Congress in April, including the review of previously set targets. The second phase is the development of the annual budget that is presented to Congress in August. The third phase concerns the presidential budget implementation decrees, which can markedly change the budget as enacted by Congress, together with other supplementary measures throughout the year.

1.3.1. The Budget Guidance Law

On 15 April, a draft Budget Guidance Law must be submitted to the Congress for approval. Congress has until 30 June to pass this as law. The law contains three major features.

According to the Fiscal Responsibility Law, the Budget Guidance Law must present a target for the primary surplus for the next year and the two subsequent years. This is currently set at 3.75% of GDP for the public sector as a whole, with specific targets for the federal government consistent with the overall target. In addition, projections of aggregate revenues and expenditure are to be presented in the law.

The main purpose of the law is for Congress to approve the level of the primary surplus as proposed by the government, which it has always done. This sets the stage for the development of the budget.

Second, the draft Budget Guidance Law stipulates which expenditures are to be designated as mandatory, meaning that they are protected from cuts in the presidential budget implementation decrees. Even though these could be changed by the annual budget, the list does give a comprehensive overview of the annual priorities. The bill also contains information concerning the lending policies of various government financial institutions.
The “primary” balance

Budgetary policy in Brazil focuses on the primary balance, i.e. before interest expenditure. As noted, the goal of fiscal policy is currently a primary surplus of 3.75% of GDP in 2003-2004 (3.88% of GDP in 2002). By contrast, the actual balance, i.e. after taking into account interest expenditure, is the main measure used in all OECD member countries to judge fiscal policy. By this conventional measure, Brazil's fiscal deficit was 3.54% of GDP in 2001. The evolution of these two measures over the past several years is summarised in the following table.

Non-financial public sector
Nominal and fiscal balance (% of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>Nominal</th>
<th>Primary</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>−7.46</td>
<td>0.01</td>
</tr>
<tr>
<td>1999</td>
<td>−5.83</td>
<td>3.28</td>
</tr>
<tr>
<td>2000</td>
<td>−3.64</td>
<td>3.55</td>
</tr>
<tr>
<td>2001</td>
<td>−3.54</td>
<td>3.75</td>
</tr>
<tr>
<td>Jan-Oct 02</td>
<td>−3.1</td>
<td>5.07</td>
</tr>
</tbody>
</table>

The use of the primary balance as a fiscal target is explained by Brazilian officials as a response to the volatility of exchange rates and interest rates. Furthermore, the level of the primary balance is designed to stabilise and reduce the level of outstanding debt in the medium term. The choice of the primary balance as the target was originally made by the Brazilian authorities themselves, and now forms an integral part of Brazil's current agreement with the International Monetary Fund.

The focus on the primary balance in Brazil does not obscure the transparency of the true state of fiscal finances because of the simultaneous emphasis on the debt dynamics. This approach captures the change in the government net worth caused by the impact of the exchange rate on the stock of the net public debt, i.e. it captures not only changes in flows but also one-off adjustments in the stock of debt, which can be significant.

Monthly statistics on the primary and nominal balance, including the change in gross and net public debt of the federal, state and local governments, as well as of the consolidated public sector, are published within four weeks of the closing of every month. The Treasury and the central bank hold press conferences at the time of the release of such statistics, discussing the factors contributing to the relevant changes.
Finally, the Budget Guidance Law contains a number of procedural issues that in OECD member countries would be found in an organic budget, or similar, law. Further discussion of this law, including its treatment in Congress, is presented in the next section.

1.3.2. The annual budget

The starting point in each year’s annual budget process involves internal reviews by the Planning Secretariat and Budget Secretariat of the Ministry of Planning, Budget and Management. The exact process has evolved in recent years, as fiscal targets have become more binding and the role of mandatory expenditures increased.

The Planning Secretariat reviews the results of the previous year’s activities in terms of outcomes and outputs. The Planning Secretariat also proposes amendments to the list of priority programmes and transmits this list to the Budget Secretariat. As mentioned, such programmes are essentially immune from cuts in the presidential budget implementation decrees and define the political priorities of the government.

The Budget Secretariat’s review incorporates the results of the Planning Secretariat’s review but focuses more on the amount of resources needed to carry out each organisation’s activities. It also carries out a review of previous years’ spending, using internal models for certain categories of expenditures and other analytical methods. At the end of May or early June, the Budget Secretariat will issue a maximum level of expenditure for each ministry. This is the culmination of the Budget Secretariat’s review of resources and will incorporate discussion in Congress on the Budget Guidance Law, i.e. whether new expenditure programmes are being identified as “mandatory”.

It should be noted that the Budget Secretariat’s review of resource needs is a very formalised process with an internal two-volume dossier prepared for each spending ministry. It is prepared by the sectoral specialists in the Budget Secretariats and is reviewed by the Director himself in extensive internal meetings. Before issuing the maximum level, the Minister of Planning and Budget and the Executive Secretary of the ministry (top civil servant) will review it. It is noteworthy that the President does not review these spending levels prior to their being issued.
Spending ministries are then given three weeks to input their detailed allocations in the computerised budget formulation system. The computer system will not accept allocations that are in excess of the overall maximum allowed. Spending ministries will appeal against their allocations, but this is not reviewed in the three-week timeframe. The Budget Secretariat will itself input the detailed allocation information based on its own views if the spending ministries fail to do this.

It is striking that spending ministries do not submit detailed budget proposals to the Budget Secretariat before the maximums are issued, although there are informal discussions of priorities and needs. This may be a function of the fact that the professional capacity of ministries varies greatly. It may also be because of the fact that a great number of items are “mandatory” in nature. However, it does offer the Budget Secretariat important tactical advantages vis-à-vis the line ministries.

The Budget Secretariat keeps a small “kitty” in order to finance additional expenditures in the appeals process. The appeals process operates on three levels. First, the Executive Secretary of the respective spending ministry will meet with the Executive Secretary of the Ministry of Planning, Budget and Management. This invariably occurs and can be described as an integral part of the budget process. A spending minister may appeal to the Minister of Planning, Budget and Management, but this is rare. Finally, a spending minister may appeal to the President, but this is extremely rare. The President has made it clear to members of the Cabinet that the Minister of Planning, Budget and Management speaks for him.

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**Box 4. Annual budget process timetable**

| March-April | Budget and Planning Secretariats review programmes and individual appropriations. |
| 15 April    | Budget Guidance Law is presented to Parliament. |
| May         | Preliminary revenue estimates. Letters of totals discussed with minister. |
| End May/Early June | Letters of totals sent to each ministry. |
| 3 weeks later | Spending ministries come back with proposals. |
| End June   | Budget Guidance Law voted by Congress. |
| July       | Refined revenue estimates. Appeals process by spending ministries. |
| 30 August  | Budget presented to Congress. |
The Budget Secretariat is then responsible for finishing the budget documentation and this is presented to the Congress on 15 August each year. The deliberations in Congress are addressed in the next section.

1.3.3. Presidential budget implementation decrees

In constitutional terms, the budget as enacted by the Congress sets a “maximum” on the amount of funds that can be disbursed under each appropriation. For non-mandatory items, ministries have the flexibility to spend any amount – including none – up to the limit set by the Congress for each appropriation. More specifically, whenever the President deems that there is a risk to the achievement of the fiscal targets in light of information prepared by the Ministry of Finance and the Ministry of Planning, Budget and Management, he/she can limit the aggregate spending of individual ministries.

According to the Fiscal Responsibility Law, a decree should be issued within 30 days of Congress enacting the budget which provides a monthly schedule of revenues and expenditures. This schedule can subsequently be revised every two months in light of the performance of revenues, with adjustments in annual cash limits for each ministry as well as the amount of commitments that each ministry can enter into during each month.

The reasons for using this device are manifold. First, it is part of Brazil’s commitment to meeting its fiscal targets. Brazilian officials emphasise that due to the volatility of the economy, there is great uncertainty about the achievement of the fiscal targets and it is deemed better to be able to adjust spending levels during the year rather than to take an extremely cautious stance at the beginning of the year.

Second, the initial presidential decree is often in direct response to actions by the Congress which are deemed in need of “correction”. Constitutionally, the Congress may only increase funding for one appropriation by reducing funding for another appropriation. There is, however, a “loop-hole” that allows Congress to identify “errors” in the revenue estimates presented by the government. Invariably, Congress identifies such “errors” and increases the revenue estimates of the budget. This “new” revenue is then all used to fund increased expenditures, most notably for infrastructure and other capital projects. The initial presidential decree may take out the bulk of these new expenditures. In some cases these factors have resulted in a significant reduction in limits in the first decree issued after the approval of the budget.

Third, there would simply appear to be a general tendency in Brazil to adjust the budget frequently during implementation. Adjustments (increases or reallocations) that are less than 10% of the initial appropriations do not require specific legislative authorisation.
The volatility argument may appear to be overplayed in Brazil as justification for the presidential budget implementation decrees, as the primary fiscal target already excludes interest expenditure. However, it has been the case that the government has had to respond swiftly to changes in the domestic or international macro-economic scenario arising during the year. Also, delays in the passage of some necessary legislative actions have required a precautionary reduction in expenditure to ensure that the annual fiscal target was not jeopardised. It should be noted that in most cases these actions do not reflect the early adoption of unrealistic economic assumptions. Indeed, the economic assumptions are professionally prepared by the Executive using appropriate techniques and have proved to be reasonably accurate in recent years, as discussed in Box 5.

One serious drawback of this adjustment process arises from the rigidity of the budget mentioned above. Expenditure reductions do not reach mandatory expenditure. As a result, any reductions deemed necessary hit a limited number of programmes very forcefully, most notably infrastructure and other capital projects that are not classified as mandatory. In many cases, these cuts are concentrated on amendments made in Congress to the original budget.

**Box 5. Preparing the economic assumptions**

The economic assumptions are established by the Ministry of Finance, in cooperation with the Ministry of Planning, Budget and Management and the central bank. They have increasingly reflected market expectations regarding the main variables for the monetary, real and external sectors. These are gathered and published monthly by the central bank, which compiles data produced by some 80 leading domestic and foreign banks, as well as from research institutions and international organisations.

For the purpose of the economic assumptions used in the budget, the “consensus” forecast is confronted with hard data from the forward and future markets. The alignment of official projections with market estimates for some key variables is deemed to increase the credibility of the budget.

The Ministry of Finance also prepares a detailed explanation of how it projects tax revenues and their linkages to macro-economic variables. The Ministry of Social Security estimates its receipts and outlays independently, although based on the same macro model used by the Ministry of Finance. A commentary on the sensitivity of fiscal estimates to macro-economic variables (e.g. the interest and exchange rates) is also presented in the annexes of the Budget Guidance Law and the methodology used for estimating tax receipts is presented with the budget. Congress has increasingly relied on this methodology during budget discussions, even when identifying “errors and omissions”.

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1.4. Conclusions

There are several conclusions to be drawn about the Brazilian budget formulation process in comparison with those found in OECD member countries.

First, there is no rolling medium-term expenditure framework in Brazil. OECD member countries have found such frameworks to be an indispensable part of an effective budgeting process and there is no reason to believe that this would not be the same for Brazil. Despite the high volatility of some macro variables, the current control systems and the high professional standards of the relevant officials strongly suggest that such a move forward is already feasible.

Second, budgeting and planning functions are separate. Both are highly developed and impressive operations. Their separateness, however, detracts from each other. Brazil has a unique opportunity to merge the two and create a results-oriented budget process on par with that found in OECD member countries. Results in the case of “priority” programmes are encouraging.

Third, there is a high degree of rigidity in the Brazilian budgeting system. Efforts need to be made to reduce those rigidities. The budget formulation process – for example, in terms of a new results-oriented focus – could assist in making that transformation. However, it will take time to build up trust in such a new process. Of course, the preservation of economic stability will be essential for that progress.

Fourth, there appears to be relatively little interaction between spending ministries and the Budget Secretariat. On the one hand, budgeting appears to be very much a top-down operation with very limited opportunities for spending ministries to have any input. On the other hand, the Budget Secretariat does not control the execution of individual programmes after the budget is adopted. The capacity of different spending ministries varies, but efforts should be made to increase their role in the budget formulation process. This is further discussed in Section 3 – Management.

Fifth, the system of budget implementation – including Congress’ role – needs to be reformed. This is discussed further in the next section.

Having said that, Brazil’s budget formulation process has produced budgets that deliver in accordance with the aggregate fiscal objectives set for them. They have thus contributed markedly to solidifying the relative economic stability that Brazil has enjoyed in recent years. The next phase for the budget formulation process is to build on that and to improve the quality of public expenditures – fostering reallocation and efficiency. The above recommendations will contribute towards that end.
2. Role of Congress

2.1. Introduction

The legislature plays a vital role in the budget process. The taxing and spending power of national legislatures is at the core of democratic accountability, and the “checks and balances” function of the legislature on the Executive is irreplaceable.

The role of the legislature in the budget process varies greatly in OECD member countries. However, it is clear that the general trend is for the legislature to take a more active role in the budget process. It is a hallmark of legislatures in OECD member countries that they establish elaborate processes for discussing the budget as they assume a greater role in the budget process. These processes focus on fostering fiscal discipline. Quite simply, legislatures have to demonstrate that they are able to take an active yet responsible role in the budget process. The challenge facing Brazil is to strengthen the institutional arrangements in Congress in order to foster fiscally responsible interventions and a greater role in the effective and efficient allocation of resources.

Historically, the role of Congress in the budget process has been limited in Brazil. Until 1989, Congress could not make any changes whatsoever to the budget proposed by the Executive, and extra-budgetary spending was quite prominent. The 1988 Constitution gave Congress powers to modify the budget and this resulted in thousands of amendments proposed each year. As a consequence, a more responsible system for examining the budget was designed, setting limits both on the number and on the content of amendments.

Box 6. The Brazilian Congress

The Congress is composed of two chambers: the Chamber of Deputies and the Senate. The Chamber of Deputies has 513 members elected for four-year terms. Each state forms a single electoral district. The number of deputies per state is based on their respective populations, although the more populated states tend to be under-represented because of the ceiling on the number of representatives that each state can send to Congress. The Senate has 81 members, comprising the representatives of 26 states, plus the federal district of Brasilia. Senators serve eight-year terms, but elections are held every four years for either two-thirds or one-third of the seats.

Brazil has a very fluid and fragmented party system: a large number of political parties are represented in the Congress, and the practice of members of Congress switching political parties is common. Regional alliances can, however, be strong and most legislative proposals, including the budget, are viewed in terms of their regional impact.
2.2. Budget approval process

The budget approval process focuses on debating, amending and approving the Budget Guidance Law and the budget itself.

Detailed congressional scrutiny of the budget takes place in the Joint Committee on Plans, Public Budgets and Auditing (the Joint Committee). The Joint Committee has a dominant role in examining the Executive’s proposal. It consists of 84 members from both houses of the Congress: 21 senators and 63 deputies. Its chairman is elected each year, alternatively from the Senate and the Chamber of Deputies.

The Committee is assisted by a Research Office, consisting of about 35 professionals. However, they are not exclusively focused on providing services to the Joint Committee. The Congress also has full access to budgeting and accounting databases of the Executive branch.

Box 7. Budget approval timetable

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>15 April</td>
<td>Budget Guidance Law proposal submitted to Congress.</td>
</tr>
<tr>
<td>30 June</td>
<td>Budget Guidance Law approved by Congress.</td>
</tr>
<tr>
<td>30 August</td>
<td>Budget proposal submitted to Congress.</td>
</tr>
<tr>
<td>September – December</td>
<td>Budget hearings by the Joint Committee.</td>
</tr>
<tr>
<td>Early October</td>
<td>Joint Committee approves the preliminary opinion.</td>
</tr>
<tr>
<td>Early November</td>
<td>Joint Committee approves sectoral reports.</td>
</tr>
<tr>
<td>Early December</td>
<td>Joint Committee approves the final report.</td>
</tr>
<tr>
<td>15 December</td>
<td>Vote by both the Chamber of Deputies and the Senate.</td>
</tr>
<tr>
<td>End December</td>
<td>Presidential signature.</td>
</tr>
<tr>
<td>1 January</td>
<td>Start of fiscal year.</td>
</tr>
<tr>
<td>End January</td>
<td>Presidential budget implementation decree.</td>
</tr>
</tbody>
</table>

2.2.1. Budget Guidance Law

The draft Budget Guidance Law is presented to Congress by 15 April and should be approved by 30 June. In general, it is approved after the deadline, but the delay has been decreasing in recent years, hovering around a week.
Hearings are held within seven days from the distribution of documents, and usually members of the Executive are called to testify. The discussion on the macro-economic context is becoming more and more relevant, but the main interest remains on sectoral aspects.

As noted in the previous section, the Budget Guidance Law can be characterised as three laws in one. First, it is a pre-budget document with the same purpose as those found in OECD member countries, i.e. to encourage debate on the budget aggregates and how they interact with the economy. As such, it serves to create appropriate expectations for the budget itself. The draft Budget Guidance Law presents targets for the primary surplus for the next year and the two subsequent years. The current overall target for 2003-05 is set at 3.75% of GDP. In addition, projections of aggregate revenues and expenditure are presented. In recent years, however, rapid changes in the macro-economic environment have sometimes resulted in important changes in these estimates during the period leading to the presentation of the budget proposal in August. A wealth of information on economic developments and projections is also presented in this document. Among the most important items are those related to the long-term viability of the social security system (including an actuarial estimate of the net worth of the public servants' scheme), a list of existing and proposed tax expenditure, and a list of issues pending court decisions that could have fiscal implications, as well as a summary of other contingent liabilities, including guarantees made by the government. Legal disputes can have a significant fiscal impact due to the numerous outstanding cases regarding the constitutionality of de-indexing various claims as the country was moving from the inflationary environment of the past.

Second, it sets out which expenditures are to be considered “mandatory” for the coming year. This simply means which programmes should be exempt from any reductions in the presidential decree. Even though these could be changed by the annual budget, the list does give an idea of the annual priorities. The bill also contains information concerning the lending policies of various government financial institutions.

Third, it contains a number of “housekeeping” provisions, which would appear to belong more appropriately in an organic budget law.

Members of Congress often show little interest in the aggregate information. A limited debate takes place on the overall direction of budget policy and most of the action is focused on the micro issues. In that sense, the objective of involving members of Congress in discussion on the economic linkages of the fiscal policy has not been fully achieved. The absence of a rolling multi-year expenditure framework and the large role of earmarked and “mandatory” expenditure accentuates this.
The most important function of the Budget Guidance Law should be the focus on aggregates and economic linkages. Consideration should be given to ending the practice of identifying mandatory programmes in this law and shifting the discussion to the annual budget law. Similarly, the housekeeping issues that are also dealt with in the Budget Directives Law should be moved into an organic budget law.

2.2.2. Annual budget law

The budget is presented by the Executive to the Congress by 30 August and should be approved by 15 December.

Following the speech by the Minister of Planning, Budget and Management, the budget is referred to the Joint Committee. The Joint Committee commences hearings within 14 days that focus on the macro-economic scenario. In the public hearings, ministers, officials and other members of the Executive are called to testify. Although the committee meetings are generally open to the public, neither representatives of interest groups nor independent research institutes are normally invited. Occasionally, sectoral experts are called to participate in the hearings.

The first concrete action of the Joint Committee is to issue a preliminary opinion setting parameters and criteria for the budget examination (for example, the maximum amount allowed for individual amendments). In addition, the preliminary opinion discusses the revision of the macro-economic scenario. A deadline – to be fixed within 15 days of the issue of the preliminary opinion – is determined for the submission of amendments.

There are two types of amendment: individual amendments, presented by a representative, and collective amendments, presented by a group of representatives. The aggregation may reflect a geographical area or the membership in a sectoral committee. The following limitations are currently in place:

- Up to 20 individual amendments for each representative, each one not reallocating more than a certain amount (last year’s preliminary opinion fixed the amount to 2 million Reais, i.e. about 750 000 Euros/Dollars).

- Up to five amendments for each sectoral committee either from the Senate or the Chamber of Deputies, with no monetary limit.

- Between 15 and 20 amendments (according to the dimension of the state) proposed by two-thirds of the representatives elected in each state, with no monetary limit.

The amendments are reviewed in tandem with a review of the President’s budget proposal by up to five sub-committees5 with the help of the general and the sectoral rapporteurs. During the discussion of the preliminary
opinion, the budget proposal is divided into 10 areas. A rapporteur for each sector is appointed and charged to evaluate the amendments related to that area. He/she then prepares a report, recommending amendments for approval or rejection. The Joint Committee will examine these reports separately and vote on them. The report being approved, the amendments given a positive opinion are considered approved, and the amendments with a negative opinion rejected. Any representative who does not agree with the rapporteur's opinion may ask, with the support of a given number of colleagues, that his/her amendments be subject to a specific vote by the Joint Committee. Rejected amendments will receive no further attention, unless the proponent, with the support of a given number of representatives, demands a specific vote by Congress.

Constitutionally, the Congress is only allowed to increase one appropriation by decreasing another one. This, however, does not take place. As mentioned previously, resources are increased by taking advantage of a “loophole” in the Constitution that allows Congress to alter revenue figures when it concludes that the Executive has made “errors or omissions” in the economic assumptions used. These findings can be said to be political in nature, rather than the result of a purely technical analysis of the government's economic assumptions. The difficult choice between funding alternative proposals (by reallocating funds) has been transformed into an easier process of adding resources in order to finance them. This, however, must be seen in the context of the presidential budget implementation decrees and the limited role that Congress enjoys in regards to supplementary budgets, as discussed in the next section.

The general rapporteur collects the sectoral reports, co-ordinates them and prepares his/her general report, being authorised to include other changes within the limits stated by the resolution and the preliminary opinion. In addition, this report co-ordinates some of the proposed amendments in order to utilise the eventual additional resources found through the above revision. The general report is discussed and voted on by the Joint Committee and then submitted to the plenary session of Congress.

The decisions of the Joint Committee are passed by the plenary of each chamber, first the Chamber of Deputies and then the Senate. In general, once the general report is approved by the Joint Committee, the final vote by the plenary is just a formality. Rarely, and due to exceptional circumstances, have new amendments been approved by the Chamber of Deputies and subsequently ratified by the Senate.
The system in place for discussing the Executive’s budget proposal could be improved by two institutional changes. First, the Congress could adopt a two-step budget approval process, where the aggregates are voted on first and specifics decided later, constrained by the targets previously agreed in the Budget Guidance Law. The Budget Guidance Law should continue the current practice of setting targets as a percentage of GDP with these then translated into nominal amounts in the budget, with Congress first voting on the nominal aggregates before beginning debate on the specifics.

Second, consideration should be given to re-assessing the roles of the Joint Committee vis-à-vis the sectoral committees. In a number of OECD member countries, the Budget Committee acts as “the policeman” of the parliamentary budget process. It discusses the aggregates and divides the aggregates among the different sectors. Then, the respective sectoral committees would propose amendments within their specific sector. This would institutionalise further the Joint Committee’s focus on the aggregates

### Box 8. Constitutional restrictions on amending the budget

According to Article 166, Paragraph 9 of the Brazilian Constitution, amendments to the budget proposed by the government may be approved only if:

- They are compatible with the plan and the Budget Guidance Law, and they are related to the provision of the budget law’s text.

The provision regarding compatibility with the plan and the Budget Guidance Law is interpreted as ensuring that it does not jeopardise the target for the primary surplus and respects the commands of the Fiscal Responsibility Law. Some officials of Congress indicated that the plan was “largely irrelevant” to the deliberation of the budget.

The provision regarding “related” business is very much respected; the Brazilian budget is not an opportunity for other omnibus legislative changes.

- They specify the necessary funds, allowing only those resulting from the annulment of expenses. Additional funds may be raised with the correction of errors or omissions.

As noted, Congress generally does not annul appropriations, but rather finances new ones through concluding there are “errors or omissions” in the economic assumptions in the government’s proposed budget.

- They do not refer to allocations for personnel and their charges (civil service payroll and pensions), debt servicing and constitutional tax transfers.

Congress cannot make any changes for these items.
and the economic linkages; the greater role for sectoral committees could improve the prioritisation of programmes and lead—through an effective use of the available performance information—to a more efficient use of resources.

2.2.3. Presidential budget implementation decrees and supplemental budgets

As noted above, the practice of Congress to deem “errors or omissions” in the economic assumptions and thereby fund additional expenditure must be seen in light of the presidential budget implementation decrees and the limited role that Congress has in supplemental budgets.

The presidential budget implementation decrees are discussed at length elsewhere in this report, but initially often authorise the spending of only about 90% of the budget as enacted by Congress. In some cases, subsequent decrees increase this amount. They are based on the notion that in the presence of uncertainty, prudent budgeting demands that expenditures be decided only when the revenues have become certain.

Congress believes that the Executive underestimates revenues so that when additional revenues come in during the year, it can spend them through decree. This can be done constitutionally provided that the proposed increase in expenditure does not exceed 10% of any individual appropriation. Above this limit, the legislation requires the Executive to propose a supplementary budget to Congress for approval. Moreover, the Executive may present special budget appropriations for new expenditures, which are not included in the budget to Congress.

The Brazilian Congress has a limited role in the spending decisions adopted during the year. Asking Congress to adopt more prudent economic assumptions is equivalent to asking it to give up a part of its decision-making power on the allocation of the additional resources that could emerge during the year. Therefore, Congress has an incentive to revise upwards the economic assumptions employed in the budget proposal. If the overall revenues match the figure set by Congress, it will have a strong say in how the “additional” revenue is allocated—since the enacted budget includes appropriations based on the higher revenue.

If the actual outcomes correspond to the Executive’s assumptions, the budget approved by the Congress remains a mere political statement on the desired allocation. The actual expenditure will then reflect the choices of the Executive as emerging in the presidential decrees and the decisions of individual ministries concerning specific appropriations (the presidential decrees only state limits for ministries, which remain in charge of allocating the available resources, respecting the “mandatory” expenditure allocated to their ministry). Congress also plays the political “game” of asking for the
inclusion of certain priorities in the presidential decree in exchange of the approval for other bills presented by the Executive. Representatives may directly lobby for the release of certain appropriations during the year.

The consolidation of all changes into a formal mid-year budget review could allow Congress to play a role more equal to that of the Executive during the year. According to some observers, such a decision on the allocation of emerging revenues in a more comprehensive context may lead to the adoption by the Congress of more prudent economic assumptions in the budget process.

In such a context, Congress will benefit from using professional advice on economic assumptions, possibly through creating an independent body on the model of the United States Congressional Budget Office. Benefits could also emerge from opening the hearings to external institutions.

2.3. Conclusion

Although the Brazilian Congress presently has an active role in the budget process, its “check and balance” function on the Executive could be strengthened. First, the adoption of a two-step budget approval process, where the aggregates are voted on first and specifics decided later, would serve to establish Congress’ commitment to fiscal discipline. The Budget Guidance Law should focus on the aggregates and their economic linkages only; the identification of priority programmes should be shifted to the annual budget law; and the “housekeeping” issues moved into an organic budget law. At the time of the budget, the Congress should first vote on the aggregates, including updated aggregates in nominal terms in order to establish an operationalised ceiling for total expenditures, before beginning deliberations on specific appropriations.

Second, consideration should be given to reassessing the roles of the Joint Committee vis-à-vis the sectoral committees. The Joint Committee would discuss the aggregates and divide the aggregates among the different sectors. Then, the respective sectoral committees would propose amendments within their specific sector. This would further institutionalise the Joint Committee’s focus on the aggregates and the economic linkages; the greater role for sectoral committees could improve the prioritisation of programmes and lead – through an effective use of the available performance information – to a more efficient use of resources.

Third, the consolidation of all in-year changes in the budget into a formal mid-year budget review would give more effect to Congress’ legitimate role in the budget process during the year. Such a decision on the allocation of emerging revenues in such a context may lead to the adoption by Congress of
more prudent economic assumptions and to greater transparency in the actual budget implementation.

In such a changed context, Congress would greatly benefit from using professional advice on economic assumptions, possibly creating an independent body on the model of the United States Congressional Budget Office. Benefits could also emerge from opening the hearings to external institutions.

3. Management

3.1. Introduction

Management practices in the federal government are characterised by a high level of centralisation: the Ministry of Planning, Budget and Management – together with other central organisations – exercises near total control over line ministries. This has both advantages and disadvantages, and must be seen in the context of Brazil’s recent history and unique constitutional restrictions.

Brazil is a young democracy: the end of military rule came only in the mid-1980s. During military rule and in the immediate years following the return to democracy, professionalism in the federal government was low.

During the past eight years, important progress has been made in improving the professionalism of the federal government. However, this has been tempered by the need for fiscal austerity. Very rigid constitutional provisions in the area of human resources management have accentuated these fiscal dimensions. As a result, recruitment of new staff on a competitive, professional basis has been largely limited to certain ministries where the need for “upgraded” staff was viewed as urgent.

The result is a mismatch in the managerial capacity of the different ministries. Some are professional and very much ready to take on increased managerial flexibility. However, others are largely mired in old patterns where increased managerial flexibility would clearly be inappropriate.

The federal government’s overall managerial model, although in transition, still has to grapple with the latter group of ministries. This entails a uniform application of rules across the federal government, fostering accountability and transparency. It does, however, come at a cost: individual managers in different ministries often do not have the flexibility to use resources in the way they judge most effective and efficient. In a country where resources are severely strained, this may entail a very heavy cost. This section reviews the main management systems within the federal government.
3.2. Organisational structure

Brazil has a presidential system of government: the Executive branch is organised into 19 ministries and six ministerial-level secretariats that are located within the Office of the President. This top tier of the Executive branch is quite fluid – ministries are merged, abolished or created at a more rapid rate than in OECD member countries. Each new President in effect re-organises the structure of ministries to align them with his priorities. The last major re-organisation took place in 1999.

The ministries are considered the “direct” government administration. Their internal structure is established in presidential decrees and tends to follow a uniform pattern: they are divided into an “Executive Secretariat” directly attached to the minister's office, and a number of functional “secretariats”. In practice, however, the boundaries between the two are often a grey area. Indeed, in some ministries, the “Executive Secretariat” has mainly a general oversight role of the functional secretariats. In other ministries, the Executive Secretariat focuses on policy formulation whereas the functional secretariats focus on implementing those policies. The senior level of the Executive Secretariat is generally staffed with presidential appointees, whereas only the head of each functional secretariat is a presidential appointee. Individual functional secretariats may have a very distinct identity within the ministry, almost akin to an “internal agency”. In addition, there are 163 “indirect administrative units” within the federal government. The vast majority of these – 128 – are universities, technical learning institutions, schools for vocational training and other institutions of learning, located within the Ministry of Education. It needs to borne in mind that Brazil is a federal system where the vast majority of government services are provided by states and municipalities – the role of the federal government is often limited to policy formulation and financing of activities provided by states and municipalities. The federal government is, however, responsible for higher education, thus explaining the large number of federal entities in this sector. (The larger states also have their own system of state universities.)

The remaining 35 agencies include federal entities implementing policies on the instruction of their “parent” ministries. All but one of these entities have a very long history, often pre-dating the creation of their parent ministry – and should not be seen in the same light as the agencies model in Scandinavia or the United Kingdom.

In 1999, however, a presidential decree established that the government’s general administrative model should entail a split between policy-making ministries and agencies that execute policies. This administrative model was also to introduce a contractual approach to management between the ministries and the agencies. However, only one such agency has been
established – the Weights and Measures Agency. Several reasons appear to explain the limited use of this model. The functional secretariats within ministries already enjoy distinct identities. This new administrative model did not relax any central input controls. Quite the contrary, it introduced a new layer of controls – a contractual approach to management. On a different dimension, the contractual approach was met by “massive” distrust among staff as the contracts were seen as potential first steps towards privatisation.

Concurrent with the government’s privatisation programme, the federal government did establish nine independent regulatory agencies, in sectors such as telecommunications, petrol, electricity, water and transport. These agencies are different in nature from the other indirect administrative units: they participate in both policy formulation and policy implementation. Their creation was meant to demonstrate that there would not be any political interference in the decisions of these bodies. This applied especially in sectors where foreign investment was sought. These bodies do enjoy genuine managerial flexibility, which has created some tensions vis-à-vis the other bodies – most notably in terms of salaries.

Since 1997, the federal government has also encouraged the creation of partnerships with so-called “social organisations” which are in effect non-governmental, not-for-profit organisations. The federal government has concluded contracts with seven such organisations in the health care, education and research sectors. These entities deliver services to the federal government on the basis of private law contracts and their employees are not considered government employees.

A notable feature of the federal government administrative structure is the prevalence of “consultative councils”. There are often several of these councils attached to each ministry. They consist of representatives of government ministries, other levels of government and non-governmental organisations. These councils typically have no decision-making roles but are a forum for policy development and for identifying areas where government action is needed or in need of improvement. These councils are to a significant degree related to the return to democracy and the government’s wish to demonstrate increased transparency and participation by civil society.

As noted in the introduction to this section, the formal organisational structure of the government only tells half the story. The degree of professionalism varies tremendously between individual ministries and entities. Aside from the regulatory agencies, all these entities face the same central input controls.
3.3. Human resources management

There are three key human resources management issues in the federal government. The first is to upgrade the professionalism of the civil service. The second is to increase the degree of flexibility. Nowhere is the centralised nature of management in the federal government more evident than in the field of human resources management. The third is to reform the overly generous system of pensions for civil servants.

In accordance with a 1998 constitutional amendment, all government employees are hired by means of competitive entry examinations except for “confidence positions”, as described in Box 9. This has reduced, if not eliminated, the traditional patronage basis for hiring employees. As a result, the educational standards of government employees have increased markedly. In 1995, a total of 39% of government employees had university degrees. By 2002, that percentage had increased to 53% of the total workforce. Fiscal constraints severely limit the possibility to hire new employees, and the government has been very selective in identifying which sectors should be “upgraded” in terms of skills. At the same time, the system of assigning individuals to rigidly-defined “careers” and “career paths” has been made more flexible for the “new” employees.

The fiscal constraints for hiring are accentuated by rigid constitutional restrictions in the human resources management field. Once hired, there is a three-year probation period after which it is, in practice, impossible to dismiss an employee except for cases of corruption. These provisions are interpreted very narrowly in Brazil to mean tenure in an individual position. For example, it is near impossible to re-deploy unwilling staff from one ministry to another where they may be more needed. If the move would require a change of domicile, it is “totally” impossible.

For example, when the government’s printing service modernised its equipment, it resulted in one-third of its staff becoming redundant. It was proposed to transfer the affected employees to other parts of the government. A number of successive legal cases were filed, which the government eventually won, but these cases postponed the effects for years. Similar legal action is taken in each and every such case in Brazil.

A constitutional amendment in 1998 did authorise the hiring of contractual employees. However, the amendment has been challenged on constitutional terms and a case is pending before the Supreme Court. The federal government decided not to apply the provisions until the Supreme Court has ruled on this issue.

A decision to hire staff is therefore a fiscal commitment for up to 60 years, or the sum of their time in government service and retirement. The Ministry of Planning, Budget and Management must approve each individual hiring.
Seeking approval for new staff by line ministries is a primary feature of the appeals system in the budget formulation process, as described in Section 1.

Box 9. “Positions of confidence”

Positions within the federal government are divided into “positions of confidence” and career positions. The positions of confidence include the minister, all officials within the Executive Secretariat, the heads of each functional secretariat, and the heads of each indirect administrative unit. A position of confidence entails that the President has the prerogative to appoint and remove those officials at any time. This, however, does not automatically mean that they are filled with political individuals. In fact, ministers are often not politicians, and in some ministries career civil servants are routinely appointed deputy ministers (Executive Secretaries). This is also the case for many other confidence positions. All in all, 70% of all confidence positions are filled by professional civil servants.

Salaries are determined unilaterally by the Ministry of Planning, Budget and Management. There is no system of collective bargaining for government employees.

Remuneration of civil servants consists of three elements: a basic salary, an individual performance bonus (up to 30% of basic salary) and an organisation-wide performance bonus (up to 20% of basic salary).

Brazilian officials assess that the actual element of performance is limited due to cultural resistance among civil servants. In practice, almost all staff receive the bonuses. In the case of individual bonuses, an informal rotating system is operated where alternative staff members receive part of the bonus in alternative months. It should, however, be noted that this practice does not apply to all organisations. The introduction of the bonuses was not accompanied by a significant increase in total remuneration, because the basic salary has risen quite moderately.

Any general salary increase has large fiscal implications, because public servants’ pensions are very generous, even more so before limited reforms which were introduced in 1998. All pensions were based on 100% of an employee’s last year’s wage and were adjusted annually in line with that reference wage and related benefits.

In order to qualify for a pension, men needed 35 years “in service” and women 30 years. These requirements were five years less for teachers. The concept of “in service” did not only apply to government service: only one year
in government service was needed. For example, a person could have worked in the private sector for 34 years, joined the government for one year, and then received 100% of that one year’s wage in perpetuity.

These benefits were all stipulated in the Constitution. Following many years of negotiations, a constitutional amendment was approved in 1998 which introduced limited reforms in this area. It required 10 years of government service and five years in the reference post last held in order to receive a full pension. It also introduced a minimum retirement age of 53 in order to receive a full pension.

Human resources management is a key area in need of reform in Brazil. The pension system for civil servants needs to be rationalised (which requires a constitutional amendment), and the 1998 constitutional amendment concerning contractual employees needs to be implemented (which requires a ruling from the Supreme Court). With those reforms in place, the process of improving the professionalism of the civil service could be accelerated, and increased flexibility by line ministries in the area of human resources management could be introduced.

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**Box 10. Monitoring and evaluation of programmes**

The plan presents results information on all government programmes parallel to the budget. An elaborate web-based infrastructure has been established to facilitate feedback of implementation of the plan. This infrastructure, SIGPLAN, allows programme managers to enter progress against pre-established performance indicators, to comment on implementation issues and to highlight risks for programme success.

In addition to the ongoing reporting on progress of “priority” programmes, the plan is evaluated annually prior to the introduction of a revised list of priority programmes in the Budget Guidance Law. Evaluation of each programme in the plan is initiated in December each year. This evaluation is organised as a self-evaluation by programme managers and must be completed by mid-April the following year when a consolidated evaluation of the plan is published.

The present purpose of the evaluation is not to introduce “hard” mechanisms of accountability on programme managers and entities implementing the programmes. No sanctions are applied for bad performance as measured by the self-assessment, especially if it can be argued that failure to reach targets is related to unexpected cuts in resources. Rather, the stated purpose is to facilitate improvement, to provide decision-making support, to entertain a learning process and to strengthen public transparency.
3.4. Financial management

The government’s financial management practices are of a high standard. This is both a legacy of the high inflation years where the necessity for timely and accurate information on receipts and outlays was of paramount concern and the government’s volatile debt management profile which places a premium on timely and accurate financial information.

Cash management is the responsibility of the National Treasury, which is part of the Ministry of Finance. As such, it is the agent of the Ministry of Planning, Budget and Management in executing the government’s cash management policies. All government revenue and expenditures are paid into or disbursed from the Treasury single account, which is maintained with the central bank. Commercial banks that receive government revenues have up to two business days to complete the transfer of funds to the account. All payments are made directly from this account through payment requests from individual ministries.

Box 10. Monitoring and evaluation of programmes (cont.)

These self-evaluations are supplemented by “performance audits” undertaken by the Internal Control Secretariat. Furthermore, the Planning Secretariat of the Ministry of Planning, Budget and Management is undertaking reviews on a case-by-case basis. In addition, the secretariat prepares a consolidated assessment of the implementation of the plan and has a designated task force closely following the implementation of priority programmes.

It is difficult to assess to what degree a results-oriented culture has been introduced in the federal government. Brazilian officials generally hold that there is still a long way to go to firmly establish a performance culture. Some observers note that the reporting structure of SIGPLAN is more suitable for reporting on the implementation of capital investments than in more “soft” areas. Related to this is the observation that the plan and SIGPLAN rest on what several Brazilian officials term a Cartesian view of the world – i.e. that everything can and must be quantified and measured. This, however, could be said of any results-focused management and budgeting system around the world.

It is clear, however, that Brazil has invested heavily in promoting a results-oriented culture in its public administration. This investment has been focused on the plan. The payoff from this investment will likely increase significantly by linking the plan directly with the budget, as outlined in Section 1.
The Brazilian budgeting and financial reporting system uses two bases of accounting: obligations basis for entering into commitments and cash basis for settlement and payment. Accruals is not employed in Brazil.

There are no incentive instruments in place to promote improved cash management by line ministries (such as carry-forwards of unused appropriations, borrowing against future appropriations, interest paid on cash balances) nor incentive systems to promote good asset management (such as a capital charge). Nor are there possibilities of transferring appropriations between line items, for example between purchase of goods and services and staff costs or between investments and transfers.

Financial reporting in Brazil is very extensive, both in terms of the quantity and the quality of information made available. Brazil’s current practices compare favourably to the provisions of the OECD Best Practices for Budget Transparency.\(^8\)

### 3.5. Conclusion

Management practices in the federal government have evolved quite significantly in recent years with a strong improvement in professionalism. Entrance to the public service is now through competitive examinations, and efforts have been made to reward effective performance throughout the federal administration. Nonetheless, capacity is still unevenly distributed across ministries, and management practices are thus still characterised by a high level of centralisation: the Ministry of Planning, Budget and Management – together with other central organisations – exercises near total control over the management practices of line ministries.

It is urgent for the government to reform the rigid constitutional restrictions regarding human resources management, including the “for life” appointment of government employees and the overly generous civil servants’ pension scheme. Once these reforms are in place, a more rapid improvement in civil service professionalism across ministries can evolve. The government can embark on a “second generation” of reforms and increase managerial flexibility. This should lead to more effective and efficient government services, based on the experiences of OECD member countries. The demand for improved government services in essential areas in Brazil, coupled with the limited resources available, make these reforms truly urgent.
ANNEX 1

List of Ministries and Ministry-level Presidential Secretariats

1. Ministry of Agriculture, Fisheries and Livestock
2. Ministry of Communications
3. Ministry of Culture
4. Ministry of Defense
5. Ministry of Education
6. Ministry of the Environment
7. Ministry of Finance
8. Ministry of Foreign Affairs
9. Ministry of Health
10. Ministry of Industry and International Trade
11. Ministry of Justice
12. Ministry of Labor
14. Ministry of National Integration
15. Ministry of Planning, Budgeting and Management
16. Ministry of Rural Development
17. Ministry of Science and Technology
18. Ministry of Social Assistance
19. Ministry of Transportation

There are also several Secretariats within the Presidency that have the status of ministries:
1. The Civil House (Chief of Staff)
2. The Institutional Security Secretariat
3. Secretariat-General of the Presidency
4. Secretariat of Communication
5. The Attorney-General’s Office
6. The Internal Control Secretariat
Notes

1. For a discussion of Brazil’s economy, see OECD Economic Surveys – Brazil.

2. All expenditures except interest on the debt are covered. The Constitution mandates a plan to be issued for capital expenditures but the inclusion of other expenditures is discretionary.

3. There is a three-year high-level fiscal framework attached to the Budget Guidance Law. This is, however, a high-level macro-economic framework with the macro variables not being operationalised.

4. For further elaboration of such frameworks, see A Longer-term Focus to Budgeting, OECD, GOV/PUMA(2002)1.

5. Three out of the five sub-committees are permanent: the Committee for the Budget Revenue Evaluation, the Committee for the Amendments Evaluation, and the Committee for the Evaluation of the Information sent from the Audit Office.


7. A list of these entities is provided in Annex 1.

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