From Analysis to Impact

Partnership Initiative Case Study Series

In 2008, INESC led a diverse coalition of organizations in producing technical budget analyses, proposing policy alternatives, and lobbying government officials against proposed reforms to the Brazilian tax system that would have exacerbated inequality and resulted in tax breaks for the wealthy and spending cuts on social policies for the poor.

Photo courtesy of INESC.

The following case study illustrates how tax policies can be a focal point for a campaign concerned with social justice. This is a summary of a more in-depth study prepared by Evilasio Salvador as part of the Learning Program of the IBP's Partnership Initiative. The PI Learning Program seeks to assess and document the impact of civil society engagement in public budgeting.

Download a PDF of the complete case study at http://internationalbudget.org/wp-content/uploads/Final-INESC-case-study-complete.pdf

BRAZIL: FIGHTING FOR SOCIAL JUSTICE THROUGH TAX POLICIES

Brazil's remarkable economic growth – a rise that has continued uninterrupted for nearly two decades – has done little to resolve the country's dramatic inequality.

Many observers blame the tax system for doing too little to redistribute growth more equitably. Indeed, the tax burden in Brazil has been placed increasingly on those who can least afford it.

The Institute for Socioeconomic Studies (INESC) has followed this issue for years as part of its budget monitoring activities, but the organization decided to ramp up its lobbying efforts when a tax reform was proposed that would exacerbate the situation by giving further tax breaks to the wealthy while eliminating sources of revenue that support social policies.

In response, INESC formed a coalition and a movement that eventually would block the proposed reform and highlight the role of the tax system in bringing about social justice. This case study illustrates how the organization's skills from its budget monitoring were critical to its success.

THE ISSUES: TAX INJUSTICE IN BRAZIL

Brazil is one of the 10 largest economies in the world, but also one of the most unequal. The Gini-coefficient, which measures inequality on a scale of 0-1 (with 0 being completely equal), declined in Brazil from 0.601 in 1995 to 0.521 in 2008. In spite of the improvement, the concentration of income in Brazil remains among the highest in the world.

The Brazilian tax system has aggravated the problem by placing a heavier fiscal burden on the poor and the working class and extending tax breaks to the wealthy.

According to a study conducted by the Brazilian Institute of Geography and Statistics (Instituto Brasileiro de Geografia e Estatística) in 2003, those who earned twice the minimum wage or less spent 45.8 percent of their incomes on consumption taxes, while for households with an income greater than 30 times the minimum wage, the share of taxes on consumption only came to 16.4 percent.

Brazil's unusually regressive tax regime is especially vexing given that the 1998 Federal Constitution explicitly calls for a tax system based on the principles of equality, universality, and ability to pay. The Federal Constitution also establishes that taxpayers must be informed of taxes levied on goods and services, and yet the preponderance of "indirect" production taxes (which are placed on producers who usually pass along the cost to consumers) means that taxes are practically invisible to most Brazilians.

The tax system remains out of line with the spirit of the Federal Constitution because a law has yet to be enacted to activate the constitutional articles regarding taxation. Moreover, tax laws in the 1990s moved Brazil further from the principles of the Federal Constitution as "stabilization policies" were adopted to ensure the free flow of financial resources, lifting taxes that would affect companies and instead shifting the tax burden further toward labor income.

During the second term of President Luiz Inácio Lula da Silva, the government – without seeking input from civil society – sent a new tax reform proposal to Congress, Constitutional Amendment 233/2008, which carried serious implications for the funding of social policies in Brazil. It proposed to simplify the tax system in order to reduce the burden on businesses, to improve the system of indirect taxes by creating a Federal Value Added Tax, and to end a commerce tax between Brazilian states that had created an internal "tax war."

TACTICS FOR CHALLENGING BRAZIL'S PROPOSED TAX REFORM

- Forming a coalition of opponents, with a common manifesto that allows all members to lobby independently while maintaining a unified message.
- Lobbying key decision makers in the executive and legislative branches.
- Promoting and mobilizing participation in public hearings on the proposed reform.
- Publishing "technical notes" that go beyond a merely principled opposition to the reform.
- Proposing alternative approaches to tax reform that would eliminate the negative impact on social policies.
- Developing a set of indicators to help the government to monitor "equity" in the tax regime.
- Urging a federal prosecutor to challenge the constitutionality of the proposed reform.

The last measure was widely welcomed, but activists were deeply concerned about the first two components of the reform. Reducing taxes on businesses would only exacerbate the unjust distribution of the tax burden, and the second measure (the creation of the Federal Value Added Tax) would end up eliminating a series of taxes that generated revenues that had been specially allocated to social spending.

The overall effect of the reform would have been to lower taxes on the wealthy while cutting earmarks for programs that benefit the poor, such as health care and pensions.

THE CAMPAIGN

INESC played a central role in coordinating and mobilizing civil society against the tax reform. Since 1991, the organization had been monitoring both the revenue and expenditure side of the budget process, and its unmatched technical knowledge was fundamental to its leadership on this particular issue.

INESC began by building a broad coalition of organizations: grassroots groups, social movements, labor unions, religious organizations, and research institutes, among them. These were assembled primarily from four existing networks, representatives of which were called together in 2008 to form the "movement to defend social rights under threat by tax reform," which came to be better known by its Portuguese acronym MDSR.

MDSR opened its campaign with a series of dialogues with government officials and parliamentarians to express its members' concerns and present alternative reform strategies that would preserve the funding for social policies.

INESC also wrote a letter, which was signed by 71 civil society organizations, to the President of the Brazilian parliament Arlindo Chinaglia asking for the immediate creation of a forum representative of society as a means to promote participatory discussion in the tax reform project. The forum would include representatives of employees, employers, and civil society organizations.

Though INESC received no reply from the parliamentary president, lawmakers sitting on the Social Security and Family Committee of the Chamber of Deputies (Brazil's lower house) were more responsive, convening a day-long public hearing at which INESC and its partner organizations were given an audience with both committee members and the national press. The movement continued to engage with the press throughout the campaign, using the ensuing controversy over the reform to bring attention to issues of tax justice that are rarely covered by the media.

Thus far, the campaign was still relying heavily on its efforts to persuade lawmakers and the public with an appeal to the principles of a fair tax system, but INESC later deepened the argument with a technical document that detailed the potential problems within the budget process that would arise from the proposed reform. This document later provided the substance of MDSR's manifesto.

A key watershed in the campaign came soon after. Different organizations in the MDSR had raised the issue of tax reform during meetings with party leaders, but INESC scored a singular victory when it was able to hand the manifesto to the president of the Chamber of Deputies. He said he was impressed by the strength of the campaign's representatives and promised to bring up the issue with party leaders.

Soon after, leaders from two major parties, including the ruling party, made public their intention to make a careful review of the proposed tax reform before it went to a vote, echoing the campaign's concern for a reform that would be viable while also preserving social justice.

The Social Security and Family Committee held a further public hearing at which the Executive Secretary of the Ministry of Health surprisingly stated that the proposed tax reform would cost health programs 15 billion reais (US$ 7.4 million). This was followed later by a statement by one of the directors of the Federal Revenue Service that the reform had a good intention to make tax collection less bureaucratic, but that the proposal had failed to calculate the impact on social policies. Clearly, opinion within the government was turning.

Meanwhile, INESC was working with the presidentially appointed Economic and Social Development Council on matters of equity related to tax reform. The letter of recommendation that the council ultimately sent to the president was directly influenced by INESC's earlier analysis of the proposed reform. The council suggested that the reform must do more to build a fairer tax system and proposed a set of indicators (jointly developed with INESC) that could be monitored as markers of equity within the tax regime.

In a move intended to exert pressure from yet another angle, the campaign requested the intervention of the public prosecutor, warning of the likely unconstitutionality of the proposed amendment. The prosecutor in turn requested a technical study to support this position. The technical note produced by INESC and its partners listed five criteria for social funding, some of which already existed in the Brazilian Constitution, the violation of which in any reform proposal would be fatal to social rights. The prosecutor then asked various ministries to respond to the points raised in the technical note. Rather than contest INESC's allegations, the Ministry of Health expressed its agreement with the campaign.

OUTCOMES OF CAMPAIGN AGAINST BRAZIL'S PROPOSED TAX REFORM

- Public hearings were held in the Chamber of Deputies to open discussion on the reform to civil society.
- Media gave attention to the reform and to issues of tax justice.
- A set of indicators were developed and recommended to the executive to monitor equity in the tax system.
- A federal prosecutor investigated the constitutionality of the proposed reform, demanding that the executive defend its proposal.
- The proposal was eventually withdrawn from congress by the executive.

The tax reform proposal was later withdrawn by the executive, a decision which (as it will be explained below) may not be entirely attributable to the campaign, though it was almost certainly influenced by it.

CHANGES DUE TO THE CAMPAIGN

INESC's technical expertise, derived from its budget monitoring experience, was crucial to the campaign in several ways. It was among the few organizations that could detail how, precisely, the proposed reform would affect tax justice and earmarks for social spending.

This allowed INESC to assume a leadership role and to mobilize such a broad swath of civil society against the bill. The technical capabilities of INESC were also crucial for persuading decision makers. INESC's analysis deepened the campaign's argument, opening up the possibility of influencing such influential actors as the President of the Chamber of Deputies and the Economic and Social Development Council. INESC's technical arguments were also essential in collaborating with the federal prosecutor investigating the constitutionality of the proposed reform.

Numerous interviews illustrate that the movement's actions, and INESC's contributions in particular, were instrumental in persuading the executive to withdraw the proposal. Still, other factors undoubtedly contributed.

The federal structure in Brazil was certainly a contributing factor. Approving any tax reform would have required the support of governors. Separate from INESC's campaign, governors were also lobbying against the proposal, arguing that they would lose revenue as a result and demanding more tax incentives from the central government as part of the reform. Another factor was the global economic recession in 2008 that resulted from the banking crisis in the United States. The crisis reached Brazil in 2009, and with its GDP contracted by 0.2 percent, it was the first downturn in Brazil's economy since 1992. This hit the public budget with a R$7 billion drop in tax receipts in real terms.

In the face of an economic environment of uncertainty about the government's revenues, the governors' resistance to the tax proposal, and the defense of social rights threatened by the tax reform – as well as the approaching presidential elections – the government withdrew the proposed tax reform from the public agenda.

Still, Brazil's tax system remains regressive, opaque, and out of line with the principles of fairness and justice established in the constitution. Blocking the reform was a significant victory for the campaign, but not a final one.

CONCLUSIONS

The main aim of the campaign was to prevent the adoption of a proposed tax reform presented by the Brazilian government that would have adversely affected funding for social programs. In this regard, the movement was successful. This, however, may not have been the movement's greatest achievement.

The movement also succeeded in introducing the issue of social rights to the tax reform agenda. Another notable achievement was the wide breadth of civil society actors that were mobilized against the reform. The example has demonstrated the strength of coalition-building for others in Brazil.

Finally, the campaign has left behind a network of organizations that is far more capable of taking on tax issues than ever before. State funding and, by extension, the question of taxation is a complex issue. The work undertaken allowed more than 100 Brazilian organizations to become knowledgeable on a seldom-discussed side of public budgets: revenue. Hundreds of organizations in Brazilian civil society still have the issue of tax reform with social justice on their political agenda, realizing that this issue is not exclusive to government technicians and businesses but a concern for society as a whole.

The skills, networks, and energy that the movement left behind are crucial for moving forward on the path to social justice in Brazil. Blocking an unjust tax reform proposal is a significant victory, but the movement faces the even greater challenge now to persuade decision makers to enact a pro-poor tax reform that will resolve the regressive and opaque nature of the country's existing tax system.