Progressive realization

Article 2 & Governments' Budgets

Retrogression due to tax reforms reducing funds for the realization of ESC rights

The case in brief

Brazil is one of the largest economies in the world, but also one of the most unequal, with a high concentration of wealth in the top 1 percent of the population. While the Brazilian tax system is supposed to be based on fiscal and social justice, solidarity, equality, universality, and the ability to pay, the complementary laws needed to enforce these constitutional principles have never been passed. Indeed, a series of steps in the opposite direction have produced an unfair and regressive tax system.

During the second Lula presidency, the government sent a tax reform proposal to Congress. If that reform had passed, provisions that earmarked specific revenue for social security, education and labor programs would have been eliminated. Such a development would have undermined the government's ability to realize the basic social and economic rights of the poorest sectors of society, thereby leading to a failure to comply with its obligation of non-retrogression.

The Instituto de Estudos Socioeconômicos (INESC) produced high-quality technical notes analyzing and explaining the impact of the intended tax reform on the funds for social policies. It linked the debate around the reform to the government's compliance or failure to comply with the principles and rights established in the Brazilian Constitution. INESC also facilitated the construction of a broad-based coalition to fight the proposal by clearly illustrating the negative impact on whole sectors of the population of an apparently technical reform. The multi-pronged advocacy strategy that they followed illustrates the many different players that are relevant and the many different strategies that have to be employed when trying to stop large, negative, structural reforms.

Human rights issue

Poverty is widespread in Brazil, and government programs in a wide range of areas, including health, labor, education and social security, are essential to enabling the poor to survive and participate in the social and economic life of the country. The Lula government's tax reform proposal would have had a substantial negative effect on funding for these key programs.

Brazil has ratified the International Covenant on Economic, Social and Cultural Rights (ICESCR) which guarantees a range of rights whose realization was threatened by the proposed tax reform, including:

- The right to work and decent conditions of work (articles 6 and 7);
- The right to social security (article 9);
- The right to an adequate standard of living, which includes the right to food (article 11);
- The right to health (article 12); and
- The right to education (article 13).

Human rights argument

A government's obligation to progressively realize ESC rights means that year-by-year an increasing number of people should be able to enjoy their rights and enjoy them more fully. This does not mean that a government has to continually increase budgets directed to ESC rights-related areas. That said, an increasing budget is normally necessary to extend and deepen benefits necessary for the enjoyment of rights, and cuts to budgets typically result in diminished access to such benefits, particularly access by the most vulnerable in the society.

Analysis not only by INESC, but also by the Brazilian Ministry of Health, showed that without a dedicated flow of funds to these social service areas, budgets of the relevant ministries would be cut significantly, resulting in fewer or poorer quality services. Where a government proposes to cut a budget for ESC rights-related areas, it should be able to demonstrate that such cuts would not result in cuts to relevant services. In this case the government made no such showing. The result of the Lula government's proposal to remove the earmarking for social services from key revenue would have constituted retrogression in people's enjoyment of their rights.

Case study in detail

Inequality and the tax system

Brazil is one of the ten largest economies in the world, but also one of the most unequal, in which a small number of people enjoy enormous wealth while a large number are mired in poverty. This despite the fact that the framework for the Brazilian tax system, set out in the 1988 Federal Constitution, promised a tax system based on fiscal and social justice, solidarity, equality, universality, and the ability to pay. It further declared that taxation should be direct, personal, and progressive.

In order for these fine constitutional principles to have effect, Congress needed to adopt a complementary law, which to date it has not done. Even worse, tax reforms enacted during the Cardoso presidency (1995-2003) produced an extremely unfair and regressive tax system. That system exacerbates inequality through high taxation on production and thus on consumption, and low taxes on income, profits, and financial surpluses. Between 1995 and 2009, the tax burden in Brazil increased from 27 to 35 percent of GDP, largely as a result of increases in taxes on consumption. According to a study by the Brazilian Institute of Geography and Statistics, in 2003 those who earned up to twice the minimum wage spent 45.8 percent of their earnings on consumption taxes. Meanwhile, households with an income greater than 30 times the minimum wage spent only 16.4 percent of their income on these same taxes. Moreover, income tax, a potentially progressive tax, has placed a huge burden on wage income, as the wealthy have found creative ways to exploit tax exemptions on income from capital, such as dividend payments.

The obligation to use the maximum of available resources (MAR) to realize ESC rights implies that governments should raise as much revenue as they reasonably can, so as to have substantial funds to direct to the realization of rights. However, in making decisions about revenue, this MAR obligation must be considered in conjunction with the government's other obligations, particularly that of non-discrimination, in order to ensure that increased revenue does not unfairly impact specific groups of people, particularly the poor.

Another unfair tax reform proposal

Article 195 of the Constitution earmarks specific taxes on income, sales, profits, and company payrolls for financing the social security budget, which funds welfare, social services, health, and unemployment policies.

During the second Lula presidency, the government sent a new tax reform proposal to Congress. The proposed Constitutional Amendment (PEC 233/2008) would have had dire consequences for social and economic rights in Brazil, because it would have ended the earmarking of particular funding sources for social security, education, and labor policies. The elimination of the earmarks would have meant that programs related to the realization of ESC rights would have to compete for resources with other functions in the budget. Since the poor depend heavily on these programs, their rights were at particular risk from the reforms.

Step one: Setting up a broad campaign

INESC has analyzed the federal budget and revenue issues for many years, identifying programs and expenditures that are relevant to the realization of ESC rights. After examining the Lula government's tax reform proposal, the organization concluded that its effects would be detrimental to poor sectors of society. It thus decided to put its energy into preventing its adoption. Used to working in coalitions and networks to gain strength and bring the government to the table, INESC built a broad coalition to oppose the reform, comprised of grassroots organizations, social movements, labor unions, religious organizations and research groups linked to universities. Under INESC's leadership, the Movement to Defend Social Rights under Threat by the Tax Reform (MDSR) was created, bringing together more than 100 civil society organizations (CSOs).

The MDSR worked for over two years, employing a variety of strategies. It produced technical and policy analyses to illustrate the negative implications of the reform for social policies; educated and mobilized civil society around these consequences; carried out a systematic campaign to educate and engage legislators; held meetings with government officials of diverse ministries; reached out to the federal prosecutors to highlight how the reform would undo key achievements of the 1988 Constitution; and turned up the heat through media outreach.

To most people governments' budgets are opaque, technical documents. In reality, however, they are a central embodiment of a government's values as well as a key to where political power in the country lies. A central challenge for CSOs seeking to mobilize large numbers of people around budget issues is to identify and speak to the values and political power that are, in reality, shaping the seemingly arcane technical issues.

Step two: Opening channels to Congress

The first challenge for the coalition was to develop channels for dialogue with the government and Congress. A letter signed by 71 CSOs, asking for an open and inclusive discussion forum on the reform, was submitted to the President of Congress.

While he remained unresponsive, the Social Security and Family Committee held a day-long public hearing, which numerous representatives as well as the Ministry of Finance's Deputy Rapporteur for the PEC 233/2008 attended.

INESC published a technical note providing its assessments of the reform. This became a reference for all the organizations in the MDSR and the backbone of the movement's manifesto, endorsed by more than 100 CSOs. The manifesto warned that the proposed tax reform would put social rights at risk, especially those of the poor, and that it required mature reflection from society, Congress and the very executive that had drafted it. The movement argued that the proposal should not even be submitted to a vote without necessary amendments.

Dozens of meetings were held with party leaders and the President of the Chamber of Deputies. All of them committed to raise the issue with the Special Committee dealing with the reform. The Social Security and Family Committee held a second public hearing, this time to examine the impact of the proposal on the financing mechanisms for social policies. Several government officials attended, including the Executive Secretary of the Ministry of Health, who stated that under its current structure, the tax reform would decrease resources for health policy by R$15 billion (US$ 6.7 billion). It became clear to the movement that even within government there were sympathetic allies who would speak out against the reform.

Step three: Working with technical bodies

At the same time, INESC used the solid analysis in its technical note to engage the Council for Economic and Social Development (CDES), a governmental body comprising the Presidency of Brazil, the Statistics Institute and other relevant agencies. The strategic and political relevance of engaging this highly qualified, public body, which is responsible for safeguarding equity and social development, was unquestionable. The collaboration resulted in a technical opinion on equity and the tax system, as well as a letter to the President. Both the CDES document and INESC's technical note underscored the need to build a fairer tax system, while safeguarding the earmarked sources of financing for the social policies that make up the Brazilian social security system. The front opposed to the tax reform proposal was broadening.

Step four: Questioning the constitutionality of the reform

In a meeting with the federal prosecutor for citizens' rights, MDSR representatives asked the public prosecutor to intervene with the executive and legislative powers on the grounds of a likely unconstitutionality of PEC 233/2008. The MDSR produced yet another technical study, identifying the criteria for social funding that should be upheld in order to guarantee social rights in line with the Constitution.

Based on this study, the prosecutor, warning them that PEC 233/2008 could be unconstitutional, called for explanations from the Ministers of Finance, Education, Health, Social Development and Hunger Alleviation, and Social Welfare, the President of the Senate and the President of the Chamber of Deputies. In line with previous statements, the Ministry of Health expressed agreement with the position of the MDSR, while the Ministry of Social Development, the Ministry of Employment, and the Ministry of Social Development and Hunger Alleviation expressed concerns about the tax reform and its negative impact on the social rights enshrined in the Constitution.

Withdrawing the tax reform proposal

Ultimately, the Presidency of Brazil withdrew the tax reform proposal from Congress, not even allowing it to be put to a vote. It was an astounding, marked success for the Movement, which by associating the tax reform with social rights, had managed to involve a wide array of players in realizing its strategy.

Questions you might ask

yourself or your government about progressive realization and taxes.

Is the government securing as much revenue as it reasonably can in order to meet its obligation to progressively realize people's rights?

What is the country's tax burden and how does that compare with the tax burden in similarly situated countries?

How does the current mix of taxes affect different groups of people in the country? The top quintile? The bottom quintile? Has there been a marked trend in recent years to greater or lesser equality in the impact of taxes on individuals?

Has the government introduced additional taxes in recent years? When it has done so, has it done a tax incidence analysis prior to introducing the tax, to determine how the tax would impact different groups in the country? If not, why not? Did it make the results of its analysis public?

If the government introduced additional taxes, did this result in an increase in overall government revenues? If so, what ministries or programs benefitted most from the increased revenue? Which saw little or no increase in their budgets?

Has the government cut taxes in recent years? If so, who has benefitted most from the tax cuts? Who least?

Did the tax cuts result in cuts in the budgets of social programs? If so, which ones? Did the budget cuts result in cuts in services? If so, who was most affected by the cuts in social programs?

Does the government earmark specific revenue for social programs? If so, which revenue and which programs?

Has the earmarked revenue increased, or decreased, over the years? If it has increased in nominal terms, has it also increased in real terms? Has the revenue allowed for a real increase in expenditure for beneficiaries of the targeted social programs? If not, why not?

If the earmarked revenue has failed to increase in real terms, or in *per capita* terms, and if the need for the social programs continues to exist, what additional revenue, if any, has the government directed to the targeted programs?

INESC

(Instituto de Estudos Socioeconômicos)

Established in 1979, INESC is one of Brazil's leading civil society organizations. Over the last 20 years, INESC has used the analysis of public budgets as a strategic tool to influence public policies, with the ultimate mission of deepening democracy, strengthening citizenship, and realizing human rights in Brazil.

INESC's work focuses on three programmatic areas:

- *Budget, Rights, and Inequalities* – measuring the government's commitments to human rights through applied budget analysis;
- *Globalization, Development, and Sustainability* – deepening work around budgetary and development issues at the subnational level; and
- *Democracy, Congress, and Society* – deepening democracy, mainly through the Platform of Social Movements for the Reform of the Brazilian Political System.

For more information on INESC, go to: Inesc.org.br

The Article 2 Project

This booklet is part of the *Article 2 & Governments' Budgets* handbook. The handbook has been developed by the Article 2 Project, a working group housed first at the Partnership Initiative of the International Budget Partnership (IBP), and then at the Global Movement for Budget Transparency, Accountability and Participation. The project aims to enhance understanding of the implications of article 2 of the ICESCR for how governments should develop their budgets, raise revenue and undertake expenditures. The project encourages the use by civil society and governments of the legal provisions of article 2 to monitor and analyze governments' budgets. Download the complete handbook at:

www.internationalbudget.org/publications/ESCRArticle2

The case is based on Evilasio Salvador, "The Role of Brazilian Civil Society in the Tax Reform Debate: INESC's tax campaign," Albert van Zyl (Coord.), *From Analysis to Impact*, Partnership Initiative Case Study Series, IBP, 2011; and INESC, *Reforma Tributária desmonta o financiamento das políticas sociais*, Nota Técnica 140, Brasilia, April 2008.

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