

DECENTRALIZING GOVERNMENT DEFICIT FINANCE IN ARGENTINA

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I. INTRODUCTION

LIKE many Latin American countries, Argentina is suffering a serious external debt problem (Table I), and the public sector deficit is one of the most crucial problems that the country needs to solve. Discussion of the public sector debt has mainly focused on the deficit of the central government and the public sector enterprises, while little attention has been given to the deficits of the local governments. To reduce the deficits of the central government and public sector enterprises, many Latin American countries have undertaken various measures to reduce central government expenditures and privatize public sector enterprises. One measure to reduce the central government deficit has been to decentralize public finance, but this has induced increased expenditures for local governments which suffer from insufficient financial revenues. Therefore this kind of decentralization has often induced serious deficit problems for local governments, and in this regard Argentina has not been an exception.

This paper studies the relation between the central government and local government finances in Argentina. It will first give a brief explanation of the administrative system in Argentina, then examine the fiscal system focusing on the composition of expenditures, revenues, and the deficit of the central and local governments. It will next analyze the revenue transfer system that shifts funds from the central government to the local governments, paying special attention to the Revenue Sharing Law of 1987. Through an examination of the above features, this paper will study the decentralization process and clarify the causes of the deficit problem in Argentine public finance.

II. ADMINISTRATIVE SYSTEM

In order to study the relation between central and local government finances, a basic knowledge of Argentina's administrative system is essential. This section will provide a brief explanation of this system.

Argentina is a federal republic based on the separation of power divided between the administrative, legislative, and judicial branches of government. Of the three, the administrative power is the strongest and is divided into the central government and the local governments. The latter is composed of the provincial, national territory, and municipal governments; there were twenty-two provinces, one national territory, and 1,617 municipalities in 1991. Each province has self-governing

TABLE I
ARGENTINE EXTERNAL DEBT

	1970	1980	1982	1984	1986	1988
Total debt stocks (U.S.\$ million) (A)	5,171	27,157	43,634	48,857	52,374	58,936
(A) / GNP (%)	23.8	48.4	83.8	67.5	70.4	60.5
Interest payments / exports of goods & services (%)	15.7	20.8	36.7	44.1	48.7	27.5
International reserves (U.S.\$ million)	682	9,297	4,504	2,591	4,427	5,158

Source: [7, p. 6].

autonomy under the federal republic and its own constitution. Each province elects its governor, congressmen, and executive officials free from central government intervention. Each province has the power to promote and introduce industries, accept immigrants, construct infrastructure, colonize the provincial land, receive foreign capital, and develop the provincial economy according to its own law and means.¹ Compared with the central government, however, the provincial governments have less power and the Argentine federal system is relatively less decentralized than that of the United States.

This historical development of the federal system in Argentina did not come about smoothly, going through a long and complicated process related closely to the country's economic and financial problems. The conflict over federalization arose soon after independence. Argentina had been colonized for three centuries by Spain, which had established the Vice Royalty of Rio de la Plata² in 1776 with its center of colonial government in the city of Buenos Aires. During the colonial period, political, economic, social, and cultural activities were concentrated in Buenos Aires which induced the development of striking regional differences. Argentina declared independence in 1810 and achieved this in 1816 with the defeat of Spain. Soon after attaining independence, various problems arose concerning national integration and nation-building. A major one concerned the governing system, which developed into a conflict between centralists and federalists and became a power struggle for political hegemony and economic gain. The centralist view was supported by the province of Buenos Aires while the federalist view by the rest of the provinces. During that period the main source of financial revenues was from customs duties, and they were collected mainly at the port of Buenos Aires. Since the city of Buenos Aires was both the national capital and the provincial capital of Buenos Aires, the collected customs duties at the port of Buenos Aires were obtained by the provincial government of Buenos Aires. This fiscal system became the main factor causing the imbalance in financial power between the province of Buenos Aires and the rest of the provinces. In order to

¹ See [1].

² The Vice Royalty of Rio de la Plata covered approximately the region which is now composed of Argentina, Paraguay, and Uruguay.

maintain its political hegemony, the province of Buenos Aires tried to maintain its hold on the customs duties, while the rest of the provinces insisted that the customs duties should be federalized and distributed to all the provincial governments. Federalization of the customs duties was essential for establishing equality among all the provinces and integrating them under the federal system.

The conflict between the centralists in Buenos Aires and the federalists in the rest of the provinces lasted more than half a century and caused serious political problems. In 1853 the latter formed a confederation and promulgated the Constitution of the Argentine Republic in 1853. Under this constitution, Argentina was declared a federal republic, and the national capital and the provincial capital of Buenos Aires were to be separated. It meant that if the city of Buenos Aires remained the national capital, the province of Buenos Aires had to establish a new provincial capital. This constitution was welcomed by the rest of the provinces, but the province of Buenos Aires did not accept it until 1862. As a result Argentina was divided for eight years between two opposing governments: the government of the confederation and the provincial government of Buenos Aires. This system of "one nation with two governments" lasted until 1862 when the province of Buenos Aires finally accepted the constitution and became a formal province in the republic. Thus Argentina was finally integrated under the federal system, but the federalization of customs duties was yet to be realized.

After a long political struggle and negotiations, the city of Buenos Aires finally became the federal capital separated from the province of Buenos Aires in 1880. As the provincial capital of Buenos Aires, the new city of La Plata was selected. This process was completed with the federalization of the customs duties.

This process of administrative change was one of the crucial steps abolishing the remaining features of the colonial system. It aimed at reforming the old centralized colonial system toward a decentralized political and administrative system which would lead to rectifying the regional imbalance in financial revenues. Through the federalization of the customs duties, the province of Buenos Aires could no longer monopolize the customs duties, and the central government could strengthen its financial base. Through this long and conflicting process, the fundamental step to forming an administrative federation was accomplished, and the basic framework of financial relation between the central and local governments was put into place.³

After attaining administrative federalization, fiscal federalization became a crucial issue for Argentina. This entailed the division of administrative services, the collection of revenues, and the creation of a revenue sharing system. Concerning this latter issue, Argentina experienced various trials and errors in the course of working out an efficient and equitable system. Especially after 1970, with the promotion of its administrative decentralization policy, some administrative services were transferred from the central government to the local governments. This process was accompanied by a reform of the fiscal system which will be examined in the following sections.

³ See [3], especially Chap. 1, "Jiyūshugiteki keizai seisakuron no keisei" [Formation of economic liberalism].

TABLE II
CENTRAL, LOCAL, AND GENERAL GOVERNMENT EXPENDITURES
FOR ARGENTINA AND SIX OTHER COUNTRIES

		(% to GDP)					
		1980	1982	1984	1986	1987	1988
Argentina	CG	28.2	23.0	19.9	23.1	22.2	15.8
	LG	10.6	6.8	10.5	11.5	12.9	12.1
	GG	38.8	29.8	30.4	34.6	35.1	27.9
Brazil	CG	24.6	27.9	28.7	36.0	46.7	58.6
	LG	7.1	7.9	7.1	9.3	9.9	9.9
	GG	31.7	35.8	35.8	45.3	56.6	68.5
Mexico	CG	18.9	31.6	23.9	29.0	31.0	27.2
	LG	4.3	3.3	3.7	3.3	3.1	—
	GG	23.2	34.9	27.6	32.3	34.0	—
U.S.A.	CG	23.8	25.4	24.6	25.0	24.0	23.5
	LG	11.1	11.8	11.8	12.4	13.0	13.0
	GG	34.9	37.2	36.4	37.4	37.0	36.5
Canada	CG	21.2	24.8	25.2	23.2	22.2	21.5
	LG	20.8	24.4	22.3	23.1	22.0	22.2
	GG	42.0	49.2	47.5	46.3	44.2	43.7
Australia	CG	26.5	26.8	30.0	30.1	29.4	27.3
	LG	7.1	7.5	8.1	9.1	9.5	9.6
	GG	33.6	34.3	38.1	39.2	38.9	36.9
Spain	CG	28.3	31.2	35.2	33.7	34.4	34.1
	LG	3.1	4.6	5.4	4.7	5.1	5.2
	GG	31.4	35.8	40.6	38.4	39.5	39.3

Source: [4, pp. 92-93, 108-9].

- Notes: 1. Because of the limited data, figures show only total expenditure and lending minus repayments.
2. CG=central government; LG=local government; and GG=general government.

III. CENTRAL AND LOCAL GOVERNMENT EXPENDITURES

We will now examine the expenditures of Argentina's central and local governments. A comparison of these expenditures with those of six other countries⁴ during the 1980s is shown in Table II. The table provides figures for the expenditures of the central government and local governments, and figures for general government expenditures⁵ as a per cent of GDP. The ratio of general government expenditures to GDP varied from 28 to 39 per cent. When compared with the

⁴ These six countries have been selected for the following comparative points: Mexico and Brazil because they are the other two countries which form the big three ABM (Argentina, Brazil, and Mexico) countries in Latin America; the United States, Canada, and Australia because they are federal countries with colonial heritages; and Spain because it is the ex-colonial power which greatly influenced Argentina in various fields.

⁵ General government expenditures are the combined expenditures for the central government and local governments.

TABLE
CENTRAL, LOCAL, AND GENERAL GOVERNMENT EXPENDITURES

	1980			1982		
	CG	LG	GG	CG	LG	GG
General public services	14.3	—	} 11.1	6.7	—	} 7.3
Public order & safety	—	—		—	9.1	
Defense	14.3	—	11.1	10.0	—	7.3
Education	—	50.0	11.1	6.7	18.2	9.8
Health	—	—	—	—	9.1	2.4
Social security & welfare	28.6	—	22.2	30.0	18.2	} 26.8
Housing & community amenities	—	—	—	—	—	
Recreation, culture & religion	—	—	—	—	—	—
Agriculture, forestry, fishing & hunting	—	—	—	—	—	—
Fuel & energy	—	—	} —	3.3	—	} 2.4
Mining, manufacturing & construction	—	—		—	—	
Transportation & communication	—	—	—	6.7	—	4.9
Other economic affairs & services	—	—	—	3.3	—	2.4
Other expenditures & adjustment	42.8	50.0	44.5	33.3	45.4	36.8
(Interest payments)	(—)	(—)	(—)	(23.3)	(—)	(17.1)
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: [4, pp. 116, 118–19].

Note: CG=central government; LG=local government; and GG=general government.

ratios of the six other countries, Argentina was roughly the same as those of the United States, Australia, and Spain, was higher than that of Mexico, and was considerably lower than those of Canada and Brazil. Among the three big ABM (Argentina, Brazil, and Mexico) Latin American countries, Argentina was in the middle, Mexico the lowest, and Brazil the highest in the ratio of general government expenditures to GDP.

Looking next at the ratio of central government and local government expenditures, the ratio of Argentine central government expenditures to GDP varied from about 16 to 28 per cent, and those of the local governments from about 7 to 13 per cent. Comparing this ratio with those of Brazil and Mexico, it is clear that the Argentine government financial expenditure system is more decentralized than those of the other two countries. This is especially true when compared with Mexico where the ratio of local government expenditures to GDP was about 3 to 4 per cent indicating that decentralization is at an extremely low level. By contrast,

III

BY FUNCTION AND INTEREST PAYMENTS

									(%)
1984			1986			1987			1988
CG	LG	GG	CG	LG	GG	CG	LG	GG	CG
4.9	24.8	} 15.9	4.6	11.3	} 13.9	5.1	16.9	} 16.3	6.1
—	8.1		3.4	13.0		3.9	10.7		5.2
8.8	—	5.4	6.0	—	3.9	6.9	—	4.2	8.6
9.5	27.8	16.6	6.0	24.5	12.5	6.9	20.7	12.3	9.3
1.8	10.3	4.7	1.9	9.5	4.4	2.1	8.0	4.4	2.0
37.9	9.9	} 29.9	32.3	6.7	} 27.2	31.7	6.2	} 25.1	40.5
0.5	7.3		0.4	10.5		0.3	8.3		0.4
0.7	—	0.4	0.7	1.2	0.9	0.8	1.0	0.9	0.9
0.9	—	0.2	0.9	3.5	1.5	1.3	2.6	1.5	1.7
5.2	0.4	} 3.2	6.5	2.4	} 6.0	5.1	3.6	} 5.3	6.1
0.1	—		1.6	0.2		1.6	0.1		2.1
9.4	4.1	6.6	7.8	5.3	6.3	8.5	2.9	5.8	9.1
4.7	6.2	5.4	1.3	4.1	2.3	1.2	2.4	1.7	1.6
15.6	1.1	11.7	26.6	7.8	21.1	24.6	26.6	9.3	6.4
(13.6)	(0.1)	(8.4)	(7.8)	(0.5)	(5.2)	(8.1)	(0.7)	(5.2)	(7.4)
100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Argentine government financial expenditures are almost at the same level as those of the United States, while they are slightly higher than Australia's, considerably higher than Spain's, and considerably lower than Canada's.

Generally speaking, federal states tend to have a higher ratio of local government expenditures than nonfederal states. Professor Ryūichi Yoshimoto [8] classified the public expenditures of the latter into three types: type 1 is composed of those states which have a higher ratio of local government expenditures than those of the central government such as Japan and Scandinavian countries; type 2 is made up of those states where central government expenditures are about twice as high as local government expenditures such as the United Kingdom; and type 3 consists of those states where the ratio of central government expenditures is very high, such as France where it is 90 per cent of general government expenditures.⁶

⁶ See [8, pp. 49-50].

TABLE IV
CENTRAL, LOCAL, AND GENERAL GOVERNMENT DEFICITS

	(%)					
	1980	1982	1984	1986	1987	1988
Deficit / GDP:						
Central government	-3.5	-7.5	-5.1	-2.6	-3.8	-2.7
Local government	-7.1	-1.3	-5.1	-7.3	-8.2	-3.0
General government	-10.6	-8.8	-10.1	-9.9	-12.0	-5.7
Deficit / (total expenditures + lending - repayments):						
Central government	-25.0	-32.4	-25.4	-11.5	-17.0	-16.9
Local government	-33.3	-27.3	-47.8	-61.6	-62.9	-24.4
General government	-27.3	-29.5	-33.3	-28.6	-34.1	-20.3

Sources: [4, pp. 45, 79, 95, 118-19].

Argentina's public finances show a typical example of a federal state with a comparatively high ratio of local government expenditures. It is very different from the example of Spanish public finance. On the other hand, Mexico, in spite of being a federal state, has not carried out financial decentralization and maintains a high level of financial centralization. Both Argentina and Mexico were colonized by Spain for nearly three centuries, but in the Spanish type of financial centralization is hardly seen in present-day Argentina, while in Mexico it can be clearly seen. This fact would be a good subject for research regarding Spanish influence on public finance in Mexico and Argentina.

Next we will examine the composition of Argentine financial expenditures (Table III). For the central government, the expenditures for social security and welfare accounted the highest share ranging from about 29 to 41 per cent. These were followed by expenditures for general public services, defense, education, and transportation and communication. On the other hand, expenditures for agriculture, forestry, fishing, and hunting, recreation, culture, and religion, and housing and community amenities account for a very small share. In the area of local government expenditures, education, general public services, public order and safety, housing and community amenities, health, and social security and welfare were the major important items. In these areas, the importance of local government activities has been increasing but without adequate increase in local government revenues, and this has caused serious financial deficit problems.

Table IV shows the deficits of the central and local governments in Argentina. The ratio of deficit to total expenditures for the central government varied from 12 to 32 per cent, and it drastically decreased after 1986. The same ratio for local governments varied from 24 to 63 per cent which was much higher than that of the central government, and this ratio tended to increase year after year until 1987. Looking at the deficit ratio to GDP, the central government deficit ratio ranged from 3 to 8 per cent, and that of the local governments from 1 to 8

TABLE V
CENTRAL, LOCAL, AND GENERAL GOVERNMENT REVENUES
FOR ARGENTINA AND SIX OTHER COUNTRIES

		(% to GDP)					
		1980	1982	1984	1986	1987	1988
Argentina	CG	21.2	15.6	14.8	20.4	18.4	13.1
	LG	7.0	5.4	5.5	4.3	4.7	9.1
	GG	28.2	21.0	20.3	24.7	23.1	22.2
Brazil	CG	22.2	25.2	23.5	22.3	34.3	43.2
	LG	5.5	7.1	6.5	8.5	7.9	8.0
	GG	27.7	32.3	30.0	30.8	42.2	51.2
Mexico	CG	15.8	16.1	16.6	15.9	17.4	17.0
	LG	3.8	2.9	3.8	3.4	3.2	—
	GG	19.6	19.0	20.4	19.3	20.6	—
U.S.A.	CG	20.9	21.4	19.7	19.8	20.6	20.3
	LG	12.0	12.6	13.0	13.9	14.3	14.0
	GG	32.9	34.0	32.7	33.7	34.9	34.3
Canada	CG	17.9	19.3	18.8	19.3	19.7	19.3
	LG	19.9	21.4	20.8	20.6	20.8	20.4
	GG	37.8	40.7	39.6	39.9	40.5	39.7
Australia	CG	24.9	26.5	25.9	27.7	28.1	27.8
	LG	6.8	7.2	8.0	8.5	8.6	9.1
	GG	31.7	33.7	33.9	36.2	36.7	36.9
Spain	CG	24.1	25.3	26.4	28.8	30.3	30.1
	LG	3.0	4.5	5.6	4.0	4.8	5.2
	GG	27.1	29.8	32.0	32.8	35.1	35.3

Source: [4, pp. 86-87, 100-101].

Note: CG=central government; LG=local government; and GG=general government.

per cent. Looking at these figures, the local government deficit ratio tended to be higher than that of the central government except in 1982. The central government, however, finances the local governments through the transfer of revenue, but the transferred revenue does little to lighten the local government deficit burden.

The interest payment burden is shown in Table III. For local governments the ratio of interest payment to total expenditures was less than 1 per cent. On the other hand, for the central government this ratio was from 7 to 23 per cent. As will be explained in more detail later, these figures indicate that the central government transfers revenue to the local governments in order to subsidize the latter, and that the financial deficit increases for the central government. We have to pay attention to this mechanism because Argentine financial deficit problems tend to be discussed both domestically and internationally by focusing on the deficit of the central government and the public sector enterprises, while local government deficits have not received proper consideration as a serious problem to be solved.

TABLE
COMPONENTS OF ARGENTINE CENTRAL, LOCAL,

	1980			1982		
	CG	LG	GG	CG	LG	GG
Tax revenue:						
Taxes on income, profits & capital gains	—	50.0	12.5	4.3	25.0	9.7
Social security contributions	16.7	—	12.5	13.0	—	9.7
Taxes on property	—	—	—	4.3	12.5	6.5
Domestic taxes on goods & services	16.7	50.0	25.0	39.1	25.0	35.5
Taxes on international trade & transactions	—	—	—	8.7	—	}19.2
Other taxes	33.3	—	25.0	8.9	25.0	
Total	66.7	100.0	75.0	78.3	87.5	80.6
Nontax revenue	33.3	—	25.0	21.7	12.5	19.4
Current revenue	100.0	100.0	100.0	100.0	100.0	100.0
Capital revenue	—	—	—	—	—	—
Total revenue	100.0	100.0	100.0	100.0	100.0	100.0
	(6)	(2)	(8)	(23)	(8)	(31)

Source: [4, pp. 115–16, 118–19].

Notes: 1. Figures in parentheses indicate millions of australes.

2. CG=central government; LG=local government; and GG=general govern-

IV. CENTRAL AND LOCAL GOVERNMENT REVENUES

Turning to the revenues of Argentine central and local governments, Table V shows the ratio of central, local, and general government revenues to GDP. The ratio for the central government varied from 15 to 21 per cent between 1980 and 1987, then in 1988 it dropped to as low as 13 per cent. The same ratio for the local governments varied from 4 to 9 per cent, and recorded the highest ratio in 1988. The same ratio for general government revenues varied from 20 to 28 per cent, with the highest ratio recorded in 1980 and the lowest in 1984. After 1986 the ratio tended to decrease.

When we compare the ratio of Argentine fiscal revenues with those of the other countries, the Argentine ratio of general government revenues to GDP was lower than that of Brazil's and higher than Mexico's. When compared with the developed countries, the Argentine ratio was comparatively low, and typical federal states like the United States, Canada, and Australia had about the same ratio which was as high as 30 to 40 per cent. As a ratio of central government revenues to GDP, Argentina was at about the same level as Mexico and considerably lower than

VI
 AND GENERAL GOVERNMENT REVENUES

												(%)
1984			1986			1987			1988			
CG	LG	GG	CG	LG	GG	CG	LG	GG	CG	LG	GG	
3.1	22.5	8.5	6.2	31.4	10.9	8.5	32.6	13.6	4.3	18.1	10.1	
24.0	—	17.6	25.2	—	20.8	26.2	—	20.9	43.3	—	25.5	
2.7	16.1	6.4	6.7	13.1	8.0	6.7	12.2	7.9	5.8	7.6	6.6	
42.1	31.2	38.5	37.4	9.6	31.7	34.8	9.7	29.1	22.3	4.9	14.3	
13.4	—	}15.5	12.0	—	}14.6	10.3	—	}14.2	11.4	—	}31.6	
4.7	8.1		3.1	11.9		4.2	12.8		4.4	53.0		
90.0	77.9	86.5	90.6	66.0	86.0	90.7	67.3	85.7	91.5	83.6	88.1	
10.0	21.1	13.2	9.4	32.3	13.7	8.7	30.5	13.4	8.2	15.6	11.4	
100.0	99.0	99.7	100.0	98.3	99.7	99.4	97.8	99.1	99.7	99.2	99.5	
—	1.0	0.3	0.0	1.7	0.3	0.6	2.2	0.9	0.3	0.8	0.5	
100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	
(783)	(298)	(1,070)	(15,179)	(3,363)	(18,369)	(32,627)	(8,594)	(40,962)	(102,854)	(73,300)	(174,506)	

ment.

Brazil. Compared with the ratio of the United States, Canada, Australia, and Spain, Argentina was roughly as high as the United States and Canada, and lower than Australia and Spain. Looking at the ratio of local government revenues to GDP, Argentina's ratio was at about the same level as Brazil's and Australia's, but lower than that of the United States and Canada and higher than that of Mexico and Spain.

From these data, we can characterize the Argentine financial revenue system as follows: firstly, the ratio of general government revenues to GDP is slightly higher than that of Mexico, while considerably lower than that of Brazil, Australia, Canada, the United States, and Spain. Secondly, the ratio of Argentine local government revenues to GDP tended to decrease during the first half of the 1980s, then increase thereafter. In 1988 especially, this ratio reached 9 per cent which shows the progress of financial decentralization.

Examining next the major components of Argentine central government revenues (Table VI), the main source of revenues is from taxes, and the share of total revenue from this source increased, reaching more than 90 per cent in the late 1980s. Social security contributions and domestic taxes on goods and services were the main sources of tax revenues, and the share for these two items ranged

from one-half to two-thirds of total tax revenues. The share for international trade and transaction taxes varied from about 9 to 13 per cent, that for taxes on income, profits, and capital gains from 3 to 9 per cent, and the share for taxes on property was from 3 to 7 per cent. The total share for the five items reached about 90 per cent or more of total tax revenues except in the year 1980.

For local government revenues, the main sources were taxes on income, profits, and capital gains, domestic taxes on goods and services, and taxes on property. The share for these items reached 70 per cent or more of total tax revenues, except in the year 1988 when the components of tax revenue changed drastically and the share for other taxes increased greatly. In that year the revenue sharing system between the central and local governments was reformed. This will be examined in the next section.

We will now compare the composition of Argentine fiscal revenues with those of the other six countries. Because of the limited data, a detailed comparison is possible only for the central governments. According to Table VII, the share of tax revenues in total revenues was around 80 per cent for Canada, and around 90 per cent for Argentina, the United States, Australia, and Spain. Brazil, however, had the extremely low share of 16 per cent. As the main sources of the tax revenue, Argentina and Spain had the highest share from social security contributions ranging from 38 to 43 per cent. On the other hand, the United States, Canada, and Australia had the highest share from taxes on income, profits, and capital gains. The share from domestic taxes on goods and services was nearly the same in Argentina, Canada, Australia, and Spain, while in Mexico it was extremely high, and in Brazil and the United States extremely low. The share from taxes on international trade and transactions was considerably higher in Argentina than in the rest of the countries.

Next we will compare the composition of Argentine general government revenues with those of the other six countries. Because of the limited data, this comparison can only be very brief. According to Table VIII, showing the ratio of tax revenue to GDP, Argentina is roughly at the same level as Brazil and Mexico, while considerably lower than the other four developed countries. In the area of tax resources, the progressive type of taxation, such as taxes on income, profits, and capital gains, makes up a considerably small share when compared with the developed countries.

There are various factors preventing the increase of tax revenues and the promotion of progressive taxation in Argentina. The main factors are: political pressure against increasing taxation, especially against progressive-type taxation, the presence of high levels of tax evasion, the proliferation of preferential treatment for taxation such as exemptions and reductions, the inefficiency of official organizations in tax collection both at the national and provincial level [2, p. 47], and the tenacious chronic hyper-inflation which induces further complications in tax collection procedures. Argentina is one of the countries well known for its high ratio of tax evasion, and until 1990 there were no effective laws or penalties against tax evasion. Under these circumstances the central government has tried to reduce the fiscal deficit by cutting down fiscal expenditures through curtailing public services, or by transferring these services to the local governments. At the same

TABLE VII
COMPONENTS OF CENTRAL GOVERNMENT TAX REVENUES FOR ARGENTINA AND SIX OTHER COUNTRIES

Country	Year	Total Revenue	Tax Revenue	Taxes on Income, Profits & Capital Gains	Social Security Contributions	Taxes on Payroll & Work Force	Taxes on Property	Domestic Taxes on Goods & Services	Taxes on International Trade & Transactions	Other Taxes	Nontax Revenue	(% of total revenue)
Argentina	1988	100.0	91.5	4.3	43.3	—	5.8	22.3	11.4	4.4	8.2	
Brazil	1989	100.0	15.8	4.8	5.8	0.8	—	3.8	0.6	—	81.7	
Mexico ^a	1989	100.0	99.8	29.4	11.5	0.7	—	53.1	5.1	—	16.5	
U.S.A.	1990	100.0	92.1	51.6	34.6	—	1.1	3.2	1.6	—	7.9	
Canada	1988	100.0	88.4	51.3	14.6	—	—	19.0	3.8	0.01	11.6	
Australia	1989	100.0	91.2	64.8	—	0.1	0.5	21.6	4.2	—	8.4	
Spain	1988	100.0	93.7	28.3	37.8	—	1.1	24.0	2.5	—	6.0	

Source: [4, pp. 38-39].
^a There is a statistical discrepancy.

TABLE VIII
COMPONENTS OF GENERAL GOVERNMENT REVENUES FOR
ARGENTINA AND SIX OTHER COUNTRIES, 1988

	(% to GDP)				
	Total Revenue	Tax Revenue	Taxes on Income, Profits & Capital Gains	Taxes on Domestic Goods & Services	Nontax Revenue
Argentina	22.2	19.6	2.3	3.2	2.5
Brazil	51.2	20.6	4.2	9.4	30.4
Mexico ^a	20.6	17.8	4.1	11.0	2.8
U.S.A.	34.3	27.9	12.8	4.6	6.3
Canada	39.7	33.7	15.6	9.5 ^b	6.0 ^b
Australia	36.9	30.8	17.1	8.2	5.4
Spain	35.3	32.1	9.6	8.8	2.9

Source: [4, pp. 100-107].

^a Year of 1987.

^b Data that are preliminary or provisional and related to a period ending on or before the date the data were compiled.

time, however, the local governments have also been suffering from a shortage of fiscal revenue, and their fiscal deficits have tended to increase. This situation has brought about the vicious circle of fiscal revenue shortages and deteriorating public services. Under these conditions, intergovernmental transfer payments have become a crucial issue between the central and the local governments.

V. INTERGOVERNMENTAL TRANSFER PAYMENTS

We will next examine Argentina's intergovernmental transfer payments. As Table IX shows, the amount of intergovernmental transfer payments tended to increase during the 1980s, but until 1987 less than 20 per cent was distributed by function, except in 1984. After enforcement of the Revenue Sharing Law in 1987, the amount of distribution by function jumped in that same year to 56 per cent of total intergovernmental transfer payments; 48 per cent of the total amount of functional distribution was directed to transportation and communication, 22 per cent to agriculture, forestry, fishing, and hunting, 14 per cent to fuel and energy, 6 per cent to social security and welfare, another 6 per cent to health, and the rest to education, housing and community amenities, general public services, recreation, culture, and religious affairs. As these figures show, intergovernmental transfer payments were mainly directed to infrastructure and primary industry, while social security and welfare, health, education, and general public services received less payments.

Moreover the total amount of intergovernmental transfer payments decreased by 21 per cent from 1987 to 1988 in nominal terms which was a primary factor for the local government deficits. In order to create a stable and sound financial base for local governments, it is essential to find measures for increasing revenues

TABLE IX
ARGENTINE INTERGOVERNMENTAL TRANSFER PAYMENTS

	(Millions of australes)				
	1982	1984	1986	1987	1988
Total intergovernmental transfers	2	59	3,901	8,513	6,696
Of which: from central government	2	59	3,901	8,513	6,696
General public services	—	—	1	2	5
Education	—	2	23	24	131
Health	—	6	64	56	207
Social security & welfare	—	5	32	82	230
Housing & community amenities	—	1	8	5	19
Recreation, culture & religious affairs	—	—	2	3	2
Fuel & energy	—	3	47	121	520
Agriculture, forestry, fishing & hunting	—	5	75	195	805
Mining, manufacturing & construction	—	—	1	1	—
Transportation & communication	—	11	176	311	1,803
Other economic affairs & services	—	—	1	2	—
Other transfers	2	26	3,471	7,711	2,974

Source: [4, p. 119].

through their own sources as well as through transfers from the central government. Concerning this point, the Revenue Sharing Law, which was enacted in 1987 and put into effect in 1988, aims at reforming the revenue transfer system from the central government to the local governments reflecting the decentralization of public finance. In the next section, we will examine this law.

VI. THE REVENUE SHARING LAW OF 1987

Since the late 1970s, decentralization of public administration has been promoted and among them has been “especially health and education, for which substantial service delivery responsibility had been transferred from the Central Government to the Provinces in the late 1970s and early 1980s” [6, p. 61]. This decentralization brought an increase in local government expenditures which in turn expanded their deficits. Argentina’s public finance deficit has become a serious problem impeding sound public finance and economic management, and the local governments are one of the main factors in public finance along with the central government and the public enterprises. The Revenue Sharing Law was passed as one of the measures to improve the deficit problem by reforming the system for transferring revenues from the central government to the local governments.

Before the Revenue Sharing Law of 1987, the transfer system for fiscal revenues was not well organized, and no clear and rational principles existed. Under such conditions, “those provinces which ran up high fiscal deficits tended to get more resources from the Central Government in the form of discretionary grants” [6, p. 20]. Under the new law the principle of revenue transfer has been changed from the distribution of discretionary grants to revenue sharing, and “discretionary grants are limited to only one percent of total shared taxes, and the percentage of

TABLE X
RELATIVE DISTRIBUTION OF REVENUE SHARING FUNDS, POPULATION, GROSS PROVINCIAL PRODUCT, AND HOUSEHOLDS
WITH UNSATISFIED BASIC NEEDS BY PROVINCE IN ARGENTINA

Provinces	Total Revenue Shared under New Law, ^a 1988		Population 1985		Gross Provincial Product 1980		Households with Unsatisfied Basic Needs 1980		A/F	
	A	B	C	D	E	F	G	F	G	
Advanced:	44.03	67.4	0.65	71.1	0.62	57.7	0.76			
1. Buenos Aires	22.00	43.6	0.50	42.4	0.52	37.5	0.59			
2. Cordoba	8.90	9.4	0.95	10.1	0.88	7.8	1.14			
3. Mendoza	4.18	4.8	0.87	5.8	0.72	3.7	1.13			
4. Santa Fe	8.95	9.6	0.93	12.8	0.70	8.7	1.02			
Low-density:	9.30	5.2	1.80	7.8	1.19	5.5	1.69			
5. Chubut	1.58	1.1	1.42	2.3	0.70	1.2	1.28			
6. La Pampa	1.87	0.8	2.26	1.1	1.68	0.7	2.66			
7. Neuquen	1.74	1.1	1.60	1.7	1.01	1.2	1.47			
8. Rio Negro	2.53	1.7	1.52	1.7	1.52	2.0	1.26			
9. Santa Cruz	1.58	0.5	3.25	1.0	1.51	0.4	3.99			
Intermediate:	19.17	12.8	1.49	11.3	1.69	15.3	1.25			
10. Entre Rios	4.89	3.5	1.40	3.4	1.43	4.0	1.21			
11. Salta	3.84	2.7	1.41	2.0	1.90	3.8	1.00			
12. San Juan	3.39	1.9	1.83	1.3	2.55	1.7	1.99			
13. San Luiz	2.29	0.8	2.74	0.9	2.67	0.9	2.47			
14. Tucuman	4.76	3.9	1.21	3.7	1.28	4.8	0.99			

TABLE X (Continued)

Provinces	Total Revenue Shared under New Law, ^a 1989	Population 1985		A/B		Gross Provincial Product 1980	A/D		Households with Unsatisfied Basic Needs 1980		A/F
		A	B	C	D		E	F	G		
Underdeveloped:	27.50	14.6	1.88	9.7	2.83	21.5	1.28				
15. Catamarca	2.76	0.8	3.36	0.6	4.90	1.1	2.60				
16. Chaco	5.00	2.8	1.78	1.6	3.09	4.4	1.13				
17. Corrientes	3.72	2.6	1.44	1.9	1.96	3.7	0.99				
18. Formosa	3.65	1.2	3.04	0.6	6.01	1.9	1.93				
19. Jujuy	2.84	1.7	1.65	1.7	1.66	2.6	1.11				
20. La Rioja	2.08	0.7	3.19	0.4	5.54	0.7	2.87				
21. Misiones	3.31	2.4	1.36	1.6	2.03	3.3	0.99				
22. Sgo. del Estero	4.14	2.4	1.76	1.3	3.13	3.7	1.12				
Total	100.00	100.0	1.00	100.0	1.00	100.0	1.00				

Source: [6, p. 24].

^a Includes the impact of the distribution of 2 per cent of total shared revenues to Buenos Aires, Neuquen, Chubut, and Sant Cruz in primary distribution, as well as secondary distribution.

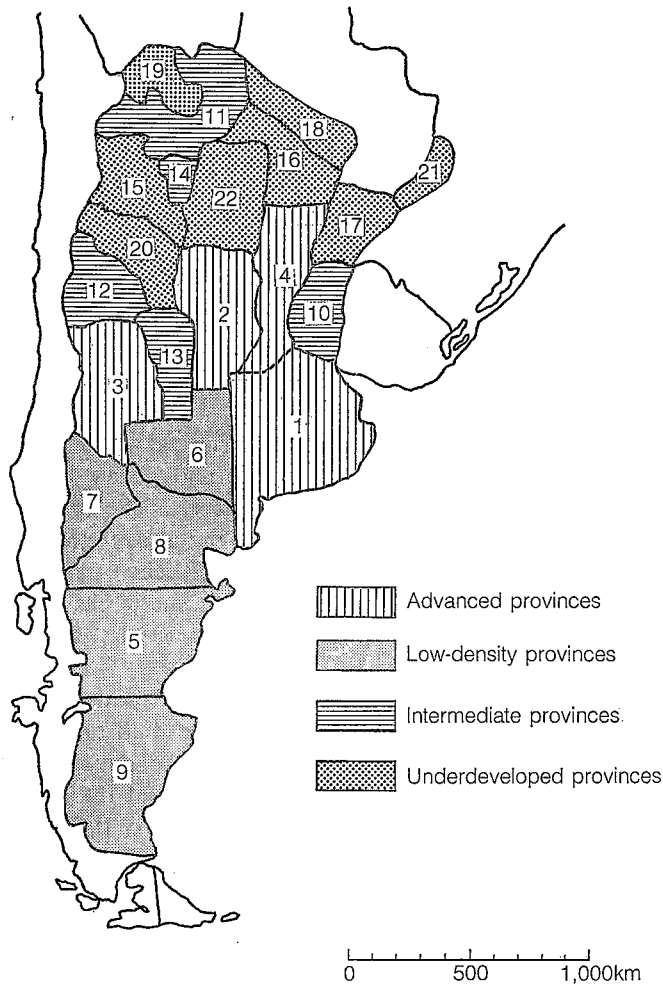
the total revenues from shared taxes going to the provinces as a whole (i.e., primary distribution), and also the percentages going to each province (i.e., secondary distribution) are fixed by the law" [6, p. 20]. The primary distribution of shared taxes is divided into two parts; 42.34 per cent of the total goes to the central government, and 57.66 per cent goes to the local governments. The latter 57.66 per cent is divided into three parts: 54.66 per cent is distributed to all twenty-two provinces, 2 per cent to four provinces⁷ in order to equalize financial revenues, and 1 per cent to be distributed as discretionary grant funds.

We will now evaluate the distribution of revenues under the law of 1987. Taking the classification of the twenty-two provinces into four groups presented by the World Bank country study [6], Table X and Figure 1 show the results of revenue distribution. According to this table, the advanced group of four provinces received 44.0 per cent of the shared revenue, while their ratio of the population was 67.4 per cent, and the share of the households with unsatisfied basic needs was 57.7 per cent. On the other hand, the low-density group of five provinces received 9.3 per cent of the shared revenues, while their share of the population was 5.2 per cent, and the share of households with unsatisfied basic needs was 5.5 per cent. The intermediate group received 19.2 per cent of the shared revenues, while its share of the population was 12.8 per cent and the share of households with unsatisfied basic needs was 15.3 per cent. Finally the underdeveloped group received 27.5 per cent of the shared revenues, while their ratio of the population was 14.6 per cent and the share of households with unsatisfied basic needs was 21.5 per cent. Comparing the ratio of shared revenue under the new law to the ratio of households with unsatisfied basic needs among the four groups, the low-density group had the highest ratio of 1.69; the underdeveloped group was second with a ratio of 1.28; the intermediate groups third with a ratio of 1.25; and the advanced was lowest with 0.76. Moreover, when we compare the ratio of shared revenues to population among the four groups, the underdeveloped group had the highest ratio with 1.88, the low-density group the second with 1.80, the intermediate group the third with 1.49, and the advanced group the lowest with 0.65.

From the data presented in Table X, we can evaluate the revenue sharing system under the new law as follows: revenue sharing was highly weighted toward the underdeveloped and the low-density groups, less weighted toward the intermediate group, and least weighted toward the advanced group. Thus the new revenue sharing law contributed considerably toward equalizing revenues among the provinces. However, it still leaves the problem of the low-density groups tending to receive an excessively high-weighted share of the revenues compared with the other groups. In other words, the provinces with small populations tend to receive overweighted revenues, while those with large populations tend to receive less weighted revenues in spite of the higher share of households with unsatisfied basic needs. Nevertheless the Revenue Sharing Law of 1987 has introduced a clear and rational system for revenue sharing from the central government to the local governments, eliminating the very considerable part that discretionary grants used to play. Decentralization of public administration tends

⁷ These four provinces are those of Buenos Aires, Chubut, Neuquen, and Santa Cruz.

Fig. 1. Classification of Argentine Provinces



Note: Province number corresponds to that in Table X.

to increase the expenditures of local governments, and therefore the increase of local revenues has become all the more important. Under these circumstances, the new law has contributed to establishing the framework for revenue transfer, and for this it should be evaluated highly. But the outstanding problem now is the shortage of total revenues for both the central and local governments, so the amount of revenues that can be transferred is far from sufficient.

VII. CONCLUSIONS

As pointed out in this paper, decentralization of the administrative system and public finance was one of the crucial issues in Argentina for nearly one century

after independence. This issue was closely related to the distribution of the fiscal revenue. At present decentralization of public finance among the big ABM Latin American countries has proceeded the furthest in Argentina.

From the late 1970s, administrative and fiscal decentralization was promoted under economic liberalism. At the same time, however, the Argentine economy was destabilized by its external debt problem, and during the 1980s the country faced a very critical situation both in its domestic economy and in its external relations. The economic stabilization and reconstruction plans recommended by the World Bank and IMF became the first and most urgent targets to be realized in order to obtain international financial cooperation. In public finance, reduction of the fiscal deficit became the important issue, and reduction of fiscal expenditures and privatization of public enterprises were designated as the principal concrete measures. The former was accompanied through fiscal decentralization. As part of this process, several laws were enacted to reform the tax system, one of these being the Revenue Transfer Law.

It must be noted, however, that reduction of fiscal deficit without adequate increase of fiscal revenues often leads to "little and cheap government" policy which tends to induce deterioration of public services. The fiscal decentralization process leads to a reduction of the fiscal deficit of the central government but tends to increase the deficits of the local governments and leave public services with a shortage of fiscal revenues. In order to cut this vicious circle, tax reform is vital for increasing revenues, equalizing the tax burden to prevent tax evasion, and for increasing administrative efficiency.

Under these circumstances, Argentina has recently introduced tax reform which simplifies tax administration and eliminates the complicated tax preference system. Concerning progressive taxation, the top marginal rate of income tax was lowered from 45 to 35 per cent [5, p. 48], while the value added tax has become all the more important as the main source for tax revenues. In 1990 "a law imposing criminal penalties on tax evaders" [5, p. 46] was adopted and the number of tax inspectors increased. Through this tax-reform policy, the central government intends to reduce tax evasion and the fiscal deficit.

At the same time the central government has been executing a drastic privatization policy for public enterprises. This plan is intended to reduce the burden of subsidizing public enterprises and to improve their management and services. More time will be needed to evaluate this policy, but the privatization process as it is being carried out at present is filled with obstacles and confusion. Many Argentines call the policy a "bargain sale of grandmother's jewelry," grandmother's jewelry being the public enterprises which were purchased and nationalized mostly from British, French, and U.S. capital immediately after the Second World War and are now in the process of being purchased by foreign as well as Argentine capital. There can be no denying that the lack of leadership and preparation for privatization has caused the present confusion and inefficiency. The role of government is still very important for less developed countries as the promoter and the coordinator of socioeconomic development. Great care is needed so that the rationalization and decentralization of public finance does not end up

causing economic stagnation and the deterioration of public services and social welfare.

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