

# **TAX POLICY CHANGES IN THE CONTEXT OF CRISIS IN BRAZIL: IDEAS, INTERESTS AND INSTITUTIONS**

**Melina de Souza Rocha Lukic**

*Professor Fundação Getúlio Vargas – Direito RIO*

The present paper aims to analyze the tax policy in Brazil since 2007 by three dimensions taken into account by neo-institutionalism approaches (Hall, Taylor, 1997): ideas, interests and institutions. According Palier and Surel (2005, p. 8), mobilize these three variables allows to take into account "the plurality of possible dimensions of analysis and the diversity of possible causes in the study of public action". Thus, the objective is to articulate these dimensions and at the same time decompose "the object studied in constituent units based on three" is "(Palier, Surel, 2005).

Firstly, analyzing the problem in terms of ideas allows the identification of cognitive and normative dimensions of the studied processes "(Palier, Surel, 2005). It means to study the transformations of the paradigms of public policies through dimensions such as: diagnoses of the problems made by the actors, the values and objectives defended by them, the standards of public action, the instruments and images or models that are at the base of the paradigm. This analysis will be based on authors of the cognitive approach of public policies, especially the processes of public policy paradigm shift as identified by Hall (1993.1997) and Surel (1997.1995).

Then the object of analysis will also be considered from the institutional dynamic. From this variable, it will be possible to examine how institutions and rules can have consequences on the behavior and the interests of stakeholders, influencing the balance of forces and the dynamics of the change process. Through this dimension we also can analyze the learning mechanisms and the scope and constraints of actors interested in decision making. So, more than a static analysis, we propose a study of the dynamics and the conditions of institutional changes, as proposed by the studies of Thelen and Mahoney (2010).

Finally, the analysis of the interests will identify not only the actors present and important to the public policy, but also issues related to collective action, "calculations and strategies used by the actors on the basis of the expected costs and benefits of any conflicts or possible cooperation and the impact of expectations made by individuals or organizations involved in public action" (Palier, Surel, 2005). Through the analysis of interests, we can identify the assumptions about the motivations and the process of decision-making as well as the preferences, balance of power, or capacity of action and mobilization and the resources and strategies of the actors.

Based on this theoretical framework, the analysis of Lula's second term (2007-2010) is characterized by a shift both in cognitive and institutional terms in the economic and fiscal policy in Brazil. After a period where the stabilization and fiscal adjustment determined the paths of fiscal policy; from this moment begins a new direction of the paradigm of public policy objectives in the field of taxation. This

change was made in part as a response to the 2008 crisis, when the Government had to make further adjustments in its economic and fiscal policy. The Brazilian Government responded to the crisis with innovative measures in comparison with the recent history of Brazil. Unlike other crises and what occurred in most countries, Lula adopted "countercyclical" monetary and budgetary measures to retrieve the level of economic activity as soon as possible.

This change in the orientation of the paradigm was followed by the implementation of institutional changes such as many taxes reductions and exemptions in various sectors (electricity, automobiles, appliances, salaries). The main consequence was, firstly, a decrease of fiscal revenues without, on the other hand, a reduction of expenses. Thus, due to the changing on the cognitive dimension of taxation paradigm (Hassenteufel, 2008), new changes of instruments - such as the "*Programa de Aceleração do Crescimento*" (Growth Acceleration Program) – were implemented, in order to adapt the system to the new model. All this can lead to budgetary imbalances and increase the public debt, since the Government is further away from the fiscal targets of 3.1% of GDP. The decrease of GDP in 0.9% in 2012 was a consequence of this new policy.

In institutional terms, the implementation of tax policy measures was a "layering" change (Thelen and Mahoney, 2010) in which the need to establish an effective system and develop the country became its main objective. Thus, after a period of economic stabilization and adjustment of public accounts, the slogan has changed to the effectiveness of the system, growth and development of the country and international competitiveness. Even if substantial reforms of the system does not have occurred since 1988, both cognitive and institutional changes in the fiscal and tax policy orientation were made through the implementation or modification of certain instruments, especially after 2008. Thus, in the light of neo-institutionalism theories and the cognitive approach of public policies, we will examine, in the first part, what were the reasons for these changes and how they have been implemented.

Concerning the analysis of the interests involved, Lula presented has a second tax reform in 2008, with proposals for deeper changes in comparison to that of the first term, including changes to the system of ICMS (*tax on circulation of goods*). However, the context of crisis and the disputes and conflicts of interests – especially from the richest States - prevented the adoption of the reform. In addition, proposals to reduce contributions to the social security financing raised a strong coalition of interests against such measures. Despite the will of the President and the support of some States and the Business Coalition (Lukic, 2012), this proposal has resulted in a strong opposition from the richest States (mainly São Paulo), main *veto players* responsible for the failure of the reform. The main argument of those States to not support the proposal was the uncertain context of crisis. We will discuss at the second part of the paper, the discussions and interests around this reform, as well as the reasons for its failure. The assumption is that, contrary to what happened during the Cardoso Government, the crisis was not the decisive reason for the failure of the reform, but much more disputes between the federative entities.

Finally, the context in which the change is proposed seems to influence the way in which the decision is made. According to the analysis proposed by Grindle and Thomas (1991), if a reform initiative appeared in a context of crisis – namely, in a period where the elites perceive a crisis, the reform is seen as a response to this crisis. This context is

therefore susceptible to create strong pressure in favor of reform, decisions are generally more radical or innovative (compared to a situation where the crisis does not exist) and the responses come very quickly (Grindle, Thomas, 1991, p. 5). On the other hand, the reform initiative may arise in conditions described by Grindle and Thomas as "*political as usual*", in which there is no perception of crisis. In this case, the issues involving a Government response are usually addressed by policy makers of intermediate level and the change tends to be more progressive (Grindle, Thomas, 1991, p. 6). Furthermore, while the proposed reforms in a context of crisis are evaluated in terms of macro politics impact, in the reforms as "*political as usual*", *clientelistic* relations and bureaucratic concerns are more important (Grindle and Thomas, 1991). Thus, we see that in Brazil, despite the proposal for tax reform have been made in a context of economic crisis, such context was raised by actors involved in the discussions as an obstacle to the its approval, given the incertitude of the financial consequences that would bring. However, despite this claim, we will see in the last part that, in fact, reasons linked to the context of Federal dispute in Brazil were responsible for the failure of the reform.

#### A) *Cognitive and Institutional Changes in tax policy from the Lula Government: from neoliberalism to development*

With the election of President Lula in 2003, the national consensus that elected him and the determination to make a tax reform can be considered as a window of political opportunity (Kingdon, 2003; Favre, 1992) to the approval of the issue. However, despite this openness, tax reform almost did not advance. On the other hand, fiscal policy during the first term of Lula followed the same principles of the paradigm of previously Government: fiscal stabilization and adjustment of public finances. Thus, the variable represented by the presidential change did not influence the discussions on the subject, at least in the beginning of the Government. Regarding the economic context and the commitments to international institutions, Lula continued, therefore, the paradigm of fiscal policy of his predecessor, respecting and guaranteed agreements concluded by President Cardoso. Thus, the beginning of his Government is strongly marked by a process of *path dependence*, with a continuation of the fiscal policy to maintain and extend the process of stabilization and adjustment of public finances. To ensure these achievements, Lula has taken measures to increase tax revenue by increasing or creating some special contributions, for example. These small changes can be seen as incremental changes and changes of instruments according to the logic of "layering" (Thelen and Mahoney, 2010), in order to preserve the degree of stabilization.

The first reform proposed by Lula shows this situation: it did not represent a profound change of tax system rules - in particular those relating to the ICMS - but a very specific measures to achieve the fiscal stability, as well as some claims of interest groups, following a logic of "layering" (Thelen and Mahoney, 2010). Although broader proposals were presented by the rapporteur in the parliament, a more consistent reform hasn't been approved. There was the presence of very divergent interests, especially on the issue of the distribution of tax revenues between the federal entities. However, the government needed to approve quickly some changes in order to maintain the level of federal income. It meant that the specific discussion about the ICMS, object of disputes since the Constitution of 1988, has been postponed. Thus, due to the impossibility of

reaching a consensus among the actors, only the less controversial issues and those necessary for the fiscal stabilization (such as the extending of the CPMF- *Contribuição Provisória sobre as Movimentações Financeiras* and the DRU- *Desvinculação das Receitas da União*) were adopted, at the end of the first term. This process shows us a very strong veto power which made therefore impossible a deeper reform (type «displacement» according to the terminology of Thelen and Mahoney (2010)). The first term of Lula seems to have shown a learning process in Government decision-making. The conflicts generated whenever the question was discussed had as consequence to limit the scope of the tax reform and an analysis of each part separately. Faced with the impossibility to regroup all interests in an "*ambiguous consensus*" (Palier, 2003), the strategy was to remove the most controversial points of the project, for the most urgent issues could be approved. This strategy, to reduce the power of *veto*, allowed the approval of certain amendments, even if specifics.

However, at the beginning of the presidential election in 2006, the difficulties of the macroeconomic model practiced since 1999 to promote growth emerged. Given the economic crisis and the increase in interest rates at the end of the year of 2005, the economic policy of the country arrived at a crossroads: maintain or deepen the measures recommended by the neoliberal vision or follow a paradigm shift. The exhaustion of the neoliberal model has contributed to the emergence of a "*developmentalist*" paradigm" (Barbosa e Souza, 2010). In this context, President Lula asked to his team to create a plan of action to "unlock" the economy and achieve an annual GDP growth of 5% (Loureiro and Santos, 2011).

### **a) The disputes around the tax policy changes**

The paradigm shift of economic policy did not occur without difficulties. Oppositions emerged within the Government around the neoliberal defense. Loureiro and Santos (2011) explain the paradigm shift of economic policy that occurred in the second term, considering that the President no longer needed to prove to investors that he was able to fulfill the promises of the election of 2002. In addition to that, the announcements in the end of 2006 of the reports about the economic situation of the country, indicating low levels of economic growth. The international context of the crisis of 2008 has also strongly influenced the Brazil. This change in the macroeconomic policy of the Government of Lula was possible due to the departure of Palocci, Minister of finance, and his main collaborators, who followed principles oriented with the budget and fiscal balance. After the departure of Palocci, Lula indicates an economic team that are identified more strongly with the growth of the internal market and wished to stimulate consumption and increase investment. According to Mattei and Magalhães (2011), this measure represents a "resumption of the ability of the State to intervene in economic dynamics, especially in terms of investment." In summary, the change of the economic team was a relevant factor in the flexibility of fiscal policy at the beginning of the second term.

If economic and fiscal policies of the Cardoso Government - characterized by primary surpluses obtained mainly with tax increases - were followed until 2006, a new paradigm emerged to guide such policies from this year. Proponents of this new paradigm "incrementalist" follow three lines of action according to Barbosa and Souza: a) the adoption of fiscal and monetary incentives to accelerate growth and increase the potential production of the economy, b) the acceleration of the social development, through transfers of income and an increase in the minimum wage and c) the increase of public investment and the resumption of the role of the State in long-term planning (Barbosa e Souza, 2010). The idea was that only a fast-growing economy could increase demand and productivity and, therefore, investments. According to this opinion, transfers of income could be implemented without causing an imbalance of public finances, since this practice leads to an increase in tax revenue for the Government. In this sense, the logic of development was designed to direct this increased tax burden for income transfers to households, in order to maintain a stable fiscal pressure (Barbosa e Souza, 2010). In this way, social expenditure continued to rise during the second term of Lula (11.9% of GDP in 2002 to 13.45% in 2008) (Mattei and Magalhães, 2011).

### **b) The return of public investment and tax exemptions in the “*Growth acceleration plan*” (PAC)**

One of the main objectives of the new Government, Lula was to resurface the debate around the need for public investment, which had been reduced during the previous period due to the need to achieve primary surpluses. According to a report made by the IPEA (2007), the reduction in public investment, particularly in the infrastructure sector and the absence of a legal framework to encourage private

investment in this sector, could bring negative effects on economic growth. Thus, the new developmental paradigm shall defend an increase in public investment, especially in infrastructure, to accelerate growth and develop economic production. To accompany this new principle, the Government proposed in 2007 the “*growth acceleration plan*” (*Plano de Aceleração do Crescimento* - (PAC)) with measures to ensure a sustainable growth (IPEA 2007). In short, this plan provided an increase in spending on public investment. To deal with these costs, the Government has relied on economic growth and maintenance (or even increase) the tax burden. In addition, investment in infrastructure could not interfere in social expenditure and on the stability of the country. The PAC provided actions both to improve the management of the State and to stimulate public and private investment. The measures cover five sections: 1) investment in infrastructure; (2) long-term budgetary measures; (3) provisions and improvements to the tax system; (4) promotion of credit and financing; (5) improve of investment conditions.

With regard specifically to tax measures, the PAC predicted cuts of taxes to stimulate private investment and increase consumption. In addition, the initially proposals made by PAC were enlarged in 2008, with the launch of the production development policy. The two plans have estimated tax reduction, especially for the construction sector, industries, heavy infrastructures and the high-tech industry (computers, semiconductor production and equipment for digital television). In addition, a change in the income tax was made, which mainly benefited the middle class. The plans also predicted a reduction in social security contributions, but this initiative failed: one of the reasons was the decrease in tax revenues after the extinction of the CPMF (tax on financial transactions), which reduced the maneuver in the budget, as we will see below. Tax exemption measures contained in the PAC represented an amount of R\$ 1.41 billion in 2007. If we include all measures of exemption in the period, the total amounted to R\$ 6.6 billion in 2007 and R\$ 11.5 billion in 2008 (Ministério da Fazenda, 2008).

In general, the main merit of the PAC was to increase public investment (0.4% of GDP in 2003-2005; 0.7% in 2006-2008) and stimulate private investment. However, the plan does not contribute with measures to limit the growth of spending, in order to strike a balance between its financing and the maintenance of fiscal stability. Thus, despite the tax exemptions in specific sectors, the implementation of the PAC was made through a significant increase in tax revenues. This increase occurred in the first half of the year 2007, due to the first steps of implementation of PAC (IPEA 2007). This increase in tax revenues was accomplished by changing the structure of the Brazilian GDP, which was based on exports until 2006 and, from then on, turned to the domestic market. In this way, taxes on consumption and domestic investment increased tax revenues, including those relating to income tax and tax on imports. As a result, revenue growth has created opportunities both to finance the actions provided in the PAC, as for increasing tax exemptions for specific sectors without compromising the fiscal stability already conquered (IPEA 2007).

Another factor had effects on taxation during this period: the extinction of the CPMF (provisional contribution on financial transactions) in 2007. In early 2007, at the launch of the CAP, the federal Government decided to not immediately send the proposal to extend the CPMF to the Congress, considering that the period of its validity would be until the end of that year. He therefore preferred to include this issue in a more general tax reform proposal, which was presented to Congress in mid-2007 (Barbosa e

Souza, 2010). However, this choice was problematic for the federal Government, considering that, on the one hand, the proposal for tax reform, due to its complexity, was not sent to Congress in 2007 and, on the other hand, the dissatisfaction of public opinion about the CPMF has been spreading because of this indecision. So, in terms of results, the federal Government's proposal to extend once again the CPMF has not been approved by Parliament.

Barbosa e Souza (2010) underline that the end of the CPMF caused, in parallel with the decrease of tax revenues of the Union, a decrease about 1.4 percent of GDP, an increase in demand and therefore inflation. Before the end of the CPMF, the Government has responded with an increase in the tax on financial operations (IOF) and Social contribution on net income (CSSL) to retrieve a portion of tax revenues and avoid the increasing demand (Barbosa e Souza, 2010). Then, the increase in international prices of *commodities* resulted in inflationary effects for the country. The Government, once again, fought against the acceleration of inflation through tax measures, such as reducing taxes on the price of wheat and their derivatives in order to reduce the impact of rising international prices and the inflation of food prices. With regard to the increase in international oil prices, the Government still responded with a decrease in the contribution for intervention in the economic domain (CIDE) on fuel and diesel.

The assessment of all these measures of economic and fiscal policy since the Government Lula opted for a paradigm of development was marked by an annual average growth of 3.2% of GDP in 2003-2005 to 5.1% in 2006-2008. However, fiscal and tax initiatives during Lula's second term have resulted in a reduction of the federal Government's primary balance: from 2.5% in 2003-2005 to 2.3% of GDP in 2006-2008. According to Barbosa e Souza (2011), this reduction of only 0.2% of GDP in the primary balance indicates that economic growth induced an increase in tax revenues and financed the expansion of primary expenditure. In addition to the PAC, the Government has taken measures to increase credit for consumer goods, income transfer programs and the minimum wage. These changes, according to Loureiro and Santos (2011), indicate "that fiscal policy is no longer just an instrument to guarantee solvency for creditors (financial credibility) but also acquired the role of policy instrument of economic growth and improving income distribution".

Thus, the orientation of fiscal and tax policy in the country has changed since the second term of Lula: from an instrument to achieving the primary surpluses set out in international agreements it has become a means to growth and to the development of the country. In other words, the change in fiscal and tax policy consisted, basically, in an inversion of the paradigm principles: if until now the idea was to consider fiscal austerity as a prerequisite for growth and development; from this moment the thought was that economic growth would lead to a fiscal balance (Loureiro and Santos, 2011). Therefore, the logic was that economic growth would generate more tax revenues, which in turn would permit the continuation of the surpluses needed to balance public finances. In addition, growth allows having more resources to public investment and social programs. Fiscal and tax policy began to acquire an additional function of an instrument for the economic growth of the country (Loureiro and Santos, 2011). However, it should be noted that changing the paradigm of economic and fiscal policy was not bound to threaten the interests of the economic actors' coalition, whose ideas were expressed by leaders of the Central Bank, international organizations and actors from financial market (Loureiro and Santos, 2011). In other words, the economic and

social development policies have advanced in the measure they do not threaten the credibility required by financial markets. In this sense, Gobetti and Amado (2011) think this paradigm shift came without breaking the foundations of orthodox economic policy, such as the defense of the autonomy and the restrictive policy of the Central Bank and the definition of interest rates based on models that guarantee the neutrality of the money.

This dispute of paradigm is represented, for example, by the statements of Minister Dilma Rousseff, in November 9, 2005, while criticizing the budget adjustment proposed by Finance Minister at the time, Antonio Palocci. The adjustment was provided for an increase in the primary surplus and, according to Dilma Rousseff: "For the public debt does not grow, it is necessary to have a consistent interest rate policy, because otherwise you "dry ice". Do a primary surplus on one side and increase the flow and stock of debt on the other "(O Estado de São Paulo, November 9, 2005, p. B01, in Gobetti, Amado, 2011).

Then, with the 2008 international crisis, the Government had to make further adjustments on economic and fiscal policy. The main effects of the crisis in the country were: a strong and rapid decrease in the supply of domestic credit, a reduction in international prices of commodities and international trade that affected, by consequence, Brazilian exporters (Barbosa e Souza, 2010). The Government responded to the crisis by innovative measures, in comparison with the recent history of Brazil, considering that the Lula administration adopted monetary and fiscal measures "countercyclical", i.e. to recover the level of economic activity as quickly as possible (Barbosa e Souza, 2011). The taxation exemption measures undertaken by the Government since 2007 were maintained, including during the period of crisis.

In addition, the Government has taken emergency tax measures, as temporary exemptions from taxes to increase trade and consumption. For example, at the end of 2008, a reduction in the IPI (tax on industrial products) of automobiles was made to prevent a buildup of inventories in the industry. In 2009, the same measure was taken for the sectors of durable consumer goods, construction materials, equipment, motorcycles, furniture and food. The initial cost of temporary measures represented 0.3% of GDP in 2009 (Barbosa e Souza, 2011). The inclusion of extraordinary transfers to the Member State Governments and municipalities in 2009 was another emergency measure, in order to maintain the levels of 2008 transfers, even with the decrease of Union tax revenues in 2009. In addition, the Union contributes to the investments made in collaboration with regional Governments to reduce spending of the States and municipalities. Finally, another structural tax measure taken during the crisis was the change in income tax rates that began to be 7.5%, 15%, 22% and 27.5%.

To conclude, we can say that the paradigm of fiscal and tax policy has experienced modifications during the second term of President Lula. If during the period 2003-2006, the policies followed the Cardoso Government model (characterized by a neoliberal agenda and conservative and orthodox characteristics), the second period (2007-2010) has been more "*incrementalist*". In other words, this model is marked by a strong State intervention in the economy, a recovery of investment capacity and a targeting private investment to develop the basic infrastructure of the country (Mattei and Magalhães, 2011). However, it must be said that this move doesn't broke completely with the logic of the previous paradigm. The measures of the growth



acceleration plan represent, therefore, changes in the instruments of the paradigm to adjust it to new guidance.

As regards the Government of Dilma Rousseff, she has already stated during the election his disagreement with the decrease of primary surplus made by Lula. According to the President, it is necessary to maintain the public finances in order (Valor Econômico, 10/31/2010). Dilma Rousseff, during her campaign, stressed the need to increase public and private investment. One of the ways to achieve these goals would be through the reduction of taxes on investment (Valor Econômico, 10/31/2010). Rousseff also highlighted the need for a tax reform to unify and reduce the ICMS as well as the contribution to social security. She also stated during her campaign that the tax reform would be a priority to give greater competitiveness to the Brazilian economy, in view of the existing tax chaos in Brazil (Valor Econômico, 10/31/2010). With her election, Rousseff had the task of adjusting public accounts, after the implementation of a more expansionary policy by Lula. Thus, the President held a contingency budget of R\$50 billion in 2011 and R\$55 billion in 2012 and a primary surplus of R \$ 91 billion in 2011. These numbers are partly the consequence of the increased tax revenues (11.69% compared to 2010) (Monteiro, 2011). As regards fiscal measures taken to encourage economic sectors, Rousseff has implemented the "Greater Brazil Plan" (*Plano Brasil Maior*) in April 2012. These are measures to support the industry, technology and international trade. The main objective of the plan is to sustain economic growth in the context of the international crisis. The implementation of the plan was made through tax measures, among others, the exemption of investments and exports. Specifically, the plan made an IPI reduction on capital goods, construction materials, trucks and vehicles, tax credits to exporters, change in the imposition of contribution to social security in several other sectors, as well as the creation of a new tax system for the automotive industry. In April 2012, the Government deepened the plan and increased the number of sectors that benefit. It is still not possible to analyze the impact of these measures on the economy.

### *B) Tax reform during the Crisis context: the veto power of some States*

President Lula decided, at the beginning of 2008, that he would present no more constitutional amendments until the end of his second term in 2010, considering that the failure of the approval of the CPMF showed that the Government did not have a stable majority in Congress to deal with the controversial battles against opposition (Folha de São Paulo, 1/2/2008). The only exception, according to the President, would be a proposal for tax reform promised during the defeat of the Government in the negotiations of the CPMF. However, the President announced publicly that the tax reform would not be a priority for the Executive. He also stated that the approval would depend on the support of Congress and society (Folha de São Paulo, 1/2/2008).

#### **a) The tax reform proposal and the construction of interests' consensus**

Before submitting the tax reform proposal to Parliament, Lula tried to obtain the support of the actors in order to reach an early consensus on the proposal to be presented. He met with Governors and representatives of the enterprises' coalition as a way to discuss the proposals and show that, contrary to what occurred with the CPMF, the interest is not just of Government but of the society as a whole (Folha de São Paulo, January 2, 2008). Thus, he received the support of the coalition of enterprises. The President of the interest group *Ação Empresarial*, the business man Jorge Gerdau, gave its support to the proposal to create a federal and state value-added tax. According to Gerdau, the creation of the State VAT, will require tolerance and vision of the future, should cover the ICMS and ISS and may reduce the fiscal war. He added that "these are extremely complex issues, but the positive moment can facilitate its approval. In addition, the opposition is mainly due to favorable tax reform and the President has great popular approval. It lacks only the political initiative. The time is now "(Folha de São Paulo, January 6, 2008).

In addition to the creation of the IVA, replacing some of the consumption taxes, the first version of the project aimed exemption of contributions on wages, including the reduction of the social security contribution and the extinction of the contribution named "salary-education". This version was discussed with congress men allied to President (Folha de São Paulo, February 22, 2008). Even with the end of this contribution, Mantega assured that the budget for education wouldn't decrease because the loss of revenue would be compensated by an increase in other taxes, such as VAT. The end of salary-education has been a controversial topic, even within the Government. The proposal was opposed by the Minister of education, Fernando Haddad, who was afraid of losing the revenue from social contributions, which corresponded to R\$7 billion in 2007. President Lula also hasn't seen the measure with enthusiasm.

Because the reduction in social security contributions included in the original proposal, the Government suffered heavy pressure from unions, in order to withdraw this measure of the tax reform package. After meetings with representatives of trade unions, President Lula said that Finance Minister Guido Mantega would return to discuss the subject, before submitting such a proposal to the Congress. The exemption was, however, the most important argument for the business sector to support the tax reform. On the other hand, according to the President of the "Força Sindical", Mr. Paulo Pereira da Silva: "We cannot approve a reform that takes away rights of retirees in the future. We must find ways of compensation" (Folha de São Paulo, February 26, 2008). Thus, workers' representatives opposed the reduction in social contribution paid by the companies, considering that the Government has not presented a way to compensate the decrease in revenue for social security. They wanted a guarantee that the loss of revenue would be compensated by other tax revenue. On the other hand, if this measure would reduce business tax burden, the coalition of enterprises feared that other taxes have to be increased to compensate this exemption (Folha de São Paulo, February 22, 2008). Minister Mantega avoided talking with parliamentarians on ways to compensate the reduction in employer contribution. In internal discussions, the Minister, however, showed that had the intention of establishing compensation through the Union budget (Folha de São Paulo, February 22, 2008). At the end, considering these objections, the project presented by the President proposed no change of these contributions.

After all these debates, Lula presents a new reform proposal in February 2008: the PEC 233/2008. The main objectives are: simplify the national tax system, reduce the tax

burden and eliminate barriers that prevent the growth of the Brazilian economy and the competitiveness of enterprises, eliminate the tax war between the States and improve the Government's regional development policy. The Secretary of economic policy of the Ministry of finance, Bernard Apy, responsible for the formulation of the project, said that the project "is not ideal from a technical point of view, but an attempt to solve the distortion and have the least political resistance to the project, in order to not impede the approval" (Folha de São Paulo, March 1, 2008). In other words, the Secretary Apy emphasized that the Government chose not to present a technically perfect project, but one that would result in less resistance. Apy said the Government did not intend to solve all the problems with the tax system, but to promote "the changes needed to solve problems within the taxation of goods and services, of indirect taxes" (Folha de São Paulo, March 1, 2008). According to the report about the tax reform released by the Ministry of Finance: «the tax reform will eliminate the obstacles to a more efficient and less costly production, reduce the tax on producers and consumers, will stimulate the formalization and allow more balanced development of States and cities.» (Ministry of finance, 2008).

The project includes, among other measures, the extinction of five taxes and the creation of a VAT-Federal, the unification of the ICMS legislation, a reduction of exports and investment burden, and the creation of the "National Fund for regional development". Thus, a simplification of certain contributions was proposed on the process of production and marketing of products and services. Such simplification could be achieved through the creation of a tax on transactions of goods and services – the federal value-added tax (IVA-F). In this scheme, the tax on industrialized products would be maintained as an instrument of industrial policy of the Government. In addition, the CSSL (social contribution on net income) would be incorporated into the corporate income tax. The other proposals that were already presented in the previous reform involved the unification of ICMS and the adoption of the principle of destination. Also the unification of the legislation of ICMS and the adoption of uniform tax rates in all States was proposed. In addition, the adoption of the principle of destination was placed on the project as the surest way to eliminate the fiscal war (Ministério da Fazenda, 2008). The Ministry of Finance (2008) admitted that "an immediate change in the system of Interstate transactions is not, however, feasible". According to the ministerial document (2008), the adoption the levy at the destination could not be immediately done because there would be a "strong impact on revenue distribution between the States, and an abrupt transition makes very difficult a creation of a reliable system of compensation". In addition to this fact, "the immediate deactivation of the benefits already granted under the fiscal war is almost impossible to be implemented, depending on the difficulty of extinguishing abruptly the commitments made by several States with companies" (Ministry of finance, 2008). Thus, the Government has proposed a gradual transition of the new ICMS collection system, with a progressive reduction in the rate in transactions between States (6.5% in 2010 to 2% in 2016). The reason for this transitional period corresponds to the fact that if the new rules of ICMS were immediately implemented "the proposal would have to predict how the benefits already granted would be approved in the new tax, which would open a huge dispute between States, leading at the edge, an impasse on reform" (Ministry of finance, 2008).

On the presentation day of the project by the Government, President Lula met with some companies and industries representatives to seek support for the tax reform

proposal. The business sector has approved the Government's proposal and sees with optimism the possibilities of reform policies. One of the leaders of the coalitions of enterprises, Jorge Gerdau Johannpeter, stated that "the project has more consistency than the previous ones; there is a negotiation with the Governors and a business mobilization. The prospect is good "(Folha de São Paulo, February 28, 2008). President Lula da Silva recalled that "if they [enterprises] want a tax reform, they need to make pressure on Congress and the opposition to support the project" (Folha de São Paulo, February 26, 2008). Lula also stated that "we need to work with the diversity of various groups. If you simply think it [do the reform] is the role of the Minister [Guido] Mantega and his team, this project is a stillborn child" (Folha de São Paulo, February 28, 2008). The Government's intention is to make pressure for large companies - major funders of deputy's campaigns - do to pressure on the congressmen to vote for the proposal. The President pointed out that the tax reform is not just a matter of executive power, but of all Federation. As a result, the Member State Governments, Congress and some sectors of society such as businesses and labor unions, would be responsible for its success or failure. According to Lula, greater pressure must be made by the coalition of enterprises against hostile opposition to the proposals of the Government. Therefore, these events show a Government strategy to not take responsibility for the approval or disapproval of the tax reform, but pass it on to the Congress. According to Lula: "if all the congressmen do enforce the speeches they made during the campaign over tax policy, we certainly approve it" (Folha de São Paulo, February 28, 2008). In this spirit, the President showed the expectation that the proposal be approved by the end of 2008, even with the municipal elections.

In this way, the coalition of enterprises supported the project presented by Lula. The President of FIESP (Federation of industries of the State of Sao Paulo), Paulo Skaf, stated that the reform contained very positive points and that "the country cannot afford to miss this chance," but that the debates in Congress would not be easy given the proximity of the municipal elections. On another occasion, the President of FIESP defended a realistic position to approve a reform that takes into account at least the most important points, even if it isn't the ideal: "we're not going to get a complete and wide reform, that meets all the points, because we're going to end up without it" (Folha de São Paulo, March 2, 2008). At a meeting of FIESP attended by about 35 businessmen from all sectors, Skaf said "society wants to reduce the tax burden of the country and therefore a cut on public spending. It is preferable to wait a few more days to accommodate all issues than to adopt in a hurry a project that is not satisfactory" (Folha de São Paulo, November 27, 2008).

However, other representatives of the coalition of enterprises called for a broader reform. The Federation of Commerce of Sao Paulo supported the gathering of consumption taxes and considered this change positive, since there was an increase in the rate of VAT. However, the Federation's representative argued that despite the importance of these measures, they will have no significant impact "on reducing the tax burden. The reform needs to be more comprehensive and contemplate the reduction of State spending" (Folha de São Paulo, February 22, 2008). Moreover, the businessman Antonio Erminio de Moraes has also expressed the view that the simplification with the creation of the VAT is good, adding: "what really matters is how it will decrease the unbearable tax burden. It is not enough to say that this tax comes out of here and move over there. The important thing is to see how is the infamous cost Brazil.. [...] it is not the first time that the Government promises to reduce taxes when, eventually, the load

increases. Anyway, it's good to know that the Executive power is willing to present a reform project "(Folha de Sao Paulo, February 24, 2008).

The concern of the coalition of enterprises focused therefore on the possibility of increasing the tax burden. Considering that the project did not provide the new rates of tax, enterprises feared that the changes could lead to increased tax burden. Another reason that led to this conclusion was the maintenance of "revenue assurance" given by the Government to the States and municipalities (Folha de São Paulo, February 29, 2008). On the issue of tax burden, Mantega said there would be no increase in taxes, but admitted a fiscal revenue growth. According to him, "we're ensuring there will be not an increase in the tax burden by the reform itself because it is neutral. But it is clear that the reform implies a formalization of the economy, which will result in an increase of the revenues" (Folha de São Paulo, February 27, 2008). To ensure that there would be no increase in the tax burden, the Minister Mantega suggested an instrument of limitation of taxes. Shortly afterwards, he admitted that this mechanism was not yet ready, because it was not the intention of the Government to establish limits. "There will be an instrument that will be established by the Constitution, but we still don't have that mechanism. And also we don't want to impose a limitation ", he said. (Folha de São Paulo, February 28, 2008). The Secretary of the Ministry of finance, Bernard Appy, stated that, since the beginning, the proposed amendments would not result in an increased tax burden, because "the current pace of economic growth of the country accommodates the possibility of raising expenses" (Folha de São Paulo, March 1, 2008). However, he admitted that the tax reform would generate an increase in the tax burden for certain sectors of the economy. Appy said in a meeting with members of Congress that the Government had chosen not to disclose the rates of VAT because it would increase the tax burden in certain sectors. As a result, the Government's strategy was to prevent losing sectors to make political pressure in Congress against the approval of the tax reform. According to him, "the federal government won't open because tax rates will certainly have a sectorial redistribution of burden. The sectors that will have increased tax burden will make political pressure ", Folha de Sao Paulo, May 8, 2008).

## **b) Oppositions during the reform discussion**

The Government project was supported by Governors of the Northeast. At a meeting in Aracaju on March 1, 2008, the Governors told the President Lula that would support the proposed reform, since they keep all agreements on tax incentives made previously. According to the Governor of Paraíba - Cassio Cunha Lima- "otherwise, it will be created an impasse, and the reform does not come out". He added: "what we call a war tax is buying employment. We [the North] have the biggest market, we don't have the best infrastructure and to ensure the attraction of investments, we must offer something" (Folha de São Paulo, 1<sup>o</sup> of March 2008). The Governor of Sergipe, Marcelo Deda said, however, that the federal Government should negotiate the transition to the end of the war tax "for the contracts already signed not be affected and to not stop investments in the Northeast."(Folha de São Paulo, March 1, 2008). In short, the Governors said they would exert pressure on the deputies and senators in Congress to the Government's proposal were approved. The Governor Teotonio Vilela Filho, from the State of Alagoas, pointed out that the proposal addressed to Congress was the ideal

reform for anyone, but he added: "but I think that is feasible (...) everyone needs to give in" (Folha de São Paulo, March 1, 2008).

The left parties, social movements, as well as some NGOs and associations have protested against the Government's proposal. In March 2008, a debate on tax reform took place in a seminar sponsored by representatives from some leftist parties: PSB, PDT, PC do B and PRB. The seminar highlighted a discrepancy between the representatives of the left on this issue. In April 2008, a group of non-governmental associations and institutions met with some parliamentarians to demand that the Government disclose the social impacts of the reform, including in education. During the same month, a manifesto was published and signed by 71 representatives of social movements, popular and church-related institutions, in addition to NGOs, associations, environmentalists and students. The manifesto said that "the proposed tax reform brings serious consequences to financing of social policies in Brazil, menacing substantially the unique sources that support Social security policies (welfare, health and Social care), education and work". The institutions seek through the manifest an immediate installation of a representative forum of society, with the aim of promoting a participatory discussion of tax reform.

In addition, the project also received strong opposition from the Southeastern States. At a meeting in Belo Horizonte, on October 30, 2008, the Governors of these States (Aécio Neves from Minas Gerais, José Serra from Sao Paulo, Paulo Hartung from Espírito Santo and Sergio Cabral from Rio de Janeiro), announced that they would ask Congress the interruption of the discussions and vote of projects which could create costs for States, including tax reform. The main reason announced to the opposition of these governors was the context of international economic crisis, according to Aécio Neves, should be accompanied by some concern. Neves said he would ask the leaders in Congress "a very great caution in approving materials that bring new expenses, expenses not provided by the States". Serra, Governor of São Paulo, noted that "it is undeniable that, faced with a crisis situation, it is very important to take care of all bills or constitutional amendment that changes expenditure and revenue". For Serra, "the current situation is not favor to start immediately a tax reform without first assessing the new situation and their impacts on the budget. The financial system is in trouble, it is the main source of taxation by the federal Government, and the ICMS is also very sensitive to all activities of durable consumer goods (...) we need to "let the dust of this juncture let down to make a more accurate assessment of it all" (Folha de São Paulo, October 31, 2008).

In April 2008, a Special Committee on tax reform was created in the congress to discuss and vote the PEC 233/08. The choice of the rapporteur and the Chairman of the Committee resulted in conflicts between the PT and the PMDB. Finally, the PT took the post of President of the Commission, with the appointment of Palocci, and the PMDB supported Sandro Mabel of the Republican party for the post of Rapporteur. The opposition parties were not satisfied with these names. According to DEM leader, Antonio Carlos Magalhães Neto "it would be an important gesture from the Government, assign one of the command positions to opposition and show that the reform is in the whole country, without political bias. But with this approach, we will adopt a more independent position" (Folha de São Paulo, April 18, 2008).

The negotiations surrounding the name of Mabel for the post of Rapporteur of the tax reform began even before the Government's defeat on the CPMF. Mabel wanted to

be the rapporteur for the constitutional amendment to extend the CPMF, but the Government has imposed the name of Palocci. In return, the Government promised to Mabel the post of Rapporteur of the tax reform. The indication of Mabel generated a strong reaction from the PT, which supported the name of Palocci for this position. The choice of Sandro Mabel is emblematic and represents the final entry of the coalition of the enterprises in the political debate on taxation. Mabel, head of a large food company, objected vehemently to the first attempt at a proposed reform by Lula in 2003. In addition, Mabel supported the continuation of the granting of tax incentives on the part of States: "the war is the granting of tax benefits that do not generate investments and jobs. On the contrary, the tax incentives are legitimate because they generate jobs (...) I think it [incentives] has to have time to finish. Because the benefits are not eternal. That's what is proposed this time, a time of transition" (Folha de São Paulo, April 23, 2008).

Mabel stressed that the main challenge of the Special Commission of the tax reform was to solve the disagreements between States: "the great consensus will be with the Governors and with the representatives of the States. No one will enter to lose" (Folha de São Paulo, April 23, 2008). In addition, during the interview, Mabel stressed the importance of Palocci that "was the President and conducted very well, he had a very large entrance with business community and Government (...) (he) was very important, led very well the voting of the proposal and we can approve it in the Commission" (interview, April 17, 2011).

The discussions in the Special Commission were held until the presentation of the report by Mr. Sandro Mabel in October 2008. According to him, "the report is not a letter of intent, but a tax reform (...) Don't let to decree to regulate later" (interview, April 17, 2011). Mabel stressed in the interview that the proposals in the report were discussed with several actors:

We built it with the help of many tax lawyers (...). We talked a lot also with the business community about it, with the various categories, several concerns with the staff of the services sector, with the municipalities that were affected (...) with a view to improving the distribution of the federative pact, opening the possibility for municipalities tax a little more (...) We made more than 180 meetings across the country, with trade associations, workers' Federation, Union Central, we discussed with everyone who we could discuss, Governors, President of the Republic (interview, April 17, 2011).

It is this openness to discussion that brought a legitimization of the report, according to Mabel: "this made us bring a reform very next than what was ideal, we arrived at one time that had no way of putting things. A lot stayed out and I said that after we would fix it" (interview, April 17, 2011). The report of Mabel kept the main provisions of the proposal presented by the Government. According to him, "the principle that we utilize was to increase the base for all taxpayers pay less, tax bases not taxed" (interview, April 17, 2011).

The most important innovation brought by the Commission was the creation of a "taxpayer defense code", predicting their rights and guarantees against the public authorities. In addition, the report kept the creation of federal VAT on goods and services, with more specific rules, particularly in relation to the exemption of investments. With regard to social security contributions, the report proposes to reduce this to 1%, as well as the extinction of education salary contribution. The report also

provides for the unification of ICMS law, with tax collections in the State of destination and the reduction in the tax rate on Interstate operations, with a transition period. Finally, it was also maintained the creation of the compensation fund for regional development.

The Secretaries of finance, Mauro Ricardo Costa, from São Paulo and Joaquim Levy from Rio de Janeiro, stated that the report of Mabel, "reflects a goldsmith's work of the rapporteur who, with great sensitivity, translated a number of demands of States, businessmen and other interested"(Folha de São Paulo, November 27, 2008). In addition, after the submission of the report and just before the vote on the Commission, a manifesto supporting the report of Sandro Mabel was unveiled by the President of the Brazilian Association of electrical and electronics industry (Abinee), Humberto Barbato, representing 18 business sector entities. The manifesto says that the report made "the best that could be presented at this time. The text developed a federative discussion and the simplification of taxes seeking to harmonize the national tax system with international experience, to create a model adapted to our conditions". Even without an agreement of some Governors and members of the opposition, the Government initiated a plan to approve the Mabel's report on the Committee. With this, the Government would be able to announce the conclusion of its responsibility and could say that reform has advanced during 2008. On this issue, Mabel said: "my part was - to make the report and approve it on the Commission - is made" (interview, April 17, 2011). However, even with the approval in November 20, 2008, the report did not make consensus among the 24 members of the Commission and, for this reason, it would not have enough votes for approval in the plenary of the House (where 308 votes in favor are required of all 513 deputies). With São Paulo and Minas Gerais, thirteen States and the Federal District have asked, unsuccessfully, the postponement of the vote of the reform within the Commission. On this issue, the President of the Commission, Palocci, said that "there is no possibility of consensus on tax matters" and a DEM Representative - Paulo Bornhausen - commented that "now they are trying to get rid of the dead" (Folha de São Paulo, November 19, 2008)

The core of disagreements concerns the amendments about the ICMS, since it is the main source of revenue of the States, including the Interstate rate, fixed at 2%. Before the voting day, Mabel tried to make a deal with the Secretaries of Finance of States, in order to facilitate the adoption of the issue within the Commission. He suggested the adoption of a 3% rate for the States of origin. While the consumer States found it excessive, the producer States thought it is insufficient and claimed the rate of 4% (Folha de São Paulo, November 19, 2008). In order to overcome the resistance of Governors and reach a consensus, the report has created a way to reduce mandatory spending on health and education, through the mechanism of "unbinding of the States' revenue" (*DRE – Desvinculação das Receitas dos Estados*), which would allow the States to not spend 12% and 25% of its revenue in health and education respectively, as provided in the Constitution. This measure has also been discussed in the first proposition of Lula, but received strong opposition, particularly on the part of members and representatives relating to the issue of education and social security. This measure was included in the text as compensation to States, particularly the poorest, which, in turn, would be prohibited from offering tax incentives to attract companies in its territory (Folha de São Paulo, November 21, 2008).

However, after the approval of the report in the Commission, the opposition parties and the Governors of some States (São Paulo and Minas Gerais specially)



expressed strong opposition to the vote in plenary in the Chamber of Deputies. Faced with this situation, the President of the Chamber, Arlindo Chinaglia, and the rapporteur Sandro Mabel, reported that the voting on the reform in the House would be completed in 2009. According to Chinaglia, "the allies of the Government have not yet demonstrated enough strength to overcome the obstruction and to vote (Folha de São Paulo, November 28, 2008). Despite pressure from the opposition to postpone the approval of the project, the Government, with the support of the Governors of the North and Northeast, declared their willingness to approve the tax reform still in 2009, at least the points of consensus. In a meeting with eleven Governors in Recife, in December 2, 2008, President Lula da Silva appealed to everyone to try to vote the question on later that month. Lula commented on the position of the Governor of São Paulo, José Serra: "it is normal that Sao Paulo, which has greater participation in Brazilian production, wants different things. What we need is to adopt a tax policy that is not beneficial to one or another State "(Folha de São Paulo, December 3, 2008).

On the other side, the Governors allies of São Paulo and Minas Gerais insisted on blocking the vote on the issue. The Governors Aécio Neves (Minas Gerais) and José Serra (SP) defended the view that the reform of the tax system was not desirable, because of the uncertainties caused by the global economic crisis. Neves and Serra also stated that their States would lose about R\$23 billion per year with the reform. Another important factor: both could be candidates of opposition to Lula for the forthcoming presidential elections and did not want to see a victory for the President on the subject (Folha de São Paulo, November 30, 2008). Mabel pointed out that, in spite of the agreement among most of the States, all veto power has been exercised by the Governor of São Paulo, José Serra:

23 States agreed, SP was against, RJ and Minas "on the fence", they didn't want to leave SP alone 9...) At that time Serra was the center of the issue. Beyond the Serra, Michel Temer not put to vote, you know, the guys when they're from the same State, they understand each other (interview, April 17, 2011).

In a meeting with Congress' members, in December 2, 2008, Serra proposed once again to discuss the proposal, arguing that the supporters of the tax reform did not know its contents. In addition, he complained of the "politicization of the Reform", stating that his political opponents had transformed technical discussions on political "in a war of São Paulo against the rest of the country" (Folha de São Paulo, December 3, 2008). Serra would still have stated that "you can't elect São Paulo as public enemy of Brazil". Whatever it is, he placed himself in favor of tax reform, but "with the global crisis, this is not the right time for its approval" (Folha de São Paulo, December 3, 2008). Serra also stressed that "the proposal does not impose losses only to Sao Paulo, but to all States of the country (...) other Governors, such as Espírito Santo, Paulo Hartung (PMDB), and Mato Grosso do Sul, André Pucinelli (PMDB), have demonstrated opposition against the text" (Folha de São Paulo, December 3, 2008). About possible losses for the States, Serra's main argument, Mabel replied:

There was no loss because there was a robust Fund made by the States themselves. (...) Minister Mantega authorized a text that States wrote. There is a very strong and robust guarantee fund that nobody would lose. The federal Government also wouldn't lose because the increase of revenues by the raise of the economic activity would cover a possible loss that the federal Government would have. It was a win-win agreement but unfortunately we had Dr. Serra disrupting the life in the country (interview, April 17, 2011).

On the strong opposition of São Paulo and Minas Gerais, the members of the PT, Ricardo Berzoini, President of the national party, and Mauricio Rands, party leader in the Chamber, said:

Although the reform is being discussed in detail for years, the opposition parties insist on blocking the agenda. They claim that they still wish to suggest changes. They imagine "a higher tax burden", without ever indicate how it would happen ... (...) And still they do not present a global alternative feasible. They invoke the uncertainties of crisis to propose another postponement. (Folha de São Paulo, November 30, 2008).

The representatives stressed that the PT and the allied parties were ready to vote the text and open negotiations in plenary. Both did not agree with the postponement of a reform which, according to them, would bring benefits for the country and for each sector of the economy. They also criticized the opposition parties saying they need to explain to the Brazilian people who insists on delaying the benefits that may be derived from the new tax model " (Folha de São Paulo, November 30, 2008). On this issue, the rapporteur Sandro Mabel did the following diagnosis:

... the Governor Serra (...), is against the tax reform for the simple reason that it is not being made by his own Government, in the hypothesis that the current Governor will be President of the Republic.(...)What I'd really like is that, like the example of the will of authorities and leaders of various segments and on behalf of all Brazilians tired of paying a lot of taxes, we could leave personal projects and join us on a crusade for the approval of tax reform. (Folha de São Paulo, December 5, 2008).

Mabel, in the interview, noted that the opposition of Serra as the cause of the failure of the reform:

There was a "group who messed up (...) President Lula has very on top of that, we approve in Committee, but we had Serra that was the great perpetrator of this tax reform. Serra, he said that Lula couldn't do tax reform, that was near campaign ... and he was undermining the tax reform with his bench, he visited a lot of people, he told a lot of lies, all political issues. Serra has done a big disservice to the nation (...) " (interview, April 17, 2011).

In addition to the opposition of some Member States, after approval of the project by the Commission, the same movement of companies who had supported the proposal earlier, turned against some points included in the project. In an event coordinated by FIESP, in November 2008, 35 representatives of industry, Commerce and services sectors gathered to criticize the additional measures which, according to them, could lead to an increase in the tax burden in the country. Even with the pressure of the President of the Republic for approval of the project in 2008 in the House, members belonging to the president coalition decided to postpone the vote on the reform for March 2009. The members of opposition parties (PSDB and DEM), in turn, agreed to put an end to the maneuvers of rules that were blocking the vote on reform and other proposals in the House. This refusal was seen as a lack of cohesion among the allied parties in the Presidency. The announcement was made by the president of the Chamber, Arlindo Chinaglia (PT-SP), that hours before was called by President Lula, who asked for the vote of the reform (Folha de São Paulo, December 4, 2008). Chinaglia was working for an agreement that would allow approval of other projects, which was possible in exchange for the postponement of the reform. The project,

however, continued without consensus and without support of the ruling parties and the opposition, including the Ministry of finance.

Faced with this situation, the approval of the second project of tax reform was not possible under the Lula Government because of the veto power of the Southeastern States (São Paulo and Minas Gerais). The central question was again the changes in the ICMS system to improving the efficiency of the system and end the fiscal war between the States. But the effects of the reform, especially for the richest States, meant that the project received much opposition and that it wasn't approved. In addition, there was a more visible participation of actors related to social issues and business questions. This could lead us to the conclusion that other actors have come to participate in the discussion of the issue in recent years.

With Rousseff's election to the Presidency of the Republic, the subject disappeared from the priority on the agenda of political debates. It seems that the new President does not intend to undertake a deep tax reform, as proposed by Cardoso and Lula, as a result of a learning process. The President said in March 2011, in a meeting with his political Council and representatives of various parties, that she would make changes in a "sliced" way. This ad has received much criticism. In a meeting on the occasion of the March of mayors in Brasilia, the President said she would try to change tax system by changing specific points which constitute obstacles to economic growth. "We've tried twice to make a larger reform. We now act, instead of arguing if the reform goes or stays "(o Estadão, May 16, 2012) told the President. By this strategy, Rousseff did not want to follow the path of its predecessors. "We know the resistances that exist in Brazil to do tax reform," added (O Estadão, May 16, 2012). Thus, since the beginning of his term, Rousseff took very specific measures - such as modifying taxation of electric energy, the reduction of social security contributions for some sectors of the industry and the adoption of the resolution that ended the war of the ports.

Thus, given the course of discussions during the attempts of tax reform during the previous Governments, conflicts of interest between the actors involved and the technical and political difficulties to implement the changes, the President Rousseff chose not to take the same path and focused on specific changes. To conclude, we can say that, so far, no concrete prospects for tax reform in Brazil due to the great conflict of interest aroused by this question..

## **Conclusion**

We analyze in this paper the fiscal and tax policy changes and the reform process during the second term of the Lula administration (2007-2010) and during the international crisis. We have seen that in Lula's second term there was a change of cognitive and institutional order in fiscal and tax policy that reflected, in turn, macroeconomic policy changes. The exhaustion of the neoliberal paradigm, characterized by primary surpluses supported mainly by the increase of taxes, contributed to the emergence of a new paradigm "incrementalist" of fiscal policy at the end of the year 2005. According to this paradigm, it would be necessary to adopt fiscal and monetary stimulus measures to accelerate growth and increase the production

potential of the economy-ensuring a reduction of social inequalities and a development of public investment. In terms of taxation, this new paradigm was materialized through measures of reduction and exemption of taxes to stimulate private consumption and investment. Thus, this process means a change in the general principles and orientation of the paradigm of public action (Hassenteufel, 2008): If, since the 90's, the fiscal austerity was at the center of tax policy; from the end of 2005 the Brazilian Government turns to the pursuit of economic growth.

In this context, Lula introduced in 2008 a second attempt at tax reform, marked by the opening of the debate to all interested parties. To facilitate the voting process, Lula tries to receive the support of all coalitions, especially as regards the creation of Value-added tax. In addition, one of the points that received strong objections on the part of the social movements and trade unions was the proposed to decrease the contributions for social security, resulting in the appearance of new social actors in discussions. Thus, unlike the first project of Lula, the second can be regarded as an attempt to do an "audacious reform", under the terms of Grindle (2000). Moreover, given the magnitude of the proposals, the project was centered on the concern to satisfy all interests and in an attempt to form a consensus ambiguous (Palier, 2003).

Despite the will to form a consensus on the part of the Government and the support of the coalition of businesses and the majority of States, the proposal has given rise to disputes, particularly with regard to changes concerning the GST and particularly wealthier States. The State of São Paulo, who had the most to lose with reform, played the role of *veto player* (Tsebelis, 1995) in attempts to project approval. In addition, we can conclude that this role of *veto player* is also connected to the interests of the political career of the Governor of the State of São Paulo at the time, since he was one of the most important opponents of Lula. The difficulty of the Government to approve the reform shows that, at that time, the degree of autonomy of the Union was limited by rich States that, in fact, prevented the implementation of the proposed amendments.

Moreover, the presence of a context of crisis, according to the grid of Grindle and Thomas (1991), is less strong than that present in the Cardoso Government. Concerns regarding the economic stability and public finances have not played such an important role as in the previous period. Considering that *interfederative* relations were at the Centre of discussions, it seems that this attempt at reform is closer to the model of "politics as usual" (Grindle and Thomas, 1991).

Thus, we can conclude that, despite the change of direction of fiscal policy since the second term of Lula, the conflicts around the tax reform are still present. If the Government has made efforts to reach consensus, the richest States, in turn, wanted to keep the *status quo*. The blocking of decisions occurred because of the interests of some actors, what suggests us a limited degree of autonomy from the federal Government on these issues. In conclusion, considering that powerful interests of certain actors have not been satisfied, the tax reform was not adopted in Lula. It is for this reason that Dilma Rousseff, elected President in 2010, chose not to present a tax reform proposal, but only make punctual changes.

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