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Budgeting and Public Expenditure in the State of Rio de Janeiro

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1. Introduction

The Brazilian society should know more about public planning and budgeting. There is a general feeling that politicians are self-interested and are always seeking privileges for themselves. Well, If one uses public resources, for personal gain or not, one must pass through the budgetary process, leaving a budgetary footprint; and if our society intends to avoid misuse of public resources, we should understand how politicians do it.

The Annual Budget Act (“Lei Orçamentária Anual - LOA in Brazil) is the most important annual law enacted at federal, state and local levels. For example, the Joint Commission for Plans, Budgeting and Supervision (CMO, in Portuguese) is the most prominent commission in the federal Legislative branch, as well as their similar at estate and local levels. The discussions regarding the annual budget takes several months in the legislative houses every year; the Congress has more budgetary advisors in any other field. If politicians give so much attention to planning and budgeting, why does our society and media give almost no attention to them?

Albeit the importance of the subject for our society, social scientists also give very little attention to the topic. It is not the case that the scientific community finds public budgeting irrelevant; but it has the idea that the matter is so close to power, money and corruption, that it should be avoided by principle. The consequence is that budgeting suffers from the knowledge specialization problem more than most other issues: if one does not work with public budgeting (hence, for government), one does not properly understand planning and budgeting. The media is not better; the perception is that the topic is so confusing and boring that people are not willing to hear about it more than thirty seconds a day.

Obviously, there is also the other side of the story. Although the Information Access Act¹ enacted in the year 2011 grants public access to virtually any public information, the Brazilian society and media have not demonstrated interest in requesting budgetary nor financial information from government. Furthermore,

¹ Brazil Government. 2011. “LEI Nº 12.527, DE 18 DE NOVEMBRO DE 2011, LEI DE ACESSO À INFORMAÇÃO”.

although federal government and state governments started to provide a lot of data in on their websites and other channels, it should go without saying that more data does not necessarily mean more useful information. More data does not build a more informed society if people do not understand what is being reported. For instance, The Annual Budget Act of the State of Rio de Janeiro for 2014² has nearly one thousand pages and more than fifty reports, but very few have some meaning for the average citizen or the media.

This paper intends to address these problems. Our main objective here is to improve the communication channel between government and the society regarding budgeting. We will show that the Expenditure Group classification is a simple and interesting way of classifying public expenses. We will also apply this tool to the Rio de Janeiro State (RJS) expenses, comparing the emerging picture with public and the media perception of the government.

² Rio de Janeiro Estate Government. 2014. "LEI 6.668 DE 13 DE JANEIRO DE 2014 – LOA 2014".

2. Brazilian Budgetary System

One may have trouble looking for books concerning the Brazilian Public Financial system written in English. Despite the extensive literature on the matter, books are entirely written in Portuguese. Therefore, unfortunately we cannot recommend a book on the Brazilian budgetary system in English. In this section, we are using the concepts found in the book *Accounting Applied to the Public Sector*³.

Maybe the most important concept in the Brazilian budgetary system is the functional classification of expenses. The idea behind it is to specify the area of governmental action where public money is being allocated. There are now twenty-nine functions, going from Education (building a school, or running one) and Public Safety (police wages, fuel for police cars, police department maintenance, etc.) to Sports (Soccer stadiums, completion prizes, etc.) and Leisure or Special Duties (debt payments). These functions classify all governmental actions, in all three levels — federal, state and local. There are also sub functions, a lower level of the same classification, containing many more items. Each function has two digits; each sub-function has three.

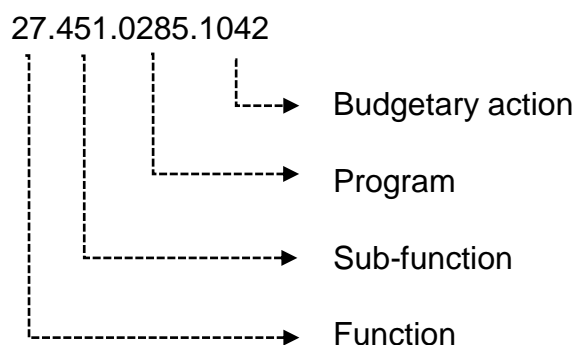
Another way one can categorize public expenses is the programmatic classification. A budgetary program is a method of organizing the governmental action, structured in a set of budgetary actions aiming to achieve one common objective. Each program is linked to one function and one sub function, depending on the area affected by governmental action. For example, the name of the program comprising the organization of the World Cup in the State of Rio de Janeiro is “0285 – World Cup 2014 and Olympic Games 2016,” and it is linked to the function Sports and Leisure. As one can see, each program has a four-digit code.

Linked to a program, we have budgetary actions: they are instruments of a program aiming to expand, improve or maintain the governmental action. There are three kinds of actions — programs, activities and especial operations. Back to the World Cup example, the program quoted above has eight budgetary actions,

³ Mota, Francisco Glauber Lima. 2009. *Contabilidade Aplicada ao Setor Público*.

like “1042– Reform of Maracanã’s Complex” and “1064- Transportation Improvements for the World Cup 2014 and Olympic Games 2016.” Budgetary actions are also four-digit coded and linked to sub-functions. For example, the action 1042 is linked to the sub-function “451- Urban infrastructure”.

Below we have one example of the classification by function and classification as stated in the Budget Acts and reports:



A third way of classifying public expenses is the economical classification. This category emphasizes what the government buys. This is a much more detailed classification, going from the economic category (one digit coded, being current or capital expenses) to sub-element (examples are wages, flags, chemicals, cleaning and insurances). Overall, economic classification codes have eight digits. Nevertheless its great importance, we are not using the economical classification in this paper.

The last classification used on budgeting is the institutional classification. It reflects the organizational and administrative structure of the government. In other words, it consists of an administrative unit to which a certain budgetary endowment is destined at the Annual Budget Act. Contrary to other classifications, each governmental level can organize its own institutional classification. The Brazilian Federal Government uses a five-digit code in each agency, whereas the Rio de Janeiro State Government uses a four-digit code. In budgetary affairs, it is usual to refer to an agency as Budgetary Unit (BU). To follow the terminology used at the budgeting agencies in Brazil, in this paper we are using the concepts “agency” and “Budgetary Unit” as synonyms. We will return to this point later in section 2.1.

We have one last important item to consider in this topic. This paper is about public expenses and transparency. Thus, the way one measures expenses is very

important. Although it might sound straightforward, defining public expense is a complex task.

Legally speaking⁴, the public expense workflow has four stages – fixation, engagement, settlement and payment⁵. Any of these stages could be considered as public expenses, but changing from one to another would change the result of any analysis radically. Then, which one should we take for expenses?

First, fixation is the total endowment one agency (more precisely, BU) is authorized to spend in one year by the Annual Budget Act. Nonetheless, one agency may have a big annual endowment and chose to spend just a small fraction of it during the year. Therefore, fixation is not a good choice if we are willing to account for public spending in the context covered by this paper.

Secondly, we have engagement. Engagements happen when the state makes a commitment to acquire a good or contract a service from a company or someone. It is closer to sense of expense that we are looking for, but it cannot yet be taken for expenses. For example, if a company does not deliver the requested good or the state withdraw from the purchase, there was no expense.

The term payment is self-explanatory and it is even closer to the concept we are looking for, but it still misses something. If the state buys a good or service but for any reason does not pay for it, there was expense but there was no payment. It has the opposite problem to fixation and engagement.

Finally, we have settlement. A settlement happens when a company or person delivers something to government and the government declares that the good or service is in good condition; the agreement is sealed. Onward, the government cannot give up the acquisition and now on the government is obliged to make the payment.

Given our choices, in this paper we are going to use the settlement stage as governmental expense; it is also the concept used by governments in Brazil in most budgetary reports.

⁴ Brazil Government. 1964. LEI N° 4.320, DE 17 DE MARÇO DE 1964.

⁵ Referred to as “fixação, empenho, liquidação e pagamento” in Brazil.

2.1. Specificities of the Rio de Janeiro State budgetary system

As mentioned above, a budgetary unit (BU) is an administrative unit to which some endowment is destined. Technically, BU is not exactly an agency. It could be a Ministry or Secretariat, but be also a subdivision of one agency, like a small office of a ministry far away in the countryside. Besides this extensive definition, in the state of Rio the Janeiro administration, the concept BU is used as a synonym of Secretariat, Autarky or other state agencies, with few exceptions. Public Funds are one them: they are created just to earmark some revenues, ensuring those resources are going to be allocated in a specific destination.

The RJS also has created a BU to manage its obligations with other federation units, as well as the state debt service. Therefore, albeit BU is not exactly the same as an agency, in this work we are using both as synonyms.

Although the Federal Government has enacted the major part of budgetary laws, states and local governments may pass laws on certain budgetary affairs – as far as they do not conflict with federal laws. The state of Rio de Janeiro has enacted some interesting budgetary laws, providing more transparency and control over public expenses, both for people and policy makers. The creation of a new classification is one of these state innovations – the expenditure group (or EG). In this classification, each budgetary action is related to an expenditure group, depending on the nature of the governmental action involved.

In exhibit 1, we can see the five EG created by the RJS government to classify its expenses using expenditure groups.

Exhibit 1. Expenditure Groups Definitions

Expenditure Group Abbreviation	Definition
L1	Expenses with staff of all kind and all social charges to It related.
L2	Expenses with administrative maintenance, except those included in L4.
L3	Expenses with Public Debt Service and other State obligations, transfers to other federative entities, excluding L1.
L4	Expenses with finalistic activities
L5	Expenses with projects

Expenditure group is a central topic in this paper. In the next sections, we are going to show some interesting analyses that only can be possible making use of this classification. Onward, we will often refer to expenditure group for its initials, EG.

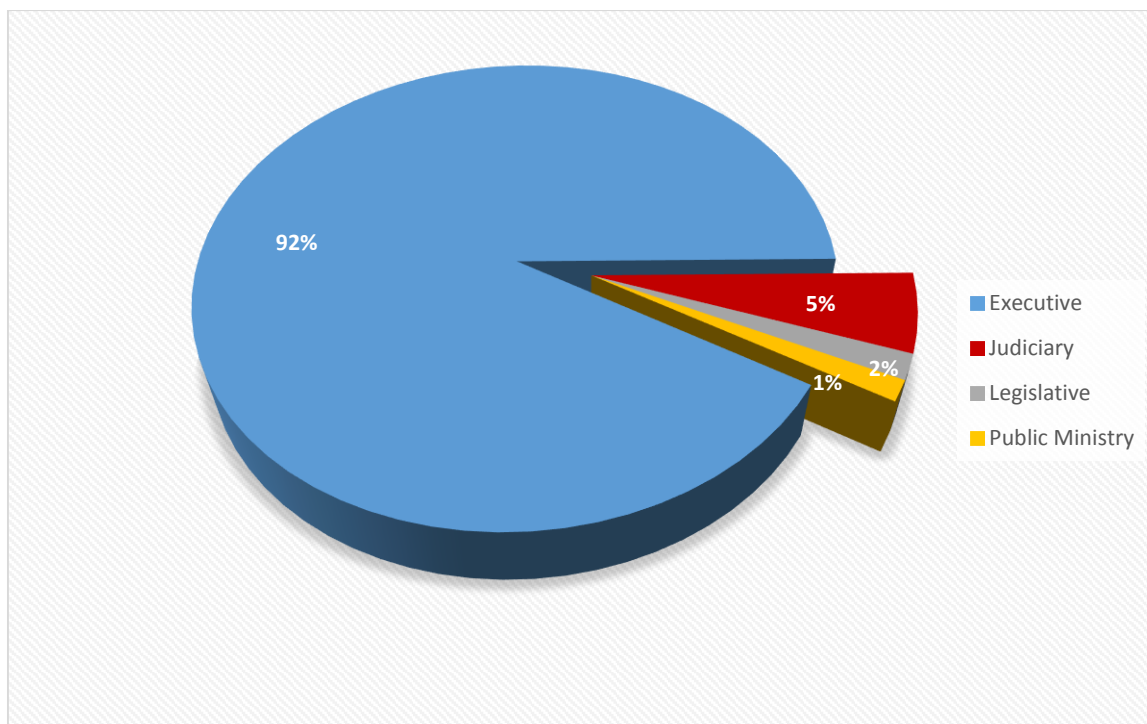
3. Analyzing public expenses in the State of Rio de Janeiro

In this section, we are analyzing the Rio de Janeiro State expenses in several different ways. Before we start our analysis, we must make some comments about the RJS budgeting.

In sections 3.1 and 3.2 we analyze the administrative organization of the RJS government by comparing the amount spent by each agency to total government expenses. In these two sections, we consider the amounts spent just by the Executive branch.

It is important to mention that in Brazil, the federal government and state governments have an agency considered as a fourth branch, the Public Ministry. This agency has the entitlement of physicalizing the most varied affairs of public life, including environmental issues, crimes against civilian life or Public Administration; it also has all prerogatives of the other branches, including when it comes to finance and budgeting.

Exhibit 2. Estate Expense by Branch - 2012



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements in the year 2012. BRL in current values.

Exhibit 2 shows the relative size of each branch expenses. It is clear that the Executive branch is much bigger than any other branch, accounting for 92% of the total state expenses in the year 2012⁶ (the same trend is observed in any other year.)⁷ Therefore, if we analyze the Executive branch expenses, we are taking into account a good share of total state expenses.

Another reason not to consider the expenses of the other branches is that the Chief Executive has no say about affairs of the other branches, even when it comes to budgeting. If presidents cannot control the Judiciary, they must not be called to answer questions about the Judiciary's budgeting.

There is still one last reason: the other branches have a very narrow range of actions when compared to the Executive. For example, the Legislative branch passes laws and supervises the Executive. Thus, it is hard to ask the Legislative to diminish his activities (although people often asks the Legislative to reduce its own benefits). At the other hand, the Executive is ahead of every state activity, besides law and court. Therefore, it is much easier to ask the Executive branch to diminish his activities, by closing some agencies or public companies.

We are restraining another category of expenses in our following analysis. Below, Exhibit 3 compares the amount of resources applied on each expenditure group. It is clear at the chart that the biggest EGs are L1 and L3.

Although L3 amounts for 36% of total expenses in the year 2012 or R\$ 20.8 billion, we are ruling these values out in the next two sections. The reason is that when asked "why are public expenses so high?" politicians tend to respond that former politicians spent much more money than they collected, and public debt is so high that now the government has to spend too much money paying the debt service. We have to admit that this is partially true. However, if one does not want to listen to such answer, one has to make questions that cannot be answered that

⁶ Some data from the year 2013 were not available when this paper was being written. In these cases, we are using budgetary data from the year 2102.

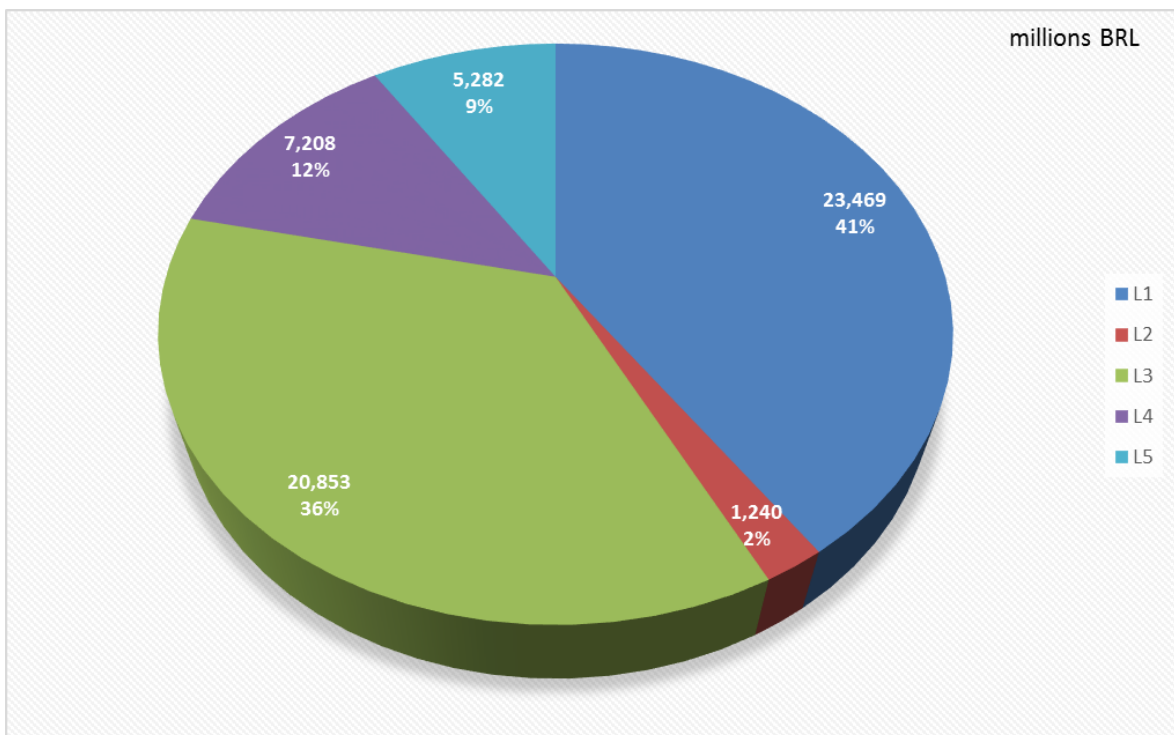
⁷ This is one of the features of the so-called dominance of the Executive over the other branches: if the Executive detains such a big share of the budget, it may detain more power. In recent years, the Congress has been fighting to gain more control over budgetary issues, especially to detain control over some share of public expenses through parliamentary amendments

way. One way to ask such question is “Why public expenses, besides debt service, are so high?”

There also other technical reasons. Notice that EG L1 is also very big when compare to the other groups, and if we compare all other expenditure groups to L1 and L3, they look too small. This would imply that the expenses of any given agency would look too small when compared to the total budget. Nevertheless, agencies in the RJS have very different sizes when compared to one another.

Finally, almost all L3 expenses are concentrated into one single agency named State General Duties carried out by Secretariat of Finance (EGE/SEFAZ in Portuguese initials). Since we are trying to analyze the role of each agency and its expenses inside total RJS budget, not accounting for Debt Service and other obligations, we decided to exclude L3 expenses in the next two sections.

Exhibit 3. Estate Budget by Expenditure Group⁸, year 2012



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements in the year 2012. BRL in current values.

⁸ Notice we have chosen to use the initials BRL for the Brazilian currency Real in tables and charts.

3.1. Expenditure over the administrative structure

There is perception in media and society that the size of Brazilian public administration is too big in comparison to the quantity and quality of public services provided by government. In other words, some citizens think that those in power tend to create new agencies aiming political support and jobs for their acquaintances– not better public services. People see it as one of the reasons behind the growing size of the government, particularly administrative expenses. This section proposes one method to analyze the relative size of public agencies, using the data from the State of Rio de Janeiro as example.

Exhibit 4 divides all state agencies into 5 categories, depending on the expenses of each BU.

Exhibit 4. Relative Budgetary size of BUs

BU Share of Total Expenses	Number of BUs	Total class Expenses (million BRL)	Cumulative share
>15%	1	10,321	28%
15% + 5%	4	12,914	62%
5% + 0.5%	22	11,406	93%
0,5% + 0.1%	18	1,661	98%
< 0.1%	54	898	100%
Total	99	37,199	100%

Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Notes: Expense considered here are settlements in the year 2012. Includes only the Executive Branch, excludes L3 expenditures and offices with no settlements in 2012. BRL in current values.

As one can see, there is one very large agency, accounting for more than 15% of all non-debt expenses. This agency is Rioprevidência, the RJS pension fund. There are also four agencies accounting each one for more than 5% of the State budget: the Secretariat of Public Works (SEOBRAS, in Portuguese initials), the Military State Police (PMERJ), the Secretariat for Education (SEEDUC) and the State Health Fund (FES).

At the bottom of the table, we have the opposite situation. There are 54 small agencies, each one accounting for less than 0.1% of the State budget. This is one interesting point. If one compares the top and the bottom of the table, the numbers are impressive. The five biggest BUs account for 62% of the state expenses, and fifty-four small agencies account for no more than 2% altogether, or R\$ 898 million. One way of reading this is: if the state government close these fifty-four small agencies, it would have to relocate just 2% of the state budget. It would be possible thereby to diminish the number of state secretaries or other chairmen by fifty-four, and a proportional number of special advisors, as well as the expenses on maintenance, and so forth. Another option could be to merge some agencies, creating more integrated agencies containing small offices. This would reduce in some extent administrative and personnel expenses, thus rising efficiency.

There is actually a common trend on the Brazilian public administration, in all government levels. When the chief of the Executive branch comes to office usually an organizational reform takes place, with the reduction in the number of existing agencies. The opposite trend is usually observed when the election period approaches. Seeking for alliances and political support, the chief Executive offers new agencies to minor parties or important politicians, which increases once again the number of agencies.

The existence of small public agencies is not a problem by itself. *Ceteris paribus*, it is of course a good sign, not a bad one. It may be the case that everyone working at one small agency are such good and efficient public servants that they can accomplish their job with few public resources.

There may be also other good reasons for the existence of small agencies. At the Rio de Janeiro State there are former public enterprises that are kept operating just for legal reasons – as labor charges or court orders. In other cases, some former agencies no longer exist, but they still have some public employees working at other existing agencies.

However, the problem is that a big share of these small agencies resources may go just to staff wages and administrative expenses, to say, L1 and L2 budgetary actions. Every agency, small or big, needs a state secretary, president

or chief. It also needs one special advisor, law advisor, finance advisor, budgeting and planning advisors, staff supervisors, and so forth. In an extreme example, it may be the case that one agency spends all its money only paying wages and administrative maintenance, providing no service to the society.

It is hard to tell what is the case of each specific agency. Our society and those in power must be properly informed to decide if one office has the ideal size to provide the intended public services –or otherwise. Sometimes, one small agency provides services to a small group of people in an efficient and proper way; in others, there is no reason to keep one office working, either because it is small or inefficient.

3.2. Ratio between maintenance and public service

We have seen that in the Rio de Janeiro State, the size of the existing agencies may vary a lot, and that it is one feature that one must take into account. Another interesting calculation we propose in this paper is the ratio between the expenses with public services and administrative expenses.

The problem is: how can one measure that? State budgets may have thousands of budgetary actions and one has to check, one by one, if each action is a public service or an administrative activity (or even a public debt action). Impressively, this is exactly what one has to do to analyze the Brazilian federal budget. The Brazilian Budgeting System does not mandate governments to use the expenditure group classification. Most states and cities do not organize their budgets this way, neither the federal government. It implies that it may be very difficult to use budgetary and financial information provided by government: you may end up with a spreadsheet with tens of thousands of lines that has no meaning.

However, if the state in case has the public expense classification, one we can simply compute the ratio $(L4+L5) / (L1+L2)$ in each agency. This result is shown below for the Rio de Janeiro State budget in the year 2012.

The idea behind exhibit 5 is that agencies should spend more money providing services to the society (this is L4 and L5 actions) than on administrative expenses (L1 and L2). In other words, government should be organized into an efficient way. Notice that the chart does not take into account Debt Service and other state obligations (L3). For instance, the average ratio for all RJS expenses is 0.51. This means that for every Real spent on administrative expenses (L1 and L2), the State spends just 0.51 cents on services and goods for the society (L4 and L5). Of course, there is no one right ratio, but the society should look at the government overall expenses, also at each agency and decide what is the minimum level of efficiency acceptable or desired.

Exhibit 5. Ratio between finalistic and administrative expenses by BUs

BU's Ratio (L4 + L5) / (L1 + L2)	BUs inside the class	Total class Expenses (million BRL)	Share of total Expenses
Finalistic only	10	1,071	2.9%
>1	22	10,945	29.4%
1 + 0.5	15	1,914	5.1%
0,5 + 0.1	23	8,862	23.8%
< 0,1	29	14,406	38.7%
Total	99	37,199	100%

Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Notes: Expense considered here are settlements in the year 2012. Includes only the Executive Branch, excludes L3 expenditures and agencies with no settlements in 2012. BRL in current values.

Let us start by looking at first column. There are ten Budgetary Units (BUs) with no maintenance or staff expenses, that is to say, both L1 and L2 equals zero. However, is it possible for an office to expend no money on its staff or maintenance? The answer is that those BUs are funds, not regular agencies. A fund is just a way to earmark public resources to a certain destination. Some examples here are 2261- FREMF, a fund for the economic recovery of RJS municipalities, 2404- FECAM, for environmental protection, and 3261- FEA, the state fund for social assistance. By law, the state government cannot spend fund money on personnel and maintenance, so all expenses are allocated in L4 and L5 budgetary actions. We may notice that just a little over one billion BRL are or 2.9% of the all expenses is in this category.

It is relevant to say that public managers and specialists do not approve funds, for two major reasons. First, they can stifle states budgeting, once it obligate the state to apply all the resources in the manner the law that enacted the fund mandates; secondly, social needs changes over time, sometimes in a sudden way (as in a natural catastrophe or an economic crisis). Even in these circumstances, the policy makers are obliged to apply the resources in predetermined areas.

Back to exhibit 5, our previous analysis can also be applied at the remaining categories. The second line “(>1)”, for example, contains twenty-two agencies that apply more than half of its resources on actions that provide services and goods to the society. A more technical way to put it is simply $(L4 + L5) > (L1 + L2)$. The good news here is that almost one third of the state expenses are in this category, almost R\$ 11 billion or more than 29% of the State Budget.

On the other hand, the bad news are those BUs at the bottom of the table. The state government has 29 agencies in the last category, and more than R\$ 14 billion or 38.7% of the RJS resources are in this group. Within this group, the State spends more than R\$10 with administrative expenses for each Real applied providing social services. Moreover, it is worth reminding that L3 expenses are not included in exhibit 5.

This picture may look to grim, but as in section 3.1, there are some reasonable explanations for these numbers. For example, Rioprevidência and EGE/SEFAZ are two BUs included in the last category. However, Rioprevidência is the office in charge of paying for the state pensions and other obligations to retired employees and pensioners. EGE/SEFAZ is mainly in charge of the Public Debt management, but in some cases it is the agency responsible for paying other State obligations, besides debt, like L1 expenses. In both cases, it is very reasonable to have agencies in charge such activities.

There is also one other explanation. There are two secretariats of major relevance included in the penultimate group of the tablet: SEEDUC, the State Secretariat for Education, and PMERJ, the State Military Police agency. In both cases, administrative expenses are so high because, in order to provide public services, these agencies have to hire public servants. In these cases, hiring people (teachers and police officers) is the way the State provide services to the society. Once these two secretariats are comparatively large, this effect may even distort the overall picture of public expenses in some cases.

To correct the problem above, the State Planning and Budgeting Secretariat, SEPLAG, is planning to create another expenditure group. The idea is to have two different groups for staff expenses: one for public servants directly responsible for providing public services, like police officers and teachers; and in

another group those in charge of administrative affairs. This would help the state managers (and by extension, the society) to differentiate even more administrative and finalistic expenses.

The aim of the last two sections is to demonstrate that the Expenditure Group classification is one significant analysis tool. With it, it becomes much easier to organize all the budgetary data in order to provide policy makers and the society a precise and useful idea of the public expenses and the state action in the society.

Even when there are some distortions in the expenditure group classification, as illustrated above, it is possible to organize existing categories in a different way to avoid those problems. It may also be the case that social demands for transparency change in a way that former expenditure groups are no more interesting, and some new categories have to be created, others extinguished. In any case, it is important to reshape the categories in a way that relevant information can be provided.

Together, sections 3.1 and 3.2 suggest an interesting line of analysis. Suppose that the Chief Executive is running for reelections and hence looking for political support. One possible line of action is to propose alliances to small parties⁹ or local political leaders and offer each them the head one agency. This can create a coalition with more funds and political space.

However, if the Chief Executive is looking just for political support, he or she does not want these parties to be in charge of public policies (surely not the important ones). One way to build such alliances is to create new agencies that have no say in governmental affairs; they have to be small agencies, with small budgets and that do not provide any public service nor administrate public policies. In budgetary terms, they have to be very small sized BUs (section 3.1) with all expenses allocated in heavily in expenditure groups L1 and L2 (section 3.2). If both come to happen together, this may be a sign of misuse of public resources.

⁹ Brazil has a multi-party political system, with 32 registered parties for the year 2014 elections.

3.3. The trend of the Public Expenditure

In this section we change our line of analyses to discuss some economic theories. Economists have suggested that once government starts providing a public service, the political cost of withdrawing it is too large. So, public expenditures with social policies tend to grow constantly over time. Does this apply to Rio de Janeiro State? Can we use the expenditure group classification to investigate that?

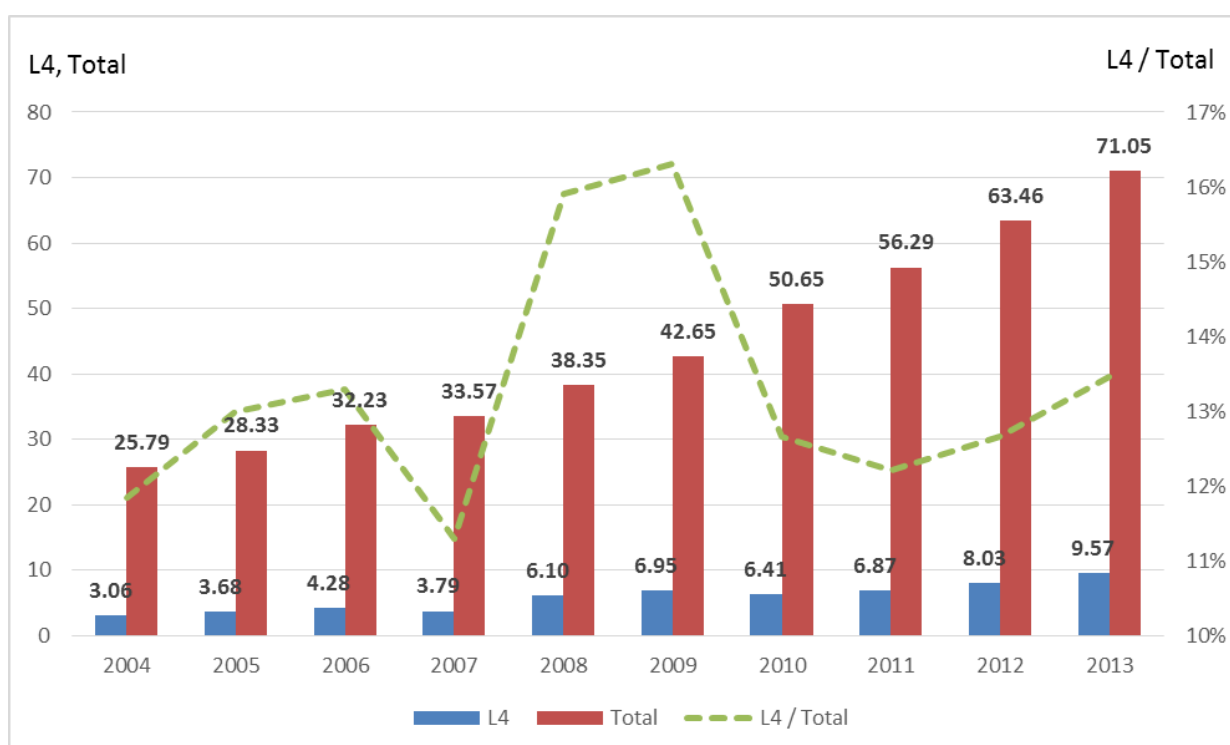
Again, we will start by trying to make this analysis without using the expenditure group classification. How can we measure expenditure on public services? The Brazilian budgeting system establishes that budgetary actions must be numbered as follows: projects starts with odd numbers; activities with even numbers and especial operations starts with the digit zero. So, one could think that this consists only of summing up the expenses with those actions starting with even numbers.

However, there are some activities starting with even numbers that do not consist of services provided to the society, for example staff wages and administrative expenses. Once again, to rule out does activities entails to look at them one by one, maybe tens of thousands of items, deciding in each case if it is a finalistic activity or a maintenance one. For the year 2014, The RJS has more than 1.100 different budgetary actions. This is one of the reasons budgeting and planning specialists established the expenditure group classification at the first place: it is often too hard to analyze some aspects of governmental action.

Once more, an easy way to compute these expenses is to use the expenditure group classification. At the RJS, all activities concerning services provided to the society are computed under L4. Table 6 displays the trend of RJS expenses on under L4 since year 2004¹⁰. As one can see, both total and L4 expenses have increased considerably in the period.

¹⁰ Although budgetary data prior to 2004 is also available, that period had a different set of expenditure groups, making the two different periods incongruous.

Exhibit 6. Expenses in L4 over time (billion BRL)



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements. All expenses groups are included. BRL in current values.

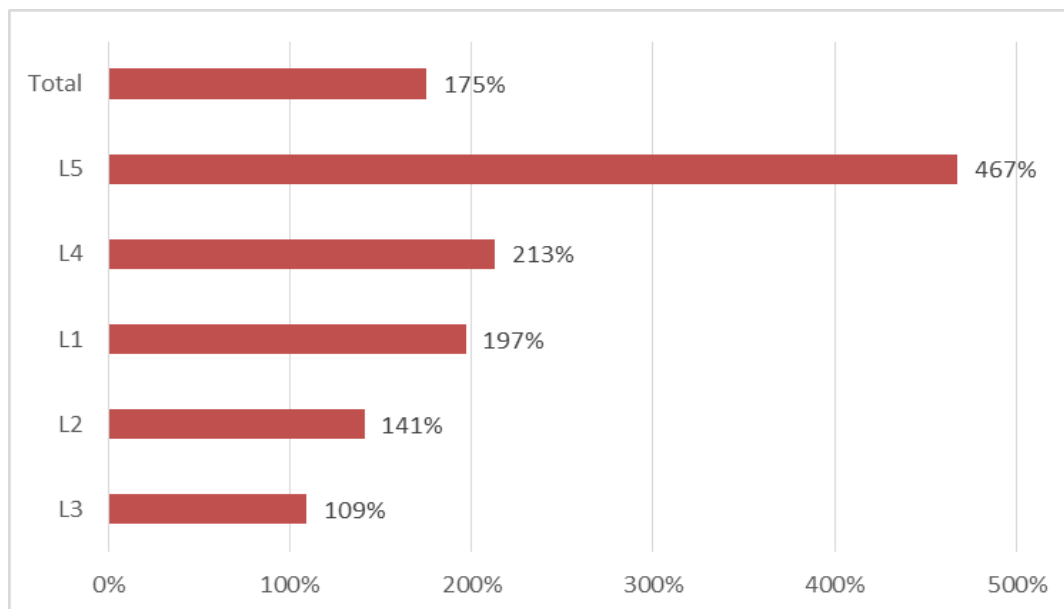
We can see in the graph that the general perception among economists concerning expenses with public services does hold in the RJS case, at least for the past ten years. In the period L4 expenses grew 213%, or 12.1% per year, while total expenses grew 175%, 10.5% per year. As we can see in the graph, despite the different growth rates, L4 share within the State budget did not change much – it went from 11.8% to 13.5%, an R\$ 6.5 billion rise in ten years.

Remarkably, notice that contrary to what is expected in an election year, when the State Governor Sérgio Cabral was running for reelection in 2012, L4 expenses decreased, even in current values; the ratio between L4 and general expenses experienced a sharp decrease. In the graphs below we will verify how each EG behaved in the period.

In exhibit 7 we can see the growth rate in the RJS Budget over the last ten, as well as in each expenditure group. As noted above, the RJS Budget grew 12.1%

per year in last ten years, or almost tripled in size, which is an astonishing growth even if we discount for inflation in the period– 61%¹¹.

Exhibit 7. EG growth rates over past ten years



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements. All expenses groups are included. BRL in current values.

Once more, exhibit 7 shows that EG is an interesting way of classifying public expenses. Although the overall budget has grown 175%, different kinds of expenses grew in very different ways. Notice that L5, the EG for new projects, grew 467%, while L3 expenses, debt service and other expenses, grew just 109%. As we will see above, the RJS is now spending a smaller rate of the budget on the debt service other state obligations.

It is important to notice that each expenditure groups differs considerably in size. As we have discussed before, L5 had an intense growth in the period; in year 2004 expenses with new projects were nearly twice the size of maintenance expenses, but now L4 is more than fourfold bigger.

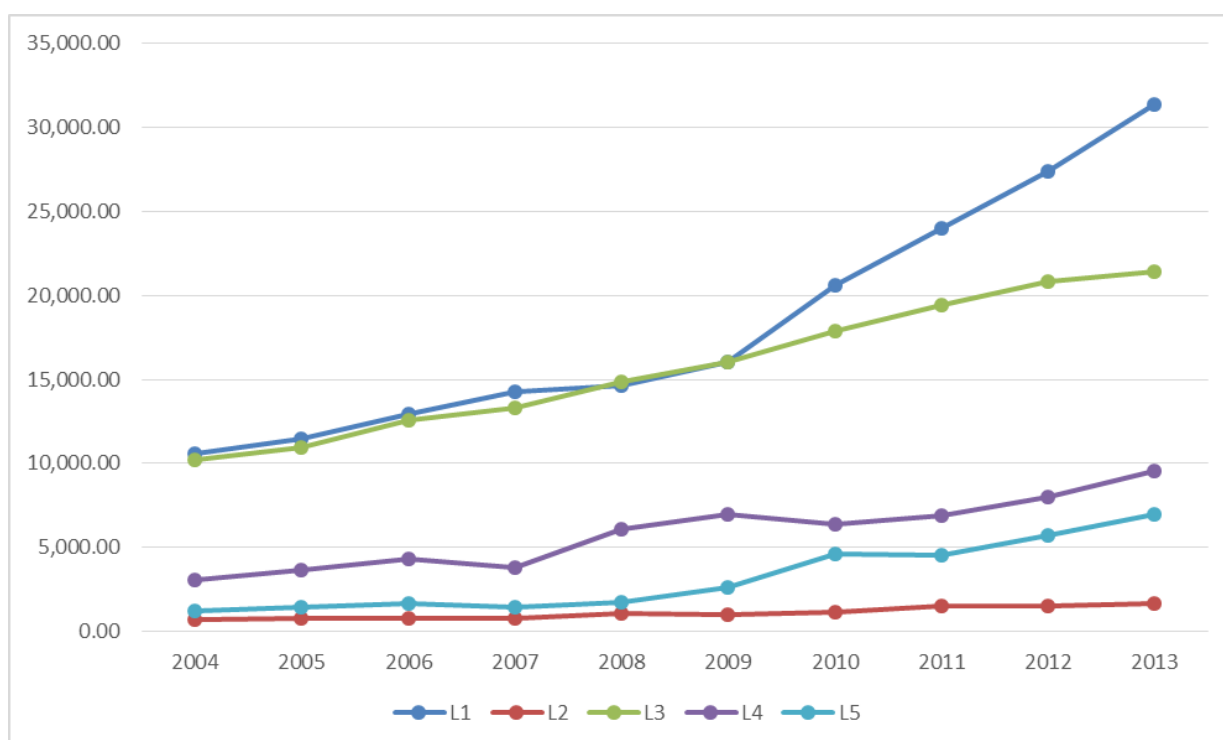
This impressive growth on L5 expenses have two main explanations: the Growth Acceleration Program (PAC, as referred in Brazil), a set of agreements between federal, state and local governments, and the World Cup 2014 and the

¹¹ IBGE. “Índices de Preços ao Consumidor - IPCA e INPC”. The comparison was made using June 2004 and June 2013.

Olympic Games 2016, both taking place in the Rio de Janeiro State. The PAC included a number of transfers from federal government to the state governments to be applied in infrastructure programs, like ports, airports, highways, and those related to the great sporting events.

Below, exhibit 8 provides information about the relative size and trend of the state expenses by EG.

Exhibit 8. EG growth over past ten years (million BRL)



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements. All expenses groups are included. BRL in current values

Firstly, we can see that L1 expenses had a sharp increase since 2009. This is associated with the Pacification Police Units¹², a RJS program aiming to increase the presence of the state and to impose the rule of law at some communities facing problems related to drugs and violence. Secondly, we can see in year 2004 that expenses in L2 and L5 were much closer to each other than in 2013, since L5 had a much stronger growth.

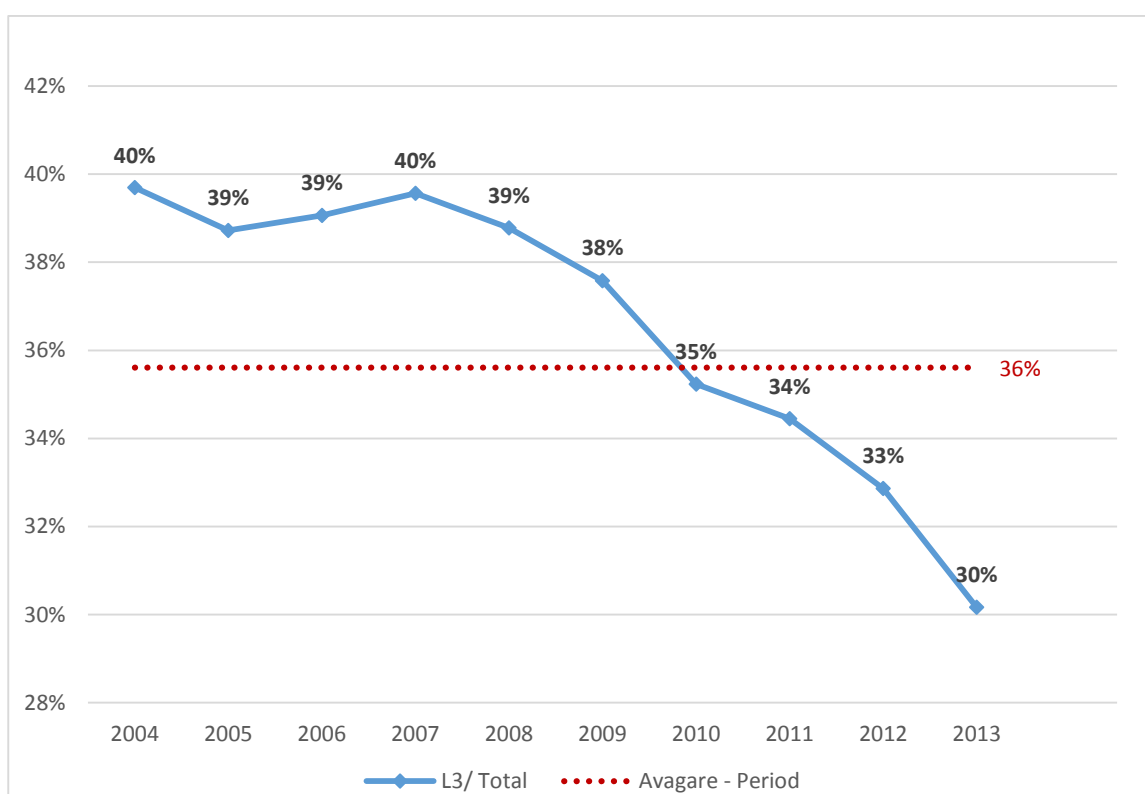
Although the ranking of each EG had not changed over the period, the relative size of them are now very different than it was before; L1 and L3 are still

¹² Referred to as “UPP- Unidade de Política Pacificadora” in Brazil.

the largest EGs, but now they account for a smaller share of the state budget. Also, the difference between then in the year 2004 were just R\$ 336 million, and now it is almost R\$ 10 billion.

Public revenues and debt management are not in discussion in this work. However, it is possible to look at the topic indirectly, using once more the expenditure group classification. In exhibit 9, we can verify how much the share of L3 decreased in comparison to the overall budget.

Exhibit 9. Expenses in L3 over total budget over time



Source: SIG/ SIAFEM-RJ, Rio de Janeiro State Government.

Note: Expense considered here are settlements.

Nevertheless the government now spends more money in public debt than it did before, and the relative size of the debt service in the state budget is lesser, going from 40% in the year 2004 to 30% in 2013.

It is also important to notice that law 4,320/64 dictates that the Annual Budget Act must be always balanced. In other words, expenses must be equal to revenues. This is the budgetary Principle of Balance. Therefore, if overall expenses grew 175% in ten years, revenues did as well. This gives the state

government three options: increasing public revenues in the same pace; increase public debt –or both. Anyhow, taxpayers will end up paying more taxes. Economist refers to this as the No Free Lunch Theorem.

4. Conclusion

Back to what we said at the beginning of this word, our society should know more about public budgeting. It is the most effective way by which we can supervise and control politicians and the action of the State. How is it possible that we accuse our politicians of misusing public money if we do not know how they are using it?

Economists are now starting to study and understand how people rationally chose to be uninformed about some aspects of the social life. Maybe the Brazilian society is rationally uninformed. People may think that politicians are always going to take advantage of public resources anyway (rent and privilege seeking), and leaning about planning and budgeting is so hard and costly that people are better off without knowing it. This is a problem created partially by laws and the public administration itself. We should put some effort into making Public Budgeting easier for citizens and media.

Using simple budgetary information, we have seeing that it is possible to know where the money from the taxpayers is being allocated. It is also possible to learn if those in power are using the administrative machinery to distribute jobs to political allies or to win elections. People are used to think that government is using too much money to run public policies, even though they do not know how much money is going to each policy. In brief, it is possible to use budgetary information to understand how state is acting within our society.

Finally, it is also important to evaluate if we are not incurring in the same mistakes of other countries. Economists are always looking past economic data and trying to understand what went wrong with the economy of countries –so we can learn from past mistakes. However, if no one is supervising the way those in power spend public money, how can we know what is wrong with it?

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