

The Political Economy of the Budget Process: The Case of Ecuador

Andrés Mejía Acosta
Vicente Albornoz
M. Caridad Araujo

Daniela Oleas M. and Luis Miguel Chiriboga provided valuable research assistance. Cristina Baus translated some sections of the paper. We are indebted to Emmanuel Abuelafia, Mark Hallerberg, José Hidalgo, Fidel Jaramillo, Diego Mancheno, Tom Mustillo, Olga Núñez, Santiago Ortiz, Carolina Reed, José Rosero, Carlos Scartascini, Ernesto Stein, Marco Varea, and seminar participants at previous workshops for sharing comments, data and other information with us. Any imprecisions and errors are responsibility of the authors.

TABLE OF CONTENTS

TABLE OF FIGURES	i
Introduction.....	1
Framework: the politics of the budget process in Ecuador.....	2
Critical shocks affecting the Ecuadorian budget process	2
The rules and politics of the budget process	5
<i>Budget Formulation</i>	6
<i>Budget Approval</i>	8
<i>Changes in legislators' agenda setting powers</i>	9
<i>Changes in coalition currencies</i>	9
<i>Sub national governments as new budget actors</i>	11
<i>Budget Execution</i>	11
<i>Budget Monitoring</i>	12
Institutional changes and the quality of budget outcomes	13
Improved sustainability with fiscal vulnerability	13
Fewer budget reallocations and more efficient outcomes.....	14
Small, poorer provinces are better represented in the budget.....	16
Budget Outcomes are rigid on the expenditures and revenues sides	18
Summary and Conclusion	19
References.....	21
<i>Datasets</i>	23

TABLE OF FIGURES

Figure 1: Political timeline of the budget process	6
Figure 2: Budget reallocations at different stages of the process	15
Figure 3: 2004-1997 changes in per capita expenditure	17
Figure 4: 2006 Fiscal Budget by Expenditure	19

Introduction

The Ecuadorian budget process offers an excellent policy arena to examine the extent to which multiple political actors, acting in a changing policy environment, have shaped the nature of fiscal outcomes over time. This chapter analyzes the impact of economic and political shocks on the budget process, the ways through which political agents reacted to those incentives, their formal and informal influence during the formulation, approval, execution, and monitoring of budgets, and the resulting fiscal outcomes.

The budget process in Ecuador takes place in an environment characterized by the presence of multiple political actors, institutional instability and few incentives to cooperate over the long run. Oil rents, when available, triggered politicians' rent seeking behavior by increasing discretionary spending or by earmarking allocations to different stakeholders. While the mechanism of hardwiring budget allocations facilitated some political compromises with the opposition in the short run, it preempted the government's ability to adjust and respond to oil price volatility in the long run. A brief historical analysis of the budget process since the country's return to democracy in 1979, reveals that politicians' rent seeking behavior prevailed despite major constitutional and economic reforms aimed at rationalizing the budget process. For example, important Constitutional reforms and other legislation approved between 1994 and 1998 sought to increase the presidents' agenda setting powers over the budget process while eliminating legislators' ability to bargain for provincial allocations. These reforms removed politicians' incentives and currencies to form budget coalitions at the national level; at the same time, sub national (municipal and provincial) governments became important political players with formal rights and prerogatives to influence on budget allocations and shape the budget process. This chapter begins to document a significant "shift" of budget politics from the national to the sub national arena. The adoption of dollarization in 2000, and the subsequent adoption of the Fiscal Responsibility Law in 2002, is another example of reforms that imposed restrictions on political agents and sought to enforce fiscal discipline. Although these legal changes helped improve the fiscal outlook after 2001, the chapter suggests that subsequent fiscal surpluses are better explained by the dramatic increase in the international price of oil, rather than by austere political actors. In fact, in the context of rising oil prices, the congress and the president abolished key aspects of a Fiscal Responsibility Law in 2005 to allow for greater government spending during an electoral campaign year.

An evaluation of budget outcomes suggests that the combination of a stronger executives and the influence of high oil prices contributed to generating more efficient and sustainable budget outcomes. The political shift from the national to the sub national arena contributed to a more representative –though not unbiased- allocation of government spending. Despite the apparent successful adoption of ideal public finance reforms, the chapter warns that the budget process in its current form is not sustainable in the long run. In the first place, politicians at the national and sub national arenas still lack incentives to form credible, effective and durable coalitions around the redistribution of ever growing government revenues. The other source of instability is the greater dependency on oil revenues caused by the resource bonanza. As a result, even the adoption of oil stabilization funds originally created to help sustain a dollarized economy, has been further earmarked with projects of short term interest.

Framework: the politics of the budget process in Ecuador

The Ecuadorian policymaking process is characterized by a permanent tension between a very strong agenda setting player (the president) and multiple veto players who are active in the national legislature, the sub national governments, organized interest groups and the streets. This perverse configuration of diverging interests and actors with few formal incentives to support government coalitions over the long run, has gained the country a reputation of being “a very difficult country to govern”. In the last decade alone, high levels of ethnic and regional conflict, military (in)action, economic decline and congressional deadlock played at different times a contributing role in the demise of three presidents before the end of their terms. Box 1 below illustrates the main features of the policymaking process in Ecuador.

Box 1. The Ecuadorian Policymaking Process.

Acting in a highly fragmented scenario, presidents have pursued two paths to produce policy change. The first one is to submit legislation to the national legislature where, on average, only 30% of the presidents’ agenda gets approved due to high number of opposition parties and the lack of political incentives to form government coalitions. To overcome institutional constraints to cooperation, governments and legislators often assembled ad hoc, clandestine (ghost) alliances to trade pork barrelling projects, provincial investment projects, patronage, particularistic policy concessions, etc., in exchange of legislative support. The overall effect was a highly ineffective and costly bargaining process that produced very little policy change.

The second avenue for policy change was to delegate decision making power to a technical bureaucracy who adopted reforms bypassing political parties in the legislature. Although decisive policies emerged from the Monetary Board, the Central Bank, or the National Council for Modernization, such reforms responded to very specific interest groups and policies were reversed with every change of government or even with every new cabinet minister. At the end of the day, political parties reasserted themselves in the policymaking game by accelerating the removal of unpopular cabinet ministers: between 1979 and 1998, the average mandate of a Finance minister was approximately 12 months.

At the end of both paths, a set of formal and informal “last ditch veto players” was ready to oppose, stall, or revert unwanted policy decisions. Some formal channels of opposition included appeals to the Constitutional Tribunal; non conventional policy channels included street protests by the indigenous, the military, or popular groups. Some of these “last ditch” players became protagonists in the ousting of three Ecuadorian presidents between 1997 and 2005.

Source: Mejía Acosta et. al. 2008.

The dollarization of the economy in January 2000 had an additional effect on the Ecuadorian policymaking process. The adoption of the US dollar as the national currency rendered ineffective the role of the Central Bank in setting monetary policy, and de facto eliminated one of the two paths for policymaking by executive delegation. Thus, fiscal policy became a highly contested policy arena in Ecuador.

Critical shocks affecting the Ecuadorian budget process

The oil factor

Oil is Ecuador’s main export and its primary source of fiscal revenues. Between 2000 and 2005, oil revenues were, on average, 26.4% of non-financial public sector revenues and 35.1% of central government revenues. Given the high dependence of public revenues on oil exports, the Ecuadorian economy is particularly vulnerable to fluctuations in the world price of oil

(Fernandez and Lara, 1998) or other natural disasters that may affect the steady supply of oil (such as the 1987 earthquake that broke the oil pipeline). An interruption in oil revenues could rapidly trigger a fiscal crisis. This vulnerability explains in part the country's unstable economic performance during the last democratic period.

Between 1998 and 2005, Ecuadorian oil prices have changed according to three different periods. During the first period, between January 1998 and October 1999, prices remained at an average low price of \$12.6 per barrel. The second period occurs between November 1999 and April 2004, when prices increased to an average of \$23 per barrel. Lastly, between May 2004 and April 2006, they rose to an average level of \$39.1 with an increasing trend. The periods that characterize the evolution of oil prices are consistent with the general pattern of variation in fiscal outcomes, as illustrated in Table 1. During the first two years, the budget reflects large deficits; the trend is reversed and it even produces positive net balances between 2000 and 2005.

Table 1. Evolution of fiscal results
(relative to the non-financial public sector and in percentage of GDP)

	1998	1999	2000	2001	2002	2003	2004	2005
Budget global deficit	-5.2	-4.9	1.5	0.0	0.8	1.1	2.1	0.7

Source: Central Bank of Ecuador

This chapter argues that fluctuations in oil prices affected the institutional aspect of the budget-making process, as well as the incentives to fiscal discipline available to budget players. In the aftermath of a significant fiscal crisis, falling oil prices and the subsequent dollarization of the Ecuadorian economy, political parties in congress adopted a Fiscal Responsibility Law (FRL), to limit the expansion of public expenditure and produce an overall sobering effect on fiscal policy. Three years later, when oil prices had reached their highest levels, the same congressional parties voted to amend the existing FRL, *de facto* eliminating constraints on public expenditure and eliminating other fiscal controls. Rather than this being an isolated event, this document argues that movements in oil prices were closely related to changes in preferences and behaviors of the actors of the budget PMP.

Given the contentious nature of the policymaking process and the high dependency on oil revenues, Ecuador has not demonstrated a capacity to adapt to shocks (policy rigidity), nor has improved its ability to sustain agreements over time (policy volatility). Fiscal policy is set within a complex frame, where the budget plays an important role, not only because of the magnitude of the resources it allocates, but because of its rigid structure due to earmarking. A rigid budget imposes one additional constraint to the capacity of fiscal policy to adapt to external shocks. This constraint is enhanced with the adoption of dollarization which *de facto* limited the range of adjustment instruments available to the executive. The windfall effect of rising oil revenues can temporarily alleviate the fiscal rigidity imposed by dollarization, but this factor does not replace the need for deeper structural reforms. During the last thirty five years, the inability to make necessary fiscal reforms has been one of the elements hindering the success of adjustment programs (Hurtado, 2006).

The 1988 Constitution

The National Assembly that produced a new Constitution between 1997 and 1998 was inspired by the need to strengthen political institutions that promoted increased governability and

improved political representation. In practice, the approved reforms strengthened presidential powers over congress (governability), *while at the same time* aiming to strengthen the connection between citizens and politicians (representativity). Together with other closely related reforms, these reforms introduced a mixed set of incentives for political cooperation.

In the first place, reforms increased the level of influence of the president in the budget process, at the expense of legislators. Presidents were granted exclusive rights to initiate the process and their decree and veto powers were increased. Congress was banned from increasing expenditures or creating new revenues, and legislators were no longer allowed to bargain provincial allocations or discretionary -off budget- funding for their districts, but rather approve budgets based on sectoral spending (*partidas de gasto*). Secondly, reforms sought to reduce the number of actors participating in the budget process. The number of legislators was reduced from 123 to 100. After 1998, congress became more provincially oriented; as provincial legislators were elected through a personalized vote and the figure of national legislators (elected on a national slate) was abolished. Internally, the seven-member budget committee gained greater agenda setting power to revise the executive's proposed budget, but the decision making power for budget approval was devolved to the entire congressional floor. Lastly, reforms extended the temporal horizons of budget players. Legislators were allowed to seek reelection since 1996 and their mandate was extended from two to four years (thus eliminating mid-term elections). Legislative appointments and committee service was also extended from one to two years. In theory, this should have had contributed to expanding the legislators incentives for making inter temporal agreements, since legislators were appointed for longer periods in congress while they accumulated more experience over time.

In practice, the 1998 Constitutional reforms produced a perverse combination. On the one hand, the increased budget powers of the president made him less dependent on gathering legislative support for budget approval and it strengthened his ability to execute budget allocations. Legislators in turn, gained greater political representation vis-à-vis their constituents (they enjoyed longer terms in office with no term limits, and were elected by personalized voting), but had lost their ability to access to investment projects for the benefit of their constituencies. This combination severely hindered politicians' prospects for developing an "electoral connection" with their voters. Concurrently to the drying out of coalition incentives at the national level, a series of institutional reforms strengthened the abilities of local governments to become successful lobbyist in the budget process and develop a successful electoral connection with voters. Suffice here to say that traditional political parties who lost their influence on the national budget process, reappeared as crucial actors in a new policy arena: the sub national governments.

The 2000 Dollarization

The decision to dollarize the economy on January 2000 came as a drastic response to contain or at least mitigate the effects of a financial crisis that threatened with hyperinflation, a stagnating economy (with GDP decreasing by 6.4% on 1999), falling oil prices, and a generalized disbelief in the government's ability to produce economic recovery. A positive effect of dollarization is that it brought inflation down to levels that the country had not experienced in over two decades and provided economic agents with signals of stability that had been very much sought after. Dollarization formally reduced the possibility that the devaluation-inflation cycle eroded the real

value of budget allocations. By bringing economic stability dollarization decreased the discount rates of economic agents.

By renouncing to monetary policy, the government gave a strong signal of its commitment to a structural reform in the hopes of stabilizing the economy and recuperating some credibility at home and abroad. In terms of the budget process, the drastic change to dollarization eliminated one of the policy arenas where presidents did have some discretionary power to adopt and resoluteness to carry out policy decisions. By renouncing to monetary policy, dollarization reduced the number of policy instruments available to the economic authorities, thus imposing an additional burden of responsibility over fiscal policy.

In the aftermath of dollarization, and while the country was still paying the economic price of the financial crisis, many government policymakers as well as development banks favored the adoption of reforms that would secure responsible fiscal management. Policies like the adoption of a FRL and the creation of an oil fund - that reveal a change in the inter-temporal preferences of agents- took place in the years following dollarization and were consistent with a change in agents' discount rates and with higher public-regardedness of the benefits of sound fiscal policy.

The rules and politics of the budget process

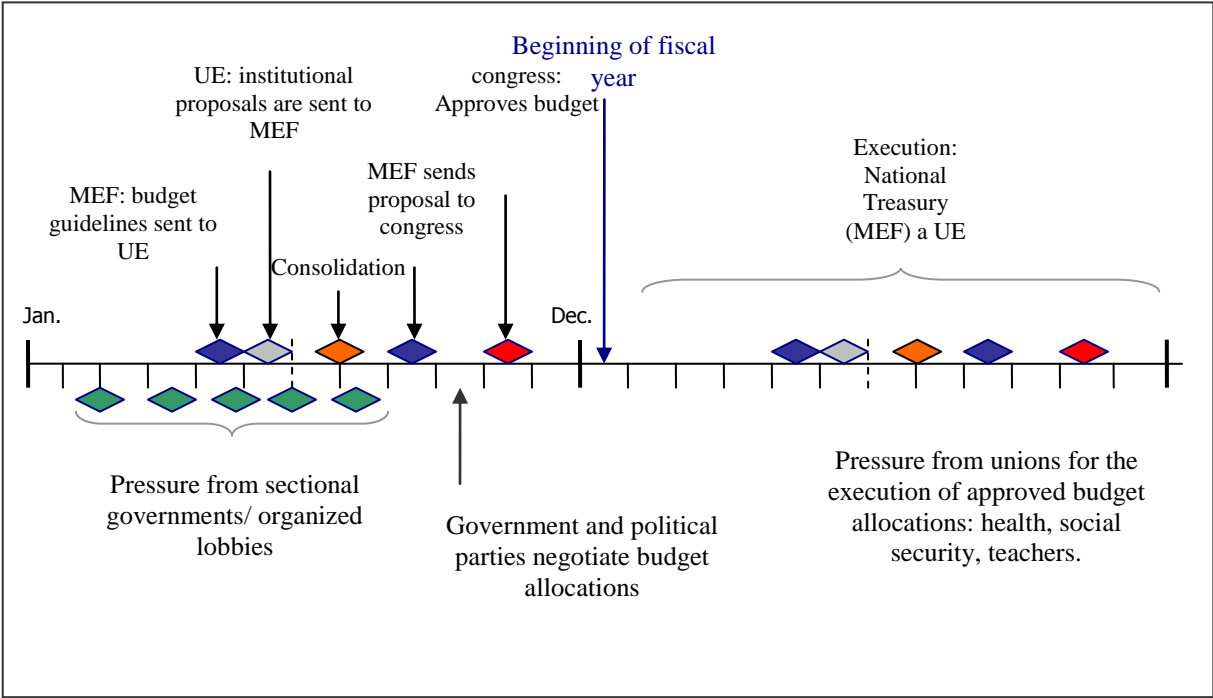
The budget making process in Ecuador is the combined product of relentless institutional change with rapidly adjusting responses from relevant budget actors. Since 1994, a series of changes to norms and budgetary procedures were adopted to produce what would have been considered a “wishlist” of reforms to ensure fiscal sustainability and discipline. A review of the actual workings of such norms reveals that for the most part, budgetary actors produced alternative patterns of cooperation around their most preferred outcomes. In this case, Ecuador illustrates a case where the adoption of constraints on political actors' spending abilities did improve fiscal discipline in the short run but at the expense of diluting political incentives to sustain longer term cooperation between the executive and the legislature.

To illustrate the discussion of the formal and actual workings of the budget process, Figure 3 maps the influence of the main political actors and lobby groups along different points of the fiscal year. The fiscal year in Ecuador follows the calendar year, from January 1st to December 31st. Three types of budget actors are identified: 1) decisive players who have the formal or informal power to influence in policy formulation (i.e. the executive, business lobbies, local governments), 2) veto players whose cooperation is needed to adopt policy changes (i.e. the legislature, political parties), and 3) last ditch veto players who may exert effective pressures to demand budget execution or revert unwanted policy decisions (i.e. courts, unorganized groups) (Mejía Acosta et. al. 2008). Budget formulation takes place between May and September and it includes the executive, the Ministry of Economy and Finance (MEF), and the Executing Units (UE) including subnational governments.¹ According to the Constitution (art. 258), the proposed budget is submitted to congress in September to be approved, ammended or rejected in 90 days, until November 30th. Budget execution begins in January, and this is the time when different interest groups demand the effective execution of budget allocations. All unspent resources are

¹ MEF website, SIGEF terminology. An Executing Unit is the administrative unit (organization or group) that executes an assigned budget.

returned to the MEF to be deposited at the Unique Treasury Account at the beginning of next year. Finally, the figure shows how the proximity of the next budget cycle leaves very little room for legislators or other political actors to undertake budget monitoring.

Figure 1: Political timeline of the budget process



Source: MEF.

Budget Formulation

Budget formulation is largely a prerogative of the executive branch. The president, through the MEF, elaborate a General Government Budget (GGB) proposal according to guidelines established by the National Planning Office (SENPLADES) and macroeconomic forecasts from the Central Bank of Ecuador (BCE). The MEF then requests that Executing Units submit their budget estimates before April 30th, taking into consideration the government’s macroeconomic guidelines and fiscal responsibility principles. The fiscal budget is mainly made up of salary and wages, maintenance, and basic services expenditures, categories that are indexed to inflation and represent an inertial amount in the elaboration of the GGB (Almeida 2005). Additional investments have to be approved by the SENPLADES, and their financial viability certified by the Sub-secretary’s office of Public Investment. The MEF analyzes, verifies, consolidates and can even ammend information submitted by EUs if the macro-fiscal rules have not been met. The budget proposal is submitted to congress for analysis and approval until September 1st.

Ecuadorian presidents remain then most influential budget players. Traditionally, presidents gained a reputation for being “fiscally conservative” at the beginning of their four year terms (1979-1996), but their discipline gradually relaxed as their mandate elapsed and the fragmented coalition partners became more to engage. Presidents also had an ample range of discretionary spending lines (*gastos reservados*) before 1997. While the availability of these funds allowed

them to extract legislative support from the opposition, it also led to corruption scandals for misuse of public funds during the Durán Ballén, Bucaram, and Alarcón administrations (1992-1997). Reforms adopted after 1997 sought to reduce or control the budget powers of the president: new legislation introduced spending caps to ensure greater fiscal responsibility and long term planning, and the General Comptroller Office imposed a ceiling on *gastos reservados*, which could only amount to 0.25% of the General Budget and limited its use to the Ministries of Defense and Internal Affairs. Eventually, the 1998 Constitution completely eliminated discretionary spending from the executive.

Despite formal limitations, presidents exert political and technical agenda setting powers over the budget process through the MEF. Since 1979, the technical responsibility over fiscal policy had been shared between MEF, the Monetary Board, and the BCE, but after the 1998 constitutional reforms and dollarization, the MEF became a powerful budget actor. Interest groups such as teacher or doctor unions, pensioners, the military and the police consistently approached the MEF with requests to increase recurrent spending and capital spending *during the budget formulation stage*. Subnational governments (municipalities and provincial governments) also lobby the president or the minister of finance to demand increases in capital spending especially during the month of April. Despite MEF's political role, nearly 80% of all Finance Ministers were chosen from a pool of technical government pundits without an explicit partisan affiliation. In the eyes of the opposition, the “technocratic” status of the finance minister made them politically vulnerable to congressional impeachments or politically motivated resignations. Thus, the MEF was a political fuse that needed replacing every time the government achieved a new legislative agreement with the opposition, and a new minister –most likely another independent- was appointed in place. Between 1979 and 1998, the average tenure of finance ministers was 11.5 months in office (346 days). Ministers did not stay longer in office despite 1998 constitutional reforms aimed at protecting cabinet members from legislative impeachment and censorship. If anything, they produced the opposite effect: until December 2005, the average tenure of a finance minister was reduced to 7.3 months (220 days) (Mejía Acosta et. al. 2008). Despite their agenda setting abilities, no minister stayed long enough to formulate and execute the same budget; thus ministerial volatility may have further contributed to strengthening the effective control of the president over budget formulation and execution.

A new set of influential actors during budget formulation since the mid nineties are sub national governments. Sub national governments comprise elected local authorities (or the *regimen seccional autonomo*) and president-appointed provincial governors. Elected officials include provincial prefects who preside over the provincial legislature made of provincial counselors. The 326 mayors preside over the municipal councils and, since 2000, local authorities are elected in off-years without term limits. The strengthening of local governments in Ecuador is due to the gradual transfer of greater resources, better technical planning, and increased legal responsibilities and prerogatives. Since the early nineties, the Association of Ecuadorian Municipalities (AME), a lobby group of mayors, received and channeled international assistance to strengthen the capacity and technical planning of local governments. AME also lobbied for greater government resources for intermediate and small municipalities with less bargaining power than Quito or Guayaquil. The adoption of a special Law that earmarked 15% of the Central Government Budget for sectional governments in 1997 further strengthened their capacity to deliver public works in their districts. Together with other transfers, it is estimated

that sectional governments benefit from at least 20% of the General Budget and that they retain around 50% of the public sectors' investment capacity. Finally, mayors initiated important reforms to have greater prerogatives and responsibilities over resource allocation in their districts. Through reforms like the *Ley Orgánica de Régimen Municipal* and a *Ley Especial de Descentralización y Participación Social* (1997), and the reform to the *Ley Orgánica de Régimen Municipal* (2004), mayors gained greater agenda setting power during budget formulation.

Budget Approval

According to the Constitution (art. 130), congress is in charge of approving the GGB, and ensuring its proper execution. The president of congress receives the executive's proposed budget and generally sends the bill to the Committee of Tributary, Fiscal and Banking Issues (TFB). The committee is made up of seven members, elected for a two-year period and can be reelected. In the absence of a congressional budget office, committee members rely on government entities such as the Internal Revenue Service (SRI) or the Executing Units (EU) to elaborate their own revenue and expenditure estimates. The committee's detailed report is submitted to the *Plenary* of congress to be discussed in only one debate, by income and expenditure sectors. All legislators can ask for specific changes to the proposal based on the general guidelines established in the report from the TFB committee. Congress has until November 30th each year to approve or reform the proposal, but if the proposed budget is not approved, the original proposal submitted by the executive is the reversal point.

Although budget approval is the policy stage where congressional parties should maximize their influence over the budget process, their effective influence in practice has diminished over time. All things equal, the high party fragmentation and malapportionment of the Ecuadorian congress generally increased transaction costs of budget approval. First, legislators had plenty of electoral incentives to cultivate a personal vote: in 1998, congress was composed of 123 legislators from 22 provinces (100 legislators after 2002) who were elected through an "open list" electoral formula.² Legislators were elected for a four year term with no term limits. Secondly, the heterogeneous territorial distribution created severe malapportionment in the transformation of votes into seats: for example, a legislator elected in 2002 from a large district such as Guayas represented approximately 22 times more voters than those in the constituency of a legislator from a scarcely populated province such as Galápagos (Snyder and Samuels 2001). These disparities skewed the proportional allocation of government spending in favor of over represented provinces.

There are two additional factors that diminished the role of congress as an effective arena for budget approval: the formal reduction of legislators' agenda setting powers, and the diminishing availability of resources used to facilitate political alliances. Together, these changes eliminated political incentives to cooperate at the national arena and pushed budget coalitions to the subnational arena.

² The personalized form of voting was adopted in 1997, by which voters could elect as many representatives as seats were available in the district, regardless of party lists or party affiliation. Before this, the electoral system featured a closed list system that gave party leaders strong prerogatives over candidate nomination and selection.

Changes in legislators' agenda setting powers

The 1998 constitutional reforms formally reduced the overall influence of congress on the budget approval, by withdrawing congress's ability to create spending lines in addition to those submitted by the executive and by allowing the president's proposed budget to become law in case no budget agreement emerges from congress by November 30th. The legislative procedure for budget approval also changed. Between 1979 and 1997, the budget committee reviewed the president's proposal but budgetary amendments had to be approved by a simple majority of the *Plenario de las Comisiones Legislativas*, a 35-legislator council composed of all members of the five Permanent Committees. The practice of approving budgets in the *Plenario* generally benefited parties with larger contingents in congress: party leaders bargained the direction and the amount of budget allocations (*partidas de gasto*) directly with the executive. Although such agreements were not cheap for the executive, the mechanism ensured the credibility of budget coalitions: legislators' constituencies benefited from investment projects and some pork (or "troncha"), and the president obtained budget approval with a simple majority of *Plenario* members.

The approval of the 1997 budget introduced important changes to budget bargaining. Lacking the support of traditional political parties, president Bucaram managed to assemble a minimum coalition in the *Plenario* with the support of his own PRE party and some independent legislators. The following year, opposition parties that were excluded from the Bucaram coalition (including PSC, ID, DP, MPD, and Pachakutik) promoted a reform to centralize agenda setting in the budget committee but opened the budget approval to the entire floor. Although the reform was approved under the discourse of increased budget accountability, party leaders sought an insurance mechanisms to prevent the executive from assembling budget coalitions with individual legislators. Predictably, traditional parties invested more resources to influence the budget process through the budget committee. Whereas partisan affiliation to the TFB had been evenly distributed across five or six political parties, 93% of the total number of committee assignments after 1998 was in the hands of four major political parties: DP, PRE, PSC and ID. The partisan take over of the budget committee also reproduced regional patterns of party competition (PRE against PSC in the coast, DP against ID in the highlands) Evidence suggests that the budget committee reinforced the representation of larger provinces. The proportion of committee members who came from the three largest provinces (Pichincha, Guayas and Manabí) nearly doubled, from 31% to 57%. While there was an effective takeover of budget approval by political parties, parties decreased their influence on the budget making process.

Changes in coalition currencies

A second factor that reduced the legislators' influence over budget approval was the 1994 reform that eliminated legislators' ability to negotiate budget allocations for their provinces, requesting that legislators approve the budget by sectorial spending instead. The proposed reforms were initiated by president Durán Ballén (1992-1996) and approved by popular referenda with the purpose of eliminating legislators' rent seeking incentives during the process of budget approval (Mejía Acosta 2006). Why would the executive voluntarily abdicate its ability and discretion to distribute funds and bargain budget coalitions with legislators? The Durán Ballén administration

perceived that budget bargaining with political parties had become too expensive to sustain. According to Vice-president Dahik:

“(a group of PSC legislators) would ask for provincial funds in return for supporting some of our laws (...) And their family members would be the contractors. It was an absurd situation because their leaders were in opposition, but meanwhile some of the deputies were constantly sitting down with us, demanding money. It was collective bargaining, and the whole process was very expensive” (Landau 2001: 47).

By limiting the ability of congress to reallocate provincial funds, the government had hoped to decrease the particularistic demands for government spending, and allow for a smoother, more technical process of budget approval. But the government’s strategy of “drying out” the availability of budgetary allocations backfired as party leaders refused to approve the 1995 budget by sectors unless their districts benefited from government allocations. Eventually, disgruntled PSC leaders clashed with government officials over an alleged scandal of vote buying which forced the resignation of vice president Dahik in 1995 and destroyed the PSC’s presidential hopes in the 1996 general election. In the aftermath of additional corruption scandals during the Bucaram and Alarcon administrations, the newly elected 1998 congress passed an “Ethics Code”, which threatened with dismissal if legislators were found negotiating material or political resources for their districts or themselves with the executive. Although the Code was never used in practice, it effectively eradicated existing coalition incentives between the executive and legislators. According to a party leader:

“In the past, corruption was very functional for governance. The Presidency, the administration’s Secretary General, the Minister of Defense and the Minister of the Interior all had discretionary expenditures. Even if many don’t like to accept it, these served in the past to buy legislators, to buy loyalties in detriment of (the discipline of) the political parties. A Budget Committee existed where, if conflicts arose, they were taken to the Plenary. It was a functional system: 18 years of democracy and there were no problems associated with the approval of the fiscal budget. The amount of the budget was negotiated by sectors, and legislators negotiated the amounts by entries, by allocations. It was an open secret. Legislators in the Budget Committee (...) negotiated giant allocations for themselves: they (arbitrarily) selected contractors, and it did not encounter problems with the Comptroller’s Office because they (political parties) controlled the provincial comptrollers, the judicial branch, etc. These mechanisms no longer exist. While there is more transparency (in the budget process), sectors feel powerless to obtain gains and vent their frustration by radically opposing government initiatives”.

In the end, the (failed) institutional attempts to de-politicize the budget process by eliminating legislators incentives and means to cultivate a personal vote not only contradicted existing electoral incentives, but also increased the costs of budget bargaining in the legislature. Some informal and clandestine mechanisms to increase capital spending and facilitate budget bargaining between the executive and the legislature prevailed, but overall, the lack of available and legal currencies affected the stability and reliability of budget coalitions.

The combined effect of institutional reforms on the process of budget approval produces an interesting contradiction. On the one hand, the most prominent political parties seek to strengthen their presence and influence on the budget committee after 1998, even when the executive retains significant powers of budget formulation and execution. On the other hand, legislators after 1998 lost access to key budgetary resources that would have facilitated more durable and reliable budget coalitions with the executive. The pending question is then: why would legislators remain interested in budget politics at the committee level if the legislature had

lost access to effective resource allocation? One proposed explanation is that parties and legislators in congress became indirect agents of provincial interests through the influence of their regional, provincial and municipal governments.

Sub national governments as new budget actors

As discussed earlier, the political context after the 1998 reforms offers an interesting combination of stronger sub national governments (especially mayors) who have gained influence over the budget process, with weaker parties and legislators at the national level who have lost access to resource allocation. Not surprisingly, political parties quickly identified this asymmetry and quickly shifted their political activism from the national legislature to the sub national arena, where they enjoyed better access to budgetary allocations to deliver better constituency services and maintain a healthy electoral connection. The fact that mayors could also pursue immediate reelection (previously banned in the nineties) gave politicians clearer opportunities to develop long term relations of accountability with their constituents. Following this logic, prominent legislators and influential party leaders abandoned the much discredited legislative arena in 2000 to successfully run for local office: Paco Moncayo (ID) became mayor of Quito (in 2000 and 2004), Jaime Nebot (PSC) became mayor of Guayaquil (in 2000 and 2004), and Jorge Marun (PRE) became Prefect of the Los Rios Province, to name a few. The “downwards” move appeared to be a good political strategy, as city mayors had enough leverage to bargain budget allocations directly with the office of the president, to run some public services of their own, and even to influence some aspects of national policy making. From a public standpoint, mayors also escaped the discredit of congressional parties while appearing as guardians of democracy and governability in their cities during times of national political crises. Looking at the partisan affiliation of mayors elected before and after 1998, evidence suggests that the four most influential Ecuadorian parties captured 332 city governments, nearly two thirds of the total number of mayoral posts available in the 2000 and 2004 elections (75% if Pachakutik is included). Mayors’ partisan affiliations reproduced regional trends of party competition.

While evidence suggests that political parties did reallocate to the subnational arena, more empirical research is needed to understand the mechanisms by which parties influenced the sub national budget making process. The case of Simon Bustamante, a PSC legislator from the province of Manabi is a good example to illustrate this possible link. Bustamante has presided over the CTFB in three of the four times in which he has been a member, and it is believed that he has played a critical role in helping channel budget allocations and regional development programs to his native province. Furthermore, his political party has gained an important presence in the provincial and municipal government over the last decade.

Budget Execution

According to the Constitution, the executive is responsible for the elaboration and execution of fiscal policies. Once the GGB has been approved by congress, the MEF ensures that it complies with the fiscal responsibility principles, and the MEF’s office of Budgets and the Treasury establishes a priority order to assign resources according to its governance needs (Political Constitution, Art. 260). Once the priority order has been established, the office of Budgets and

the Nation's Treasury are in charge of transferring the approved resources to the UE's who are ultimately responsible for budgetary execution. Sometimes, the government faces cash flow problems because tax collection revenues tend to increase in April, whereas budget expenditures tend to be constant throughout the year. Thus, the MEF has the ability to reassign and adjust approved budget allocations up to a 5% in government expenditures during the fiscal year and without congressional approval.

The priority order is directly related to the budget structure by expenditure accounts and is applied when the effective, current non-oil revenues in the GGB are less than what was budgeted for the quarter. The MEF can amend allocations in the expenditure budget, as long as they do not affect those allocations determined by the Constitution. In the event that amendments are made to investments, they have to be subject to prioritization according to the multi-annual plan of government and to the hierarchy of the projects that are being carried on by the executive. The MEF can also reallocate funds within the approved budget based on the spending capability of the UE's, or through the interpretation of *budgetary classifiers* (although this is not officially established). In general, the minister of finance has significant leverage to establish the rules of transfers, spending increases or reductions and other budgetary modifications.

The actual allocation of resources across spending items at each stage of the budget process between 1990 and 2006 reveals that nearly half of the spending contained in the executive's budget proposal is absorbed by four sectors: education, defense, health, and social welfare and labor. In general, these are sectors with the largest share of civil servants, thus contribute with a higher wage bill. Throughout the budget process, allocation across sectors remains relatively stable with few exceptions. Perhaps for sector with the most dramatic decrease in its total spending allocation is social welfare and labor, which at the proposal stage is set to receive 6.7% of total spending, but at execution stage, only gets an average of 3% of total spending. At the other extreme, (and consistent with the large degree of discretion of the MEF throughout the budget process), the MEF has the most dramatic average budget increase, from a projected 2% of spending at proposal stage to an actual 6% of budget executed.

Further research is needed to understand the political mechanisms by which some sectors are better able to protect their original budget allocations, and their capacity to effectively execute allocated spending. At this point, the executive through the MEF appears to be the most influential player to determine the degree and direction of budget execution.

Budget Monitoring

The follow-up and control of the budgetary execution is responsibility of congress and the General Comptroller's Office, through its system of Control, Censuring and Auditing of the State. This system in turn, has mechanisms for internal and external control. The EUs have to ensure the creation and maintenance of their internal control system, through which public servants and functionaries report on and make themselves responsible for the execution of their attributions, the use of public resources and the results obtained. The internal control exercise has to be applied before, during and after through the specialized units in each of the EUs, which have to comply with the regulations in force established by Law. Even the MEF has some role in enforcing internal control of EUs when it can adjust the correspondent cash programming based

on the Unit's budgetary execution record. External control is exercised by the General Comptroller's Office, which is an independent institution, and congress, being the active participant the General Comptroller's Office. Even though there is a constitutional mandate for congress to follow-up on the budgetary execution, in practice it has no technical capacity to do it. The participation of the General Comptroller's Office is ex-post the budgetary execution; therefore, timely alerts on the execution quality of expenditure of the EUs have to come from the internal control. It is worth mentioning that the large number of EUs makes it impossible for the General Comptroller's Office to exercise external control on all of them systematically.

The approval of the Access to Public Information and Transparency Law (LOTAIP) in 2004 established a legal framework to facilitate the participation of citizens in the supervision of governmental actions and decision-making. The LOTAIP mandates that the government agencies must disclose information regarding its legal status, directory board, budgetary information, auditing results, plans and executed programs, and forms of accountability to citizens. Furthermore, the Law also establishes specific sanctions to illegitimate acts of omission or denial of access to public information by state functionaries. A number of citizen observatories have also been organized to supervise the allocation and execution of fiscal expenditures. Some of the most relevant organizations that have an influence on the fiscal exercise are the Observatory of Fiscal Policy, the Observatory of Human Resources of the Health Sector, the Social Contract for Education, the Observatory of Children and Youth, the Observatory of Public Services, and the Observatory of Public Policies in the South, among others. In the long run, these watchdogs can play a complementary role to that of the governmental institutions to improve the quality of budgetary execution and distribution.

Institutional changes and the quality of budget outcomes

This section presents empirical evidence to assess the impact of institutional reforms on the sustainability, efficiency, and flexibility of budget outcomes. The level of detail and the type of analysis chosen is contingent on data availability.

Improved sustainability with fiscal vulnerability

During the first half of the 2000s, Ecuador experienced an improvement along several dimensions of its fiscal standing, reflected in healthier debt and current accounts indicators. This is not too surprising for different reasons. First, the period coincides with the recovery from the severe crisis of 1999. Second, Ecuador's budget relies heavily on oil revenues- which experienced a period of stability (2002-2003) followed by a dramatic increase in the international prices of oil (2003 onwards).

There are two questions of relevance. The first is to what extent the Constitutional reform and dollarization also had an effect of their own on the improved sustainability of budget outcomes. The second question is whether this trend can be sustained over time.

Unfortunately, there are no studies that attempt to empirically disentangle the effects of the different factors influencing the sustainability of budget outcomes. An exception is the paper by

Barnhill and Kopits (2003) that explores the impact of dollarization. Their main finding is that dollarization substantially reduced fiscal vulnerability (the order of magnitude is between 14-16% of the net worth of Ecuador's public sector). They also identify the components of the government's balance sheet whose volatility has the largest contributions to fiscal vulnerability: oil income, profits from state-owned enterprises, outstanding external liabilities, and liabilities of the pensions system.

This document argues that the Ecuadorian economy remains vulnerable to external shocks and therefore, its capacity to maintain fiscal sustainability in the future is, to a large extent, tied to the evolution of oil prices. This claim is based on three facts and also supported by related research (Barnhill and Kopits, 2003 and Díaz Alvarado, Izquierdo and Panizza, 2004). First, as long as oil remains to be the principal source of government revenues (taxes account for less than half of current revenues), variations in oil prices constitute a meaningful source of volatility. Second, expenditures are quite rigid. This in part because public wages represent a high a share of primary spending in Ecuador and have been experiencing an increasing trend since 2000 (remaining at around 45%). Other aspects of budget rigidity are discussed on the section on earmarks. And third, rigidity in expenditures becomes even more critical in a dollarized regime where government's main policy tool is on the fiscal front.

Fewer budget reallocations and more efficient outcomes

The role of institutional changes on efficiency of budget outcomes is explored by assessing the trends in the magnitude and direction of budget reallocations at different stages of the budget process between 1990-2006. The focus is on changes in budget reallocations before and after the 1998 Constitutional reform and dollarization.

Following the model proposed in this book, this section presents a measure of the total change in the composition of spending for each pair of stages in the budget process. Specifically, the changes in the composition of spending are defined by the following variables:

CBL = Total change in the composition of spending between the executive's proposal and the budget law approved by congress.

CBR = Total change in the composition of spending between the executive's proposal and the budget law *really* approved by congress. This indicator accounts for the hidden costs of the budget approved by congress and that are present in the detail of the budget but not in the summary text that is formally approved by congress.

CRD = Total change in the composition of spending between the budget law *really* approved by congress and execution.

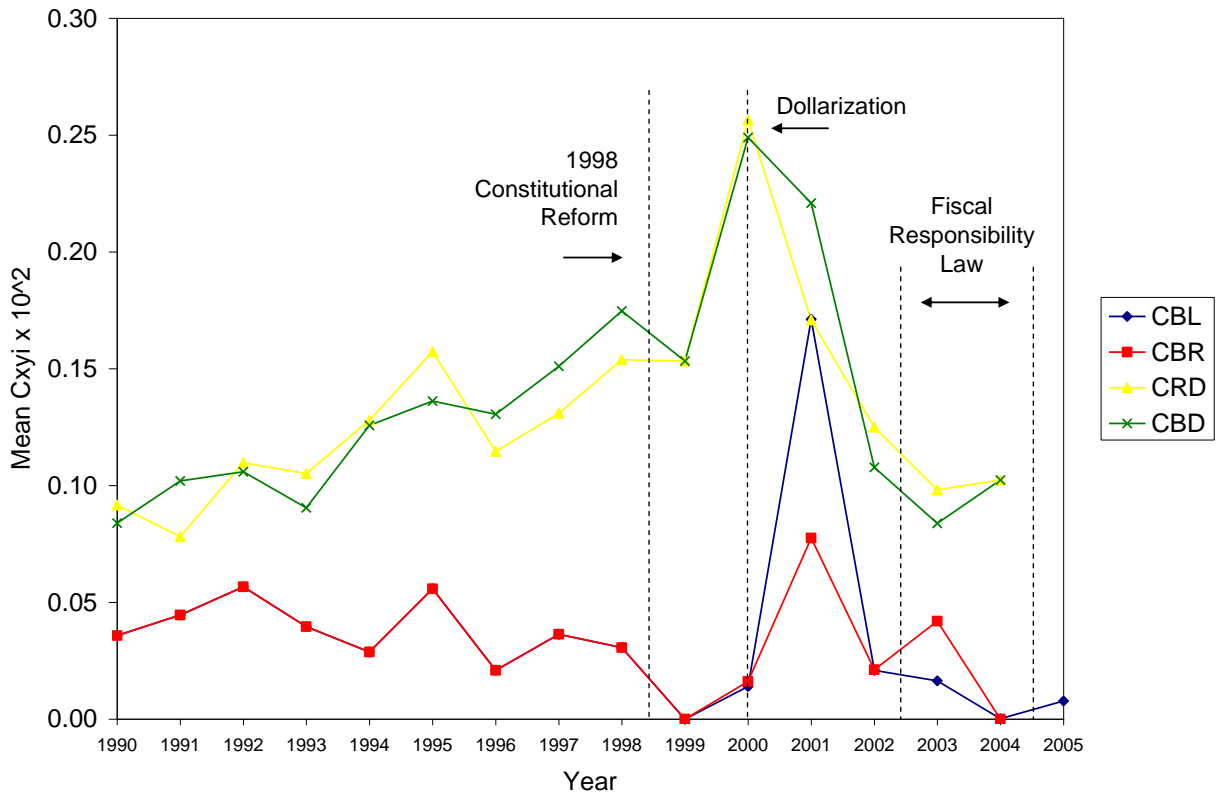
CBD = Total change in the composition of spending between the executive's proposal and execution.

Both *CBL* and *CBR* are approval intervals where the main actor responsible for budget reallocations is congress. Congress decides on these reallocations based on the laws (and the "acceptable" loopholes around them). Political pressure for reallocations - through different interest groups - can and does affect congress's behavior. Alternatively, *CRD* and *CBD* are execution intervals, where it is the executive that has the largest discretion. At these stages, organized groups -and especially those with capacity to mobilize - are the most likely to succeed

in obtaining budget reallocations in their favor. The data allow to compute CXY_{it} for years $t=1990 \dots 2005$ (and thus the addition of time subscripts) across 19 budget items. 2005 data were only available for proposal and approval stages.

Figure 2 depicts the evolution of the annual total spending reallocations at each stage of the process. It illustrates that for every year, the total magnitude of the changes during execution is much larger than that of those which occur during approval. In other words, the executive plays a more important role than congress on budget outcomes. Second, it is clear that after the 1998 Constitutional reform, the real reallocations in the budget approved by congress are smaller than the ones that appear masked in the budget law. Third, the shape of the lines reveals that the overall magnitude of the reallocations in spending at all stages of the process (and in particular execution) decreased after dollarization to levels comparable to those in the early 90s. Although, the interval is short, the magnitude of reallocations also seems to decrease for approval, especially in the interval when the FRL was in place. However, further research and longer time series would be needed to conclude that the FRL was effective in restraining budget reallocations at approval stage. While all of the actors of the budget process seem to have experienced a reduction in their capacity to reallocate resources across items, the post-reform series are not long enough to find this evidence conclusive.

Figure 2: Budget reallocations at different stages of the process



Note: B=composition of spending in executive budget proposal, L=composition of spending in budget law approved by congress, R=real composition of spending in budget law approved by congress, D=composition of spending in the total executed expenditure. Within each year, n=19 expenditure items. For comparability, debt payments have been excluded from the budget.

Source: Data collected by the authors for this paper from congress and the MEF.

An alternative way of looking at the data is to focus not on *total* reallocations by year (i.e. the sum of the absolute value of reallocations across items), but on the yearly *mean* budget reallocation across items³. These measures quantify whether the dispersion in reallocations across items experienced any systematic differences over time. Although sample sizes are small ($n=19$), *t*-tests of the equality of means comparing *t* to *t+1* reveal two trends. First, most differences that are statistically significant concentrate in the post-1998 period and at the approval stage. And second, the magnitude of the dispersion in reallocations across items at approval stage seems to be decreasing, in particular after 2001. This data seems to support the hypothesis that the period after the institutional reforms analyzed in this document was indeed characterized by smaller reallocations and more efficient budget outcomes.

Small, poorer provinces are better represented in the budget

The 1998 Constitution and related reforms adopted significant electoral changes that affected the level and quality of representation. This section discusses how these changes affected the representativity of budget outcomes. Representativity is measured as the provincial per capita spending: the higher the per capita spending, the better represented were its residents in the budget process (Albornoz et. al. 2000, Hidalgo and Albornoz 2007). Available data allows for comparisons of two points in time, 1997 and 2004, one of them before and another one after the 1998 constitutional reform.

Since the unit of observation for this section is the province, there are two likely mechanisms through which the constitutional reform could have affected provincial budget outcomes. First, the electoral reforms could have altered the incentives of congressmen, in detriment of the national party structures and favoring their local constituencies. And second, the implementation of a decentralization law that mandated that 15 percent of all government spending had to be distributed across sub national governments is also expected to alter the provincial budget dynamics.

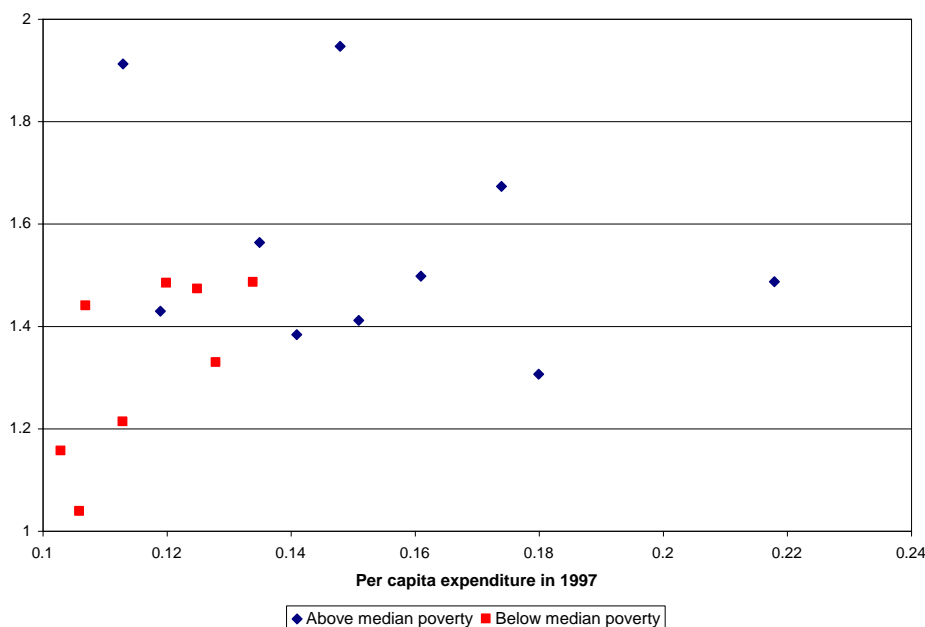
An inspection of the provincial-level spending data reveals a few facts. First, there is a large dispersion in per capita spending across provinces. Second, spending in per capita terms is inversely correlated to population size. Third, spending in per capita terms is positively associated to poverty, suggesting a relatively progressive pattern of spending. These are not surprising findings, as differences in spending could be explained by differences in provinces' needs (or poverty) as well as by differences in their characteristics (geographic, ethnic, historic, and other), or by the presence of economies of scale in the provision of services in areas with higher population densities.

Figure 3 illustrates the changes in per capita expenditure between 1997 and 2004. Each dot represents one province. The vertical axis depicts the ratio of the 2004 per capita expenditure over that in 1997. The horizontal axis illustrates per capita expenditure in 1997, the base year. This figure also distinguishes across provinces above and below median provincial poverty. With two exceptions (one of them an outlier that was taken out of the figure for clarity), most provinces experienced increases in their per capita spending. The growth in per capita spending

³ Data on these means are not reported but can be obtained from the authors upon request.

was larger in provinces where per capita spending was also bigger in 1997, as this scatter plot would seem to follow a positively sloped trajectory. Poorer provinces were also more likely to see bigger increases in their per capita expenditure. It seems then that provinces that are found to be more marginal (and possibly smaller in population and more remote) experienced higher increases in the per capita spending determined by the budget. This is interpreted as evidence of improved representativity of the budget.

Figure 3: 2004-1997 changes in per capita expenditure



Note: Galápagos and Morona Santiago are not included in figure.

Sources: Provincial expenditure data from Albornoz (2000) and from data collected by the authors for this study. Population data from INEC. Poverty data from 1990 poverty map constructed by the World Bank.

The institutional reforms introduced after 1998 significantly altered the electoral dynamics in Ecuador. Electoral reforms were adopted to elect legislators through a personalized vote, first by simple plurality (1998) and then through some form of proportional representation rule (2000, 2002). Secondly, the total number of legislators was increased from 82 in 1996 to 100 in 2002 and the election of national legislators was eliminated. In theory, these changes should have encouraged legislators to cultivate personal and local followings as opposed to being responsive to their party leaderships, and should have contributed to the proliferation of political parties and the fragmentation of the legislative landscape. From the presidents' perspective, these would, in turn, increase transaction costs for forming budget coalitions, since more fragmented and provincial players were involved in the budget process.

One useful measure of equity in the electoral representation is captured by the concept of malapportionment, defined as the discrepancy between the share of legislative seats and the share of population held by geographical units (Samuels and Snyder 2001). The measure of

malapportionment illustrates deviations from the democratic “one man one vote” principle and it shows differences in the relative weights of citizens’ votes across districts.

It is possible to track the evolution of provincial malapportionment in the periods before and after the 1998 Constitution. The malapportionment measure computed at the provincial level suggests that the Constitution led to a very small decrease in malapportionment (mean malapportionment went down from 41 to 37 and the difference is not significantly different from zero). This means that the reform had a minuscule effect. The direction of this effect was towards the reduction the relative weight of a vote in all but four relatively small provinces. This change could be consistent with change in representativeness of budget outcomes in favor of smaller provinces that was observed after the reform.

Budget Outcomes are rigid on the expenditures and revenues sides

The budgetary rigidity comes from factors that limit the government’s capacity to modify its budget in the short run. When analyzed from this perspective, the rigidity in Ecuador’s fiscal budget presents itself in various ways. To the extent possible, Ecuador’s budget rigidity is quantified in this section. The main finding is that Ecuador’s high budget rigidity has only worsened since 1998⁴.

Estimates suggest that 92% of the Central Government’s Budget is inflexible (Almeida, 2005). The discussion that follows focuses on earmarks. However, another cause of budget rigidity are the various subsidies –many of them of a regressive nature- that are perceived as entitlements and thus difficult to remove (for example, electricity or fuel subsidies).

Two types of factors prevent the budget from showing all real revenues and expenditures and make quantifying budget rigidity complex. First, some earmarked revenues are handed directly to the beneficiaries before they enter the National Treasury (i.e. earmarks on revenues). And second, certain expenditures such as fuel subsidies accounted as costs for the state oil company and thus subtracted from total oil revenues even before these are registered in the budget (i.e. earmarks on expenditures).

Earmarks are revenues and expenditures that are assigned by law to a specific purpose. They were created as a means for congress to ensure the allocation of resources to determined constituencies and offset its lack of formal access to the budget (Gallardo, 2001 and Almeida 2005). The laws provide contradictory signals regarding the existence of earmarks. The Budget Law specifically prohibits earmarked expenditures, and limits them those that can be technically justified. The Constitution, nevertheless, determines that 30% of the budget must go to education.

A disaggregation of the 2006 Central Government’s budget proposal (MEF, 2006) illustrates the large magnitude of earmarks. For example, on the 2006 proposed budget, 20.9% of total tax collections were earmarked to be distributed among a number of institutions. The main beneficiaries of tax revenue earmarks are universities and sectional governments, that receive 32% and 11% of the total earmarked tax revenues, respectively.

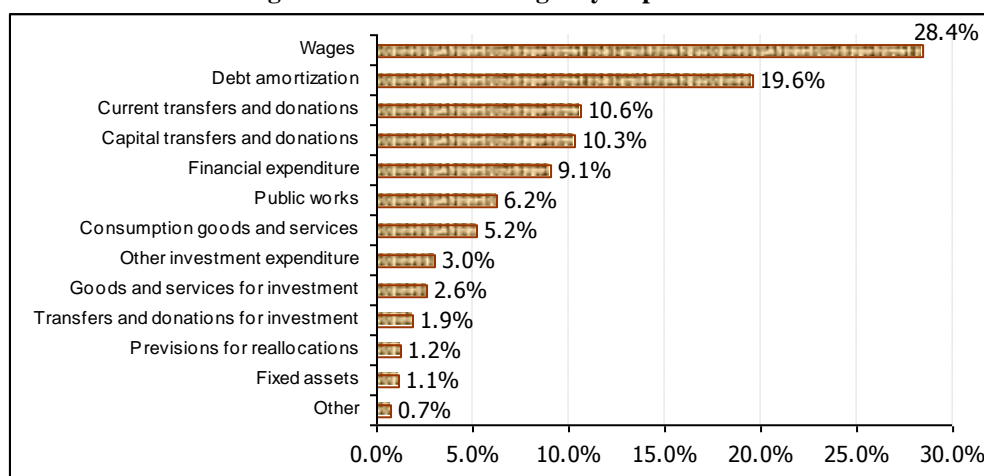
⁴ The significant changes to earmarks that were introduced since 2006 are beyond the scope of this paper.

Earmarks represent 14.52% of total oil revenues. These resources are allocated into education, health, roads, and to autonomous and decentralized entities. In addition if oil revenues are larger than what was budgeted, they are transferred to an Oil Stabilization Fund managed by the BCE. All of the surplus of this fund is also earmarked: 45% towards the management of liabilities, 35% for roads in the Oriente region where oil is produced, 10% for development projects in five provinces, and 10% for the police.

Regarding earmarks on expenditures, resources for sectional governments are the main item. By law, a 15% of all current income ought to be transferred to municipalities and provincial governments.

On the expenditure side, there are also other sources of budget rigidity, specifically inflexible expenditures such as wages, subsidies, projects with domestic and foreign debt, and foreign debt interest payments (Almeida, Gallardo, and Tomaselli, 2005). The relative weight of these and other expenses in the 2006 budget proposal is depicted in Figure 4.

Figure 4: 2006 Fiscal Budget by Expenditure



Source: MEF, 2006 budget

Summary and Conclusion

Ecuador offers an interesting case study to analyze –from a political economy perspective– the impact of major political and economic reforms on the budget process and, consequently, on budget outcomes. The focus on budget outcomes reflects this paper’s concern to find a comprehensive account of the changing incentives for cooperation that budget players have under different political and budgetary arrangements.

The paper finds that the set of constitutional reforms adopted in 1998 and other political reforms adopted in previous years (1996-1998) offered relevant budget players a contradictory set of incentives for cooperation. On the one hand, they gave legislators incentives to be more responsive and accountable to their constituents by allowing them to seek reelection and stay longer terms in office. On the other hand, it constricted the role of congress in the general budget

process, by giving the executive greater agenda setting power over formulation and execution, and by banning legislators from accessing or negotiating budget allocations for provinces. In the end, the greater agenda setting powers of the executive contributed to more sustainability of the budget process. From a political standpoint, the budget became more efficient as fewer budget reallocations took place. The electoral reforms aimed at adjusting the proportionality of the electoral system were also reflected in more representative budget outcomes. Finally, legislation approved since 1998 contributed to greater earmarking and therefore more rigid budget outcomes, despite constitutional provisions to the contrary.

Dollarization reforms and the subsequent FRL significantly constrained the choice of fiscal policy instruments available to governments. Dollarization imposed a de facto need for fiscal discipline as the government could no longer print money. By eliminating the role of the monetary authority, dollarization also contributed to shifting policy choices to the legislative arena, where policy change has been traditionally rigid. At the same time, a rise in international oil prices and therefore an increase in oil revenues further encouraged earmarking of oil reserve funds and therefore greater budget rigidity. The lower discount rates that came with dollarization are likely to have contributed to greater budget sustainability and efficiency. Although it is not possible to calculate the net effect of different reforms on budget outcomes, institutional changes have improved budget governance (in the sense of more sustainable, representative, and efficient budget outcomes), at the expense of adaptability to changing needs.

Although current budget outcomes appear desirable, this paper claims they are outside an equilibrium path, largely because budget players do not have incentives to sustain political agreements over the long run. This instability is due to the prevailing asymmetry of powers between a strong executive, weak legislatures and newly empowered sub national governments, and the disrupting effects of rising oil revenues on actors' incentives for budget discipline. While the 1998 Constitution improved the representativity of legislators, it also reinforced the powers of the executive over the budget process at the expense of the legislature. Under the new rules, legislators had very little space to influence budget allocations in favor of their constituencies. As a result, rational politicians migrated from a resource-dry policy arena to local governments, where they could access government resources and develop clearer electoral loyalties. The mechanisms through which municipal governments accessed government resources (through legislative parties or directly with the president) remain unclear and deserve further research. Oil dependency also had negative effects on sustained budget cooperation. While politicians were willing to adopt legislation to ensure fiscal responsibility in the aftermath of an economic crisis at the end of the nineties, the rapid growth of oil revenues in the following years reversed incentives for fiscal austerity. In the context of high oil prices and in anticipation of an electoral year congress effectively eliminated spending constraints imposed by the FRL in 2005.

The migration of politicians to subnational governments and the eroding incentives for fiscal discipline during an oil bonanza are examples that illustrate the fickle nature of budget coalitions in Ecuador. Most importantly perhaps, they illustrate politicians' success at influencing the budget process despite institutional reforms aimed at depoliticizing the process. This permanent tension between changing budgetary rules and politicians' cooperation incentives has challenged the long-term sustainability of quality budget outcomes in Ecuador.

References

- Albornoz, Vicente et al. (2000), Gobierno Central, Autonomías y Finanzas Provinciales, Cuadernos de Descentralización, CORDES, Quito-Ecuador
- Alesina, A., Ricardo Hausmann, Rudolf Hommes and Ernesto Stein (1999). "Budget institutions and fiscal performance in Latin America." Journal of Development Economics **59**: 253-73.
- Alesina, Alberto and Perotti, Roberto (1999). "Budget Deficits and Budget Institutions" in *Fiscal Institutions and Fiscal Performance*. Jim Poterba and Jürgen von Hagen (eds.) Chicago: The University of Chicago Press.
- Almeida, María Dolores, Gallardo, Tomaselli 2005, Gobernabilidad Fiscal en Ecuador, mimeo, GTZ
- Araujo, Caridad. 1998. Gobernabilidad durante la crisis y políticas de Ajuste. Quito: CORDES-Konrad Adenauer Foundation and Spanish Cooperation.
- Arteta, Gustavo, and Osvaldo Hurtado. 2002. Political Economy of Ecuador. Quito: CORDES.
- Díaz Alvarado, Carlos, Alejandro Izquierdo and Ugo Panizza, Fiscal sustainability in emerging market countries with an application to Ecuador, Inter American Development Bank, Working Paper#511, August 2004
- Díaz Alvarado, I. a. P. (2004). Fiscal Sustainability in emerging market countries with an application to Ecuador. Washington DC, Inter American Development Bank.
- Elbers, Chris, Jean Lanjouw and Peter Lanjouw (2003), Micro--Level Estimation of Poverty and Inequality, *Econometrica* 71(1):355-364.
- Fernandez G. and Lara C., 1998. Los shocks exógenos y el crecimiento económico del Ecuador, Banco Central del Ecuador, Nota Técnica # 48.
- Gallardo Jorge 2001, Reforma Fiscal, mimeo, MEF
- Gibson, Edward L., and Ernesto Calvo. 2000. Federalism and Low-Maintenance Constituencies: Territorial Dimensions of Economic Reform in Argentina. *Studies in Comparative International Development* 35 (3):32.
- Hallerberg, M. and P. Marier (2004). "Executive Authority, the Personal Vote, and Budget Discipline in Latin American and Caribbean Countries." American Journal of Political Science **48**(3): 571.
- Hidalgo, José and Vicente Albornoz (2007), Las finanzas provinciales del gobierno central, Cuadernos de Descentralización, CORDES, Quito-Ecuador

Hurtado, Osvaldo 2006. Los costos del populismo, CORDES, Quito, Ecuador.

Jácome, Luis I. 2004. The Late 1990s Financial Crisis in Ecuador: Institutional Weaknesses, Fiscal Rigidities, and Financial Dollarization at Work: International Monetary Fund Working Paper # 04/12.

Jones, M. P. and S. P. Mainwaring (2003). "The Nationalization of Parties and Party Systems." Party Politics 9(2): 139-166.

Mateos, A. and M. Alcántara (1998). Los Diputados Ecuatorianos: Actitudes, Valores y Percepciones Políticas. Quito, Ecuador, Convenio del Gobierno del Ecuador - Banco Interamericano de Desarrollo.

Mejía Acosta, A. (2003). La Reección Legislativa en Ecuador: conexión electoral, carreras legislativas y partidos políticos (1979-2003). El legislador a examen. El debate sobre la reelección legislativa en México: una perspectiva histórica e institucional. F. F. Dworak. Mexico, Fondo de Cultura Económica.

Mejía Acosta, Andrés. (2006). Crafting Legislative Ghost Coalitions in Ecuador: Informal Institutions and Economic Reform in an Unlikely Case. In *Informal Institutions and Democracy: Lessons from Latin America.*, edited by G. Helmke and S. Levitsky: Johns Hopkins University Press.

Mejía Acosta, Andres, M. Caridad Araujo, Aníbal Pérez-Liñán, and Sebastián Saiegh. 2008. Veto Players, Fickle Institutions, and Low-Quality Policies: the Policymaking Process in Ecuador. In *Policymaking in Latin America : how politics shapes policies*, edited by E. Stein, M. Tommasi, C. Scartascini and P. T. Spiller. Washington, DC; Cambridge, MA: David Rockefeller Center for Latin American Studies. Harvard University Press.

Samuels, D. J. (2003). Ambition, Federalism, and Legislative Politics in Brazil. Cambridge; New York, Cambridge University Press.

Scartascini and Filc. (2004). Budget Institutions and Fiscal Outcomes. Ten years of inquiry on fiscal matters at the research department. Research Department 10th year anniversary conference. Washington DC, Inter-American Development Bank.

Scartascini, C. a. M. O. (2003). Political Institutions, Policy making processes and Policy outcomes: A guide to Theoretical Modules and possible Empirics, Latin American Research Network, IADB, Design Paper.

Scartascini, C., and Ernesto Stein (2004). The Bolivian Budget: A Year Long Bargaining Process. Washington DC, Inter-American Development Bank.

Snyder, R. and D. Samuels (2001). "Devaluing the vote in Latin America." Journal of Democracy 12(1).

Spiller, Pablo, and Mariano Tommasi. 2003. The Institutional Foundations of Public Policy: A Transactions Approach with Application to Argentina. *Journal of Law, Economics and Organization* Forthcoming.

Theodore M. Barnhill, Jr. and George Kopits, 2003. *Assessing Fiscal Sustainability under Uncertainty*, IMF Working Paper WP03/79.

World Bank and Inter American Development Bank. 2005. *Ecuador Public Expenditure Review*. Washington DC.

Datasets

Estudio de finanzas provinciales a nivel provincial (CORDES)

Indicators from OECD-IDB-WB Budget Survey Project

Monthly Statistical Information from the Central Bank of Ecuador

Development Data Platform time series data from the World Bank

Ecuador 1990 and 2001 poverty maps prepared by the World Bank

Ecuador 1990 and 2001 population censuses from Instituto Nacional de Estadística y Censos - INEC

Sistema Integrado de Indicadores Sociales del Ecuador SIISE, 2006