

# Debt and the 2009 National Government Budget

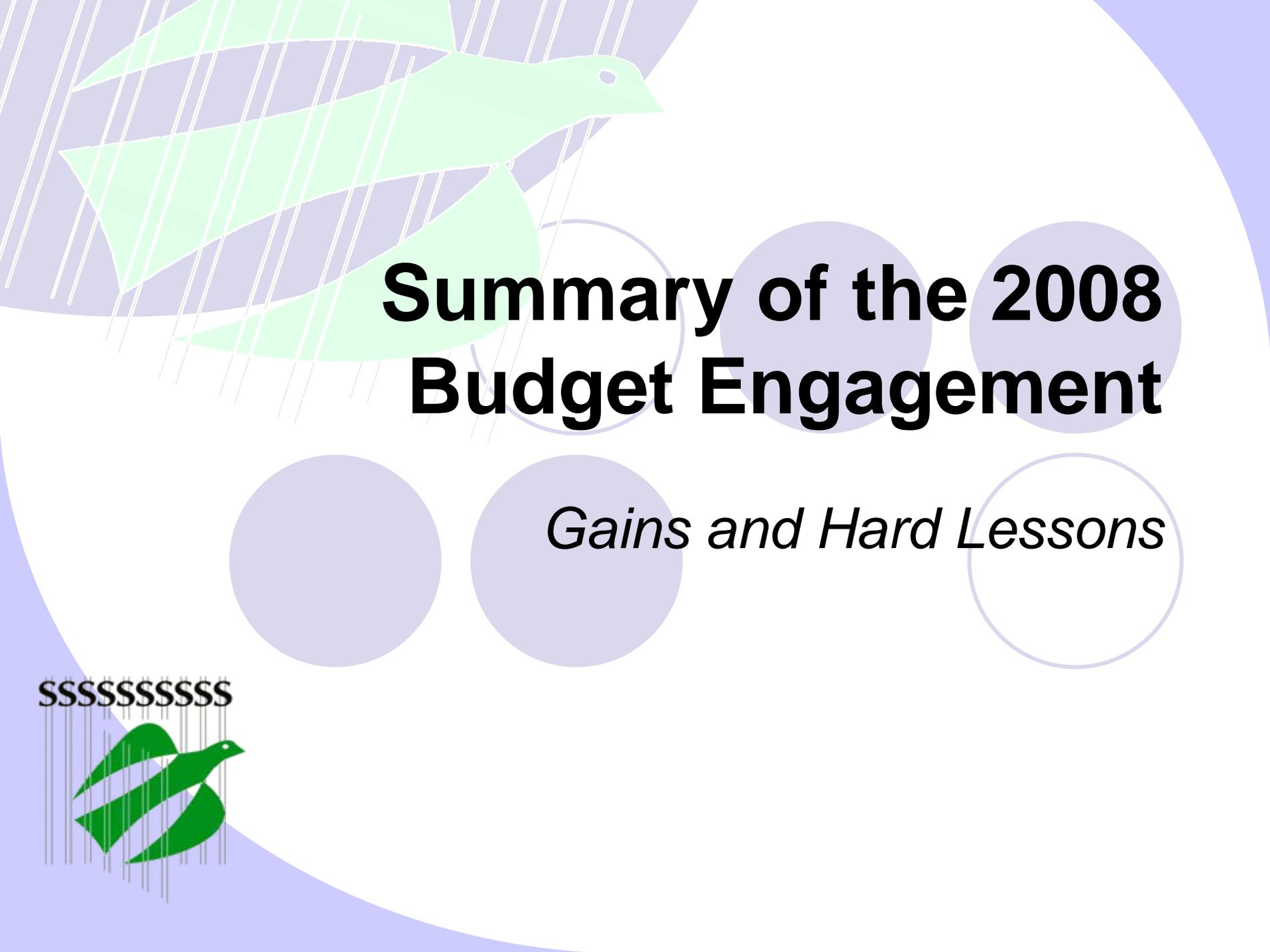
*Analysis and Recommendations*

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*Freedom from Debt Coalition*

House of Representatives  
September 30, 2008



# Summary of the 2008 Budget Engagement

*Gains and Hard Lessons*

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# Summary of 2008 Budget Engagement

- FDC's engagement of the 2008 National Government Budget in partnership with the 14th Congress as well as other social movements resulted in the passage of the said Appropriations Act with a special provision stating that *“no amount shall be used for the payment of interest payments on debts which are challenged as fraudulent, wasteful and/or useless.”*



# Summary of 2008 Budget Engagement

- The said provision is historical as the 14th Congress concurred that illegitimate debts/loan agreements do exist and are being serviced by the government as provided by our annual government budgets at the great prejudice of social spending.
- It is also widely seen as a step in the right direction in Congress' valiant attempt to re-assert its constitutional power of the purse.



# Summary of 2008 Budget Engagement

- Because of this, debt payments in the 2008 budget were drastically reduced by P 25.9 billion. It is comprised of:
  - P 5 billion worth of suspended interest payments to loan agreements challenged as fraudulent, wasteful and useless;
  - P 5 billion worth of premature payments to proposed loans still in the pipeline and;
  - P 15.9 billion savings due to a more realistic forecasting of the foreign-exchange rate.
- The said debt reduction was used as the primary alternative source of financing to accommodate civil society's alternative budget proposals on perennially neglected social services like education and health.

# Summary of 2008 Budget Engagement

- However, the said measures particularly the special provision suspending interest payments to dubious loan agreements were vetoed by President Gloria Macapagal Arroyo.
- President Arroyo in her 2008 Veto Message cited the non-violation of contract laws and the protection of the country's crediting-rating as pretexts for the said action.

# Summary of 2008 Budget Engagement

- Fortunately, the alternative allocations by civil society organizations which used the debt reduction as alternative sources of financing were not vetoed.
- However, the alternative budget is not entirely being funded.

# Hard Lessons: Executive Veto and the Failure to Override

- Lawmakers failed to override the veto despite repeated appeals from civil society groups.
- Unless the fiscal powers of the President is regulated and unless the institutional mechanisms that provide for automatic debt servicing is rescinded, any meaningful reform concerning debt reduction as well as the alternative reallocation of state resources in the budget will always be undercut by a powerful executive department.



# Hard Lessons: Executive Veto and the Failure to Override

- While immediate budget reforms such as alternative allocations are needed to effectively respond to the needs of the people, the best way to serve this purpose is for Congress to dismantle all the impediments resulting to a scarcity of democracy in the budget process and the diminution of Congress' Constitutional power of the purse.





# The 2009 National Government Budget

*Standing on Soft Grounds*

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# Same loans Congress suspended last year, still in the 2009 budget

- Unfortunately, the loans which interest payments for had been suspended by the House of Representatives and the Senate in this year's (2008) budget are still in the 2009 budget.
  - The 17 questionable loans we identified will still be paid for in 2009, with a total of \$63.99 million or P2.88 billion in interest payments.
  - Proposed loans doubled for 2009, amounting to \$237.74 million or P10.698 billion in interest payments.
- The total would be \$301.73 million or P13.57 billion.

# National Budget, US Financial Crunch, and the Domestic Economic Crisis

- The 2009 budget is set in a backdrop of converging domestic economic crisis and global financial crunch.
- Credit will be harder to access next year as foreign interest rates are expected to jack up, with the U.S. government set to borrow \$700 billion for financial bailout, and with foreign banks tightening credit in an effort to ward-off inflation.
  - National Treasurer Roberto Tan himself announced that DoF will be “pre-funding” its financial requirements last year, expecting a more inaccessible credit next year.
- Revenues may not go as strong as last year, with the declining price of oil and decreasing personal consumption.



# 2009 National Government Budget *(in billion pesos, dollars)*

Budget		<u>Revenues</u>	<u>Surplus / Deficit</u>
Interest Payments	Productive Expenditures		
<b>302.650</b>	1,112.35	1,393.34	<b>-21.664</b>
<b>6.726</b>	24.719	30.963	<b>-0.481</b>

- The Budget of Expenditures and Sources of Financing for 2009 lists a P1.415-trillion budget to be funded by P1.393 trillion revenues. In effect, we have a deficit of P21.66 billion.
- Of the P1.415-trillion budget, P302.650 billion will go for interest payments of outstanding debts.

# 2009 National Government Budget *(in billion pesos, dollars)*

<u>Expenditure</u>			<u>Revenues</u>	<u>Real Surplus / Deficit</u>
Off-budget	Budget			
Principal Amortization	Interest Payments	Productive Expenditures		
<b>378.866</b>	302.650	1,112.35	1,393.34	<b>-400.530</b>
<b>8.419</b>	6.726	24.719	30.963	<b>-8.901</b>

- However, the budget does not count the **Principal Amortization** for outstanding debt, which is pegged at P378.866 billion.
- This makes the real deficit to be at P400.53 billion pesos.

# 2009 National Government Budget *(in billion pesos, dollars)*

		<u>Expenditure</u>			<u>Revenues</u>
		Off-budget	Budget		
Gross Borrowings	Principal Amortization	Interest Payments	Productive Expenditures		
<b>437.086</b>	378.866	302.650	1,112.35	1,393.34	
<b>9.713</b>	8.419	6.726	24.719	30.963	

- To cover for the deficit, we are borrowing a total of P437.086 billion pesos. This is on a period of tightening global credit as the U.S. government borrows massively.

# 2009 National Government Budget *(in billion pesos, dollars)*

	Budget		<u>Revenues</u>	<u>Real Surplus / Deficit</u>
Net Borrowings	Interest Payments	Productive Expenditures		
58.22	302.650	1,112.35	1,393.34	-21.664
1.294	6.726	24.719	30.963	-0.481

- However, the “gross borrowings” does not go to pump-up the budget. It automatically goes to “rolling over” the payment made for the principal amortization.
- Whatever will be left will be the “net borrowings” which to be used to cover for the deficit.

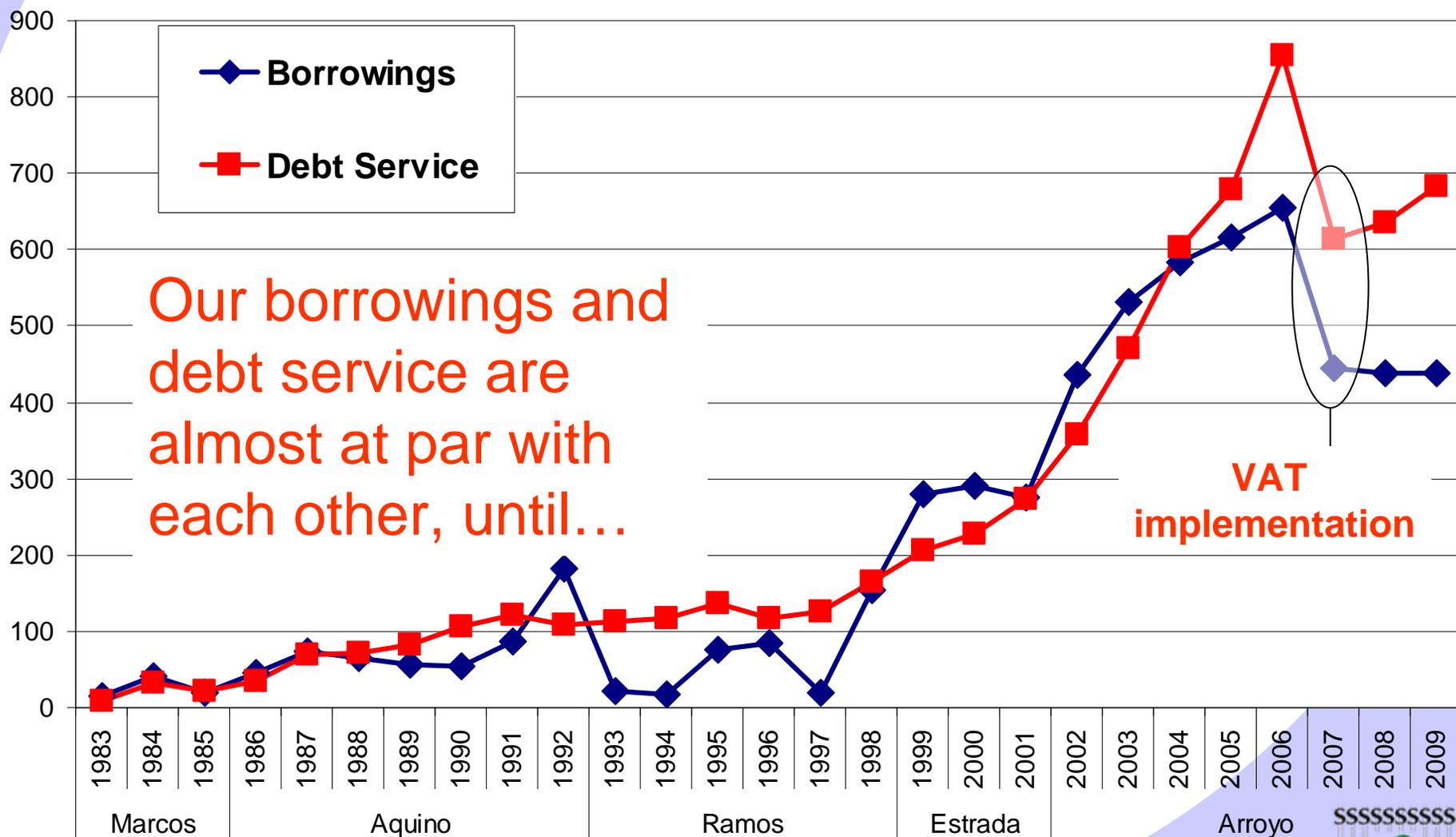
# 2009 National Government Budget *(in billion pesos, dollars)*

Budget		<u>Source of Financing</u>		<u>Excess Borrowings</u>
Interest Payments	Productive Expenditures	(plus) Net Borrowings		
302.650	1,112.35	58.22	1,393.34	<b>36.556</b>
6.726	24.719	1.294	30.963	<b>0.812</b>

- The “net borrowings” that will be used to cover the deficit will eventually be part of the sources of financing for the budget. Thus, we will have an excess borrowings of P36.556 billion.
- The problem is if the government fails to raise the P378.866 billion worth of borrowings, or if it does so at high interest rates, given the financial crunch. This can only result to more debts for the country.

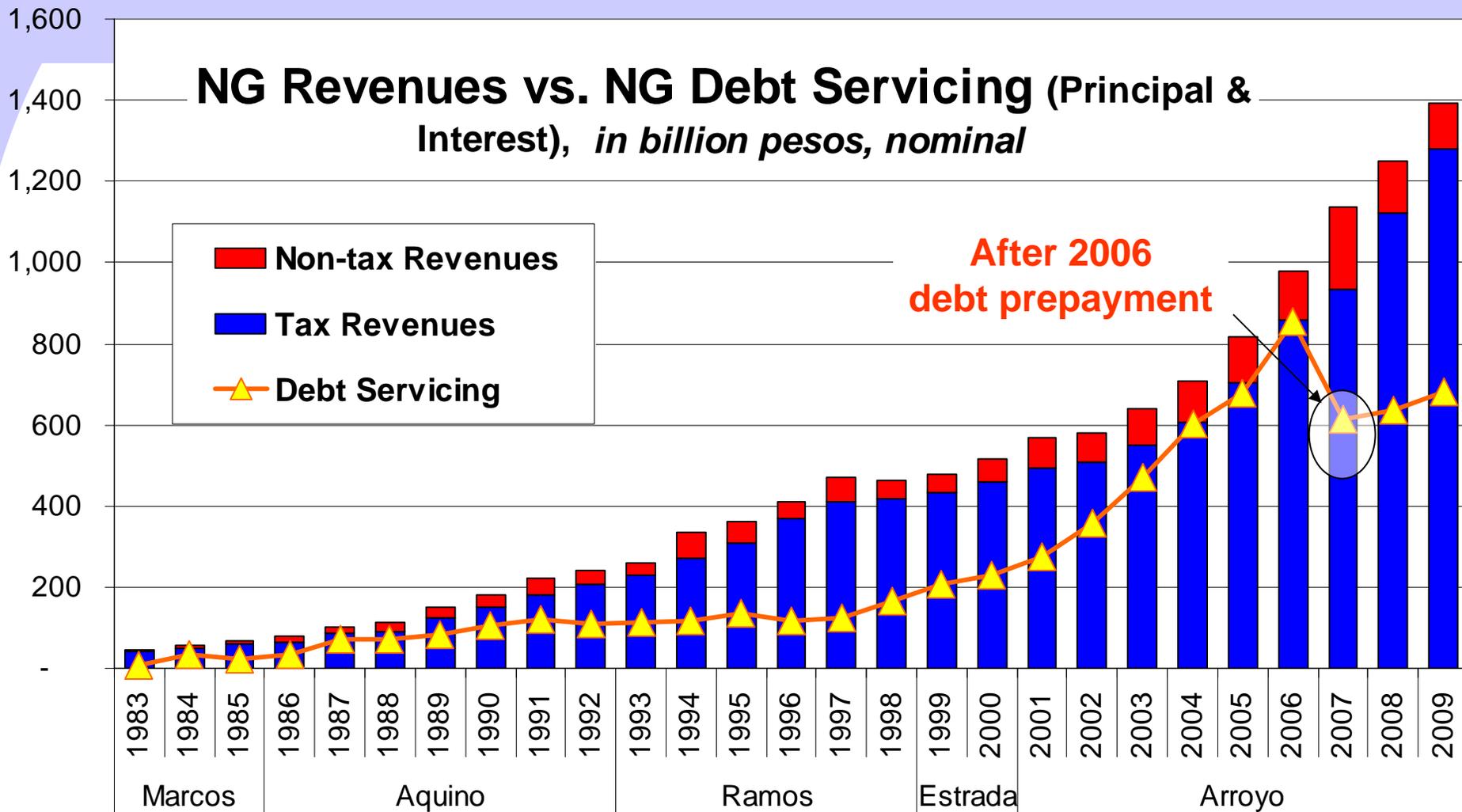


# National Government Borrowings, Debt Service (principal and interest) *in billion pesos, nominal*



# The Tax Crunch

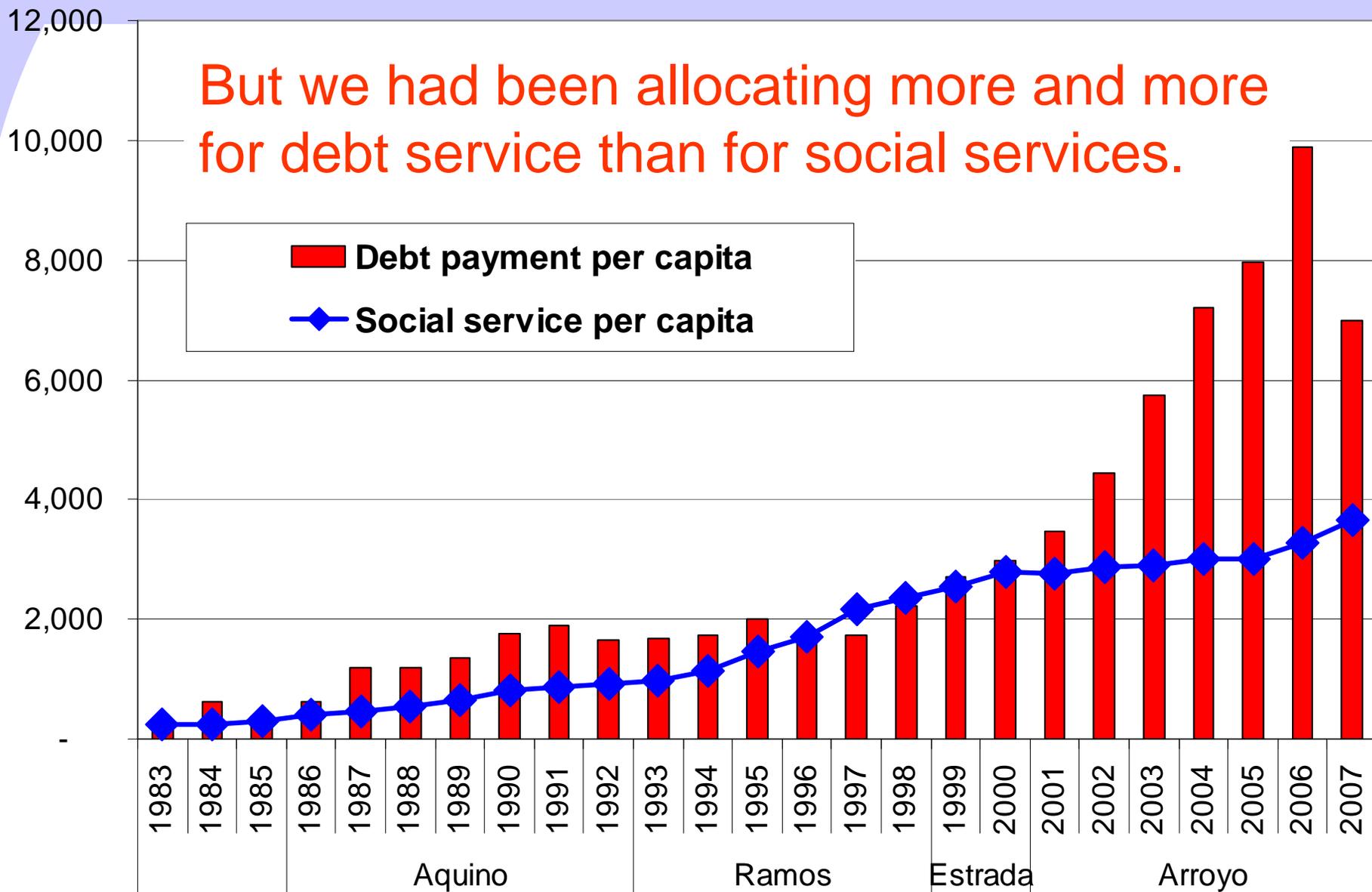
**NG Revenues vs. NG Debt Servicing (Principal & Interest), in billion pesos, nominal**



Large part of our taxes, including VAT, go to debt service.

# Debt per capita vs. Social Services per Capita *in pesos - nominal terms*

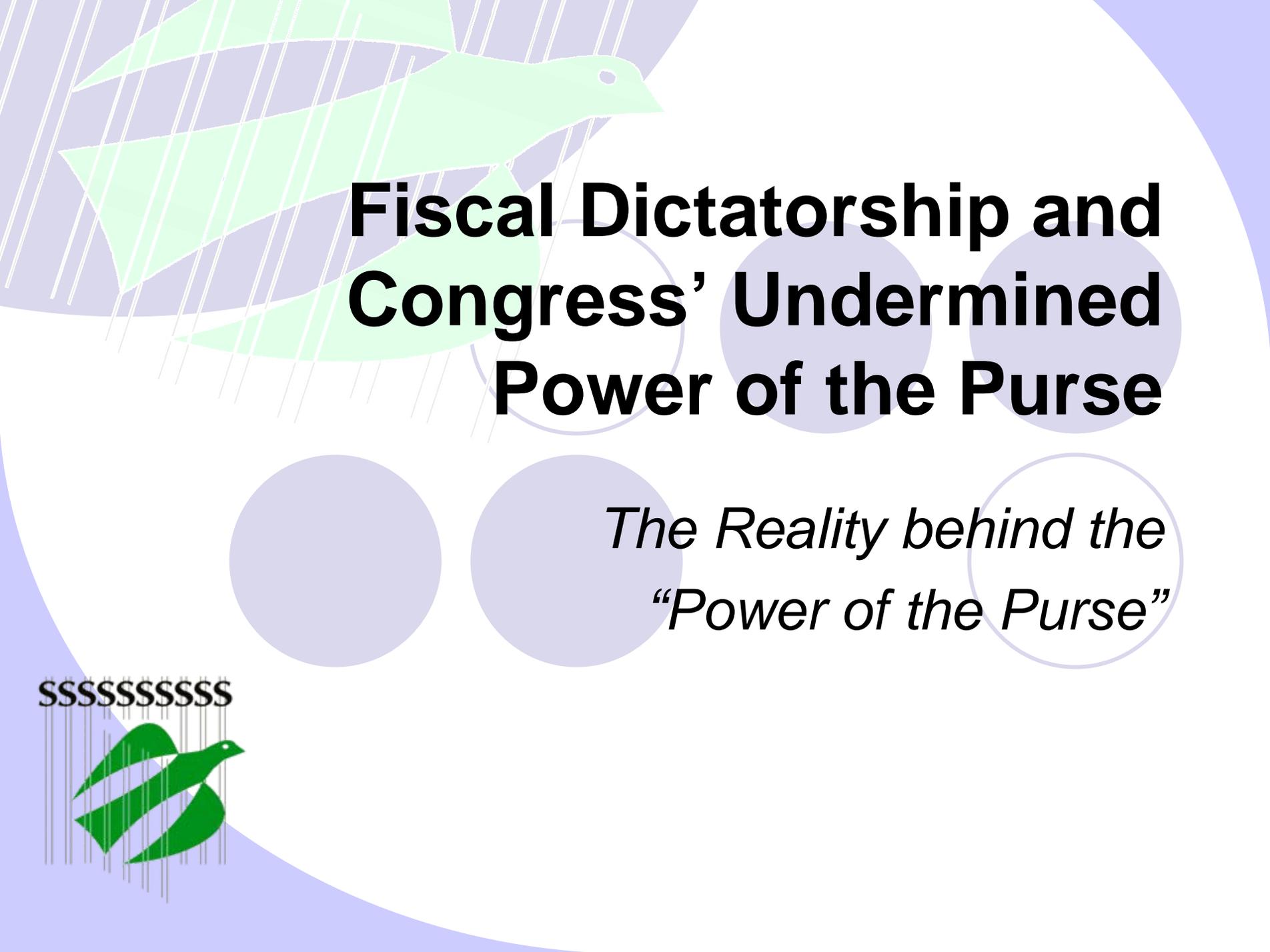
But we had been allocating more and more for debt service than for social services.



# Does the budget prepare us for the global financial crunch?

- **No.** We are still heavily dependent on the availability of foreign credit.
- We are still experiencing a massive financial hemorrhage because a large chunk of the debt we are paying are in dollars, and we are still paying for **illegitimate debts**.
- We are still not spending enough on social services to prepare our labor force to survive the crisis and meet the challenges in the future. Instead, **we are heavily taxing the people to pay for debts.**





# **Fiscal Dictatorship and Congress' Undermined Power of the Purse**

*The Reality behind the  
“Power of the Purse”*

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# Fiscal Dictatorship

- The 1987 Constitution accords the Congress “the power of the purse” as a testament of the principle of checks and balances, a divergence from the Marcosian authoritarian power over the budget.
- In practice, however, legal restrictions prevent the legislature from effectively exercising this power.
  - Ironically, most of these restrictions are inherited from a Marcosian statute – the Presidential Decree 1177 by Aquino’s Revised Administrative Code of 1987.
- The integrity of our budget institution as it stands is rendered highly vulnerable to rent-seeking prospects for an overtly powerful president.



# 1. The Power of Impoundment

- Contained in Section 38, Book VI of the 1987 Revised Administrative Code as derived from Section 43 of Presidential Decree 1177, the provision ensures that the President can refuse to allocate the money that had been appropriated by Congress.
- While the General Appropriations Act included prohibitions of impoundment in the General Provisions, the executive can always impound because of the constitutional guarantee of this power.
- The government wielded this power in order to “tame the deficit” and to reach fiscal balance, at the expense of its promised expenses.



## 2. The Power to Reallocate “Savings”

- Contained in Section 39, Book VI of the 1987 Revised Administrative Code as derived from Sections 44 and 45 of Presidential Decree 1177, this empowers the President to channel savings to cover deficits of other items in the budget.
- When the powers to impound and to reallocate savings are combined, it is tantamount to **a power to realign appropriations** itself.
- The power also incentivizes artificial generation of savings which can be reallocated elsewhere. For example, FDC already reported that the Arroyo administration had been borrowing more than it should, and reporting the excess as savings.



# 3. The Power to Line-Veto

- Contained in Article VI, Section 27(2) of the 1987 Constitution, which is similar to Article VIII, Section 20(2) of the 1973 Philippine Constitution, this guarantees the power of the executive to veto specific items of the budget while retaining the others.
- Since it is the executive which proposes the budget via the DBM, the executive can simply veto changes that had been made by Congress on the budget proposed by itself.
- While Congress can override the presidential veto as stipulated in the Article VI, Section 27(1) of the 1987 Constitution, the onus of ensuring that the budget they appropriated remains legislated is shifted back to the Congress.



## 4. The Power to Veto leading to a Reenacted Budget

- Contained in Article VI, Section 25(7) of the 1987 Constitution, which is similar to Article VIII, Section 16(6) of the 1973 Philippine Constitution, the provision shields the executive from exhaustion of funds should the Congress refuse to come up with the budget.
- Reenacted budgets allow the government to save money. The 2005 budget's reenactment allowed the Palace to save as much as P135 billion.
- The Arroyo administration operated under three budget reenactments during its seven-year term – in years 2001, 2004, 2006.



# 5. The Power to Unilaterally Contract Loans

- Contained in Article VII, Section 20 of the 1987 Constitution, which is Article IX, Section 15 of the 1973 Philippine Constitution
- Allows the presidency to raise as much money as (s)he can, using future revenue-generation capacity as collateral.
  - Loans are simply a tax levied on future generations, as they will be beholden to pay it later when the payments are due.
- There is a requirement to submit a Congressional report, but submission of a report is neither a request for Congressional approval, nor even a semblance of consultation.



# 6. The Automatic Debt Servicing

- Contained in Section 26(B), Book VI of the 1987 Revised Administrative Code, as copied en toto from Section 31(B) of Presidential Decree 1177,
- Responsible for the fact that for all post-EDSA governments, from 1986 to 2008, debt service for **interest payments alone already averaged around 25.72% of the national budget**, severely compromising the Congressional “power of the purse”.
  - Unfortunately, Congress cannot increase the budgetary ceiling (Article VI, Section 25(1)).
- The level of borrowings too, is effectively set by the amount of principal amortization to debts which are to be “rolled over”, since they are not part of the budget but instead deducted to new “financing” of the government.



# Consequences of an “Executive Budget”

- These provisions combine to create an executive-biased budget which concentrates all fiscal powers in the hands of the president.
- It directly impedes on the dictum of separation of powers and compromises checks and balances. Discretion lays the conditions for corruption.
  - While corruption may not actually happen, the suspicion alone that it can, withers away the confidence on the integrity of the budget process.
- It will also be more difficult to orient institutional responses to legitimate social interests. Centralization limits forward and bottom-up transmission of what social needs are and how they can be addressed.



# Fiscal Dictatorship = An Undermined Congress

- Because of an executive budget, the Legislature's constitutional power of the purse is gravely diminished.
- A concentrated fiscal power contributes in making political parties weak.
- The control of resources inevitably has impact to the development of political parties.
  - Because an incumbent President can cause the immediate release or delay of IRA, PDAF and other local funds.



## Recommendations

# ***Towards an Alternative Public Finance System***

- *The following measures are recommended, with the end view of democratizing the budget process and strengthening the budget institutions:*

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# I. Regulating Executive Powers

- Amending the Revised Administrative Code of 1987 as instituted by Executive Order 292, which includes the executive powers of impoundment (Section 38) and realignment of savings (Section 39).
- Amending the Foreign Borrowings Act of 1966 (as amended by PD 1939) and the Official Development Act of 1996 to place more Congressional limits and parameters on the unilateral contracting of loans,
- Legislating parameters for the line-veto and reenactment.



# The Executive and the Debt Malady

- Sec. 31(B) of Presidential Decree 1177 in Sec. 26(B), Book 6 of the Revised Administrative Code of 1987 ensures the automatic appropriation of payments for principal and interest on public debt
- The automatic appropriation for debt, on top of other automatic appropriations, severely compromise the Congressional “power of the purse” since only a little amount of the budget is left for Congressional reallocation **as Congress cannot increase the budgetary ceiling** (Article VI, Section 25(1)). The level of borrowings too, is effectively set by the amount of principal amortization to debts which are to be “rolled over”, since they are not part of the budget but instead deducted to new “financing” of the government.



# Arguments against the Congressional “Power of the Purse”

- A critique of the strong Congressional powers on the budget is that it compromise the methodological rigor and rationality with which the budget and planning departments developed the national budget.
  - Unnecessary realignments and insertions, increases on projects or cuts that would make them unviable
- However, the current system does not provide venue for a more rational intervention on the part of the legislator.

## II. Redefining the Congressional “Power of the Purse”

- The “*power of the purse*” need not be compartmentalized to the “*budget legislation*” phase alone. In fact, the “power of the purse” can be more effectively and rationally exercised during the budget planning stage.
- Congressional intervention can happen in the start, rather than in the end, of the process – allowing for more strategic and “big picture” adjustments by the executive without encroaching Congressional “power of the purse”.

# III. Institute policies towards “Participatory Budgeting”

- The budget agency must be reoriented from an agency that simply budgets for the needs of the bureaucracy and the economy, to a one that facilitates people’s direct participation.
- **We must institutionalize grassroots people’s participation and involvement in all stages (proposal, legislation, authorization, evaluation) and levels (agency-level, region-level, etc.) of budget development by decentralizing budget decision-making.**

*The task of democratizing the budget process, of reclaiming Congress' power of the purse, and of freeing it from the burden of automatic debt servicing must begin with the institutionalization of necessary reforms to change the current public finance system.*

***Without doing so, would only repeat the sins of the past in unparalleled proportions.***



# Thank you.

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