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Fiscal equalisation in Brazil, Canada and Australia

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As federative countries, Brazil, Canada and Australia follow distinct fiscal equalisation models in the interrelationships between federal and state or provincial governments to provide satisfactory public services. These models address features of supply or revenue (administrative structure and tax collection) and demand or expenditure (the cost of public services and social needs), seeking to reduce vertical and horizontal distortions in fiscal capacities across various levels of government.

Six essential elements make up a fiscal equalisation model (Shah 2017):

1. Source of funding: total federal government revenue (Canada); taxes on goods and services (Australia); and taxes on income and industrial products (Brazil).
2. Extent of equalisation: level of public services offered and fiscal capacity (Australia and Canada); and constitutional principles on states' socioeconomic conditions (Brazil).
3. Format of transfers: carried out by the federal government (Canada, Australia and Brazil).
4. Programme design based on: revenue of provinces (Canada); fiscal capacity, social needs and cost of providing public services (Australia); and states' populations and per capita household income (Brazil);
5. Governance structure: the federal government defines the equalisation formula, with provincial (Canada) and exclusive (Brazil) participation, and via the Commonwealth Grants Commission (Australia).
6. Legal arrangements: constitutional and unconditional (Canada and Brazil), and non-constitutional and conditional (Australia) requirements.

The Australian model is more institutionally centralised, legally flexible and broad in design (ibid.), while the Canadian model is more decentralised, rigid, and restricted (Béland et al. 2017). The presence of institutions comprising the various levels of government in the management of the model is decisive in both cases. The Brazilian model lies in the middle, as it adopts specific demand criteria (income and population) like the Australian model, but it does not address the supply criteria considered in both cases.

The main instrument for the fiscal equalisation of Brazilian states is the State Participation Fund (*Fundo de Participação dos Estados*—FPE), with clear constitutional guidelines. However, the legal and methodological criteria adopted are insufficient in light of fiscal (supply) or socioeconomic (demand) outcomes. Mendes (2022) subdivides Brazilian states into four distinct categories regarding the national average per capita household income (USD268.93) and population (7.9 million inhabitants): higher population and income (category 1), lower population and income (category 2); lower population and higher income (category 3) and higher population and lower income (category 4). Categories 1 and 2 (in opposition to each other) depict the traditional socioeconomic differences between the wealthiest states in the Southeast and South regions and the poorest states in the North and Northeast regions of the country. Categories 3 and 4 are intermediate, mainly comprising all states in the Centre-west region.

The deficiency of states' own and available revenues demonstrates that the FPE is not enough to fulfil their social needs, although it supplements their fiscal capacities. Moreover, this deficiency reflects the distinct productive and administrative structures between states. Finally, if population equity is not a goal, then the household income index does not fully compensate for states' fiscal capacities, given its high volatility and structural inequalities between states.

Thus, a proposal for an adjustment of the Brazilian equalisation model should include: boosting the basis of transferable fiscal resources; building a more flexible legal framework; designing broad supply and demand criteria; establishing clear equalisation goals; and developing institutions for federative governance.

As in Canada and Australia, an ideal equalisation model should feature a systemic view of fiscal capacities and social needs. This view is particularly important for Brazil, considering the significant heterogeneities and inequalities in the socio-economic structures of the country's 26 states, substantial transfer distortions and different impacts of other types of resource transfers to states, such as discretionary transfers and sectoral funds (health care and education).

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