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Death of the Partisan? Globalization and Taxation in South America, 1990–2006

Austin Hart[1]

Abstract

Correcting the relative lack of attention to the revenue side of public finance, this article examines to what extent globalization constrains partisan tax policy. The author hypothesizes that political ideology is still a good predictor of taxation in the neoliberal era, advancing this argument against the prominent globalization thesis: that global economic pressures have supplanted political ideology as the driving force of revenue policy. Although research in developed democracies identifies a resilient link between partisanship and policy outcomes, the impact of the drastic neoliberal transition on partisan policy making in the developing world remains poorly understood. Using time-series cross-section data to evaluate partisan taxation in South America, the author finds that partisanship is a reliable indicator of tax revenue in the neoliberal era. Counterintuitively, however, the promarket Right generates more tax revenue than the interventionist Left. The author argues that this previously unexpected revenue gap is driven by ideological concerns for equity versus growth.

Keywords

taxation, globalization, partisanship, South America, neoliberal reform

[1]University of Texas at Austin

Corresponding Author:
Austin Hart, University of Texas at Austin, 1 University Station A1800, Austin, TX 78712
Email: austinhart.ut@gmail.com

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In examining economic policy following South America's sudden and dramatic shift to the market, a number of scholars argue that international economic forces, rather than domestic political agents, drive policy outcomes. These globalization theorists argue that the need to attract and retain highly mobile capital impels politicians to pursue the policy preferences of the market rather than the electoral mandates of constituents. Building on older theories of dependency, convergence scholars in this tradition posit that the competition for global capital drives economic policy toward a narrowly defined neoliberal ideal (Appel, 2006; Dupuy, 1998). The absence of convergence in the postreform era, however, led globalization theorists to eschew this race-to-the-bottom thesis, arguing instead that persistent economic policy variation reflects the evolving balance of power between fundamentally heterogeneous economic actors (notably Cohen, 1998; Frieden, 1991; Garrett & Lange, 1991; Kingstone & Young, 2008; Santiso, 2005; Strange, 1996). Even in light of the "pluralization" of global economic forces, however, the empirical implication of the globalization thesis for domestic partisans remains unchanged. If policy decisions in the neoliberal era are merely responses to international market pressures, the ideology of a country's ruling party should be a poor predictor of future policy outcomes.

Yet despite the rising specter of mobile capital and the wavelike advance of the neoliberal model, a substantial body of research in advanced industrialized democracies finds that global economic forces have not dwarfed partisan dynamics (in particular, Alesina & Rosenthal, 1995; Boix, 1998; Garrett, 1998; Maxfield, 1998). Even in the neoliberal era, the election of an ideologically rightist party, for example, signals a desire among voters for less intervention in the economy and greater reliance on market-based mechanisms of resource allocation, a desire that should be reflected in the policy efforts of reelection-minded candidates (Stevenson, 2001). The generalizability of these findings to South America remains unclear, however, particularly in the wake of the region's simultaneous transition to democracy and the market.

South American governments on both the Right and the Left initiated dramatic shifts to the neoliberal economic model. This led a number of researchers to conclude that elected officials carried out "reform by surprise"—advocating a particular policy agenda during their campaigns and implementing quite another once in office (Dominguez, 1998; O'Donnell, 1994; Stokes, 2001). That parties traditionally known for state expansion adopted draconian, orthodox reforms suggests that partisan cues are no longer reliable indicators of economic policy outcomes.

Furthermore, the speed and severity of South America's neoliberal transition disarticulated the traditional constituencies of leftist parties. Although

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economic liberalization strengthened the Left–labor link in Organisation for Economic Co-operation and Development (OECD) countries (Garrett, 1998), the retrenchment of the state and the dissolution of corporatist structures of interest representation in South America weakened labor's influence over economic policy (Kurtz, 2004; Roberts, in press; Ryan, 2001). In combination with the erosion of economic barriers and the ability of capital to exit "unfriendly" markets, there is legitimate concern that global economic pressures have supplanted ideology as the driving force of economic policy in postreform South America.

Yet despite its conventionality, relatively few empirical evaluations of the argument that neoliberalism stifles partisanship exist outside the OECD context. Interestingly, this small, but rapidly growing, body of literature indicates that globalization's constraint on policy makers in the developing world varies substantially across policy arenas.[1] This finding not only highlights the multifaceted nature of globalization but also demonstrates the need for additional policy-specific, rather than comprehensive, examinations of the globalization thesis. As such, this research aims to assess the extent to which neoliberal reforms and market integration constrain partisan tax policy. Specifically, has economic liberalization eliminated the partisan divide over taxation, or do parties continue to implement distinct, partisan-motivated revenue polices?

I focus on the revenue side of public finance, first, because it offers a difficult test for critics of the globalization hypothesis. Global capital owners are affected both directly and indirectly by the magnitude and distribution of domestic tax burdens. Highly progressive tax burdens, a narrow tax base, and heavy reliance on non-neutral forms of taxation all create disincentives for capital entry and incentives for capital flight. As a result, politicians face strong pressures to alter the tax system in accordance with the demands of the international market. Second, taxation remains a vital, yet understudied, component of public finance. States that are unable or unwilling to finance their own expenditures must either reduce spending or plunge into fiscal imbalance. Finally, an analysis of resource extraction, rather than distribution, offers unique insights into the strength and reach of the neoliberal state and its evolving relationship with both business and societal constituencies.

Contrary to the conventional wisdom of the globalization thesis, I hypothesize that political ideology is still a good predictor of tax revenue in the postreform developing world. Although global capital is not bereft of policy influence, partisans continue to alter the magnitude and distribution of the domestic tax burden in ideologically consistent ways. Counterintuitively, however, I argue that the conventionally hypothesized partisan divide over taxation has been reversed in South America's neoliberal era.[2] Specifically, the interventionist

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Left collects less tax revenue than the pro-market Right. I contend that this revenue gap is driven by competing ideological preferences for growth versus equity. To stimulate economic growth, policy makers on the Right augment tax hauls by deemphasizing the corporate income tax in favor of the more efficient value-added tax (VAT), the cornerstone of the neoliberal tax system. This signals fiscal stability and encourages long-term direct investment. Conversely, I argue that the Left limits reliance on regressive consumption taxes, including the VAT, as a means of softening the burden levied on lower classes. Forgoing the revenue-generating capacity of the VAT in favor of a progressive, but hard to collect, personal income tax, however, restricts tax takes to levels much lower than previously expected, particularly with respect to the Right. To test these arguments empirically, I conduct a cross-sectional time-series analysis of the relationship among market integration, domestic partisanship, and tax revenue in South America from 1990 to 2006. These results are supported by additional analysis of domestic tax rates.

Market Liberalization and Revenue Extraction

The wave of market reforms that swept across the developing world in the 1980s and 1990s led a number of early globalization theorists to predict that regional economic policy would converge at the lowest common denominator regardless of domestic partisanship (Dupuy, 1998). These convergence scholars suggest that regional policy harmonization occurs via two separate but complementary mechanisms. First, states are forced to lower capital restrictions and offer substantial fiscal incentives to attract new inflows of foreign capital. Although resistance to the market is an option for policy makers, the cost of noncompliance is severe: States that refuse to compete for foreign investors are left to stagnate economically while neighboring countries prosper. Second, as states become increasingly dependent on the growing supply of mobile capital, the threat of capital exit impels partisans to kowtow to the demands of the markets.

This "race-to-the-bottom" logic extends easily to the issue of taxation in South America. To attract much needed foreign capital, policy makers across the region will lower marginal corporate and personal income tax rates for the highest income brackets. Second, as global economic forces gain domestic political power, states will deemphasize commercial and financial transaction taxes to promote economic activity and limit intervention that could incite capital flight. Together, these changes in the distribution of the tax burden and the verticality of the marginal rate structure should depress domestic tax

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revenue. As such, the convergence thesis suggests a negative relationship between market liberalization and domestic tax revenue, regardless of the party in power.

This basic logic of the race-to-the-bottom thesis, however, fundamentally mischaracterizes both the neoliberal tax regime and the preferences of international economic actors in the postreform era. Although it is true that South America's declining marginal corporate and personal income tax rates could reduce tax revenue, the general system of taxation adopted alongside the broader package of neoliberal reform is designed to capitalize on the complexities of a liberalized marketplace. These new institutions aim to promote a simple tax code and a more efficient tax administration. The increased reliance on consumption-based taxation, primarily the VAT, has expanded the tax base and made tax collection easier and more efficient (Mahon, 2004; Tanzi, 2000). In a globalized market that places a premium on fiscal stability and extraction capacity, there is little reason to expect overall tax revenue to decrease as a result of international pressure. In fact, regional trends in tax revenue demonstrate quite the opposite: Tax hauls in South America have increased dramatically in the wake of the neoliberal transition (Bird, 1992; Mahon, 2004; Morley, Machado, & Pettinato, 1999; Tanzi, 2000).

Despite this rebuttal of the assertion that tax revenue and market liberalization are negatively related, the capacity of partisans to pursue ideologically motivated economic policy in the postreform era remains unclear. Even if policy makers are not racing to the bottom, the absence of downward harmonization does not necessarily imply the assertion of domestic partisanship. As Figure 1 demonstrates, revenue policy in South America has converged toward a neoliberal ideal, albeit an ideal point distinct from that conceived of by early globalization theorists. Charting the regional mean and variance of the tax reform index created by Morley et al. (1999) from 1972 to 2000, these data indicate, first, that even in the aftermath of dramatic stabilization measures, policy makers across the region continue to pursue and implement "market-friendly" revenue policies. Marginal tax rates have been lowered, and less reliance has been placed on direct, non-neutral forms of taxation. Second, looking at the dashed line, it is clear that cross-national policy variance is waning.[3]

Although suggestive of the movement toward a broadly defined neoliberal tax paradigm, this regional trend conceals important and persistent variation in the magnitude and, in particular, the distribution of domestic tax burdens. Eschewing the race-to-the-bottom logic of global capital, globalization theorists increasingly argue that these differences are driven by the variable policy preferences of heterogeneous international actors. International financial institutions (IFIs), for example, pressure policy makers to balance their

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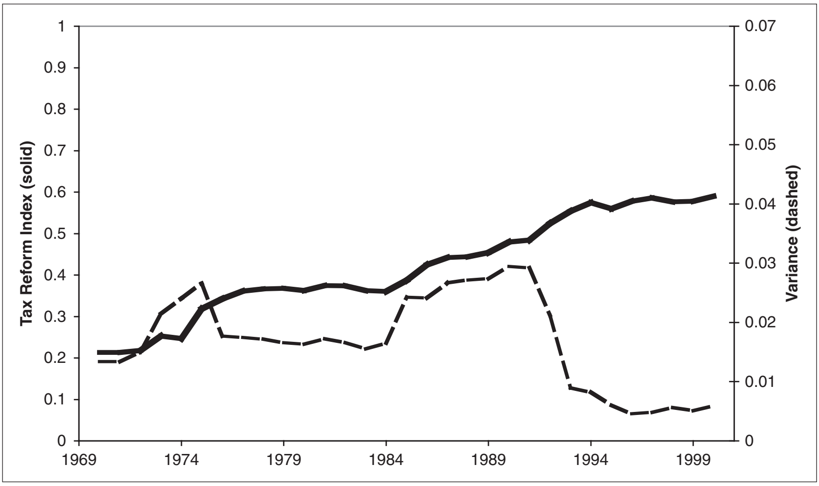

Figure 1. Neoliberal tax reform in South America,, 1970–2000
Note: Data are from Morley, Machado, and Pettinato (1999).

finances by increasing the magnitude of the tax burden but may be less concerned with its distribution.[4] Alternatively, capital owners have more distinct preferences regarding the burden's distribution. Based on their short time horizon, portfolio investors focus their policy efforts on shifting the tax burden away from corporations rather than shoring up fiscal deficits. And although multinational corporations (MNCs) also place downward pressure on the corporate tax burden, their relative lack of mobility motivates additional long-term concerns. To promote a stable, yet robust, business environment, MNCs pressure states to promote tax neutrality by emphasizing VAT revenue.

Despite the pluralization of global economic forces, however, the implication is that policy changes in the neoliberal era reflect the evolving balance of power between capital owners rather than domestic partisans (Kingstone & Young, 2008). As such, the globalization thesis suggests that the ideological divide between Left and Right has been eroded under the weight of variable international pressures. Parties on all sides of the ideological spectrum suffer these constraints, but although the Right may be limited in its capacity to promote economic activity via tax incentives, it is the Left that faces disproportionately high restrictions. To appease international creditors without compromising stocks or flows of foreign direct investment (FDI), it is assumed that governments on the Left must increase tax revenue through regressive, consumption-based forms of taxation. This presents the Left with

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an unpalatable dilemma: cut social spending or extract more revenue from low- and middle-class urban citizens.[5] As a result, it is unclear that parties on the Left will continue to generate more tax revenue than the Right.

Although the conventional wisdom of the globalization thesis thus suggests that the ideologically based divide between Left and Right is not analytically meaningful in the postreform era, I argue that rumors of the "death of the partisan" have been greatly exaggerated. Despite the broad convergence of tax institutions and the policy pressures of heterogeneous capital owners, partisans retain the latitude to pursue distinct, ideologically motivated revenue policy without inciting capital flight. In other words, parties will continue to distinguish themselves in empirically predictable ways. I develop this argument in the next section.

Partisan Assertion Under International Constraint

Partisan preference for taxation is driven by deeply rooted beliefs about the economic purpose of the state and its limitations in the public sphere. It has long been assumed that leftist parties across the developed and developing world prefer a large, interventionist state and extract high levels of tax revenue to finance generous, equity-oriented welfare programs. Alternatively, political parties on the Right favor state retrenchment, collecting fewer taxes to promote private business and stimulate economic growth.[6] The strength of the relationship between a policy maker's partisan identification and behavior in office in the developing world, however, has come into question in the neoliberal era.

Despite the conventionality of the arguments discussed above about the erosion of partisan tax policy under the weight of market forces, this assessment is far from unanimous. Outside of the substantial literature on advanced industrialized democracies (notably Boix, 1998; Garrett, 2001; Swank, 2002), a number of scholars contend that partisan policy makers in the developing world remain resilient. Although international economic forces are not powerless, this growing body of research finds that the extent of globalization's constraint on partisans varies dramatically across policy arenas (e.g., Avelino, Brown, & Hunter, 2005; Murillo, 2005; Murillo & Schrank, 2005; Mosley, 2003, Mosley & Uno, 2007; Wibbels & Arce, 2003). These diverse findings highlight the multifaceted nature of globalization and underscore the need for additional policy specific research.

Until recently, the extant literature exploring the impact of international economic pressure on partisan policy making in South America addressed

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the causes rather than the effects of neoliberal restructuring (see, e.g., Haggard & Kaufman, 1995; Weyland, 2002). Although this endeavor engendered a wide and productive debate over the political and economic factors motivating the sudden adoption of orthodox economic reform, theories of dramatic change offer little explanatory power in South America's current period of relative stability. As a result, this literature provides few insights into the dynamics of taxation in the postreform era. The recent "second wave" of research on partisanship and market reform moves beyond the question of why the developing world adopted neoliberal reforms and attempts to explain cross-country heterogeneity in the degree of liberalization (e.g., Biglaiser & Brown, 2003, 2005; Nielson, 2003). The majority of research on taxation falls into this category, analyzing structural reform indices such as the one displayed in Figure 1 (Johnson & Crisp, 2003; Kingstone & Young, 2008; Mahon, 2004). Because this literature considers the evolution of orthodoxy over a longer period of time, it provides valuable theoretical leverage on the extent of revenue policy constraint in the neoliberal era. Johnson and Crisp (2003), for example, find that legislative partisanship, but not presidential partisanship, is an effective predictor of the degree of structural reform in the neoliberal era. Thus, voters are able to rely on a party's ideological reputation to discriminate between legislative candidates and predict revenue policy outcomes. Although these arguments are suggestive, I contend that research on structural reform underestimates the reliability of partisan cues as predictors of postreform policy outcomes.

Despite the constraints of neoliberalism, I do not expect political parties on the Right or Left to simply reject their historically embedded and ideologically motivated policy-making reputations. Given the nature of the neoliberal tax paradigm, however, this leads to a counterintuitive theoretical expectation: The interventionist Left will collect *less* tax revenue than the retrenched Right.

First, I contend that parties on the Right, in making a credible commitment to the "Washington Consensus," are more likely to embrace the neoliberal tax system than parties on the Left. To enhance fiscal rectitude, rightist policy makers will increase the magnitude of the tax burden. Though previously unexpected, this signal of stability to international markets in general, and debt markets in particular, complements the economic goals of the Right by augmenting credit ratings and thus promoting economic activity. So as not to stymie FDI, however, I argue that the Right will simultaneously promote tax neutrality by emphasizing the VAT and flattening income tax rates. Reductions in the verticality of the rate structure will appeal to MNCs and mobile subcontractors but will not shore up fiscal deficits. The broad-based VAT, on the other hand,

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not only is cheaper and easier to collect than direct forms of taxation but also is a neutral, or nondistortionary, tax in that it affects all economic sectors equally. In this way, the neoliberal tax system offers the Right an opportunity to promote economic growth by generating high levels of tax revenue efficiently and neutrally.

Although counterintuitive, the argument that the Right will increase tax revenue is certainly not without empirical merit. During Álvaro Uribe's first term in office, for instance, the rightist Colombian president twice increased the VAT rate on food as a means of increasing tax revenue to eliminate budget deficits. This reform signaled Uribe's commitment to both fiscal stability and tax neutrality.

Alternatively, I argue that the Left will reduce the amount of tax revenue it generates because of its aversion to the regressive, but highly efficient, VAT. To reduce the tax burden levied against the poor and lower middle class, the Left will deemphasize VAT revenue by limiting tax rates. In 2007, and in contrast to his Colombian counterpart, Ecuadorian president Rafael Correa of the leftist Alianza PAIS passed a tax reform that reduced the nation's VAT rate 2 points to 10%. Under the watchful eye of bond traders and mobile investors who may be wary of leftist control (Campello, 2007), partisans can neither disregard the highly touted VAT nor recover the lost revenue through progressive corporate taxes. As Mosley (2003) suggests, however, policy makers in the developing world maintain a level of latitude in choosing what types of domestic taxes to levy. Thus, I argue that the Left will aggressively reduce corporate tax rates to appease investors while, at the same time, maintaining a more progressive personal income tax structure than the Right. This policy combination may satisfy creditors and domestic constituents, but it underutilizes the revenue generating capacity of the VAT. As a result, the interventionist Left will actually generate less tax revenue than the promarket Right.

In this way, I expect partisanship to be a reliable indicator of domestic tax revenue, but the political incentives created in the postreform era lead to an unexpected outcome. This suggests the following hypotheses:

Hypothesis 1: The political ideology of the ruling party will be a good predictor of the magnitude and distribution of the tax burden in the neoliberal era.

Hypothesis 2: Leftist governments will generate less tax revenue than their counterparts on the Right.

Hypothesis 3: Leftist governments will rely less on revenue generated by regressive consumption taxes than rightist governments.

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Research Design and Method

The following analysis focuses on the relative impact of domestic politics and global economic integration on taxation in South America. I focus on South America as opposed to other regions of the developing world in part because the speed and depth of the region's neoliberal transition suggest that international market forces should be extremely powerful relative to the region's partisans. Thus, the South American case provides a difficult test for any critic of the globalization thesis. I also choose to focus on South America because the relative homogeneity of political institutions in the region facilitates effective analysis of the impact of presidential and legislative partisanship on tax hauls. Finally, limiting the analysis to South America allows for greater control on cultural and historical characteristics that, although potentially important, are difficult to observe and measure.

To evaluate the globalization thesis against the hypotheses presented here, I conduct a cross-sectional time-series analysis of both the magnitude and the distribution of the domestic tax burden across the countries of South America from 1990 to 2006.[7] Consistent with existing literature on taxation, I focus on the tax burden, defined as tax revenue, rather than tax rates because income exclusions, investment incentives, and high rates of tax evasion make rates unreliable indicators of actual tax burdens (Inclán, Quinn, & Shapiro, 2001; Wibbels & Arce, 2003). Because tax rates convey important information regarding possible policy measures taken to alter the tax burden, however, I supplement the regression analysis with an examination of the bivariate correlation between tax rates and partisan control.

The regression analysis proceeds in two sections. The first evaluates Hypotheses 1 and 2 using total tax revenue as a percentage of gross domestic product (GDP, current local currency unit [LCU]) as the dependent variable.[8] This includes all revenue collected through taxation minus revenue generated by social security taxes. I exclude social security taxes because they are shaped largely by demographic factors (e.g., the size of the working-age population). In addition, the cross-national variation in social security tax revenue may inflate the apparent strength of otherwise weak states or, for states that collect very few social security taxes, understate tax collection. The findings from the model of total tax revenue will highlight the relative influence of both partisans and global economic actors in shaping the magnitude of the domestic tax burden in South America's neoliberal era.

The second stage of the analysis evaluates Hypothesis 3, that parties on the Left will shift the distribution of tax revenue away from regressive consumption taxes. I do so by reestimating the model of total tax revenue for six different types of tax revenue: VAT and sales tax, total income tax, property

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tax, commercial and financial transaction tax, and personal income tax. I estimate the model for personal income tax measured as a percentage of total income tax revenue because it permits a more detailed analysis of the distribution of the income tax burden between individuals and corporations.[9] Examining the results for these six taxes independently, rather than constructing a broad indicator, will elucidate the heterogeneous preferences of global economic actors and the capacity of partisans to redistribute the tax burden in an ideologically consistent manner.

To enhance comparability, these dependent variables, with the exception of personal income tax, are calculated as a percentage of total tax revenue rather than as a percentage of GDP. Using GDP to standardize these dependent variables would provide additional information regarding only the absolute magnitude of tax hauls. The total tax revenue transformation, on the other hand, increases variation on the dependent variable and facilitates interpretation regarding actors' differential preferences over specific types of taxation.

To evaluate the relationship between economic liberalization and tax revenue, I include six measures of market integration in the model: trade dependence, FDI stock, FDI flows, portfolio investment, capital account openness, and multilateral debt. Trade dependence, measured as the total value of exports plus imports as a percentage of GDP, captures the domestic power of internationally competitive sectors. The two FDI variables, calculated as a percentage of GDP, are introduced as a means of assessing the policy impact of relatively long-run capital owners while also controlling for the potential policy implications of volatile FDI inflows. To highlight the impact of highly mobile, short-term capital, I also include a variable for portfolio (the sum of bond and equity) investment in the model.[10]

A measure of capital flows, however, may not capture effectively the manner in which capital owners exert their influence over domestic policy (Frankel, 1993). Specifically, capital owners rely on the threat of exit, rather than actually exiting, to apply policy pressure. The efficacy of this pressure is enhanced as the level of financial openness increases. As a result, I include the Chinn–Ito index of capital account openness. This measure is calculated based on the dummy variables that codify the tabulation of restrictions on cross-border financial transactions reported in the International Monetary Fund (IMF) Annual Exchange Arrangements and Exchange Restrictions and incorporates the extent and intensity of capital controls (Chinn & Ito, 2008). Higher scores on this index indicate high levels of openness and, as a result, the capacity for capital exit.[11]

The final measure of market integration is multilateral debt.[12] As the percentage of a nation's debt owed to multilateral lending institutions increases, it is likely that the power of those institutions over domestic policy decisions

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also increases. Given the attention paid by both the World Bank and IMF to fiscal stability in the developing world, I expect the magnitude of the tax burden to be positively associated with multilateral debt.

Increases in each of these indicators, the expected effects of which were discussed previously, suggest that international economic forces are gaining power in the domestic economy. If the globalization thesis is correct, these variables will wash out the effects of domestic partisanship. Based on my theoretical expectations, however, I anticipate strong partisan effects despite rising levels of market integration.

To evaluate the resilience of domestic partisanship in the age of globalization, I include two measures of party control. First, I include a dummy variable for a Left or Center–Left president. The variable assumes a value of 1 in years when a president from the Left or Center–Left holds office and 0 otherwise. Second, I include a measure of Left or Center–Left control in the legislature. This variable records the percentage of legislative seats held by parties on the Left and Center–Left.[13] To code political parties by ideology, I rely on data from Huber, Mustillo, Pribble, and Stephens (2005). Adopting the coding criteria of the commonly used Coppedge (1997) data, Huber et al. coded all parties as Left, Center–Left, Center, Center–Right, or Right.[14] At the time of writing, however, the data set codes Latin American parties only through the year 2000. Thus, following Huber et al., I coded all presidential and legislative elections from 2001 to 2006. To code newly emerged parties or existing parties that shifted ideology, I relied heavily on official party Web sites and third-person assessments. To account for the potentially confounding effects of variation in the timing of elections (e.g., January vs. November), results of elections that occurred later than March 31 are recorded in the following year. Brazilian President Luiz Inácio Lula da Silva's victory in the October 22, 2002, election, for instance, is not recorded until 2003. If the theoretical alternative to the globalization hypothesis I present here is correct, the magnitude of the tax burden and the reliance on the VAT should decrease as the Left gains power.

In addition to these variables of greatest substantive interest, I also include five control variables. First, I control for the growth of GDP to account for the potential effect of economic health, rather than domestic partisanship, on tax revenue. Second, I include the size of the rural population to control for cross-country variation in tax revenue that may be driven by the composition of a country's population. Largely based on geographic dispersion, tax collection in rural areas is expensive and inefficient relative to collection in urban areas. Despite the efforts of most South American countries to formalize the economy, however, I expect total tax revenue and VAT revenue to be limited by the size of the rural population.

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Next, to control for variation in natural resource wealth, which may allow politicians in resource-rich countries to deemphasize domestically oriented taxation, I include both the value of fuel exports and non-fuel mineral exports into the model.[15] Finally, I introduce a variable for linear time to control for evolving regional or global factors that may influence tax revenue across South America as a whole, rather than on a case-specific basis.

To summarize, the model to be estimated is the following:

$$\begin{aligned} TAX\ REVENUE_{k,i,t} = {} & \alpha_i + LEFT\ PRES_{i,t-1} + LEFT\ SHARE_{i,t-1} \\ & + FDI\ \ FLOW_{i,t-1} + FDI\ STOCK_{i,t-1} + TRADE_{i,t-1} \\ & + CAPITAL\ OPENNESS_{i,t-1} + DEBT_{i,t-1} \\ & + PORTFOLIO_{i,t-1} + GDP\ GROWTH_{i,t-1} \\ & + RURAL\ POPULATION_{i,t-1} + FUEL_{i,t-1} \\ & + ORES_{i,t-1} + TIME_t \end{aligned}$$

Because the data analyzed here are time series cross sectional, autocorrelation and heteroskedasticity are concerns as ordinary least squares (OLS) estimates of the standard errors may be misleading. Beck and Katz (1995) suggest using OLS with panel-corrected standard errors once serial correlation has been removed from the disturbances. While a number of methodologists suggest including a lagged dependent variable, Achen (2000) demonstrates that lagged dependent variable models can produce biased coefficient estimates when the time series are short and there may be unmeasured political factors that don't vary from year to year. Given that these concerns are relevant to the data here, I use the standard Prais-Winsten transformation to deal with autocorrelation. I lag all independent variables in the model one year to make the causal direction explicit. Estimates from these models will allow for a thorough assessment of the hypotheses in question.

Results and Analysis

Beginning with the question of how global integration and partisanship influence the magnitude of the domestic tax burden, Column I of Table 1 presents the estimated slope coefficients for the model of total tax revenue discussed above. What is immediately noteworthy is that the estimated slope coefficients for the economic integration variables, with the exception of multilateral debt and trade dependence, fail to reach statistical significance. The two FDI variables, though oppositely signed, are insignificant. This suggests that, despite a longer time horizon, MNCs, like short-term portfolio investors, are either unconcerned with or unable to influence the magnitude of the tax burden. The

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Table 1. Determinants of the Magnitude and Structure of the Tax Burden in South America, 1990–2006

	Tax Burden		Distribution of Tax Burden (by Tax Type)									
Independent Variable	I. Total Revenue	*SE*	II. VAT and Sales	*SE*	III. Income (All)	*SE*	IV. Property	*SE*	V. Financial Transaction	*SE*	VI. Personal Income[a]	*SE*
Left executive	–0.806*	(0.332)	–4.595*	(1.771)	1.133	(0.909)	1.032	(0.881)	0.442	(1.031)	6.761*	(2.421)
Legislative seats held by the Left	0.018	(0.010)	–0.003	(0.051)	–0.071*	(0.031)	0.061*	(0.022)	–0.043	(0.028)	–0.215*	(0.065)
FDI flows	0.067	(0.057)	0.715*	(0.275)	0.192	(0.145)	–0.328*	(0.126)	0.060	(0.144)	–0.556	(0.371)
FDI stock	–0.034	(0.021)	0.037	(0.091)	–0.053	(0.044)	0.060	(0.036)	–0.037	(0.043)	0.050	(0.121)
Trade dependence	0.035*	(0.015)	–0.092	(0.079)	0.116*	(0.037)	–0.058*	(0.025)	0.115*	(0.040)	–0.034	(0.052)
Capital account openness	–0.186	(0.104)	0.196	(0.556)	0.773*	(0.301)	–0.351	(0.272)	–0.149	(0.329)	2.018*	(0.820)
Multilateral debt	0.019*	(0.006)	–0.010	(0.028)	–0.011	(0.017)	0.009	(0.011)	0.014	(0.015)	–0.018	(0.042)
Portfolio investment	–0.104	(0.090)	–1.356*	(0.574)	–0.078	(0.293)	0.316	(0.325)	0.054	(0.358)	0.059	(0.762)
GDP growth	0.026	(0.017)	0.060	(0.106)	0.029	(0.055)	–0.071	(0.059)	0.038	(0.066)	0.190	(0.129)
Rural population	–0.184	(0.163)	–3.373*	(0.748)	1.318*	(0.409)	0.745*	(0.285)	1.463*	(0.424)	3.071*	(0.711)
Fuel exports	0.070*	(0.025)	0.065	(0.113)	–0.113	(0.066)	–0.149*	(0.056)	0.039	(0.063)	–0.119	(0.201)
Ore exports	–0.053	(0.294)	0.290	(0.155)	0.015	(0.077)	–0.081	(0.056)	–0.018	(0.055)	0.595*	(0.225)
Time	0.294*	(0.070)	–0.679*	(0.311)	0.809*	(0.198)	0.371*	(0.126)	0.011	(0.184)	0.916*	(0.346)
Observations	159		159		159		159		159		96	
R^2	.98		.96		.95		.89		.89		.96	

Note: VAT = value-added tax; FDI = foreign direct investment. Models are estimated using ordinary least squares with panel-corrected standard errors. Country dummies are estimated for each model, but the results are suppressed.
a. Calculated as a percentage of total income tax revenue.
*Significant at the .05 level.

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negatively signed coefficient for capital account openness, though not statistically significant, lends support to the notion that the influence of capital owners increases with the credibility of the threat of exit. Whether this result reflects direct pressure to reduce the overall tax burden or is the indirect result of pressure to alter the distribution of the tax burden will be examined in the next section. The estimated slope coefficient for multilateral debt indicates that the magnitude of the tax burden increases with the domestic power of multilateral lending institutions. This finding is not surprising given the premium these institutions place on fiscal stability, but it does provide additional evidence against the older race-to-the-bottom logic of global integration.

That the impact of rising levels of trade dependence is also positive and statistically significant is intriguing. In the South American context, this result points to the ease with which governments are able to extract revenue from imports and exports to cover revenue shortfalls. In the wake of Argentina's financial crisis, for example, a 20% tax on exports and financial transactions was imposed to increase tax revenue and protect the urban poor of Buenos Aires from rising food prices. Though this tax was intended to be a temporary measure, the tax has been increased to 40% on some products and, with a booming international soybean market, now generates about 20% of Argentina's tax revenue.[16]

Turning away from the global integration variables, the estimated effects of domestic partisanship on the magnitude of the domestic tax burden suggest that partisanship is not dead in South America's neoliberal era. Beginning with Hypothesis 1, it is immediately clear that, despite the restrictions of neoliberalism, the partisanship of the president is a reliable predictor of tax revenue. Substantively, the election of a president from a Left or Left-of-Center party should create a 0.36 standard deviation decrease in tax revenue. This finding raises serious doubt about the conventionally hypothesized constraints of globalization on the capacity of policy makers to pursue partisan revenue goals. In the wake of "reform by surprise" the assertion of presidential partisanship in the neoliberal era is remarkable. Furthermore, in support of the counterintuitive Hypothesis 2, presidents from the Left generate less tax revenue than presidents of the Center or Right. This difference is obvious and statistically significant.

The estimated slope coefficient for the power of the Left in the legislature, on the other hand, is statistically insignificant. This finding is not surprising given the strength of South American presidents relative to the legislature, both in general and with regards to taxation in particular. Many short-term changes in tax policy are made by administrative rule or executive decree rather than by law. This is not to suggest, however, that the partisan composition of the legislature has no impact on revenue policy. Instead, as will become

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clear in the next section, legislators are far more effective at influencing the distribution, rather than the magnitude, of the tax burden. This also explains why the estimated coefficient is positively signed. Rather than an indication of ideological inconsistency, this result reflects differences in the specific manner by which presidents and legislators alter the distribution of the tax burden.

Turning briefly to the control variables, GDP growth appears to put upward, but insignificant, pressure on tax revenue. The size of the rural population has the expected sign but is statistically indiscernible from zero. The coefficient for fuel exports, though not mineral exports, is positive and statistically significant. Finally, the estimated slope coefficient for linear time is positive and significant, suggesting an upward regional trend in the magnitude of the tax burden.

Understanding the Right–Left Tax Gap

Although limiting the analysis to total tax revenue is consistent with the taxation literature, this design ignores any heterogeneity that may exist in the preferences of political parties and foreign economic actors regarding the distribution of the domestic tax burden.[17] It is still unclear, for example, whether lower tax takes under leftist governments are the result of a fundamental difference in these parties' preference against regressive taxes. As argued previously, parties on the Left are ideologically averse to regressive consumption taxes, particularly the VAT. As a result, the Left deemphasizes VAT and sales tax revenue and redistributes the tax burden toward the progressive personal income tax. Policy makers on the Right, alternatively, prefer the efficiency of the VAT and its capacity to increase tax neutrality. Understanding how preferences for specific taxes differ across economic and partisan actors is necessary to uncover the mechanisms driving the findings obtained in the first phase of the analysis. This should also provide a more rigorous test of the globalization thesis and the specific hypotheses under evaluation.

The results of the regressions for the second phase of the analysis are presented in Columns II through VI of Table 1. I organize the discussion of these results by independent, rather than dependent, variable to highlight each actor's overall impact on the distribution of the tax burden.[18] Beginning with the measures of economic integration, these results reiterate the multifaceted pressures of globalization on the distribution of the tax burden. As expected, new inflows of FDI are associated with significantly greater reliance on neutral, consumption-based taxes. This is because the longer time horizon of MNCs leads to more domestically oriented revenue policy concerns. Following this

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logic, the negative and statistically significant relationship between FDI inflows and property tax is indicative of MNCs' direct ownership of domestic enterprise. Unlike new inflows of FDI, however, the results demonstrate that the existing stock of FDI is ineffective in altering the distribution of the tax burden.

As expected, increases in portfolio investment are associated with declining reliance on the neutral VAT. Surprisingly, the estimated slope coefficients in the other models are all statistically indiscernible from zero. Rather than an indication of short-term capital's weakness, however, these findings point to the fact that mobile capital owners also influence revenue policy via the threat of exit. This claim is buttressed by the fact that, as predicted, the estimated slope coefficient for capital account openness is positive and significant in the personal income tax equation. Given that personal income tax is calculated as a percentage of total income tax, this implies that the income tax burden levied against corporations declines as restrictions on the movement of short-term capital are removed.

The estimated slope coefficients for the fourth measure of economic integration, trade dependence, are intriguing. As the level of trade increases, the distribution of the domestic tax burden shifts away from property tax and towards income and transaction taxes. This last finding is not surprising given that trade constitutes commercial transaction by definition. The impact of trade dependence on income and property tax, however, is less clear. That trade does not have a significant effect on the distribution of income tax revenue suggests that this relationship is the indirect result of trade's capacity to stimulate domestic income. And in light of rising income and transaction tax revenue, the percentage of total revenue generated by property taxes may decline despite rising trade dependence.[19] Finally the estimates for multilateral debt are not statistically significant in any of the equations. Despite the positive impact on the magnitude of the tax burden identified in the first phase of the analysis, it seems that multinational lending institutions are either unconcerned with or unable to influence the distribution of the tax burden.

Although the results presented in Table 1 demonstrate the capacity of globalization's component parts to influence the distribution of the domestic tax burden, they also affirm the argument presented here, that partisans are not hamstrung in postreform South America. Instead, partisans continue to alter the distribution of the tax burden in ideologically consistent ways. Turning to the partisanship variables, these results begin to unravel the complexities underlying the findings from the first phase of the analysis. Consistent with Hypothesis 3, presidents from the Left and Center–Left are associated with significantly reduced reliance on VAT and sales tax revenue. This finding is

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important for two substantive reasons. First, consumption-based taxes (including the VAT) are regressive in that the poor consume a greater percentage of their income than the wealthy. As a result, lower-income groups bear a disproportionately high burden when VAT or sales tax rates increase. Second, the shift in South America towards the VAT, and other consumption-based taxes, has been astonishingly broad in scope and swift in implementation. Yet, despite the international importance of the VAT, the Left has been reluctant to expand its use. Interestingly, the estimated slope coefficients for a leftist executive are not statistically significant in the property, transaction, or total income tax equations.

While the results from the first phase of the analysis demonstrate that the partisan composition of the legislature is not a reliable indicator of the magnitude of the tax burden, parties in the legislature are able to alter its distribution. Parties on the Left rely more heavily on revenue from progressive property tax than the Right. Surprisingly, however, as the power of the Left increases in the legislature, the share of tax revenue generated by the income tax decreases. Furthermore, while presidents on the Left shift the income tax burden away from corporations, legislators do the opposite.

Together, these findings explain, in large part, the estimates from the first phase of the analysis that governments on the Left collect less tax revenue than governments on the Right. Based on ideological motivations and consistent with Hypothesis 3, this previously unexpected partisan tax gap is driven primarily by the Left's de-emphasis of regressive VAT and sales tax revenue. The mechanisms driving this gap and the divergent income tax gap, however, remain unclear. To gain leverage on these issues, I calculate the bivariate correlations between partisan control and both income and VAT rates.[20] These data are not suitable for regression analysis but should highlight the manner in which partisans are able to achieve the revenue policy outcomes identified above. The results are presented in Table 2.

As expected, the Right compresses the tax rate structure while the Left increases the progressivity by altering both the highest and lowest rates. The preferences of presidents and legislators on the Left, however, diverge regarding corporate tax rates. Each prefers to reduce the minimum corporate rate but leftist legislators raise the maximum tax rate while presidents do the opposite. I argue that these divergent outcomes reflect the additional pressure from international economic forces faced by presidents. While legislators are able to be more domestically oriented in their policy decisions, presidents on all sides of the ideological spectrum are under the watchful eyes of the market. That this scrutiny is even greater for the Left (Campello, 2007) explains the aggressiveness of leftist presidents in reducing the highest corporate rates. As such,

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Table 2. Correlation Between Domestic Partisanship and Marginal Tax Rates

	Highest and Lowest Statutory Income Tax Rates				
	Personal Minimum	Personal Maximum	Corporate Minimum	Corporate Maximum	VAT Rate
Left executive	−.26	.39	−.70	−.46	−.09
Left majority in legislature	−.21	.23	−.38	.30	−.16
Observations	73	73	90	90	129

Note: VAT = value-added tax. Correlations are calculated using data from the Economic Commission for Latin America and the Caribbean.

legislators are able to increase the corporate tax burden, whereas presidents on the Left must act decisively to quell concerns about state intervention.

The correlations for the VAT rate, on the other hand, are negative but quite low. This suggests that the gap identified above is not caused by fundamental differences in VAT rates. Instead, following Cárdenas et al. (2005), this difference is caused by the more efficient VAT administrations created by the Right. Increasing the rate of tax collection, cutting the cost of tax collection, and stymieing tax evasion are all distinctly rightist goals in South America's neoliberal era. Interestingly, the authors find no partisan difference in the efficiency of income tax administrations. Though rudimentary, these results highlight the mechanisms underlying South America's tax gap. In particular, they point to the preference of the Right for rate neutrality and the competing pressures faced by presidents and legislatures on the Left regarding the progressivity of the corporate income tax.

Conclusion

The extant literature on partisanship and global integration in the developing world argues that international economic forces limit the significance of partisan ideology as a predictor of economic policy outcomes. This suggests that, while the election of a leftist party signals a strong desire among the electorate for state expansion into the private economic sphere, there is little reason to believe that policy makers retain the partisan latitude necessary to satisfy popular demand. The results presented here, however, indicate that the constraints of neoliberalism on partisan taxation have been vastly overstated.

Using time-series-cross-section data from South America, I present three theoretically interesting empirical findings. First, the impact of globalization

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on the understudied revenue side of public finance is anything but monolithic. The heterogeneous, even conflicting, impact of international economic actors on the magnitude and distribution of the domestic tax burden becomes clear when globalization is divided into its component parts. While owners of mobile, short-term capital pressure policy makers to shift the distribution of the income tax burden away from corporations, longer-term MNCs seek to augment reliance on the non-distortionary VAT. Furthermore, contrary to the expectations of the convergence thesis, IFIs demand fiscal equilibrium and exert upward pressure on the magnitude of the tax burden.

Second, even in light of the influence of global economic actors, party ideology is still a good predictor of total tax revenue. Despite the formulaic prescriptions of the neoliberal tax regime and the overwhelming political influence many scholars attribute to globalization, policy makers in the developing world retain the capacity to pursue ideologically driven, electorally mandated revenue policy. This is a surprising conclusion given the implication of the globalization hypothesis that neoliberalism stifles partisan tax policy.

Third, and most intriguingly, the pro-market Right generates more tax revenue than the interventionist Left. While this may raise the eyebrows of some, I contend that there is a compelling theoretical explanation for this finding. This partisan tax gap is driven by the ideologically based aversion of the Left to regressive but highly efficient forms of taxation. To reduce the tax burden imposed on low-income citizens, policy makers on the Left deemphasize the VAT. Under pressure from multilateral lending agencies to maintain fiscal stability, the Left seeks to recover foregone VAT revenue by increasing the progressivity of the income tax. The acute, but divergent, international pressures on leftist presidents and legislators, however, leads the former to increase the highest marginal corporate income tax rates and the latter to aggressively reduce them. Alternatively, the premium foreign investors place on the neutrality-enhancing VAT and the emphasis of international creditors on fiscal stability allows the Right to raise tax revenue by shifting the tax burden away from businesses while signaling its commitment to the "Washington Consensus." Together, these ideologically motivated changes in the distribution of the tax burden lead to higher tax hauls under rightist governments. The Right drives this tax gap by compressing tax rate schedules and building a more efficient VAT administration than the Left. The empirical findings presented here support this argument.

These findings raise a number of fascinating questions. First, how do these patterns of taxation impact spending? If the Right is extracting more tax revenue than the Left, what are they doing with it? Given how the Right distributes the tax burden, are they also spending more regressively than the

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Left? Normatively, if leftist governments can generate more revenue via VAT and sales tax, should they follow the example of many of their counterparts in the developed world and bear the costs of burden shifting to increase the provision of social goods? Answering these questions is beyond the scope of this project but constitutes a task for future research.

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Notes

1. See, for instance, Johnson and Crisp (2003), Kingstone and Young (2008), Murillo (2005), Murillo and Schrank (2005), Mosley and Uno (2007), and Wibbels and Arce (2003).
2. It is typically thought that the Left increases tax revenue to finance broad welfare-oriented policies whereas the Right prefers to lower tax levels to promote growth and competitiveness. For a detailed discussion of this divide, see Hibbs (1977, 1987).
3. The precipitous decline in policy variance in Figure 1 is because of Venezuela's 1993 adoption of the value-added tax (VAT), the latest of any country in South America.
4. Although IFIs promote the VAT as their preferred method of revenue extraction (Bird 1992), strengthening the income tax has been a similarly important goal in the neoliberal era. Furthermore, as in the case of Argentina at the turn of the century, IFIs accept non-market-conforming measures taken to cover fiscal deficits.
5. Although all consumers are subject to the VAT in theory, tax collection and enforcement in rural areas remain low. As a result, tax yields are heavily drawn from urban consumers.
6. For an incisive analysis of the emerging partisan divide over economic policy, see Boix (1998).
7. Specifically, the analysis includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay, and Venezuela. The data for the dependent

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variables come from the Economic Commission for Latin America and the Caribbean's CEPALSTAT (http://websie.eclac.cl/sisgen/ConsultaIntegrada.asp).
8. To facilitate comparability, tax revenue is calculated as a percentage of GDP. This is a necessary step to control for inherent disparities in absolute values of tax hauls across the region.
9. It is important to note that as the share of income tax revenue coming from individuals increases, the share coming from corporations decreases by the same amount.
10. The data for foreign direct investment (FDI) flows and portfolio investment are acquired from the World Bank's World Development Indicators (WDI). Data on FDI stock come from UNCTAD.
11. For additional information on the calculation of this index, see Chinn and Ito (2008).
12. Data taken from WDI.
13. For ease in computation and coding, parties that receive less than 3% of seats in the legislature are not included.
14. Deviating from Coppedge (1997), Huber, Mustillo, Pribble, and Stephens (2005) do not code parties as secular/religious, as populist, or as other. For more extensive details on how parties are coded, see the original sources. The author is very thankful to Evelyne Huber, Tom Mustillo, Jenny Pribble, and John Stephens for being so generous with their data set.
15. The data for each of these five control variables come from the WDI.
16. For a brief discussion of this tax hike, see "Kirchners v the Farmers" (2008).
17. For an example in the literature that does analyze the composition of tax revenue, see Lieberman (2003, chap. 6).
18. To simplify the analysis, I focus my discussion on those variables of greatest substantive importance and choose to exclude additional discussion of the estimated slope coefficients for the five control variables.
19. If these models are reestimated without the time variable, the estimated coefficient for trade is not significant in the property tax equation. With this exception, the substantive conclusions drawn in this phase of the analysis are robust to this alternate specification.
20. These data on tax rates are from CEPALSTAT. To simplify the analysis, I use a dummy variable for a leftist majority in the legislature.

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Bio

Austin Hart is a PhD student at the University of Texas at Austin.

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