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| RESEARCH ARTICLE

Institutional Learning and the Limits of Fiscal Rules: A Public Choice Perspective

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| ABSTRACT
This article investigates the process of constructing fiscal discipline in Brazil from the Camata Law (Lei Complementar No. 82/1995) to the approval of the Fiscal Responsibility Law (FRL) in 2000, and examines its subsequent deterioration from 2014 onwards. It analyses the evolution of personnel expenditure limits, sanction mechanisms and enforcement instruments over the period 1995 to 2000. Using a qualitative approach based on documentary and institutional analysis, the study draws on the relevant legislation and historical fiscal data series. The paper identifies the initial lack of effective sanctions and enforcement tools in the Camata Law, as well as the advances introduced by Constitutional Amendment No. 19/1998 and the New Camata Law (Lei Complementar No. 96/1999). This work shows how, through learning-by-doing, these successive reforms culminated in a broader institutional framework with the FRL and it concludes that fiscal discipline depends on societal pressure.

| KEYWORDS

Fiscal Responsibility Law, Camata Law, fiscal discipline, enforcement, fiscal rules

| ARTICLE INFORMATION

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1. Introduction

The Fiscal Responsibility Law (FRL), enacted in 2000, was designed to ensure the lasting balance of public accounts. This goal was socially justified, as in the post-stabilisation context, this fiscal framework also helped to mitigate sources of price instability, particularly those that the population associated with inflation, by strengthening fiscal consistency. The new regime of fiscal discipline established limits, targets and transparency requirements applicable to the Union, the 26 states, the Federal District and, at present, the 5,569 municipalities. This institutional framework was conceived as part of a broader fiscal pact.

At times, statistics are adjusted to accommodate otherwise irreconcilable targets. A clear example of this is the emergence of quasi-fiscal deficits and debts that remain unreported for long periods. Quasi-fiscal deficits arise from societies' difficulty reconciling ambitious targets with limited resources. According to Allan (1994), in most OECD countries, quasi-fiscal expenditure is budgetary, as it is included in the budget through estimates. Such expenditure is subject to reporting and accounting requirements. Quasi-fiscal spending is difficult to control and characterised by limited transparency.

The drafting of these provisions required an interdisciplinary approach, combining economics, public accounting, budgetary administration, and law to transform targets and limits into verifiable rules. The effort involved in the conception and systematisation of this public finance law was considerable, which contributed to the perception that the statute was difficult to understand at the time of its publication. Brazil's Fiscal Responsibility Law was not merely a pioneer but also came to be considered one of the most successful fiscal frameworks worldwide. However, dissonant comments and expressions of scepticism were not lacking. Some actors claimed that the statute was merely an extension of Law No. 4,320/64; others argued that it would not "take hold", that is, it would not be effectively observed by the Union and the federative entities.

Historically, the construction of this regime was not sudden; it resulted from an incremental process that culminated in the FRL and passed through the Camata Law (1995), Constitutional Amendment No. 19 (1998), and the so-called New Camata (LC 96/1999). Each stage not only introduced new institutional elements but also reflected a learning-by-doing approach, in which practical experience informed subsequent reforms. The purpose was to render credible restrictions that had previously been fragile or scarcely enforceable.

In the first ten years following its enactment, many public managers believed that the statute alone would be enough to secure fiscal adjustment. Early improvements in fiscal indicators, both at the subnational level and within the Union, seemed to confirm this expectation. Over time, however, the debate shifted. Economists and policymakers began to argue that reforms were necessary if Brazil was to restore external balance, sustain economic growth, and expand employment opportunities. Among these initiatives were the proposals of Nunes and Nunes (2005) and Senate Complementary Bill No. 229/2009 to improve the quality of public expenditure, reduce the fiscal deficit (Giambiagi, 2000; 2004), and generate incentives for private investment.

With the fight against inflation no longer a priority on the national agenda, greater scope opened up for individual and group interests to once again prevail in national politics. The parties began to use the budget more intensively as a political bargaining currency to increase the number of their elected members in Parliament, a practice known as catch-all politics.

In order for the State to spend more, an increasing number of draft bills were introduced, based on heightened difficulties or on temporary or localised constraints. Some of these complementary bills were eventually converted into law, thereby reducing fiscal discipline. Among these measures, the following complementary laws may be cited: LC 148/2014, LC 156/2016, LC 177/2021, LC 195/2022 and LC 206/2024.

Thus, fiscal discipline was eroded by expenditures linked to education, health, mandatory spending, and electoral outlays, particularly in social assistance. Not even the constitutional spending cap established by Constitutional Amendment No. 95/2016 succeeded in controlling public expenditure. This was because, in order to maintain these expenditures and create new ones, practices of creative accounting (or earnings management) and successive legislative amendments were introduced. As a result, Articles 17 and 18 of the FRL were no longer complied with.

This article investigates the process of constructing fiscal discipline in Brazilian federalism, from the Camata Law (LC No. 82/1995) to the approval of the Fiscal Responsibility Law (FRL). It analyses the evolution of limits on personnel expenditure, sanction mechanisms and enforcement instruments over the period 1995–2000, identifying the initial weaknesses of the Camata Law, the advances introduced by Constitutional Amendment No. 19/1998 and the New Camata Law (LC No. 96/1999), as well as the consolidation of a broader framework with the FRL. It seeks to show that the approval of the Law occurred in a specific context of deterioration in public accounts and that non-compliance with the FRL was due to the perception that the inflationary threat had dissipated.

Methodologically, this study adopts a qualitative approach based on the analysis of legislation (the Camata Law, Constitutional Amendment No. 19/1998, Complementary Law No. 96/1999 and the Fiscal Responsibility Law), fiscal data and academic literature, in addition to the examination of institutional arrangements. Historical fiscal series were also considered, with particular attention to personnel expenditure indicators and mechanisms of transparency and enforcement.

After situating the socio-economic and political context that preceded the approval of the Fiscal Responsibility Law, the article traces the incremental evolution of personnel expenditure limits, sanction mechanisms and enforcement instruments within Brazilian federalism — from the initial weaknesses of the Camata Law, through the advances introduced by Constitutional Amendment No. 19/1998 and the New Camata Law (LC No. 96/1999), to the broader and more robust institutional framework established by the FRL in 2000. It then examines the subsequent erosion of fiscal discipline and discusses the limits of formal rules from a Public Choice perspective, highlighting the importance of effective enforcement, transparent accounting practices and sustained societal pressure.

2. Hyperinflation, Financial Fragility and the Rentier Economy in Brazil (1980s–Early 1990s)

Hyperinflation in the 1980s and early 1990s disorganised key parts of the Brazilian economy and brought significant costs to society (Baer, 2001). Rapid price increases disrupted consumption, investment and the public budget. The persistence of inflation at the time can be explained by inertial inflation theory (Simonsen, 1983; Modiano, 1992; Bresser-Pereira & Nakano, 1987).

Another important feature of Brazilian hyperinflation was the loss of confidence in the national currency. The currency gradually stopped working well as a store of value and to a lesser extent as a medium of exchange. Even its role as a unit of account became unstable. Prices had to be changed almost constantly and indexation became widespread. Periodically, the government removed three zeros from the currency to make accounting and daily life simpler without actually changing its real value. Still, many transactions, especially the bigger ones, were done in US dollars, even though Brazilian law only allowed payments in the national currency. This pattern was reminiscent of the German hyperinflation in the early 1920s.

In practice, this meant that people began to replace the national currency with the US dollar whenever possible. This process of currency substitution reflects Gresham’s Law, according to which good money tends to drive bad money out of circulation. In Argentina, there was also hyperinflation, a deterioration of public accounts, and a widespread search for the substitution of the national currency with the US dollar during the 1980s.

The rise in interest rates increased the returns to rentiers through short-term financial operations, while productive investment declined. Short-term financial operations became more attractive. Moreover, the rise in interest rates further aggravated both inflation and the recession, as resources that could have been used for productive investment were instead channelled into the financial market, a phenomenon known as the “financial merry-go-round”.

The financial fragility was so severe that supermarket profits came mainly from financial investments instead of from actual sales (Silveira, 1996; DIEESE, 1997). Rentiers profited handsomely from these financial operations, to the detriment of the Brazilian economy as a whole. This favouring of rentiers drew sharp criticism from David Ricardo, who famously argued that the interests of rentiers were "always in direct opposition to those of all the other classes of the community".

In this context, inflation control proved costly and politically sensitive until the Real Plan provided a comprehensive solution that stabilised prices and paved the way for subsequent fiscal reforms. Rising prices also drove up debt-servicing costs, forcing the government to replace earlier low-interest obligations with new ones carrying higher rates. Although inflation also provided some protection to public accounts by eroding the real value of programmed expenditures and contributing to revenue collection through the inflation tax (Bacha, 1994), its net effect was nevertheless to weaken public finances, as evidenced by the marked increase in public debt. The public sector net debt, for example, rose from 23.7 per cent of GDP in 1981 to 35.5 per cent of GDP in 1990 (Giambiagi, 1996).

Even small producers adjusted their prices in response to currency devaluation, fuel price increases, and other factors, such as food price rises reported in the press. Thus, when a 20 per cent devaluation was announced, entrepreneurs raised their prices by the same index. Inflation had been high in the past, and the expectation that it would remain high sustained it. This was inertial inflation.

The deterioration of Brazil's economic conditions was severe enough to make the fight against inflation a national priority that overrode individual and group interests. This favoured the implementation of the Real Plan, the election of politicians associated with it, and, subsequently, the sorting out of public accounts through the Fiscal Responsibility Law (FRL). Individuals believed that the greatest increase in their benefits would come from resolving the national situation, through the end of inflation and the restoration of public finances via the FRL. People were unable to secure wage increases and could only strive to preserve their purchasing power.

As a result of the widespread indexation of the entire economy, the decline in well-being led Brazilians to view price stabilisation as the main national priority, above the interests of individuals and groups. This process transformed monetary stability into a collective good that transcended class, political and personal divisions. From a public choice perspective, this broad consensus helped make the Real Plan and, later, the Fiscal Responsibility Law (FRL) possible.

At the same time, there was an increase in the financial fragility of the Union and the subnational entities. The deterioration of the states' fiscal situation, characterised by immoderate and recurrent deficits, high public debt, and fiscal war among them, rendered their financial position unsustainable, culminating in the renegotiation of their debts. This renegotiation had as its main consequences the privatisation of state-owned banks and the prohibition, set out in Article 35, § 2, of Complementary Law No. 101/2000 (the Fiscal Responsibility Law – FRL), on any state-owned financial institution granting financing to the federative entity that controls it.

This experience was so traumatic for the country that the fear of renewed price and fiscal instability influenced subsequent elections. Fernando Henrique Cardoso, then Minister of Finance, was elected President of the Republic for two successive terms because his name was closely associated with the Real Plan, which brought inflation under control and paved the way for the restoration of fiscal order through the Fiscal Responsibility Law.

3. From the Camata Law to the Fiscal Responsibility Law: Building Fiscal Discipline

The Camata Law (Complementary Law No. 82 of 27 March 1995) was approved shortly after the implementation of the Real Plan. Until June 1994, Brazil had been experiencing uncontrolled hyperinflation, with monthly rates reaching 47.5 per cent and annual rates close to 2,500 per cent. Wage adjustments were made monthly, and prices were changed daily.

Before the Real Plan, the magnitude of public expenditure, particularly the heavy burden of public servants' salaries and wages, was eroded by payment delays. This effect was especially damaging to state finances. These personnel costs had a particularly harmful impact because they represented around 60 per cent of revenue and exhibited automatic growth through the incorporation of advantages and gratifications provided for in state legislation. Those states that did not anticipate in the success of the Real Plan and granted real wage increases to their civil servants ended up in the worst financial situation, since they paid salaries with gains indexed to inflation.

In this context, the Camata Law (Complementary Law No. 82/1995) and, subsequently, the New Camata (Complementary Law No. 96/1999) were enacted with the purpose of limiting expenditure on active civil servants, retirees and pensioners, which at the time were recognised as the principal source of imbalance in public finances. Later, the Fiscal Responsibility Law (FRL, 2000) broadened this framework, consolidating personnel expenditure limits and extending fiscal discipline to other dimensions of public finances, with greater rigour in enforcement and transparency.

The fiscal impact of personnel expenditure can be interpreted through the Public Choice literature on bureaucracy, according to which public employees and organised groups have incentives to support political actors who promise wage increases and employment protection. Civil servants and their representative organisations may exert pressure for wage increases, employment stability and ancillary benefits, while supporting politicians who favour such claims (Borcherding, Bush & Spann, 1977).

In response to the rapid growth in personnel expenditure that had accompanied this inflationary period, the government enacted the Camata Law. The legislation established a limit of 60 per cent of net current revenue for personnel expenses (active staff, retirees and pensioners) across all three levels of government. The law imposed a ceiling and prohibited salary adjustments, new hires and any increases in expenditure while the limit was exceeded. It also required the publication of monthly transparent financial statements. This fiscal containment mechanism aimed to curb public spending growth.

However, the Camata Law proved ineffective. As the saying goes, "a law without sanctions is a dead letter." The legislation lacked proper control mechanisms and did not include effective sanctions for non-compliance. It also failed to require the broad disclosure of accounting data by the federative entities or to impose any real punishment on non-compliant governments or their managers — something that only appeared years later with the Fiscal Crimes Law.

Prior to the enforcement of the Camata Law, the States presented a fiscal framework characterised by significant personnel expenditure. The table 1 below provides a snapshot of this situation in 1997, detailing the number of active civil servants, average monthly salaries, and total annual personnel costs. It also projects the law's fiscal impact, including expenditure cuts, personnel reductions, and resulting financial adjustments.

Table 1. Fiscal Impact of Implementing the Camata Law in the States (1997)

Brazilian States	Number of Active Civil Servants	Average Monthly Salary (Active Staff)	Total Annual Personnel Expenditure (R$ thousand)	Camata Law Projection 1997	Expenditure Cut (%)	Fiscal Impact (R$ thousand)	Personnel Expenditure after Cut (R$ thousand)	Dismissed Civil Servants
AC	29,914	626	276,805	77.90%	17.90%	49,548	227,257	5,355
AL	43,8	919	650,832	94.10%	34.10%	221,934	428,898	14,936
AP	14,112	1.135	281,284	60.40%	0.40%	1,125	280,159	56
AM	52,275	659	649,629	44.00%			649,629	
BA	124,51	876	1,875,194	49.20%			1,875,194	
CE	86,381	784	1,096,310	61.00%	1.00%	10,963	1,085,347	864
DF	112,459	1.361	2,963,172	79.00%	19.00%	563,003	2,400,169	21,367
ES	59	801	1,133,603	64.00%	4.00%	45,344	1,088,259	2,36
GO	145,974	375	1,216,774	67.10%	7.10%	86,391	1,130,383	10,364
MA	132	288	694,154	57.20%			694,154	
MG	375,311	647	4,786,502	80.00%	20.00%	957,3	3,829,202	75,062
MS	42	791	516,466	74.50%	14.50%	74,888	441,578	6,09
MT	42,949	997	724,482	67.30%	7.30%	52,887	671,595	3,135
PA	96	541	979,637	60.90%	0.90%	8,817	970,82	864
PB	76	337	497,45	49.40%			497,45	
PE	112	788	1,672,341	73.90%	13.90%	232,455	1,439,886	15,568
PI	68	432	509,712	67.10%	7.10%	36,19	473,522	4,828
PR	96,3	1.354	2,895,116	68.80%	8.80%	254,77	2,640,346	8,474
RJ	244,433	854	4,750,692	82.10%	22.10%	1,049,903	3,700,789	54,02
RN	75,702	435	625,151	66.60%	6.60%	41,26	583,891	4,996
RO	34	731	367,912	66.30%	6.30%	23,178	344,734	2,142
RR	12,31	443	73,254	21.50%			73,254	
RS	210,518	852	3,905,016	84.90%	24.90%	972,349	2,932,667	52,419
SC	86,227	890	1,513,953	67.40%	7.40%	112,033	1,401,920	6,381
SE	39,049	712	505,688	66.00%	6.00%	30,341	475,347	2,343
SP	834,175	685	14,722,836	63.40%	3.40%	500,576	14,222,260	28,362
TO	28,348	689	258,608	40.60%			258,608	
BRASIL	**3,273,747**	**741**	**50,142,573**			**5,325,255**	**44,817,318**	**319,987**

Source: Brazilian Ministry of Finance, drawing on data provided by the States, 1997.

These figures illustrate the scale of personnel expenditure prior to the fiscal law and highlight the projected impact of its enforcement on both finances and employment.

Table 2 illustrates the severity of the situation prior to the Camata Law. In 1995, most states had personnel expenditure well above the 60 per cent limit of Net Current Revenue that was to be introduced, with several cases exceeding 80 per cent. From 1996 onwards, a gradual reduction can already be observed, although it was still insufficient.

Table 2 State personnel expenditure between 1996 and 2000

Brazilian states	1995	1996	1997	1998
RR	39%	42%	40%	33%
PB	63%	55%	59%	44%
TO	45%	41%	42%	49%
RN	79%	73%	67%	52%
AP	79%	61%	70%	54%
BA	55%	55%	52%	54%
PA	64%	66%	67%	54%
CE	67%	58%	61%	55%
MT	47%	74%	57%	57%
AM	28%	37%	40%	57%
SE	78%	70%	65%	58%
ES	70%	65%	65%	62%
MA	69%	65%	61%	64%
PI	86%	72%	70%	64%
GO	73%	69%	66%	69%
SP	69%	67%	66%	69%
SC	73%	70%	71%	71%
AC	79%	73%	74%	71%
PE	83%	78%	71%	71%
MS	69%	77%	64%	73%
DF	80%	82%	77%	74%
RO	80%	77%	77%	77%
MG	87%	80%	76%	77%
PR	73%	75%	74%	78%
AL	75%	73%	73%	79%
RS	82%	88%	85%	80%
RJ	87%	81%	80%	84%

Source: Ministry of Finance. Own elaboration.

In addition, after 1995 salary adjustments were granted only to specific sectors rather than to the public service as a whole. This enabled the Union to remain within the limits established by the Camata Law throughout the entire period. For example, in 1997 personnel expenditure as a proportion of net current revenue stood at only 43.8 per cent, and at 45.2 per cent in 1998.

However, a more detailed breakdown of Union personnel expenditure reveals quite evident potential sources of imbalance. At the same time, it shows that the burden of the adjustment fell essentially on active civil servants in the Executive Branch.

The distribution of the adjustment in personnel expenditure is a matter of considerable importance, especially since the asymmetries described in the case of the Union, which resulted from administrative decisions, tend to be reproduced with even greater intensity in the states, given the legal requirement to comply with the established limits.

Furthermore, the deadline established by Complementary Law No. 82 gave the law a temporary character on the law, since it referred only to the fiscal year in which it was published. The legislator appears to have assumed that the Law would not only be complied with within the stipulated period, but also that, once the "stock" of excess expenditure had been eliminated, no new situations would arise capable of generating fresh imbalances in the "flow". As a result, a legal gap was created regarding the timeframe for compliance with the limits in respect of subsequent adjustments.

Thus, despite the stimulus to fiscal discipline generated by the imposition of limits, at least four problems in the application of the Camata Law became evident: a) the criteria and instruments for the dismissal of excess staff; b) the sanctions applicable in the event of non-compliance; c) the distinction between temporary and permanent rules; and d) the manner in which the distribution of the adjustment would be carried out, particularly among the branches of government.

This realisation of the absence of adequate provisions in these norms paved the way for the enactment of Constitutional Amendment No. 19 of 1998, which aimed to fill those gaps. However, the first two gaps were only effectively addressed in June 1998, with the approval of Constitutional Amendment No. 19 itself. Among other advances, Article 21 of the Amendment stipulated that, in order to comply with the limits within the timeframe set by the complementary law, the federative units should reduce expenditure on commissioned posts and trust functions by at least 20 per cent and dismiss non-stable civil servants. If such measures proved insufficient to ensure compliance with the complementary law, stable civil servants could lose their positions, provided that the provisions of federal law were observed.

Another innovative provision introduced by Constitutional Amendment No. 19 concerned the suspension of all transfers of federal or state funds to the states, the Federal District and the municipalities that failed to comply with the aforementioned limits. This was undoubtedly an important sanction, which helped ensure the effectiveness of Constitutional Amendment No. 19 and of the provisions laid down in Article 169 of the Federal Constitution.

However, sanctions should be applied only when the federative unit has the effective capacity to comply with the legal provisions. Such conditions could only be established through the regulation of Constitutional Amendment No. 19, particularly with regard to the federal law determining the criteria for dismissal on grounds of excess expenditure.

In this regard, Complementary Law No. 96 of 31 May 1999, known as the New Camata Law, replaced Complementary Law No. 82 in the regulation of limits on personnel expenditure, pursuant to Article 169 of the Federal Constitution. Its role was both to introduce several modifications that helped clarify key concepts and to make compliance with personnel expenditure limits feasible, while extending the adjustment period by two years. It also established an adaptation rule, under which the adjustment was to be carried out at a minimum rate of two-thirds in the first 12 months and one-third in the following period, thereby preventing any further postponement of this much-needed adjustment.

Furthermore, the limits on personnel expenditure received more comprehensive treatment. In this regard, the New Camata Law set the new limit for the Union at 50 per cent of net current revenue, while maintaining the 60 per cent limit for the states, the Federal District and the municipalities. In order to comply with these limits, in addition to the provisions set out in the Administrative Reform, it established that a reduction in working hours with proportional salaries could be used as an independent or combined measure.

With regard to the distinction between temporary and permanent rules, Complementary Law No. 96 represented a major advance. Regarding the stock of excess expenditure (a temporary rule), it established the measures to be taken in the event that non-compliance with the limits persisted, as well as in cases of failure to meet the stipulated adjustment deadline. It defined corrective provisions and institutional penalties, including suspending federal or state fund transfers and prohibiting the Union from granting guarantees and from contracting credit operations with federal financial institutions.

With regard to the possibility of new imbalances in future flows (a permanent rule), the New Camata Law established that, while the federative entities remained non-compliant with the limits, increases in remuneration, the creation of posts or jobs, the granting of any benefits not provided for constitutionally, and new admissions would be prohibited, except for replacements resulting from death or retirement in the areas of health, education and public security.

It remained, therefore, to address the distribution of the adjustment among the branches of government. In this regard, the New Camata Law determined that the Legislative and Judiciary branches would be jointly responsible for complying with the limits, although it did not explicitly establish any proportionality. The draft Fiscal Responsibility Law complemented this initiative. In addition to consolidating provisions from the Administrative Reform and the Camata Law, it proposed maximum and prudential limits for personnel expenditure as a proportion of Available Tax Revenue for each branch of government in each of the three spheres of government. This initiative aimed to correct one of the most sensitive distortions in the structure of public spending in various Brazilian states and municipalities — namely, the high concentration of expenditure in the Judiciary and Legislative branches. This was undoubtedly the greatest demand for changes identified in the preliminary draft during the public consultation process.

The change in the percentages of personnel expenditure commitment was justified by the change in the revenue base. Since the Fiscal Responsibility Law (FRL) uses a more restricted revenue base than the Camata Law, the percentages had to be recalibrated upwards. On average, the aim was to maintain the same degree of rigour as the Camata Law. Furthermore, this adjustment was justified because Available Tax Revenue establishes that the prudential limit will be 90 per cent of the maximum limit. The same sanctions provided for in the Camata Law apply in the event of non-compliance at any time, along with a permanent rule allowing a return to the maximum limit over a 24-month period, at a rate of 1/24 per month, whenever the limit is exceeded for three consecutive months.

When the Fiscal Responsibility Law (FRL) was approved in 2000, following a succession of international crises (Mexico in 1995, Asia in 1997 and Russia in 1998), Brazil appeared to be finally building solid macroeconomic foundations that would enable the country to withstand the capital volatility triggered by international financial crises.

Indeed, the Fiscal Responsibility Law marked a structural break in the behaviour of the Federation’s public finances in 2000, leading to improvements across almost all indicators. Contributing to this outcome was the Law’s requirement that accounting and fiscal data be publicly disclosed, thereby reflecting each federative entity's true fiscal position.

Table 3 illustrates the significant improvement in fiscal indicators following the approval of the Fiscal Responsibility Law. By December 2000, most states had already brought personnel expenditure below the prudential limit of 49 per cent of Net Current Revenue. The reduction in net debt was equally notable, with the majority of states recording levels well below the reference value of 2.00.

Table 3. Personnel Expenditure and Net Debt as a Percentage of Net Current Revenue – Brazilian States
(December 2000 and December 2009)

Brazilian states	% PE/NCR Reference value: 49%	% PE/NCR - Reference value: 49%	% Net Debt/NCR - Reference value: 2.00	% Net Debt/NCR - Reference value: 2.00
	Dec. 2000	Dec. 2009	Dec. 2000	Dec. 2009
AC	47,32	46,10	1,04	0,37
AL	44,29	50,96	2,23	1,81
AM	44,76	46,16	1,00	0,24
AP	36,86	41,77	0,05	0,11
BA	35,89	46,75	1,64	0,63
CE	42,59	40,80	0,87	0,17
DF	32,89	43,45	0,36	0,17
ES	44,90	35,60	0,98	0,08
GO	49,17	46,10	3,13	1,28
MA	48,54	38,56	2,58	0,69
MG	63,86	46,16	1,41	1,79
MS	45,68	39,69	3,10	1,14
MT	45,22	39,80	2,50	0,54
PA	42,26	45,56	0,57	0,24
PB	42,10	51,63	1,53	0,34
PE	49,22	44,83	0,86	0,43
PI	45,22	42,83	1,73	0,60
PR	45,58	45,10	1,29	1,12
RJ	39,90	27,00	2,07	1,63
RN	41,15	49,79	0,71	0,17
RO	45,03	38,54	1,11	0,56
RR	38,68	35,73	0,31	0,31
RS	61,68	40,46	2,66	2,20
SC	52,03	37,10	1,83	0,61
SE	57,88	45,56	0,88	0,27
SP	49,27	41,29	1,93	1,51
TO	34,15	44,06	0,35	0,11

Secretariat of the National Treasury (SISTN/Ministry of Finance) – information self-reported by the states. Author's own elaboration.

In the Brazilian case, the creation of fiscal rules was not enough to contain the expansion of public spending. Over the following years, it became evident that fiscal fundamentals weakened as the rules were systematically disregarded. This result was driven in large part by the absence of strong societal pressure and by the influence of organised interest groups over public institutions. Enacting legislation alone has not been sufficient to secure lasting fiscal discipline.

4. Relaxation of the Fiscal Responsibility Law and the Rise in Public Debt

The government's economic policy, initiated in 2014 and characterised by increased expenditure, resulted in a public deficit of R$ 23 billion in 2014, compared with a surplus of R$ 73 billion in 2013, generating uncertainty regarding the stability of public accounts. Primary deficits became recurrent, and fiscal indicators deteriorated. In 2016, the President's impeachment and the volatility in financial markets and a rise in economic uncertainty, as reflected in indicators such as the FGV Economic Uncertainty Index (IIE-Br, FGV IBRE). Between 2014 and 2016, fiscal deterioration intensified amid economic recession and political instability.
This shift from a surplus to a deficit position coincided with the gradual flexibilisation of the Fiscal Responsibility Law, through legislative amendments and more permissive interpretations of its provisions, and with the spread of accounting practices that reduced the transparency of fiscal results. It also reflected a weakening commitment to primary surpluses.

The deterioration of the debt-to-GDP ratio in the context of the weakening of the FRL should be understood as the result of a broader erosion of fiscal discipline. The legal and accounting flexibilisation of the FRL, together with the growing tolerance for exceptional fiscal measures, did not operate in isolation. They opened room for persistent primary deficits, tax expenditures, extraordinary operations and expenditure expansion in other policy areas. These elements weakened the capacity of the fiscal framework to generate sustained primary surpluses. High real interest rates, low growth and recessionary episodes then amplified the effect of this weakened fiscal position on public debt.

These primary deficits contravened the principles of fiscal balance enshrined in the Fiscal Responsibility Law, as can be inferred from the combined reading of Articles 1, §1, 4 and 9, since there was no longer a sufficient result to contain public debt. The evolution of the result is presented in Table 4 below.

Table 4.Evolution of the Federal Primary Balance between 1995 and 2024

Year	Primary Balance (R$ million)	Observation
1995	3,336.00	Surplus
1996	2,908.00	Surplus
1997	-2,375.00	Deficit
1998	5,042.00	Surplus
1999	22,072.00	Surplus
2000	20,431.00	Surplus
2001	21,869.00	Surplus
2002	31,910.00	Surplus
2003	39,328.00	Surplus
2004	43,484.00	Surplus
2005	52,488.00	Surplus
2006	46,874.24	Surplus
2007	57,540.00	Surplus
2008	71,438.38	Surplus
2009	38,436.41	Surplus
2010	77,891.17	Surplus
2011	84,887.36	Surplus
2012	73,318.15	Surplus
2013	-23,482.41	First structural deficit
2014	-120,302.22	Deficit
2015	-161,275.63	Deficit
2016	-142,421.48	Deficit
2017	-124,021.38	Deficit
2018	-50,064.76	Deficit
2019	-743,087.00	COVID-19 pandemic
2020	-391,003.00	Deficit
2021	-248,499.00	Temporary surplus
2024	-11,032.00	Deficit

Source: Ministry of Finance and Ministry of Planning. Author's own elaboration

As primary surpluses gave way to persistent deficits, the capacity of the central government to stabilise and reduce public debt was weakened. Debt accumulation reflected both the loss of fiscal space for amortisation and the need to finance current expenditure through additional borrowing. According to the World Bank (2017), this rise in indebtedness was still due to a reduction in available revenues, especially as a result of the increased granting of tax benefits. This situation also affected the country's states, even though they did not issue bonds themselves, as prohibited by the Fiscal Responsibility Law. These entities incur debt through bank loans and by delaying payments to suppliers.

In both the Union and the states, the uncontrolled growth of current expenditure, in addition to obliging these governments to continue increasing the tax burden, restricted the level of public investment to below that required to finance economic growth. In this context, the most concerning development was the growth of public debt outpacing economic growth, leading to an increase in the debt-to-GDP ratio. With the continued expansion of this ratio, even the rise in taxation, intended to generate larger primary surpluses, was insufficient to prevent the mounting public indebtedness. In the federal government, the growth can be observed in the DBSP due to the primary deficit results, as can be seen in Table 5. This expansionary stance was supported by economists and policymakers associated with the governing coalition, who argued in favour of a more active fiscal policy.

Table 5. Evolution of the Debt-to-GDP Ratio – Federal Government
(Selected Years)

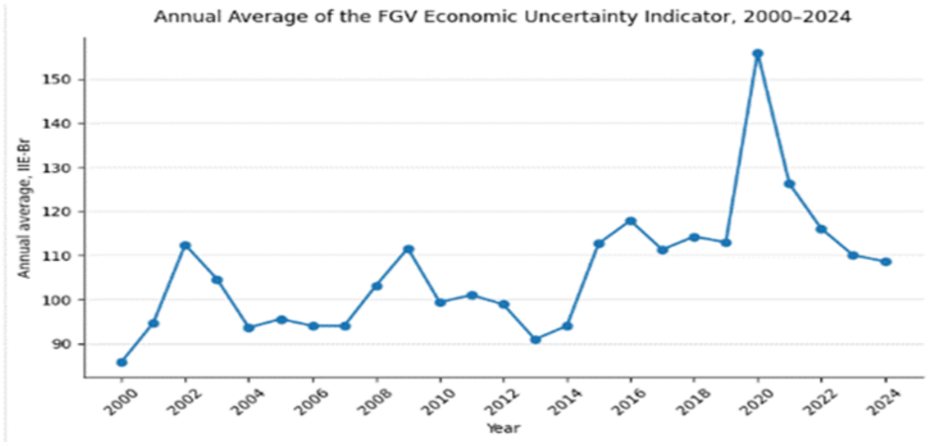
Year	Debt-to-GDP (%)	Fiscal Context
2000	52%	Post-Plano Real consolidation
2006	60%	Economic growth, but debt remained high
2010	60%	Post-global crisis
2014	55%	Last year with primary surplus
2016	70%	Beginning of persistent deficits
2020	88%	Pandemic and emergency fiscal expansion
2023	74%	Partial recovery
2024	76%	Persistent deficit and high interest rates

Source: Ministry of Finance and Ministry of Planning. Author's own elaboration

Although enforcement and transparency mechanisms were formally in place, organised professional groups were able to circumvent remuneration limits through allowances and other ancillary payments. These practices persisted because their benefits were concentrated among specific groups, whereas their fiscal costs were dispersed across society. Transparency alone was therefore insufficient to prevent rule circumvention, since the public disclosure of remuneration data did not necessarily translate into effective political, social or institutional constraints. This pattern is consistent with environments in which formal rules coexist with weak social sanctions of fiscal non-compliance (de Soto, 1989). This pattern is consistent with environments in which formal rules coexist with weak social and institutional enforcement mechanisms, as observed in several Latin American federations. This stands in contrast to the perspective of Poterba (1996, p.47), for whom fiscal rules do work: '…fiscal institutions do matter. Although the evidence is not conclusive, the preponderance of studies suggests that institutions are not simple veils …, but are important constraints on the nature of political bargaining. Studies of the demand for public spending, whether by state and local governments or by nations, should recognise that this demand is mediated through a set of budgeting rules".

5. The Post-2014 Evolution of Fiscal Discipline: Flexibilization, Shocks and New Institutional Arrangements

Between 2014 and 2016, fiscal deterioration intensified in a context of economic recession and political instability. The impeachment of the President was accompanied by fluctuations in financial markets and an increase in economic uncertainty, as reflected in indicators such as the FGV Economic Uncertainty Indicator.



Source : Fundação Getúlio Vargas (FGV).

The economy's capacity to respond to this economic crisis was severely constrained by the government's adoption of an expansionary fiscal policy amid intense spending pressures, even as government revenues declined, within a budgetary structure that offered almost no fiscal space for investment. This budget rigidity arose from rigid fiscal obligations and persistent expenditure pressures. Thus, there were no resources available to reallocate towards debt consolidation.

The budgetary straitjacket, with more than 95 per cent of government income already allocated to mandatory outlays, particularly expenditures on education and health as well as debt servicing including interest payments and amortisation, left little budgetary provision to finance priority spending such as research and development. This structural rigidity persisted regardless of revenue performance and was further compounded by off-budget liabilities. Consequently, public investment became the adjustment variable. Ultimately, the very budgetary category whose expansion could have contributed to increasing government revenue and GDP was constrained.

From an institutional perspective, this period reveals a loss of credibility in the set of rules, institutions and mechanisms that structure fiscal policy (responsibility laws, expenditure limits, debt rules, etc.). There were also tensions between policymakers and oversight institutions regarding the interpretation of fiscal rules. The increasing reliance on mechanisms to circumvent legal constraints, such as the so-called "pedaladas fiscais" (fiscal pedaling), which involved delaying transfers to public banks to disguise budgetary results, further undermined the effectiveness of the existing framework. The political crisis that culminated in the 2016 impeachment process reinforced the perception that fiscal discipline depends on formal rules and institutional stability.

Paradoxically, in response to this deterioration and the demands for new expenditure, the period between 2016 and 2019 was marked by debt expansion alongside attempts to re-establish fiscal discipline, most notably through the introduction of the constitutional expenditure ceiling. The simultaneous expansion of spending and the constitutional provision of a limit can be explained by the fact that the government is not a monolithic bloc; while some segments advocated an increase in public expenditure, others were concerned about the rising debt. This explained the introduction of the constitutional expenditure ceiling.

In other words, public debt kept climbing while awareness grew about how the pressure to spend was making everything worse. This constitutional rule tried to hold back the rise in primary expenditure with a strict cap adjusted only for inflation. But in practice it was full of loopholes written into ordinary laws and quite a bit of creative accounting. Its real impact was limited by deeper structural problems. Without key reforms such as pension overhaul, the steady increases in the minimum wage automatically drove up costs for things such as the Benefício de Prestação Continuada (BPC), a social assistance payment set at minimum wage levels for vulnerable elderly people and those with disabilities, along with minimum pensions, unemployment insurance and the annual wage bonus. All of that made it harder to control spending.

The COVID-19 pandemic in 2020 was the toughest stress test the fiscal framework had faced since the Fiscal Responsibility Law was enacted. At the time, the debate centered on whether to stick to the fiscal rules or meet the urgent needs of the population. This tension was resolved once it became clear that those rules ultimately exist to promote society's well-being. That conviction guided the institutional response, which included exceptional measures such as the creation of a special budgetary regime that temporarily suspended the fiscal constraints.

From 2023 onwards, the replacement of the expenditure ceiling with a new fiscal framework relaxed the rules, including exceptions for certain expenditures that were meant to be restricted. To meet this demand, a statute was introduced that combined primary balance targets, tolerance bands and expenditure growth limits linked to revenue performance. In institutional terms, this change replaced a rigid rule with a more flexible, results-based framework. Once again, expenditure was not effectively constrained.

This flexibility did not contain pension deficits or the rise in personnel expenditure, which circumvented the rules in force. As a result, fiscal targets failed to restrain spending, particularly at the lower bound of the tolerance range, alongside a continued reliance on compressing discretionary expenditure to achieve short-term adjustments. Public investment remained low, and primary deficits persisted.

In this context, the systematic pursuit of the lower bound of the fiscal target may generate procyclical effects, compressing aggregate demand and ultimately undermining the sustainability of fiscal adjustment itself. The persistence of low growth, high interest rates and limited fiscal space reinforces a dynamic in which efforts to contain expenditure may coexist with rising debt levels, thereby weakening the credibility of the fiscal framework.

The post-2014 trajectory thus reinforces the argument that fiscal rules, while necessary, are not sufficient to ensure sustained fiscal discipline in a complex federative context. The effectiveness of such rules depends on the quality of their institutional design, the capacity for enforcement and the existence of sustained political and social commitment. Excessively rigid rules tend to be circumvented or abandoned, while overly flexible frameworks risk losing credibility. Similarly, transparency mechanisms, although essential, do not automatically translate into effective constraints when social and institutional sanctions are weak.

The Brazilian experience since 2014 suggests that fiscal deterioration has resulted not only from adverse economic shocks but also from a misalignment between formal rules, political incentives and institutional capacities. The erosion of discipline reflects a gradual weakening of the mechanisms that had previously supported compliance, including credible enforcement, standardised accounting practices and a shared political commitment to fiscal sustainability.

From a public policy perspective, the reconstruction of fiscal discipline requires more than the adoption of new rules. It depends on strengthening the institutions responsible for interpreting, monitoring and enforcing fiscal norms, improving the quality and comparability of fiscal data and re-establishing a minimum level of political consensus around the objective of debt sustainability. Without these elements, even well-designed fiscal frameworks are likely to face the same limitations observed in the post-2014 period.

Conclusion

The FRL permitted fiscal discipline in Brazil for at least 10 years by imposing spending limits, fiscal targets, and transparency obligations on the Union, the states, and the municipalities. The creation of these rules had already been proposed by Public Choice authors, such as Buchanan (1986).

These fiscal measures were essential to keep federal spending under control, especially during electoral cycles. In these periods, elections intensify the competition for political office. This leads politicians from both the governing party and the opposition to broaden their electoral base by ramping up the supply of public goods to voters, behaviour that Public Choice theory has consistently described. Such exchanges of votes for public benefits are possible because a part of the electorate, especially those who rely on social assistance programmes, ends up paying only a fraction of the cost of the goods they receive.

There is a perception that even Public Choice authors did not foresee the resilience of fiscal indiscipline, as they assumed that creating rules would be sufficient to solve the problem. In practice, however, bureaucracy finds ways to circumvent them. It reached the point where new constitutional amendments stated that such norms would not be subject to exceptions. Understanding the factors that led to the flexibilisation of the Fiscal Responsibility Law is relevant to society, enabling citizens to better orient their decisions about what to demand of their parliamentarians.

Public deficits emerged at all three levels of government due to a populist national policy that followed a catch-all approach to decision-making, in which fiscal expansion was used as a tool to broaden electoral support. Governing and opposition parties alike sought to secure voter support by distributing public goods. Consequently, the Executive and Legislature expanded public expenditure and signalled to society that they had no intention of curbing spending.

Although subnational entities possess budgetary autonomy, the primary responsibility for maintaining the stability of public spending rests with the Union. Since the 1988 Constitution, however, the share of revenue accruing to states and municipalities has increased while that of the Union has declined. Consequently, to ensure that any potential inflationary pressures are not attributed exclusively to the Union, the legislation established common obligations to be observed by all federative entities.

The trajectory reconstructed in this article suggests that the main advance in the period 1995–2000 was the transition from barely credible limits, with weak sanctions and low enforcement capacity, to a more comprehensive framework whose design sought to reduce the scope for postponements and circumvent the ineffectiveness observed in the initial Camata Law experience. Thus, in its first ten years, the FRL succeeded in bringing fiscal discipline to the country, drawing on the lessons learned from the application and results of the Camata Law, and came to be regarded as a success.

In the following years, members of Parliament continued to introduce bills aimed at amending the FRL, resulting in the approval of five complementary laws that modified it: Complementary Law No. 148/2014, Complementary Law No. 156/2016, Complementary Law No. 177/2021, Complementary Law No. 195/2022, and Complementary Law No. 206/2024. Furthermore, the fiscal results revealed that formal rules, by themselves, were not sufficient to ensure the balance of public accounts, as divergent concepts were adopted, supported by differing interpretations from the Courts of Accounts of the states and municipalities, as well as by practices of creative accounting. In this way, the primary results largely lost their capacity to faithfully represent the solvency of the federative entities.

From a public policy perspective, the implication is clear: effective compliance with fiscal rules depends on auditable metrics, national standardisation of criteria, and less discretionary correction and sanction mechanisms, in order to reduce the scope for earnings management and to strengthen comparability across federative entities. However, the most essential element for the country to achieve lasting fiscal discipline is sustained pressure from society and voters on Parliament, together with the requirement that fiscal documents accurately and faithfully reflect the true situation of the public entities.

In comparative terms, advanced economies tend to operate with a more consolidated fiscal architecture, characterised by greater transparency, standardisation of information and established scrutiny routines involving legislatures, oversight bodies, markets and public opinion. This raises the reputational and political costs of persistent deviations. Esta divergência de diagnóstico entre as instituições é esperada em países em desenvolvimento com herança colonial, como apontado por Acemoglu, Johnson & Robinson (2001).

This combination of transparency and well-designed budgetary institutions helps to mitigate the deficit bias associated with the common-pool problem and reduces the scope for opportunistic cycles, although it does not eliminate cross-country heterogeneity.

By contrast, the literature indicates that many emerging economies face greater vulnerability to shocks and more frequently display patterns of fiscal procyclicality and "debt intolerance". As a result, fiscal sustainability in these economies tends to be more sensitive to shifts in market confidence and to historical episodes of inflation and default.

This article has explored one central aspect of Brazil's fiscal discipline framework: the containment of personnel expenditure through the Camata Laws and, later, the Fiscal Responsibility Law. The FRL also addressed other vulnerabilities, such as indebtedness, credit operations, fiscal targets, transparency requirements and the creation of permanent expenditure. A further step in curbing public spending was introduced by Articles 16 and 17 of the FRL, which restricted expenditure by requiring that any new commitments be backed by identified sources of financing. The extent to which these provisions strengthened fiscal discipline, or failed to prevent its subsequent erosion, remains a significant question for future research.

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