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New fiscal framework: Analysis of the substitute text to PLP 93 of 2023

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New fiscal framework: Analysis of the substitute text to PLP 93 of 2023

Vilma da Conceição Pinto, Alexandre Andrade[1]

This Technical Note aims to explain the details of the new fiscal rule that intends to replace the current spending cap. To this regard, we will analyze some of the changes proposed by PLP No. 93, published on April 18, 2023, authored by the Executive Branch, and the changes made in the House of Representatives, addressing the following topics: the new system for primary result targets, the new fiscal framework to control the real growth of expenses, the mechanisms to preserve public investments, and the changes in the Constitutional Fund of the Federal District (FCDF).

Based on the simulations performed, it is concluded that the proposed new fiscal framework compromises fiscal transparency since it is extremely complex and largely dependent on revenue generation, which, for now, is still uncertain.

I – Introductory Statement

After the end of the Covid-19 pandemic, many countries faced the need to restore reliability in the management of public finances[2]. In Brazil, the main fiscal cornerstone was the spending cap, which, after several modifications, lost its effectiveness[3].

Due to this difficult diagnosis and the several changes in the spending cap, Constitutional Amendment (EC) No. 126, dated December 21, 2022 (Transition EC), authorized a last round of spending increases on an exceptional basis, however, conditioned to the implementation of a new fiscal rule to replace the current regime.

According to Art. 6 of EC 126: "*The President of the Republic shall forward to the National Congress, until August 31, 2023, a complementary bill to establish a sustainable fiscal regime to ensure the macroeconomic stability of the country and create the appropriate conditions for socioeconomic growth*," including the golden rule.

The expenses expanded and/or perpetuated by EC No. 126 are no longer compatible with the current fiscal rule, and any proposal that the Executive would address would most likely not contemplate short-term adjustments to the newly expanded expenses. In this context, the new fiscal framework was presented: to provide the possibility of expanding primary expenditures above inflation, conditioned to the real growth of primary revenues and with primary result targets with tolerance intervals.

Therefore, Supplementary Bill (PLP) No. 93, dated 2023[4], presented by the Executive Branch, brought important elements regarding the fiscal policy guidelines for the coming years. This technical note aims to evaluate the new fiscal rule in terms of effectiveness, regulatory instruments, and design.

Besides this introduction, this note recalls the fiscal rules in effect since the Fiscal Responsibility Law (LRF) until EC No. 126. After that, the main points of the new tax framework are presented, highlighting the measures proposed by the Executive and the changes made to the text in the House of Representatives. The subsequent section seeks to simulate the effects of the new fiscal rule, while the following section discusses the results and presents the conclusions.

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[2] View: Davoodi H. R., P. Elger, A. Fotiou, D. Garcia-Macia, X. Han, A. Lagerborg, W.R. Lam, and P. Medas. 2022. "Fiscal Rules and Fiscal Councils: Recent Trends and Performance during the Pandemic", IMF Working Paper No.22/11, International Monetary Fund, Washington, D.C. at: http://bit.ly/3NizjWl and New economic governance rules fit for the future (European Commission), available at: https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/economic-governance-review_en.

[3] For example, check out Issue No. 72 of the IFI's January 2023 Fiscal Follow-Up Report (RAF). Available at: https://www2.senado.leg.br/bdsf/bitstream/handle/id/604617/RAF72_JAN2023.pdf.

[4] Available at: https://www.congressonacional.leg.br/materias/materias-bicamerais/-/ver/plp-93-2023.

II The Federal Government's fiscal rules: from the LRF to the EC 126, of 2022

Currently, the main fiscal rules in effect for the Federal Government are (i) the primary result targets, (ii) the golden rule, and (iii) the spending cap. Rules related to debt limits are foreseen in the Fiscal Responsibility Law (LRF), but they have not yet been regulated for the Federal Government[5].

The primary result targets are supported by the Supplementary Law (LC) No. 101, of May May 4, 2000, also known as LRF[6]. Paragraph 1 of Art. 4 of the LRF establishes that the annual Budget Guidelines Law (LDO) will contain an annex of fiscal targets with annual targets, in current and constant values, related to revenues, expenses, nominal and primary results, and the amount of public debt for the year to which they refer and for the following two years.

According to Barbosa (2022)7[7] , since its creation, 57% of the time, the primary result targets have been changed. Table 1 presents information regarding the Federal Government's primary result targets, comparing the value initially set in the LDO, the changes made in the LDO throughout the year, and the data realized for purposes of verifying compliance with the rule. It is worth mentioning that in some years, although the target has not changed, the exclusion of some items and/or compensation was allowed among the results of the federal state-owned companies.

[5] According to item VI of Art. 52 of the Federal Constitution, it is up to the Federal Senate to set global limits for the consolidated debt of the Union, States and Municipalities. These limits, however, depend on a proposal by the President of the Republic. According to item I of Art. 30 of the LRF, within 90 days, the President of the Republic should send a message to the Federal Senate with a proposal for the debt limit as a proportion of the Net Current Revenue (RCL) for the three spheres of government. On August 8, 2000, the Executive Branch sent a message (MSF 154, 2000) to the Federal Senate with a proposal for a debt limit for all three spheres, being 3.5 of the Gross National Income (GNI) for the Federal Government, 2.0 for states and 1.2 for municipalities. MSF 154 resulted in Resolution #40, 2001, with limits set only for states and municipalities.
Link to MSF 154, 2000: https://www25.senado.leg.br/web/atividade/materias/-/materia/44833.
Federal Senate Resolution No. 40, 2001: https://www2.camara.leg.br/legin/fed/ressen/2001/resolucao-40-20-dezembro-2001-429320-normaatualizada-pl.html.
Constitution of the Federative Republic of Brazil of 1988 (CF): https://www.planalto.gov.br/ccivil_03/constituicao/constituicao.htm.
[6] https://www.planalto.gov.br/ccivil_03/leis/lcp/lcp101.htm.
[7] https://blogdoibre.fgv.br/posts/21-anos-de-meta-de-resultado-primario.

TABLE 1. EVOLUTION OF COMPLIANCE WITH THE CENTRAL GOVERNMENT'S PRIMARY SURPLUS TARGETS (R$ BILLION AND % OF GDP)[8]

Year	Goal		Changed goal		Realized (bottom line)		Discounting realized	Note regarding goal achievement
	R$	% OF GDP*	R$	% OF GDP**	R$	% OF GDP***	R$	
2001	32.3	2.6%	28.1	2.3%	22.0	1.7%	0.0	The goal was accomplished with compensation for the excess of the federal state-owned companies.
2002	26.4	2.0%	29.2	2.3%	31.9	2.1%	0.0	The goal was accomplished.
2003	32.0	2.3%	39.1	2.4%	38.7	2.3%	0.0	The goal was accomplished.
2004	43.3	2.5%	43.3	2.5%	52.4	2.7%	0.0	The goal was accomplished.
2005	44.5	2.4%	44.5	2.4%	55.7	2.6%	0.0	The goal was accomplished.
2006	53.0	2.5%	53.0	2.5%	51.4	2.1%	2.8	The goal was accomplished.
2007	56.2	2.4%	53.0	2.1%	59.4	2.2%	5.1	The goal was accomplished with the abatement.
2008	60.8	2.2%	60.8	2.2%	71.3	2.3%	7.8	The goal was accomplished.
2009	68.5	2.2%	43.3	1.4%	42.4	1.3%	17.9	The goal was adjusted due to the economic crisis of 2008-09. Accomplished with abatement.
2010	72.6	2.1%	76.3	2.1%	78.7	2.0%	22.1	The goal was accomplished.
2011	81.8	2.1%	81.8	2.1%	93.0	2.1%	28.0	The goal was accomplished.
2012	97.0	2.1%	97.0	2.1%	86.1	1.8%	39.3	The goal was accomplished.
2013	108.1	2.2%	108.1	2.2%	75.3	1.4%	35.1	The goal was accomplished.
2014	116.1	2.1%	116.1	2.1%	-20.5	-0.4%	161.7	The goal was accomplished.
2015	55.3	1.0%	-51.8	-0.9%	-116.7	-1.9%	66.9	The goal was accomplished with state compensation of state-owned companies and abatement.
2016	24.0	0.4%	-170.5	-2.8%	-159.5	-2.5%	0.0	The goal was accomplished after the change.
2017	-139.0	-2.0%	-159.0	-2.4%	-118.4	-1.8%	0.0	The goal was accomplished.
2018	-129.0	-1.8%	-159.0	-2.2%	-116.2	-1.7%	0.0	The goal was accomplished.
2019	-139.0	-1.8%	-139.0	-1.8%	-88.9	-1.2%	0.0	The goal was accomplished.
2020	-124.1	-1.6%	-124.1	-1.6%	-745.3	-9.8%	0.0	The goal was suspended as a result of the pandemic.
2021	-247.1	-3.2%	-247.1	-3.2%	-35.9	-0.4%	79.4	The goal was accomplished.
2022	-170.5	-1.9%	-170.5	-1.9%	54.9	0.6%	40.5	The goal was accomplished.

Source: LDO, various years, and Quarterly Reports of Fiscal Goals Evaluation, multiple years. Elaboration: IFI.
** GDP projected in the LDO; ** GDP projected in the last LDO amendment; *** GDP accomplished according to SCN 2010 methodology.*

Table 1 shows that the system of primary result targets has been made exceptional at various points in time, either by changing the target, or by allowing some primary result items to be disregarded for purposes of determining the rule, or by authorizing the over-target of some entity to be used to compensate for the frustration of another entity, etc. Even so, the primary surpluses were enough to maintain a sustainable trend for the public debt/GDP ratio until before the economic crisis of the 2014-2016 period.

According to the current system, the targets are set annually in the Budget Guidelines Law, and during the budget execution, the Federal Government incorporates the data held up to the assessment date, reviews the macroeconomic parameters, and updates the estimates of primary revenues and mandatory expenses for the fiscal year. When comparing the spending needs of discretionary expenditures with the expenditures likely to meet the primary target, contingencies are made, if necessary – Art. 9 of the LRF.

The contingency of discretionary spending is, therefore, a way to correct deviations from the primary target during the execution of the budget. If, in the following evaluations, the scenario proves to be better than the previous one, it is possible to reverse the contingency.

Besides the primary result targets, the prohibition on the possibility of using debt to pay current expenses constitutes another rule in the current fiscal framework. Such rule, known as the Golden Rule, aims at ensuring that the credit operations carried out by the state entity are smaller than the capital expenditures, essentially public investments, which generate assets with an economic or social return over time.

According to item III of Art. 167 of the Federal Constitution, it is forbidden to carry out credit operations that exceed the amount of capital expenditures, except for those authorized through supplementary or special credits with a specific purpose and approved by the Legislative Branch by an absolute majority.

In 2017, compliance with the golden rule relied on extraordinary resources, which reduced the need for capital revenues to pay current expenses. According to the National Treasury, early payments of loans to the BNDES were crucial for compliance with the rule in 2017[8].

Table 2 below shows the history of borrowings and repayments between the BNDES and the National Treasury from 2008 until May 2023.

TABLE 2. HISTORY OF BORROWINGS AND REPAYMENTS OF THE BNDES TO THE NATIONAL TREASURY (CURRENT R$ BILLION).

Year	Borrowings	Returns to the National Treasury		
		Principal + Interest	Anticipated liquidation	Total returns
2008	22.5		-	0.0
2009	105.0	4.1	-	4.1
2010*	107.1	10.4	-	10.4
2011	50.2	14.6	-	14.6
2012	55.0	13.3	-	13.3
2013	41.0	14.7	-	14.7
2014	60.0	6.2	-	6.2
2015	-	8.9	15.8	24.7
2016	-	6.2	113.2	119.4
2017	-	2.6	50.0	52.6
2018	-	1.0	130.0	131.0
2019	-	23.0	100.0	123.0
2020	-	16.0	-	16.0
2021	-	12.8	63.0	75.8
2022	-	10.9	72.3	83.3
2023**	-	1.8	-	1.8

Source: BNDES (https://www.bndes.gov.br/wps/portal/site/home/transparencia/recursos-do-tesouro-nacional).
**Includes R$ 24.7 billion related to* Petrobras capitalization. ** last update on 05/09/2023.

In 2019, the rule was changed through Law No. 13,843 of June 17, 2019, which opened a supplementary credit of R$ 248.9 billion to reinforce current budget appropriations[9]. Article 4 of Constitutional Amendment No. 106 (the War Budget Amendment) suspended the golden rule during the period of public calamity caused by the Covid-19 pandemic in 2020. In 2021, however, two Constitutional Amendments (EC No. 109 and EC No. 113) changed the golden rule to create some exceptions and clarify some points.

EC No. 109 inserted § 6 to Art. 167 of the Federal Constitution to state that, for the purposes of determining compliance with the golden rule at the end of the fiscal year, *"revenues from credit operations carried out in the context of the management of the federal public securities debt will only be considered in the fiscal year in which the respective expense was incurred."* In addition, the EC authorized the payment of Emergency Aid in 2021 and excluded them, up to the amount of R$ 44 billion, from the calculation of the primary result targets, the spending cap (established by EC No. 95, 2016), and the calculation of the golden rule.

[8] It is worth noting, however, that compliance with the Golden Rule in 2017 relied on extraordinary resources that reduced the need for credit operation revenues. We highlight the anticipated return by BNDES of resources that the National Treasury had lent to the bank in the amount of R$ 50 billion. It is noted, therefore, that these resources were critical to compliance with the Golden Rule in fiscal year 2017." STN, 2018. Debt Report: Golden Rule. Available at: https://sisweb.tesouro.gov.br/apex/f?p=2501:9::::9:P9_ID_PUBLICACAO:29302.
[9] Available at: http://www.planalto.gov.br/ccivil_03/_ato2019-2022/2019/lei/L13843.htm.

EC No. 113 changed the adjustment factor for the spending cap, previously determined by the accrued inflation over 12 months until June of the previous year. The change was to use the accrued inflation from January to December. As the budget proposal was submitted to Congress in August for the months of the second half of the year, it was necessary to use inflation estimates. This change in the indexer for adjustment of the cap was exempted from the golden rule up to the limit of R$ 15 billion.

Table 3 below shows the evolution of sufficiency for the golden rule, indicating the constitutional exceptions and changes that made it possible to comply with it over time.

TABLE 3. EVOLUTION, COMPOSITION AND MARGIN FOR THE GOLDEN RULE (% OF GDP)

	Capital expenditures (i)	Credit Op. Revenues (ii)	Var. of the debt subaccount (iii)	Considered revenues (iv) = (ii) - (iii)	Constitutional exceptions (v)	Margin for the Golden Rule (vi) = (i) - (iv) + (v)
2000	30.6	29.1		29.1		1.5
2001	23.6	20.4		20.4		3.1
2002	22.6	19.2		19.2		3.4
2003	28.7	27.4		27.4		1.3
2004	23.9	22.4		22.4		1.6
2005	27.1	27.1		27.1		0.0
2006	22.6	22.5		22.5		0.1
2007	19.8	19.7	0.2	19.5		0.2
2008	17.0	13.2	-0.6	13.8		3.1
2009	17.9	14.9	2.8	12.2		5.8
2010	15.5	12.9	-0.3	13.2		2.3
2011	15.2	12.9	0.0	12.9		2.3
2012	15.5	11.5	1.9	9.5		5.9
2013	13.4	9.5	-0.8	10.3		3.1
2014	16.3	14.3	-0.2	14.5		1.7
2015	14.4	17.1	3.8	13.4		1.0
2016	16.6	16.7	1.5	15.2		1.4
2017	13.7	14.4	1.2	13.2		0.4
2018	12.9	13.3	0.9	12.4		0.5
2019	11.8	13.2	-1.1	14.3	3.3	0.7
2020	15.9	21.7	1.2	20.5		-4.6
2021	20.6	22.8	3.1	19.7	0.5	1.3
2022	17.8	15.7	-1.4	17.1		0.6

Source: STN and IBGE. Elaboration: IFI.

Until 2016, the targets for primary results and the golden rule were the main fiscal rules in force in the country. However, as emphasized by Barbosa (2022) and Barros & Afonso (2013), primary targets began to be also met with the increasing use of non-recurring fiscal operations. Thus, the severe economic and fiscal crisis between 2014 and 2016, with the consequent loss of investment grade, raised the debate about the need to introduce a new fiscal anchor capable of providing greater credibility in implementing the fiscal policy in the following years. In this context, the rule that started to limit the evolution of the Federal Government's primary expenses emerged, introduced by EC No. 95 of December 15, 2016[10].

The spending cap, formally called the "new fiscal regime", aimed to limit the growth of the Federal Government's primary expenses (by inflation) for 20 years. According to the rule, primary expenses, with a few exceptions, would have no real growth. The spending limit corresponded to the cash concept spending (payment of expenses of the fiscal year and accrued liabilities) of 2016, adjusted annually by the previous year's inflation accrued over 12 months until June[11].

[10] The original text is available at: https://www.planalto.gov.br/ccivil_03/constituicao/emendas/emc/emc95.htm.
[11] For 2017, the first year of the rule, a factor of 7.2% was used to correct the limit instead of the inflation over the twelve months up to June 2016.

Constitutional Amendment No. 95 also provided that this correction factor could only be changed after the 10th year of the fiscal rule, that is, in 2026.

It was justified to consider the accumulated inflation over 12 months until June of the previous year, instead of the inflation of the previous calendar year, for predictability reasons so that the budgeting was done with an already known inflation. Since the budget is submitted annually by August 31 of the year prior to the reference year, using inflation centered on June would bring this predictability.

Initially, the spending cap did not have an enforceable character; that is, it would be possible to disregard the rule with the condition that automatic triggers would be activated until expenses returned to the limit (Art. 109 of EC No. 95). The constitutional minimums for health and education were also changed to follow the same correction factor of the cap rule for the other expenses.

As already demonstrated in the IFI reports, the spending cap has undergone several changes, the last through EC No. 126 of December 21, 2022 (Transition PEC). The modification increased the cap for 2023 by R$ 145 billion, expanded the list of expenses not subject to the rule, such as investments (up to a certain limit), and socio-environmental projects funded with donations, among others, and determined that the President of the Republic would send a proposal for a new rule to replace the current one. The current rule would therefore be repealed as soon as a new framework is approved.

According to RAF No. 72, January 2023[12], in the first six years of the new fiscal regime, the spending cap underwent at least five constitutional changes that directly or indirectly influenced the rule, the last being made through EC No. 126. All the amendments, to a greater or lesser degree, contributed to weakening the current fiscal regime, either by expanding the space provided in the original rule, removing expenses from the limits imposed by the rule, or making changes to spending outside the cap.

The first change in the original spending cap rule occurred in 2019 with EC No. 102, which authorized the payment of the revision of the onerous assignment contract for oil exploration[13] outside the cap. In 2020, although primary expenditures were very high after the outbreak of the Covid-19 pandemic, these expenditures were not subject to the cap and were made through extraordinary credits. The cap rule approved in 2016 provided for spending in calamity situations outside the rule's limits.

Constitutional Amendment No. 109 of 2021 authorized a new round of spending through extraordinary credits, dispensing with the rules set forth in § 3 of Art. 167 of the Federal Constitution. It occurred even though the aforementioned paragraph states that extraordinary credits will only be admitted to meet unforeseeable and urgent expenses.

Another change made in Constitutional Amendment No. 109 of 2021 was to improve the provision that deals with some sanctions in case of non-compliance with the rule. For these situations, the original cap rule provided for automatic triggers. The modification introduced a trigger activation in situations where it is verified, during the preparation of the Annual Budget Bill (PLOA), that the ratio between mandatory expenses and total expenses subject to the cap exceeds 95%.

Later on, but in the same year, Constitutional Amendments No. 113 and No. 114 changed the system of court-ordered payments and the index for correction of the cap, using the inflation rate from January to December. The adjustment made in the indexer occurred retroactively, widening the space in the spending cap. The creation of a cap for payment of court-ordered debts within the fiscal rule also opened space for other primary expenditures. It was established, however, that the rule will expire at the end of 2026, being necessary to discuss and measure its impacts on the Federal

[12] Available at: https://sisweb.tesouro.gov.br/apex/f?p=2501:9::::9:P9_ID_PUBLICACAO:29302.

[13] I analyzed this topic in the January 2019 issue of IBRE's Boletim Macro. Available at: https://portalibre.fgv.br/sites/default/files/2020-02/boletimmacroibre_1901.pdf

Government's public accounts. Both measures generated an impact of R$ 113.1 billion for the Federal Government in 2022, according to RAF No. 60, from January 2022[14].

In July of last year, Constitutional Amendment No. 123, known as the State of Emergency PEC, authorized new spending outside the cap. This Constitutional Amendment recognized a state of emergency due to the sharp rise in oil and fuel prices and authorized several extraordinary expenses in the last months of 2022, which would not be subject to the spending cap. The authorization of expenses reached R$ 41.3 billion, of which R$ 36.4 billion, or 88.1%, were actually spent during the year.

Finally, it is worth pointing out that these are not the only fiscal rules in effect in the country. They all had the common goal of promoting responsibility in fiscal management and reached different points of fiscal policy. In January 2018, IFI surveyed the different instruments provided in the Brazilian legal system, including the Federal Government, states, and municipalities. The following chart aims to update this survey, which indicates the importance of harmonization and transparency of the different fiscal management instruments.

CHART 1. FISCAL RULES IN BRAZIL

Rule	Description	Legal Basis	Scope	Type	Situation
Rule of thumb	It prohibits credit operations that exceed the amount of capital expenditures.	Federal Constitution (Art. 167, III); Fiscal Responsibility Act (LRF) (Art. 32, § 3º); and Resolution Federal Constitution 48/2007	All levels of government	Result	Current
Spending Cap	It limits the amount of primary expenditures, equivalent to the previous year's limit adjusted for inflation. The limit is individualized by autonomous branches and agencies.	Federal Constitution (articles 107 to 112, Temporary Constitutional Provisions Act - ADCT)	Federal Government	Expense	Effective until a new rule is approved via LC.
Generation of Social Security Expenses	It prohibits the creation, increase, or extension of social security benefits or services without a source of funding.	Federal Constitution (Art. 195, § 5)	All levels of government	Expense	Current
Primary result target	It sets annually, in the Law of Budget Directives, the primary result target to be pursued in the fiscal year to which the law refers.	LRF (Art. 4, § 1)	All levels of government	Result	Current
Generation of obligatory expenditure	It prohibits the creation or increase of mandatory expenses of a continuous nature without demonstrating the origin of the resources to fund them. Financial effects must be offset by permanent increases in revenue or permanent reduction in expenses.	Federal Constitution (Art. 113, ADCT) and LRF (Art. 17)	All levels of government	Expense	Current
Revenue waiver	It prohibits the concession of revenue waiver without demonstrating that the benefit will not affect the fiscal goals and without compensation measures for revenue increase.	Federal Constitution (Art. 113, ADCT) and LRF (Art. 17)	All levels of government	Result	Current
Personnel Expenditure Limit	It sets limits for total personnel expenditures as a function of the net current revenue of the level of government. The limits are fixed by the level of government and, in each of them, by branch and autonomous agency.	Federal Constitution (Art. 113, ADCT) and LRF (Art. 14)	All levels of government	Expense	Current
Debt Limit consolidated	It sets overall limits for the amount of consolidated debt of the Federal Government, the states, the Federal District, and the municipalities. The limits are defined by the Federal Senate (resolution) by a proposal of the President of the Republic.	Federal Constitution (Art. 52, VI); LRF (Art. 30, I); and Resolution SF 40/2001	All levels of government	Debt	Federal Government: not created; Other levels of government: in effect

[14] Available at: https://www2.senado.leg.br/bdsf/bitstream/handle/id/595062/RAF60_JAN2022.pdf.

Rule	Description	Legal Basis	Scope	Type	Situation
Securities debt limit	It sets global limits for the amount of securities debt of the Federal Government, state, Federal District, and municipal. The limits are defined by the Federal Senate (resolution) by a proposal of the President of the Republic.	Federal Constitution (Art. 48, XIV and Art. 52 IX); LRF (Art. 30, I and II); and Resolution SF 40/2001	All levels of government	Debt	Federal Government: not created; Other levels of government: in effect
Limit for credit operations	It establishes global limits for external credit operations and of the Federal Government, the states, the Federal District, and the municipalities. The limits are defined by the Federal Senate (resolution) by a proposal of the President of the Republic.	Federal Constitution (Art. 52, VII); LRF (Art. 30, I); Resolution SF 48/2007; and Resolution SF 43/2001	All levels of government	Debt	Current
Limits for granting guarantees in credit operations	It sets limits for granting Federal Government guarantees in foreign and domestic credit operations. The limits are defined by the Federal Senate (resolution) by a proposal of the President of the Republic.	Federal Constitution (Art. 52, VIII); LRF (Art. 30, I); and Resolution SF 48/2007	Federal Government	Debt	Current
Entering into outstanding liabilities	It prohibits the heads of branches or autonomous agencies, in the last eight months of the term in office, from contracting an obligation of expenditure that cannot be fully met within it or that has installments to be paid in the following year without sufficient cash available.	LRF (Art. 42)	All levels of government	Debt	Current
Budgetary rigidity (95% rule)	It establishes automatic triggers for situations in which the mandatory primary expenses are above 95% of the total primary expenses, considering the forecast in the Annual Budget Law.	CF (Art. 109, ADCT)	Federal Government	Expense	Effective until a new rule is approved via LC.

Source: IFI.

III – Summary of some points of the proposed new fiscal framework and changes made in the Chamber of Deputies

The new fiscal framework proposed by the Executive branch had the objective of complying with the provisions of Art. 6 of Constitutional Amendment No. 126, which establishes: *"The President of Brazil must submit to the National Congress, by August 31, 2023, a complementary bill to establish a sustainable fiscal regime to guarantee the macroeconomic stability of the Country and create the appropriate conditions for socioeconomic growth", including with regard to the* Golden Rule.

In the substitute approved by the Chamber of Deputies, the rapporteur also included the conduct of fiscal policy compatible with sustainable levels of public debt as an objective. Thus, the project starts to comply not only with Art. 6 of the Amendment. No. 126, but also to item VIII of Art. 163 of the Federal Constitution, inserted by Amendment No. 109, of 2021 (derived from the so-called Emergency amendment Bill).

In accordance with item VIII of the Art. 163 of the Federal Constitution: "*Complementary law shall provide for: (...) VIII – debt sustainability, specifying: a) indicators for its assessment; b) levels of compatibility of fiscal results with the debt trajectory; c) convergence trajectory of the amount of debt with the limits defined in the legislation; d) adjustment measures, suspensions, and prohibitions; e) asset disposal planning with the purpose of reducing the amount of debt. Sole paragraph. The complementary law dealt with in item VIII of the caput of this article may authorize the application of the prohibitions provided for in Art. 167-A of this Constitution*".

The substitute approved in the Chamber of Deputies (CD) and now being discussed in the Federal Senate (SF) contemplated these and other alterations in relation to the initial text. Some of these points are detailed below.

1. On debt sustainability

The text approved by the Chamber of Deputies provides that "*the Union's fiscal policy must be conducted in such a way as to maintain the public debt at sustainable levels, preventing risks and promoting fiscal adjustment measures in the event of* *deviations, guaranteeing the solvency and intertemporal sustainability of the public accounts*" (**Paragraph 2 of Art. 1 of PLP No. 93**).

In this way, the proposal defines debt sustainability as establishing primary results targets compatible with *stabilizing* the General Government Gross Debt ratio (DBGG) in relation to GDP (economic growth). This verification consists of calculating, based on information released monthly by the Central Bank of Brazil, the ratio between debt and economic growth, called DBGG/GDP.

The project provides that the Budget Directives Law (LDO) should demonstrate, for ten years, the expected effect and the compatibility of meeting the primary result targets on the path of public debt convergence, evidencing the values of fiscal results consistent with the stabilization of the DBGG/GDP ratio.

The project also provides for adjustment measures in case of deviations and defines them as follows:

(i) Obtaining a primary result compatible with the sustainability of DBGG/GDP;
(ii) Adoption of expenditure growth limits;
(iii) Application of triggers of Art. 167-A of the Federal Constitution; and
(iv) Recovery and management of public revenues.

The main rules governing each adjustment measure provided for in PLP No. 93 of 2023 are detailed below.

2. Obtaining a primary result compatible with the sustainability of the public debt

The new fiscal framework provides that, annually, through the Budget Directives Law (LDO), targets are set for the primary result compatible with the sustainable trajectory of the public debt. According to the project, the goals will be defined annually for the reference year and the next three years, expanding the horizon of the PLDO from three to four years (Art. 2 of the PLP No. 93).

PLP No. 93 also proposes the creation of fixed tolerance intervals for the primary result targets of plus or minus 0.25 percentage points (p.p.) of GDP (Art. 11 of PLP No. 93). The proposal sent by the Executive branch allowed changing these ranges every four years, while the wording given to the text during its processing in the Chamber made these intervals fixed.

The text of PLP No. 93 amended by the Chamber also began to provide for sanctions in case of non-compliance with the primary target, that is, in the situation where the result achieved is below the lower limit of the tolerance interval, as well as bonuses for cases of primary results performed above the upper limit of the tolerance interval.

It is worth mentioning that this triggering mechanism already exists in the current spending ceiling (Federal Constitution, Art. 109 of the ADCT), however, as soon as the PLP is enacted, the aforementioned constitutional provision will be revoked. In the Executive branch bill, this mechanism would not be reestablished. The current text provides for the possibility of activating triggers according to the systematic below.

According to the project:

a) Bonus (Art. 9 of the PLP No. 93): If the primary result of the previous year is above the upper limit of the tolerance interval (primary target plus 0.25 p.p. of GDP), the excess primary result, limited to 70% and/or 0.25% of GDP, can be used for public investments. Thus, if the excess primary result (described in equation 1) is above 0.25% of GDP, an amount equivalent to this percentage can be used for public investments. In the situation where 70% of the surplus primary result is less than 0.25% of GDP, the entire surplus value may be used (already with the application of 70%).

$$surplus = 70\%\ x\ (\ RP_{completed} - (RP_{goal} + 0.25\%\ of.GDP)) \tag{1}$$

b) Sanction (Art. 6 of the PLP No. 93): If the primary result of the previous year is below the lower limit of the tolerance interval (primary target minus 0.25 p.p. of GDP), the automatic triggers provided for in Art. 167-A of the Federal Constitution will be activated, until the next annual calculation, following the following criteria:
   - First year of non-compliance with the primary goal: Items II, III, VI, and X of Chart 2.
   - Non-compliance with the primary target from the second consecutive year onwards: all triggers of Art. 167-A of the Federal Constitution - Chart 2.

CHART 2. TRIGGERS PROVIDED IN ART. 167-A OF THE FEDERAL CONSTITUTION

Item of Art. 167-A of the Federal Constitution	Description (prohibitions)
I	Granting, in any capacity, of advantage, increase, adjustment, or adequacy of remuneration of members of any branch or agency
II	Creation of a position, job, or function that implies an increase in expenses
III	Career structure change that implies an increase in expenses
IV	Entry or hiring of personnel, in any capacity, except replacements
V	Conducting a selection for public office.
VI	Creation or increase of allowances, advantages, bonuses, payments, representation allowances, or benefits of any nature, including those of compensatory nature
VII	Mandatory expense creation
VIII	Adoption of a measure that implies adjustment of mandatory expenses above the inflation variation
IX	Creation or expansion of subsidies and grants
X	Concession or extension of tax incentive or benefit

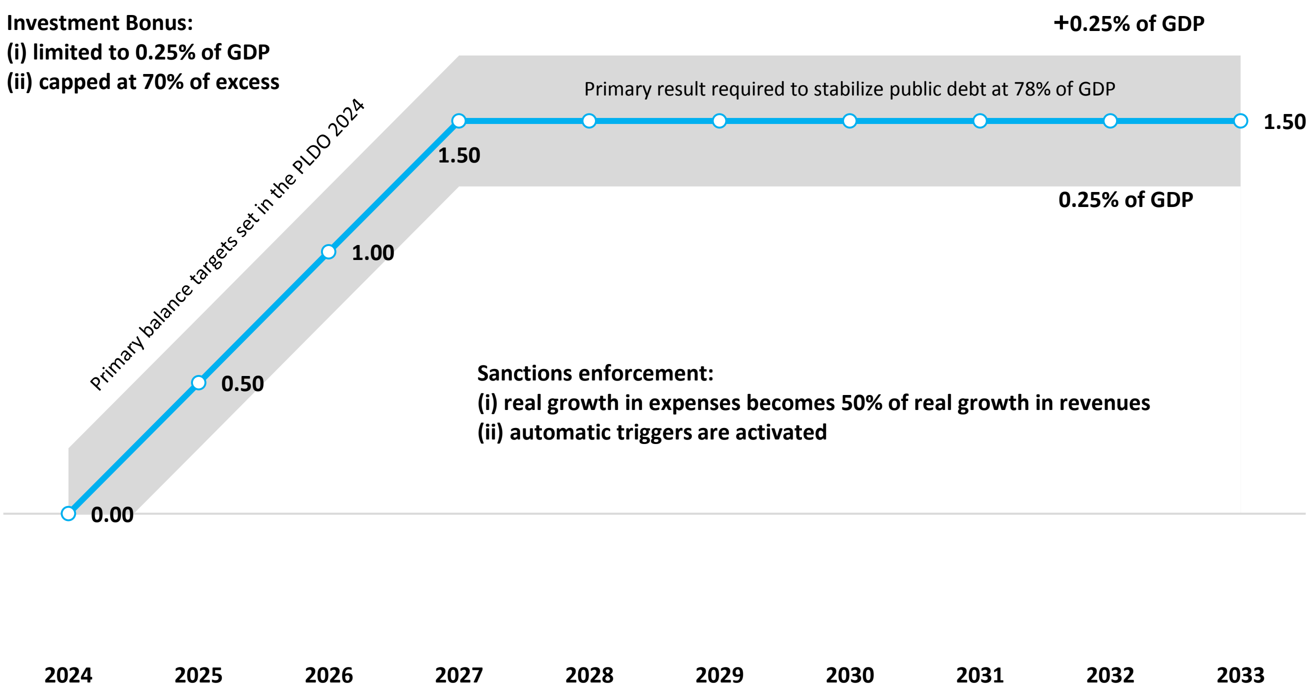
Source: Federal Constitution. Elaboration: IFI

In addition to the sanctions provided for in Art. 167-A of the Federal Constitution, the proposed new rule provides for a penalty for the dynamics of expenditure in case of non-compliance with the primary result targets. According to the bill, the growth of primary expenses is limited to 70% of the growth of primary revenues, but in case of non-compliance with the primary target, this percentage drops to 50% (Art. 5 of the PLP No. 93).

Graph 1 below illustrates the rule for the primary result over the relevant 10-year horizon envisaged in the bill. For the period from 2024 to 2026, the IFI used the primary result targets set out in the 2024 Budget Directives Bill (PLDO 2024). For the period from 2027 to 2033, the value of 1.5% of GDP was used as a target, as it is compatible with the primary required to stabilize the DBGG/GDP ratio at 78.1% of GDP in a scenario of 2, 0% real growth (GDP) and 3.9% real implicit interest on the debt, according to the latest medium-term macroeconomic and fiscal scenario updated by the IFI[15].

[15] Included in Fiscal Follow-Up Report (RAF) No. 76, of May 2023. Link to access the document: https://www2.senado.leg.br/bdsf/bitstream/handle/id/610420/RAF76_MAI2023.pdf.

GRAPH 1. GOALS FOR PRIMARY RESULT (PR) WITH TOLERANCE INTERVAL (IN % OF GDP)



Source: PLN 4 of 2023 (PLDO of 2024), PLP 93 of 2023 and IFI. Elaboration: IFI.

3. Adoption of expense growth limits

The new fiscal framework approved by the Chamber of Deputies maintains some characteristics of the rule currently in force, such as setting a limitation by branch/agency and excluding some expenses from the rule. An important difference between the two models is the concept of primary expenditure that will be subject to limitation. In the current rule, verification of compliance with the ceiling is carried out by calculating the expenses paid (for the year, plus the remainder to be paid)[16], while in the new fiscal framework, the concept adopted will be that of budget allocation (Art. 3 of the PLP No. 93). Another important difference lies in the fact that the new framework provides for a floor for total primary expenditures.

Under the proposed fiscal framework, the floor for real expenditure growth will be 0.6%, while the ceiling will be 2.5%. Expenditure growth will be linked to revenue growth and will respect the systematics illustrated with formulas in Chart 3.

CHART 3. CALCULATION OF ANNUAL LIMITS (COMMON TO ALL YEARS)

If...	Then...
$(\alpha \cdot \Delta\%Rec_{t-1}) \leq 0{,}6\%$	$\Delta\%Desp_t = 0{,}6\%$
$0{,}6\% < (\alpha \cdot \Delta\%Rec_{t-1}) < 2{,}5\%$	$\Delta\%Desp_t = (\alpha \cdot \Delta\%Rec_t)$
$(\alpha \cdot \Delta\%Rec_{t-1}) \geq 2{,}5\%$	$\Delta\%Desp_t = 2{,}5\%$

Source: IFI.

[16] See Federal Constitution of 1988.
Art. 107 Individualized limits for primary expenses are established for each year: (...)
*Paragraph 10. For purposes of verifying compliance with the limits referred to in this article, **the primary expenses paid will be considered, including the remaining payable paid** and other operations that affect the primary result for the year.*

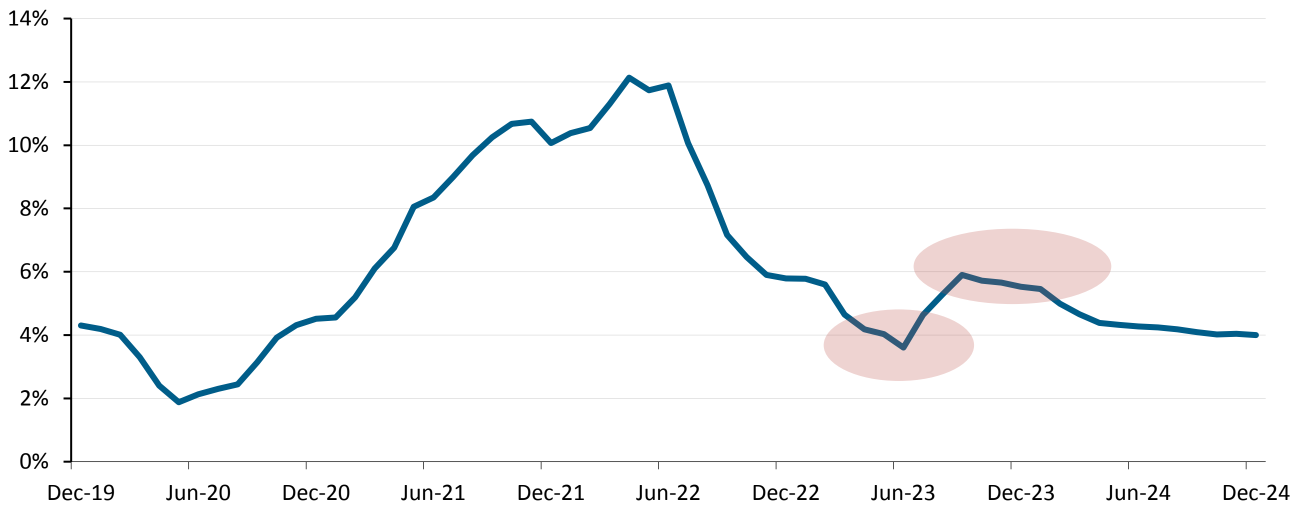
The α parameter can take on two values: 70% or 50%. It will be 70% if the primary target is met and 50% if the primary falls below the lower limit of the tolerance interval, that is when the target is not met.

The new framework considers the 2023 LOA (Annual Budget Law) as the basis for calculating the Union's primary expenditures. According to §. 1 of Art. 3 of PLP No. 93, the budget appropriations contained in the LOA of 2023 (Law No. 14,535 of 2023), plus supplementary credits (CS 2023) and special credits (CE 2023), in force on the date of enactment of PLP No. 93, will compose the basis of calculation in the first year of validity of the rule. Thus, the basis for calculating the limit of 2024 ($Base$ t=2024) will be

$$Base_{t=2024} = LOA_{2023} + CS_{2023} + CE_{2023}$$

The new fiscal framework provides that the inflation to be used to correct the spending ceiling will be the one accumulated in the 12 months up to June of the year prior to the reference year (Art. 4 of PLP No. 93). According to the bill, if the accumulated inflation in 12 months until December is higher than the inflation used to correct expenses, this excess can be used to increase expenses through supplementary credits, respecting the tolerance intervals for actual expenditure growth of a minimum of 0.6% and a maximum of 2.5%. These supplementary credits cannot be incorporated into the basis for calculating the limits for subsequent years, except for 2024. As the estimated inflation for June 2023 (accumulated in 12 months) should be 1.9 p.p. lower than the year-end inflation, the difference could result in a potential increase in expenses of R$ 42.2 billion. Graph 2 and Table 4 illustrate this situation.

GRAPH 2. IPCA ACCUMULATED IN 12 MONTHS (%)



Source: IBGE and IFI. Elaboration: IFI.

TABLE 4. DIFFERENCE IN PERCENTAGE POINTS BETWEEN THE INFLATION IN JUNE AND DECEMBER 2023 (% AND P.P.)

IPCA accumulated in 12 months		
	FOCUS	IFI
Jun/23	3.7	3.6
Dec/23	5.7	5.5
Δ p.p.	**2.0**	**1.9**

Source: Central Bank and IFI. Elaboration: IFI.

Art. 15 of the substitutive bill to PLP No. 93, included by the rapporteur in the Chamber of Deputies, allows for additional supplementation of expenses for 2024 based on the difference between the forecasted revenue growth for the year and the revenue growth used to define the limit. The same article defines that if the prediction is not confirmed, the difference must be offset against the ceiling for the 2025 fiscal year. In other words, the provision allows for the opening of supplementary credits in the 2024 budget if the revenue calculated in the 12 months to June 2023 is lower than that calculated in the first four months of 2024 (second bimonthly evaluation).

The potential effect of Art. 15 inserted in the new version of the PLP No. 93 is R$ 19.67 billion. Based on the IFI's revenue and inflation scenario for 2023 and 2024, it is possible to estimate the potential impact of the article included by the rapporteur in the Chamber of Deputies. The exercise compares the actual growth in revenues subject to the limitation for the period July 2023 to June 2024, with the same period of the previous year, with the estimated growth for the period January 2024 to December 2024. Applying the 70% reducer to expenses growth in both accounts makes it possible to conclude that expenses can be increased by up to 0.9%, or R$ 19.7 billion. It is worth mentioning that the use or not of this space will also depend on achieving the goals in 2024.

Under this rule, the credit opening in the 2024 budget can be included in the 2025 spending limits. Paragraph 1 of Art. 4 explains that the difference between inflation at the end of June and the end of December may be used as a supplementary credit, but that these credits will not be part of the base for calculating future limits. However, the rule will not apply to loans opened in 2024, which will be incorporated into the basis for the central government spending ceiling.

The original proposal from the Administration provided for a change of parameters of expenditure growth every four years, while the wording passed by the Chamber of Deputies defined fixed parameters (0.6% and 2.5%).

4. Application of the triggers set forth in Art. 167 of the Federal Constitution

The substitute to PLP No. 93 added a provision for sanctions in case of non-compliance with the primary result targets set in the LDO for the following situations:

(i) Mandatory primary expenditures as a percentage of total primary expenditures greater than 95%:
(i) All triggers of art 167-A (See Chart 2 of this note) apply, except for the prohibition of granting or expanding tax incentives or benefits.

(ii) Primary result below the lower limit of tolerance range in the first year
Only the following prohibitions apply:
(a) creation of positions, jobs, or functions that increase expenses.
(b) change in career structure that increases expenses.
(c) creation or increase of allowances, advantages, bonuses, payments, representation allowances, or benefits of any nature.
(d) concession or expansion of tax incentives or benefits.

(iii) Primary result below the lower limit of the tolerance interval from the second year of non-compliance
All triggers of Art. 167-A of the Federal Constitution apply.

Cases (ii) and (iii) may be replaced, partially or totally, by a bill of complementary law with adjustments that offset the savings generated by the application of the triggers, as detailed below:

Art. 6th (...)

§ 2. In the hypotheses of this article, the President of the Republic may send a message to the National Congress, along with a bill of complementary law proposing the partial suspension or gradation of the prohibitions provided for in this article, demonstrating that the impact and duration of the measures adopted will be sufficient to compensate for the difference between the calculated primary result, referred to in the caput, and the lower limit of the tolerance interval" **(§ 2 of Art. 6 of the PLP No. 93)**

The trigger regarding the prohibition to adopt measures that imply an adjustment of mandatory expenses above the inflation rate does not apply to the appreciation of the minimum wage, as specified in **§ 3 of Art. 6 of PLP No. 93.**

5. Revenue recovery and management

The PLP No. 93 of 2023, supported by the recompositions and expansions of expenses made possible by the Amendment to the Constitution for the Transition of Power (EC No. 126), was designed to recover and preserve the primary expenses of the Federal Government, conditioning the increase of expenses to the actual increase of revenue. The little leeway for cutting expenses puts a strain on revenues in meeting the stipulated fiscal targets. It is an element of uncertainty regarding the sustainability and credibility of the framework.

Revenue calculation methodology:

For purposes of calculating the maximum growth limit for expenditures subject to the ceiling proposed by the framework, not all primary revenues will be considered. Limits for defining expenses will exclude the following income items:

- Exploitation of natural resources (R$ 132.5 billion in 2022)
- Concessions and permissions (R$ 46.8 billion in 2022)
- Dividends and participations (R$ 87 billion in 2022)
- New Refis programs (the amount will depend on the special installment programs that may be created)
- Accounts referring to PIS/Pasep accumulated assets (R$ 23.0 billion expected for 2023)
- Legal and constitutional transfers by revenue sharing, discounting those resulting from the items mentioned above to avoid double counting (R$ 379.1 billion – 2022)

The purpose of excluding certain revenues from the base of the limits for expenditure growth was to bring more predictability to spending, given the volatile nature that some primary revenues can assume. For example, the revenue from the exploitation of natural resources depends on the oil prices in the international market and the R$/US$ exchange rate, in addition to the domestic production of the product. In 2021 and 2022, according to the National Treasury of Brazil (STN), these revenues will total, for the Federal Government, R$ 94.1 billion and R$ 132.5 billion, respectively, after R$ 56.5 billion in 2020 and R$ 64.7 billion in 2019. The increase in oil prices was the main variable explaining the increase in this source of revenue in the last two years.

Besides the more volatile revenue, other sources of revenue were excluded from the base of the primary spending limits due to other factors. For example, the transfers of unclaimed funds by individuals from PIS/Pasep accounts were left out because they represent a one-off revenue for the Treasury in 2023 only. The exclusion of any new Refis programs is justified by the temporary nature of that revenue.

However, despite the exclusion of these items from the base of revenues for purposes of verification of the expenditure limit, it is also known that some of these variables can also influence economic activity and, consequently, the revenue from taxes in certain sectors. The graph below shows the real average growth rate of the primary revenues of the Federal Government, excluding the items above. Based on the graph, in the period of the commodities boom (2004 to 2012), for example, revenues had a more expressive growth than in the following decade, when economic activity no longer had the same performance as before[17]. It is worth mentioning that other effects also had some specific impacts, such as the end of the CPMF in 2007, affecting the variation in this period, and the growth of tax exemptions from 2012 onwards.

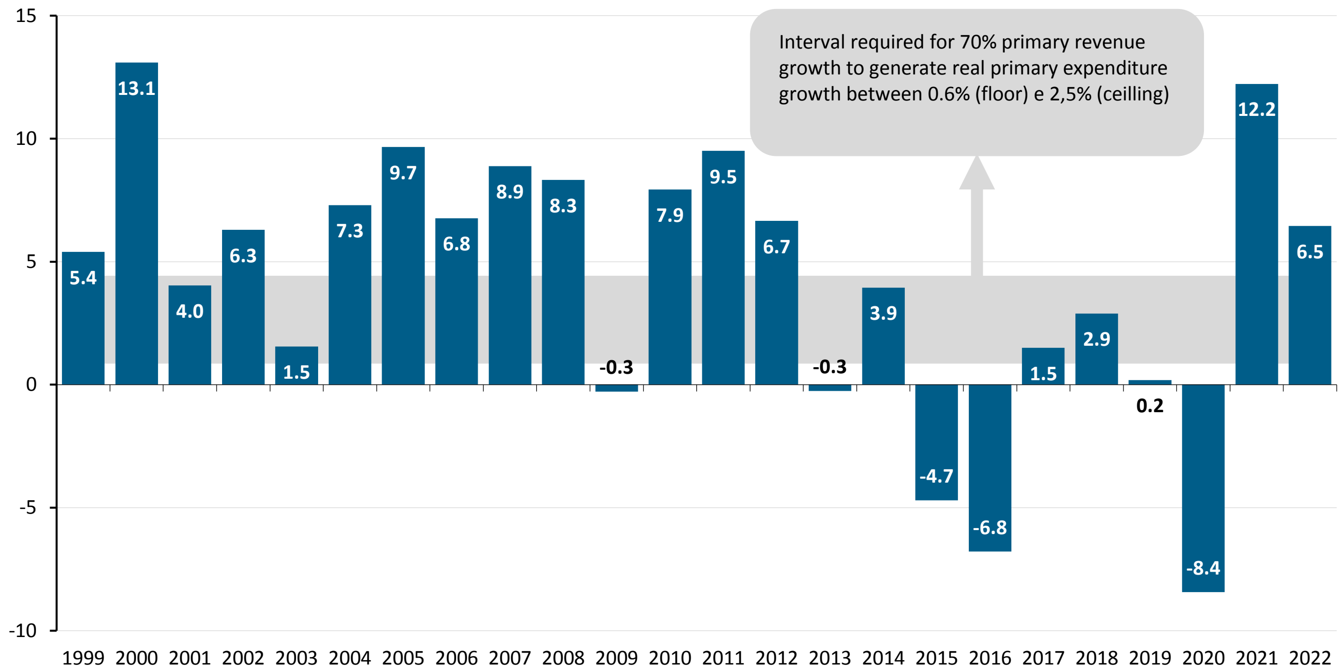
Graph 2 also shows the years in which real revenue growth was between the tolerance intervals for the expenditure limit. That is, when real revenue growth is below 0.9%, primary expenditure will grow according to the minimum of 0.6% (70% of revenue growth), and whenever this rate is above 3.6 %, the expense will follow the maximum of 2.5%. When

[17] It is worth mentioning that, according to the Brazilian Economic Cycle Dating Committee of the FGV (CODACE), the Brazilian economy went through periods of recession in the years 1998-1999, 2001, 2003, 2008-2009, 2014-2016 and 2020, with the longest lasting recession was in 2014-2016, and the most intense was in 2020. See: https://portalibre.fgv.br/sites/default/files/2023-02/comunicado-do-comite-de-datacao-de-ciclos-economicos-31_01_2023_minuta.pdf.

real revenue growth falls between this range, in the gray part of the graph, real primary expenditure growth will be the equivalent of 70% of real revenue growth[18].

According to Graph 3, in the selected period, in just five years, real revenue growth was within the expected ranges, corresponding to a rate of 20.8% of the total years considered in the graph (24 years). In 25% of the cases, the revenue grew below the considered range (0.9% in real terms), while in 58.3% of the cases, the real revenue growth was above 3.6%, that is, above the range which would make real spending growth only 70% of revenue growth. The situations in which revenues grow, in real terms, systematically above 3.6% are more optimistic scenarios and, consequently, with greater potential for achieving the primary targets necessary to stabilize the debt/GDP ratio.

GRAPH 3. REAL GROWTH RATE OF PRIMARY REVENUES SUBJECT TO THE RULE



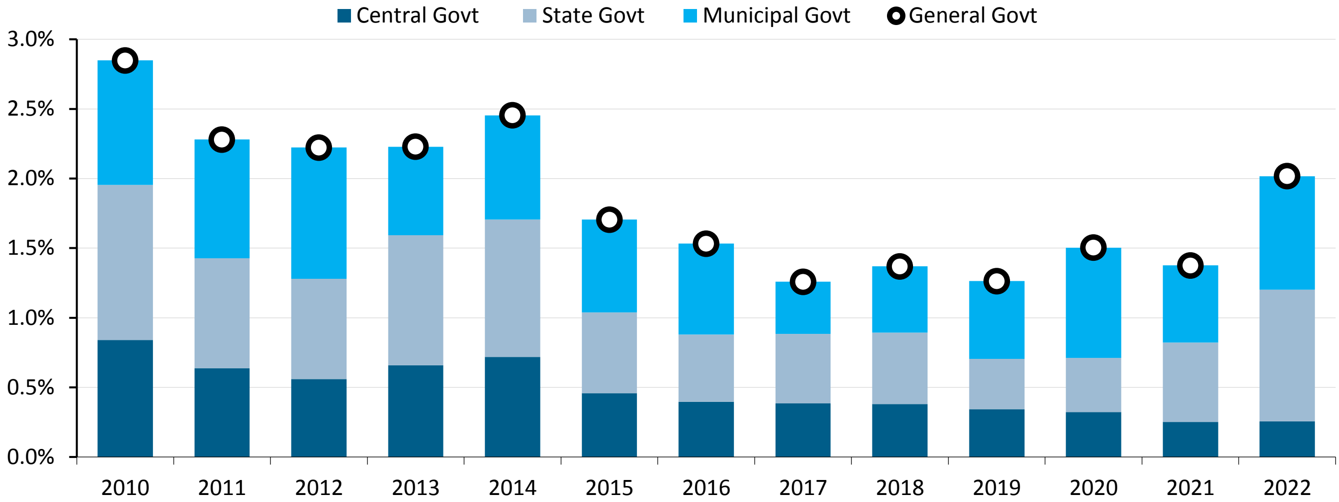
*Source: IBGE, Brazilian National Treasury. Elaboration: IFI. *Excluding operations with assets, such as capitalization of Petrobras and sovereign wealth fund.*

6. Rule for the preservation of public investments

Besides the adjustment measures mentioned above, the new fiscal framework proposes the creation of a minimum level for the government's public investments so that the actions aimed at this expenditure are preserved in periods of fiscal adjustment. Graph 3 shows the evolution of public investments by the general government, detailing the information by federal entity. It can be seen that, even though they grew in 2022, general government investments are still below the average level from the period prior to 2014, when the fiscal framework of the federal entities worsened. Also, in relation to the pre-2014 period, investments were more concentrated in the subnational entities and not in the Federal Government.

[18] It is worth mentioning that this 70% percentage can be reduced to 50% if the primary target is not met.

GRAPH 4. ACQUISITION OF NON-FINANCIAL ASSETS (% OF GDP)



Source: STN. Elaboration: IFI.

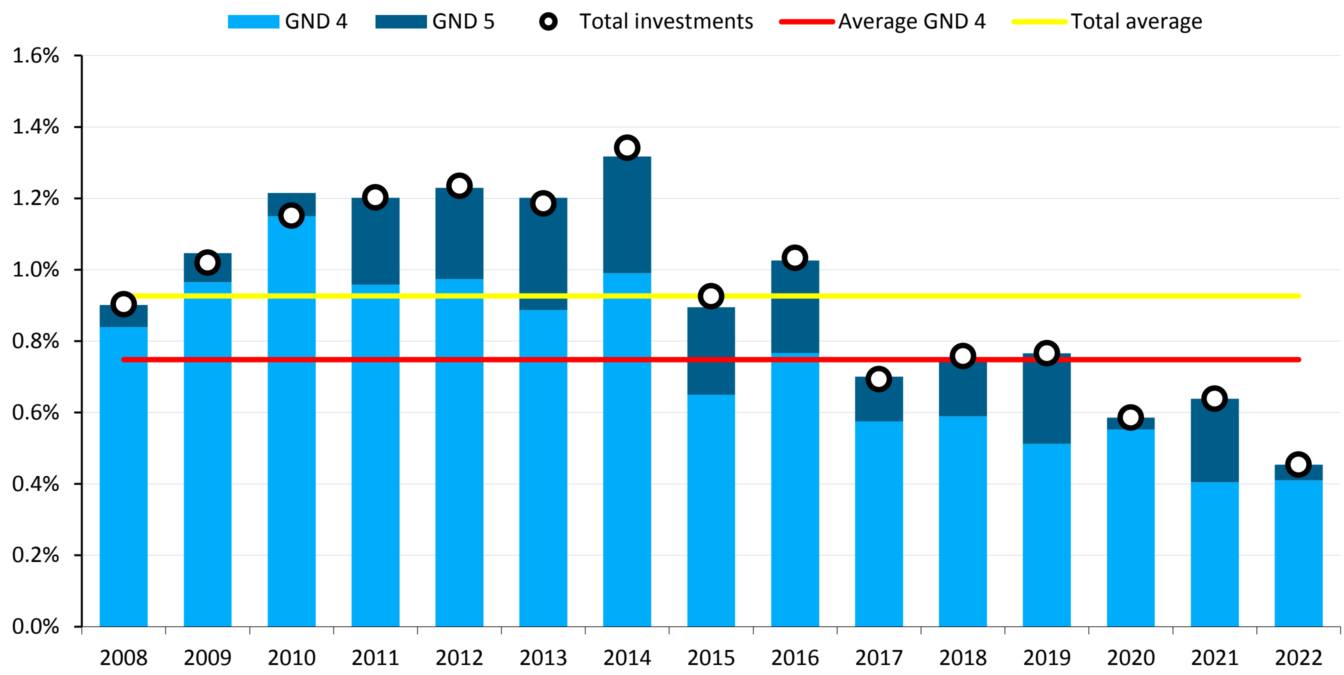
Data also shows that the investments of the Federal Government reached an all-time low in 2022, and net investment has been negative since 2015[19]. And despite the great need to replenish this expenditure, these investments must be accompanied by an expansion in the evaluation mechanisms to ensure greater efficiency in the application of resources and thus enhance the fiscal multipliers of spending for the economy.

The initial wording presented by the Administration had already provided for the creation of a minimum level for investments, but the amendment made and approved by the Chamber of Deputies changed the rule associated with this mechanism. Previously, the bill provided that public investments would have as a minimum level the value observed in the 2023 LOA, being adjusted for inflation in the following years. According to the amendment to PLP No. 93, the minimum level for investments will now be fixed at 0.6% of GDP (Art. 10 of PLP No. 93). It is worth mentioning that the current year's updated appropriation is at 0.7% of GDP.

Graph 5 shows the evolution, in % of GDP, of groups by nature of expenditure (GND) 4 (investments) and 5 (financial investments) for the period from 2008 to 2022 for the Federal Administration.

[19] See Chart 12 of the STN Bulletin. "Overall government fiscal statistics: 2022 output (annual and quarterly)". Available at: https://sisweb.tesouro.gov.br/apex/f?p=2501:9::::9:P9_ID_PUBLICACAO:46775.

GRAPH 5. EVOLUTION OF INVESTMENTS AND FINANCIAL INVESTMENTS (% OF GDP)



Source: STN. Elaboration: IFI.

Much of investment spending is discretionary. With the establishment of a minimum level, they can be classified as mandatory. In an exercise considering the 2023 budget, that is, the composition of primary expenditures contained in the last government assessment, referring to the second two months of 2023, if discretionary investments are considered mandatory, budgetary rigidity would be increased by 2.8%, from 90.5% to 93.3% (Table 5).

TABLE 5. COMPOSITION OF PRIMARY EXPENDITURE - BIMONTHLY EVALUATION OF THE GOVERNMENT

	R$ million	PArt. %
Primary expenses	**2,047,457**	**100.0%**
Mandatory	1,853,606	**90.5%**
Discretionary	193,851	9.5%
Discretionary investment	56,743	**2.8%**
Other discretionary	137,108	6.7
Mandatory + Discretionary investments	1,910,349	**93.3%**

Source: Federal Government Revenue and Expenditure Assessment Report for the 2nd Bimester. Elaboration: IFI.

Considering this aspect, the Substitutive Bill sent to the Federal Senate provides for the possibility of contingency in part of the public investments.

Under Art. 7 of the PLP 93, failure to meet the primary target will not be considered a violation of the LRF, provided that measures have been adopted to limit commitment and payment ("contingency"), and that measures have not been implemented in violation of the prohibitions against breaching the primary target (Art. 167-A of the Federal Constitution) and the limitation of real growth in expenses.

However, this limitation of commitment and payment needs to respect the minimum limit of discretionary spending to the regular operation of the administration (to avoid shutdown). This minimum limit was defined by PLP No. 93 as 75% of the authorized in the LOA for the corresponding year. The investments can also be contingent within this same limit of 75%.

IV – Fiscal impact of the new fiscal framework

For the simulations of the fiscal impact arising from the changes proposed in PLP No. 93, public data referring to the 2023 budgets (LOA and budget execution reports) and 2024 (PLDO) were used. Additionally, the macroeconomic assumptions used in the simulations correspond to those of the government, the IFI, and/or the Central Bank's Focus Bulletin.

The hypothesis for expenditures not subject to the expenditure limitation rule is that they will remain constant over time as a proportion of GDP. This assumption ensures that the difference between total primary expenditure and expenditure subject to the ceiling does not vary so that the path drawn in this simulation only reflects the effects of the new fiscal rule. Finally, the risks inherent to the materialization of this hypothesis are discussed.

For the preparation of scenarios, different scenarios were adopted for the real growth of primary revenues since the evolution of expenses is conditioned to the real growth of revenues. Here, once again, the assumption is made that the revenues used to calculate the expenditure limit will follow the same trajectory as the revenues not considered for the purpose of calculating the rule.

Another hypothesis is that the starting point for the simulations is the year 2024 and the center of the primary target is considered fulfilled, that is, primary revenues equal to primary expenditures and consistent with the numbers presented in the 2024 PLDO.

As already evidenced in the previous section through Graph 2, for most of the period, the real growth of primary revenues was above 3.6%, with the result that expenses were limited to the real growth of 2.5%. Based on the historical evolution of revenues, the following scenarios were designed:

- **Scenario 1**: The real growth of the Union's primary revenues will grow at an average annual rate of 4.1%, equivalent to the average observed between 1999 and 2022. In this case, the average real growth in expenses will be 2.4% in real terms, already considering the cases in which the balance results in non-compliance with the primary target and, therefore, the percentage of revenue growth that will guide that of expenses will be 50% and no longer 70%.
- **Scenario 2**: The real growth of the Union's primary revenues will grow at an annual average rate of 6.5%, equivalent to the average observed in the period from 2000 to 2009. In this case, the average real growth in expenses will be 2.5% in real terms, corresponding to the ceiling established in the new framework. It is worth mentioning that the period considered in scenario 2 coincides with the commodity boom, so that the final simulation results will be presented in average terms and not in the trajectory per year, as in the other scenarios. The objective would be not to harm the visual analysis of the other scenarios in relation to this one.
- **Scenario 3**: The real growth of the Union's primary revenues will grow at an annual average rate of 2.0%, equivalent to the average observed in the period from 2010 to 2019. In this case, the average real growth in expenses will be 1.1% in real terms, already considering the cases in which the balance results in non-compliance with the primary target and, therefore, the percentage of revenue growth that will guide that of expenses will be 50% and no longer 70%. It is worth mentioning that the period considered for the hypothesis for revenues does not include the period of the pandemic and subsequent years.
- **Scenario 4**: The real growth of the Union's primary revenues will grow at an average annual rate of 2.6%, equivalent to the scenario in which revenues evolve according to economic growth, that is, revenue elasticity in relation to GDP is 1, as suggested by the results found in the Special Study (EE) of IFI No. 16[20], of 2021. In this case, the average real growth in expenses will be 1.5% in real terms, already considering the cases in which the balance implies non-compliance with the primary target and, therefore, the percentage of revenue growth that will guide that of expenses will be 50% and no longer 70%.

[20] Link to access the document: https://www2.senado.leg.br/bdsf/bitstream/handle/id/593776/EE16.pdf.

- **Scenario 5**: The Union's primary revenues will have an average annual growth of 0.9%, equivalent to the scenario in which revenues evolve according to the minimum necessary for expenditure growth to remain at 0.6%, and that the difference between revenue growth and expenses is 70%. In this case, the average real growth in expenses will be 0.6%, equivalent to the floor of expenses.
- **Scenario 6**: The Union's primary revenues grow at an average annual rate of 3.6%, equivalent to the scenario in which revenues evolve according to what is necessary so that the increase in expenses remains at 2.5% and that the difference between revenue growth and expenses is 70% for cases of compliance with the rule and 50% for cases of non-compliance with the primary target. In this case, the average real growth in expenses will be 2.2% in real terms.

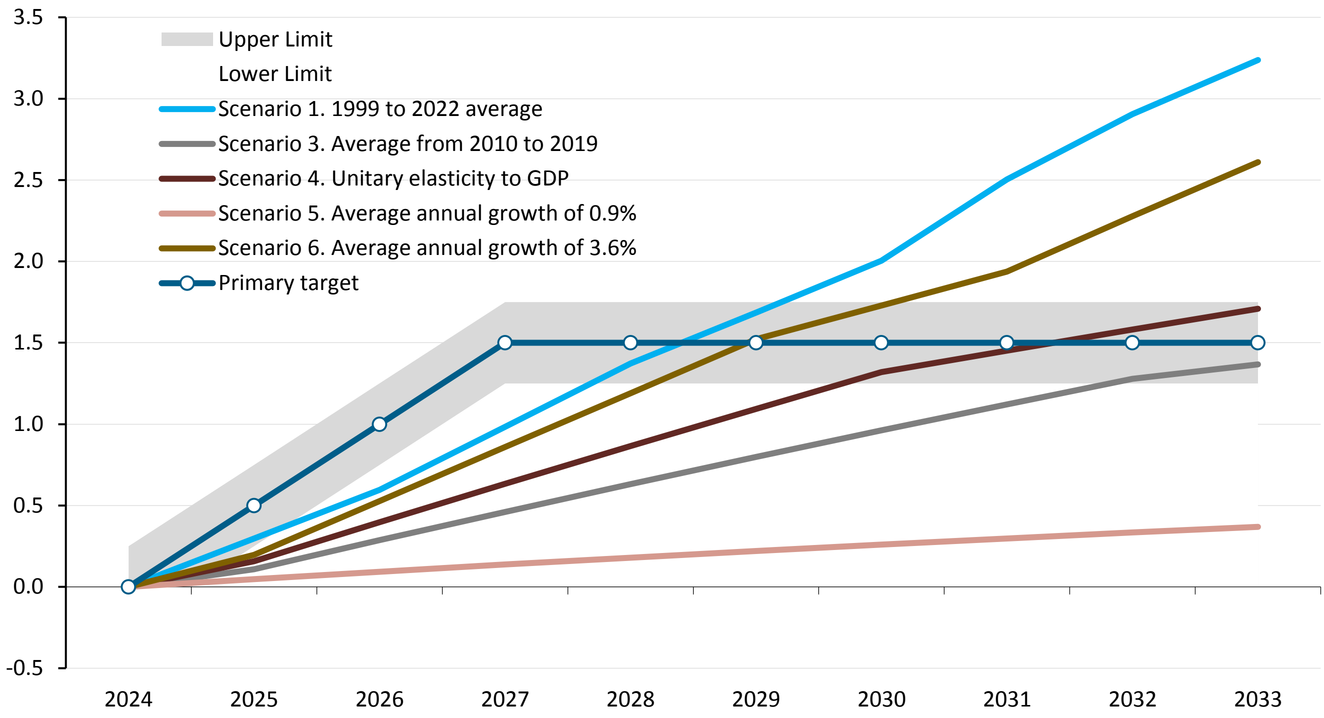
The outlined scenario also incorporates the effects of bonuses for investments and sanctions for cases of non-compliance with the primary target. Thus, following the trajectory resulting from the application of the percentages indicated in the different scenarios, it is observed that, except for scenario 2 (more optimistic), in all other scenarios the target for the primary result is not met in the first years of the effectiveness of the rule. In scenario 1, the primary target is met within the lower limit of the tolerance interval in the first year (2025), failing to be met between 2026 and 2027, when it is met again and levels higher than the upper limit of the tolerance interval target are reached, allowing the use of the excess for investment bonuses.

In scenarios 3, 4, 5 and 6, the primary target is not met as of 2025, and it is possible to observe scenarios of compliance with the rule in different periods of the outlined horizon (2029 in scenario 6, 2030 in scenario 4 and 2032 in scenario 3). Only in scenarios 1, 2 and 6 there is the possibility of using bonuses for public investments. In scenario 5, the primary target is not met in any year.

Graph 6 and Table 6 show the trajectory for the primary balance considering the different scenarios, except for scenario 2 for the graph, since this shows a growth in the primary balance as a percentage of GDP in very expressive volumes, jeopardizing the analysis of other scenarios. It is also worth mentioning that scenarios 3 and 4 are the most realistic in relation to the others. The exercise is important to demonstrate that the simple application of the rule will not be enough to allow the obtaining of fiscal results consistent with the sustainability of the public debt, being necessary an additional effort so that the real growth of the primary revenues is high. These results can come through increased economic productivity or measures to obtain recurring and consistent revenues to help achieve the intended objectives.

It is worth mentioning that the challenges are greater than those presented in this exercise, since achieving a zero deficit for 2024 is still uncertain. As the scenarios start from the point where the goal will be achieved in the next exercise, this exercise does not consider these very short-term risks in the simulations.

GRAPH 6. PRIMARY BALANCE OF THE UNION IN DIFFERENT SCENARIOS (% GDP)



Source: PLDO, IBGE, STN and IFI. Elaboration: IFI.

TABLE 6. SCENARIOS FOR PRIMARY BALANCE: NEW FISCAL FRAMEWORK

	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	average 25-33
Scenario 1: Average from 1999 to 2022	0.0	0.3	0.6	1.0	1.4	1.7	2.0	2.3	2.7	3.0	1.7
Scenario 2: Average from 2000 to 2009	0.0	0.7	1.5	2.3	3.1	4.0	4.8	5.8	6.7	7.7	4.1
Scenario 3: Average from 2010 to 2019	0.0	0.1	0.3	0.5	0.6	0.8	1.0	1.1	1.3	1.4	0.8
Scenario 4: Unitary elasticity in relation to the GDP	0.0	0.2	0.4	0.6	0.9	1.1	1.3	1.5	1.6	1.7	1.0
Scenario 5: Growth annual average of 0.9%	0.0	0.0	0.1	0.1	0.2	0.2	0.3	0.3	0.3	0.4	0.2
Scenario 6: Growth annual average of 3.6%	0.0	0.2	0.5	0.9	1.2	1.5	1.7	1.9	2.1	2.4	1.4
Primary target center (% of GDP) 0.0	***0.0***	***0.5***	***1.0***	***1.5***	***1.5***	***1.5***	***1.5***	***1.5***	***1.5***	***1.5***	***1.3***

Source: IFI.

As already mentioned, the expenses subject to the correction of the new fiscal framework differ if one considers the original text of the Executive Branch and the substitute bill approved by the Chamber of Deputies. Regarding the current spending ceiling rule, the text approved by the Chamber innovated by reducing the number of exceptions to the rule. The Executive Branch's proposal and the House's substitute also differ in the exceptions to the proposed limit. Chart 4 compares the expense items excluded from the rule's limits and calculation base, in both versions of the bill.

CHART 4. METHODOLOGY FOR CALCULATION OF EXPENSES

Initial text of PLP No. 93, 0f 2023	Substitute to PLP No. 93, of 2023
Paragraph 2 The following are not included in the calculation base and limits established in this article:	**Paragraph 2 The following are not included in the calculation base and limits established in this article:**
I - the constitutional transfers established in Paragraph 1 of Art. 20, in item III of the sole paragraph of Art. 146, in Paragraph 5 of Art. 153, in Art. 157, in items I and II of the head of Art. 158, in Art. 159 and in Paragraph 6 of Art. 212, the expenses related to item XIV of the head of Art. 21, all of the Constitution, and the additions dealt with in items V and VII of the head of Art. 60 of the Act of Temporary Constitutional Provisions;	I - the transfers established in Paragraph 1 of Art. 20, item III of the sole paragraph of Art. 146, in Paragraph 5 of Art. 153, in Art. 157, in items I and II of the head of Art. 158, in Art. 159 and in Paragraph 6 of Art. 212 of the Federal Constitution;
II - the additions dealt with in items IV and V of the head of Art. 212-A of the Constitution;	
III - the extraordinary credits referred to in Paragraph 3 of Art. 167 of the Constitution;	II - the extraordinary credits referred to in Paragraph 3 of Art. 167 of the Federal Constitution;
IV - transfers to the health funds of the States, the Federal District and the Municipalities, in the form of complementary financial assistance for compliance with the national wage floors for nurses, nursing technicians, nursing assistants and midwives, in accordance with the provisions of Paragraphs 12, 13, 14 and 15 of Art. 198 of the Constitution;	
V – the expenses with socio-environmental projects or related to climate change funded with resources from donations, and expenses with projects funded with resources resulting from consent decrees and settlements out of court signed as a result of environmental disasters;	III - expenses in the amounts that refer to amounts funded with funds from donations or with funds arising from consent decrees and settlements out of court signed to repair damages as a result of a disaster.
VI - the expenses of federal public universities, state-owned companies of the Union that render services to federal university hospitals and federal institutions of education, science and technology, linked to the Ministry of Education, and other scientific, technological and innovation institutions funded with their own revenues, donations or agreements, contracts or other sources entered into with other federative entities or private entities;	IV - the expenses of federal public universities, state-owned companies of the Union that render services to federal university hospitals and federal institutions of education, science and technology, linked to the Ministry of Education, federal military educational establishments, and other scientific, technological and of innovation institutions, in amounts funded with own revenues, or agreements, contracts or other sources, entered into with other federative entities or private entities;
VII - expenses incurred with funds arising from transfers from other federative entities to the Union for the direct execution of engineering works and services;	V - expenses in amounts paid with funds from transfers from other federative entities to the Union intended for the direct execution of works and engineering services;
VIII - expenses for complying with the provisions of Paragraph 20 of Art. 100 of the Constitution, in Paragraph 3 of Art. 107-A of the Act of Temporary Constitutional Provisions and the adjustment for inflation of the court-ordered debts registered in the fiscal year;	VI - expenses for complying with the provisions of Paragraph 20 of Art. 100 of the Federal Constitution, in Paragraph 3 of Art. 107-A of the Act of Temporary Constitutional Provisions;
IX - expenses for compliance with the provisions of Art. 4 of Constitution Amendment No. 114 of December 16, 2021;	Art. 13 The court-ordered debts resulting from demands related to the complementation of the Union to the States and the Municipalities on account of the Fund for the Maintenance and Development of Elementary Education and the Enhancement of Teaching (Fundef), in the form established in Art. 4 of Constitutional Amendment No. 114, of December 16, 2021, will not be included in the calculation base and in the limit of the Executive Branch established pursuant to Art. 3 of this Supplementary Law.
X - the non-recurring expenses of the Electoral Court System with the holding of elections;	VIII - the non-recurring expenses of the Electoral Court System with the holding of elections;
XI - expenses with capital increase of non-financial and non-dependent state-owned companies;	
XII - the legal transfers established in subitems “a” and “b” of item II of the head of Art. 39 of Law No. 11,284, of March 2, 2006, and in Art. 17 of Law No. 13,240, of December 30, 2015; and	IX - the legal transfers established in subitems “a” and “b” of item II of the head of Art. 39 of Law No. 11,284, of March 2, 2006, and in Art. 17 of Law No. 13,240, of December 30, 2015; and
XIII - expenses related to the collection for the management of water resources by the National Water and Basic Sanitation Agency, pursuant to the provisions of Law No. 9,433, of January 8, 1997, and Law No. 10,881, of June 9, 2004. Paragraph 6 For the purposes of the provisions of the head of this article, acts performed in compliance with the provisions of Paragraphs 11 and 21 of Art. 100 of the Constitution;	VII - expenses for complying with the provisions of Paragraphs 11 and 21 of Art. 100 of the Federal Constitution;

Source: PLP 93 of 2023.

Among the items that were reintroduced to the expenditure limit, the Union's supplement to Fundeb and the Constitutional Fund of the Federal District (FCDF) stand out. Both Fundeb and FCDF were no longer considered for the purpose of calculating the primary expenditure limitation rule since the creation of the expenditure ceiling in 2016. The Executive Branch maintained this rule in the new fiscal framework, but the rapporteur changed the text of the proposal to include these items in the general rule for limiting expenses.

The table below shows, in percentage of GDP, the difference between the exceptions established in the original expenditure ceiling rule (2016) and its modifications (2022 and 2023) and that expected for 2024, according to the original wording submitted by the Executive Branch and the Substitute Bill (PRLP-CD No. 02) passed by the Chamber of Deputies. According to Table 7, the adjustment carried out by the rapporteur of the bill in the Chamber reduced the exceptions by 0.7 p.p. of GDP in relation to the text submitted by the Executive Branch. International literature highlights that fiscal rules should have the least possible exceptions, and when they exist, they should have a justification based on technical arguments for the adoption of this direction.

TABLE 7. COMPARISON OF EXPENSES NOT INCLUDED IN THE BASIS OF CALCULATION FOR THE EXPENDITURE CEILING AND THE PLP 93, 2023. (% OF GDP).

% of GDP	2016	2022	Annual Budget Law 2023	2nd Re-examination 2023	PLP 93 (2024)	PRLP-CD 02
4. EXPENDITURE NOT INCLUDED IN THE CALCULATION BASIS OFTHE CEILING OF CONSTITUTIONAL AMENDMENT 95/2016 (CF 1988, ADCT, Art. 107, Parag. 6) AND PLP 93	4.2	6.2	5.1	5.2	5.2	4.5
4.1 Constitutional Transfers (CF 1988, ADCT, Art. 107, Parag.6, Item I)	3.9	4.9	4.8	4.7	4.7	4.1
4.1.1 FPM / FPE / IPI-EE	3.0	3.4	3.2	3.3	3.3	3.3
4.1.2 Education Salary Contribution	0.2	0.2	0.2	0.2	0.2	0.2
4.1.3 Natural Resources Exploitation	0.2	0.8	0.7	0.6	0.6	0.6
4.1.4 CIDE - Fuels	0.0	0.0	0.0	0.0	0.0	0.0
4.1.5 Others	0.4	0.5	0.6	0.6	0.6	0.0
4.1.5.1 IOF (Tax on Financial Transactions) Gold	0.0	0.0	0.0	0.0	0.0	0.0
4.1.5.2 ITR (Rural Real Estate Tax)	0.0	0.0	0.0	0.0	0.0	0.0
4.1.5.3 FUNDEB (Federal Government's Supplementation)	0.2	0.3	0.4	0.4	0.3	0.0
4.1.5.4 Constitutional Fund of the Federal District - FCDF	0.2	0.2	0.2	0.2	0.2	0.0
4.1.5.4.1 FCDF - OCC	0.0	0.0	0.2	0.2	0.2	0.0
4.1.5.4.2 FCDF - Personnel	0.2	0.1	0.0	0.0	0.0	0.0
4.2 Extraordinary Credits (CF 1988, ADCT, Art. 107, Parag. 6, Item II)	0.2	0.6	0.0	0.0	0.0	0.0
4.2.1 Of Which Extraordinary Credits for the Primary Impact of FIES	0.0	0.0	0.0	0.0	0.0	0.0
4.3 Nonrecurrent Expenses of the Electoral Court System to Carry Out Elections (CF 1988, ADCT, Art. 107, Parag. 6, Item III)	0.0	0.0	0.0	0.0	0.0	0.0
4.3.1 Elections - OCC	0.0	0.0	0.0	0.0	0.0	0.0
4.3.2 Elections - Personnel	0.0	0.0	0.0	0.0	0.0	0.0
4.4 Expenses to Increase the Capital of Non-dependent State-owned Companies (CF 1988, ADCT, Art. 107, Parag. 6, Item IV)	0.1	0.0	0.0	0.0	0.0	0.0
4.5 Onerous Transfers (CF 1988, ADCT, Art. 107, Parag. 6, Item V)	0.0	0.1	0.0	0.0	0.0	0.0
4.6 Socio-Environmental or Climate Change-Related Projects (CF1988, ADCT, Art. 107, Parag. 6-A, Item I)	0.0	0.0	0.0	0.0	0.0	0.0

% of GDP	2016	2022	Annual Budget Law 2023	2nd Re-examination 2023	PLP 93 (2024)	PRLP-CD 02
4.7 Scientific, Technological and Innovation Institutions (CF1988, ADCT, Art. 107, Para. 6-A, Item II)	0.0	0.0	0.0	0.0	0.0	0.0
4.8 Direct Execution of Engineering Works and Services (CF1988, ADCT, Art. 107, Parag. 6-A, Item III)	0.0	0.0	0.0	0.0	0.0	0.0
4.9 Investments (CF 1988, ADCT, Art 107, Parag. 6-B)	0.0	0.2	0.2	0.2	0.2	0.2
4.10 Installment Payment of Court-Ordered Debts (CF 1988, ADCT, Art.107-A, Parag. 6)	0.0	0.1	0.1	0.1	0.1	0.1
4.11 Settlement of Accounts (CF 1988, ADCT, Art. 107-A, Parag. 6)	0.0	0.2	0.0	0.0	0.0	0.0
4.12 Financial Support to Subnational Entities for the National Wage Floor for Nursing Professionals	0.0	0.0	0.0	0.1	0.1	0.0

Source: STN (National Treasury Department), PLP (Bill of Supplementary Law) 93, Constitutional Amendment 95. Elaboration:IFI.

We briefly analyze below the changes and some data from the aforementioned funds.

(i) Constitutional Fund of the Federal District

The Constitutional Fund of the Federal District was created by Law No. 10,633, dated December 27, 2002. Art. 2 of the law establishes that, from 2003 onwards, the Federal Government's annual contribution to the fund shall be R$ 2.9 billion, annually adjusted by the change in the Federal Government's net current revenues (RCL, in the original acronym) accumulated over a 12-month period until June of the year prior to the fiscal year in relation to the immediately previous 12-month period. The figure below shows the values updating system:

TABLE 8. CALCULATION RULE FOR THE CONSTITUTIONAL FUND OF THE FEDERAL DISTRICT

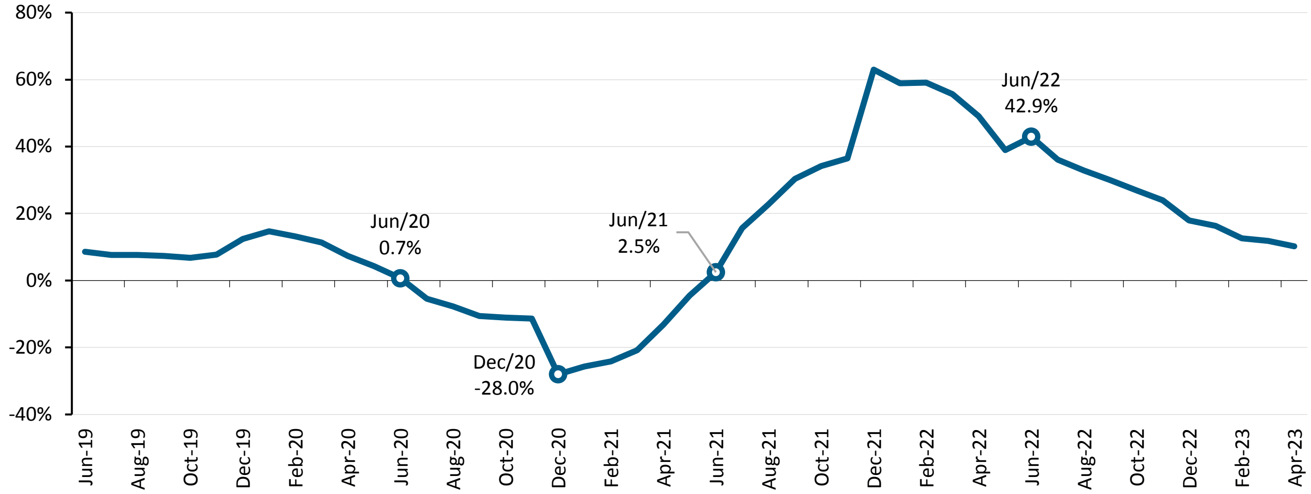
Year	Annual Value		Annual Value		Accumulated over 12 months		Accumulated over 12 months
2003	Transfers in 2003	=	R$ 2.9 billion	*	RCL (sum from Jul/01 to Jun/02)	÷	RCL (sum from Jul/00 to Jun/01)
2004	Transfers in 2004	=	Transfers in 2003	*	RCL (sum from Jul/02 to Jun/03)	÷	RCL (sum from Jul/01 to Jun/02)
2005	Transfers in 2005	=	Transfers in 2004	*	RCL (sum from Jul/03 to Jun/04)	÷	RCL (sum from Jul/02 to Jun/03)
(...)							
2022	Transfers in 2022	=	Transfers in 2021	*	RCL (sum from Jul/20 to Jun/21)	÷	RCL (sum from Jul/19 to Jun/20)
2023	Transfers in 2023	=	Transfers in 2022	*	RCL (sum from Jul/21 to Jun/22)	÷	RCL (sum from Jul/20 to Jun/21)
Year	**R$ billion**		**R$ billion**		**R$ billion**		**R$ billion**
2003	R$ 3.4	=	R$ 2.9	*	R$ 182.4	÷	R$ 157.6
2004	R$ 4.0	=	R$ 3.4	*	R$ 216.1	÷	R$ 182.4
2005	R$ 4.4	=	R$ 4.0	*	R$ 241.8	÷	R$ 216.1
(...)							
2022	R$ 16.1	=	R$ 15.7	*	R$ 846.9	÷	R$ 826.5
2023	R$ 23.0	=	R$ 16.1	*	Accumulated over 12 months	÷	R$ 846.9

Source: STN, Law No. 10,633/2002 and IFI. Elaboration: IFI.

In other words, the adjustment of the values of the Constitutional Fund of the Federal District depends on the behavior of the Federal Government's RCL in June of the year prior to the respective fiscal year. For example, in 2021 and 2022, the fund's amount grew due to the positive change in the Federal Government's RCL in June of the previous year (accumulated over a 12-month period). The graph below shows the evolution of the Federal Government's RCL change accumulated over a 12-month period.

Between 2022 and 2023, the balance of the Federal District Fund increased from R$ 16.2 billion to R$ 23.0 billion due to the Federal Government's RCL growth recorded in June 2022 (42.9%). It is worth mentioning that the Federal Government's RCL includes, for example, revenues from dividends and the exploitation of natural resources, headings that have registered a sharp increase in the last two years.

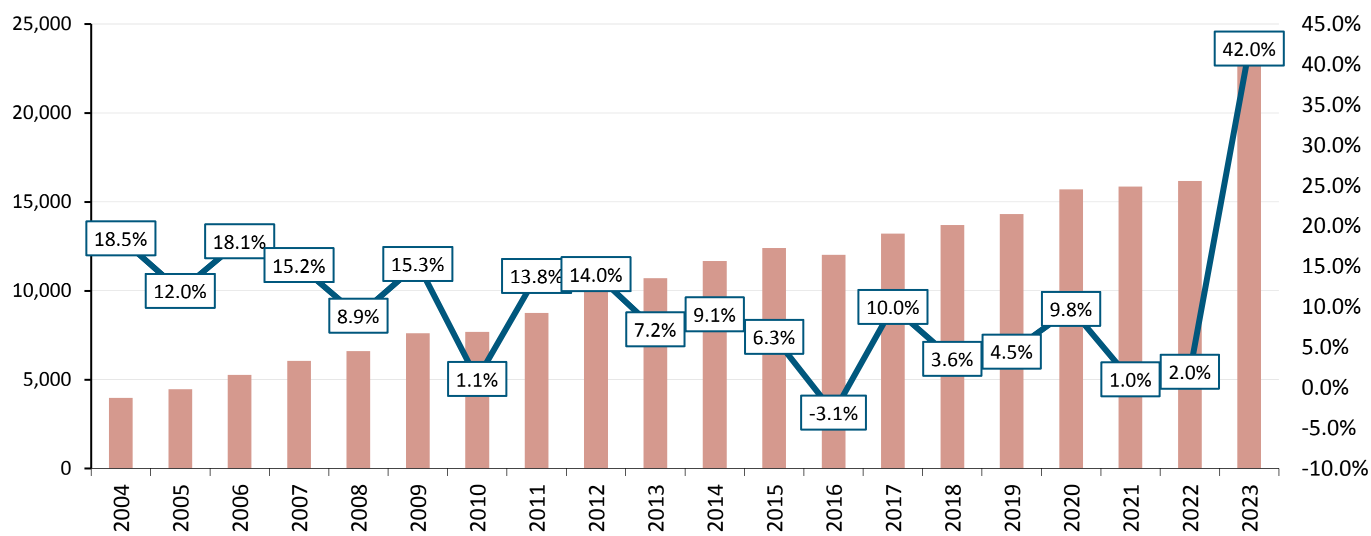
GRAPH 7. NOMINAL GROWTH OF NET CURRENT REVENUES



Source: National Treasury. Elaboration: IFI.

That is, the volatility of current revenues can influence the transfers and, consequently, the fund's resources. In situations of high growth in the Federal Government's revenues, transfers can exceed the fund's real budget needs. In turn, in case of low Federal Government RCL growth, lower transfers to the fund may influence the quality of public services in the Federal District. In 2016, compared to 2015, for example, the fund's resources were reduced by 3.1% in nominal terms due to the drop registered in the Federal Government's revenues (Graph 8).

GRAPH 8. FCDF TRANSFERS - R$ MILLION AND % GROWTH (NOMINAL)



Source: GDF, STN. Elaboration: IFI.

During the processing of PLP No. 93 in the Chamber of Deputies, the rapporteur included the FCDF in the limitation rule for the Federal Government's expenditure and changed the system for adjusting the fund's resources so that now they will grow according to the rule for total primary expenditure. Thus, the transfers to the fund will have a 0.6% minimum and 2.5% maximum real growth, being limited to 70% of the real growth in revenues.

According to the text passed by the Chamber, the new way to adjust the FCDF will be in force in 2025. Thus, to calculate the impacts of the measure, three scenarios have been simulated: (i) the FCDF resources grow by 0.6% per year, in real terms; (ii) FCDF grows 2.5% per year, in real terms; and (iii) FCDF grows between 0.6% and 2.5% per year, in real terms, limited to 70% of the growth of the Federal Government's revenues.

The revenue and inflation growth projections correspond to the IFI's base case scenario, available in the previously mentioned RAF No. 76, May 2023.

TABLE 9. SCENARIOS FOR THE GROWTH OF THE CONSTITUTIONAL FUND OF THE FEDERAL DISTRICT (R$ MILLION)

			Projections for real growth in expenditures Scenario			Scenarios for the Constitutional Fund of the Federal District – R$ Million			
	Broad Consumer Price Index 12 months up to June	Real Growth of Net Current Revenues	Scenario (i) Minimum Real Gain	Scenario (ii) Maximum Real Gain	Scenario (III) 70% of-- Revenue Growth	No Rule Change Scenario	Scenario (i)	Scenario (ii)	Scenario (iii)
2024	5.0	3.5	0.6	2.5	2.5	25,418	25,418	25,418	25,418
2025	3.6	2.7	0.6	2.5	1.9	27,035	26,495	26,995	26,826
2026	3.2	3.3	0.6	2.5	2.3	28,833	27,511	28,560	28,333
2027	3.2	2.3	0.6	2.5	1.6	30,444	28,572	30,222	29,716
2028	3.2	2.2	0.6	2.5	1.5	32,119	29,674	31,980	31,149
2029	3.2	2.5	0.6	2.5	1.8	33,999	30,819	33,841	32,729
2030	3.2	2.5	0.6	2.5	1.8	35,991	32,008	35,810	34,389
2031	3.2	2.5	0.6	2.5	1.8	38,086	33,242	37,894	36,124
2032	3.2	2.5	0.6	2.5	1.7	40,300	34,525	40,099	37,945
Average difference over 10 years (compared to the scenario with no rule change)						0	-23,962	-1,405	-9,596

Source: IFI. Elaboration: IFI.

According to Table 9, it is possible to notice that the potential impact of the rule change for the adjustment of the funds transferred to the FCDF (Constitutional Fund of the Federal District) may range from R$ 1.4 billion to R$ 9.6 billion. In an extreme scenario, in which the growth in expenditure follows the floor in all years and there is a high real growth for revenues, such an impact could reach R$ 24.0 billion. It is worth mentioning that this scenario would only be reached in situations where the primary balance target would not be met for an entire decade, even with a scenario of high real revenue growth. That is, it is a very improbable scenario.

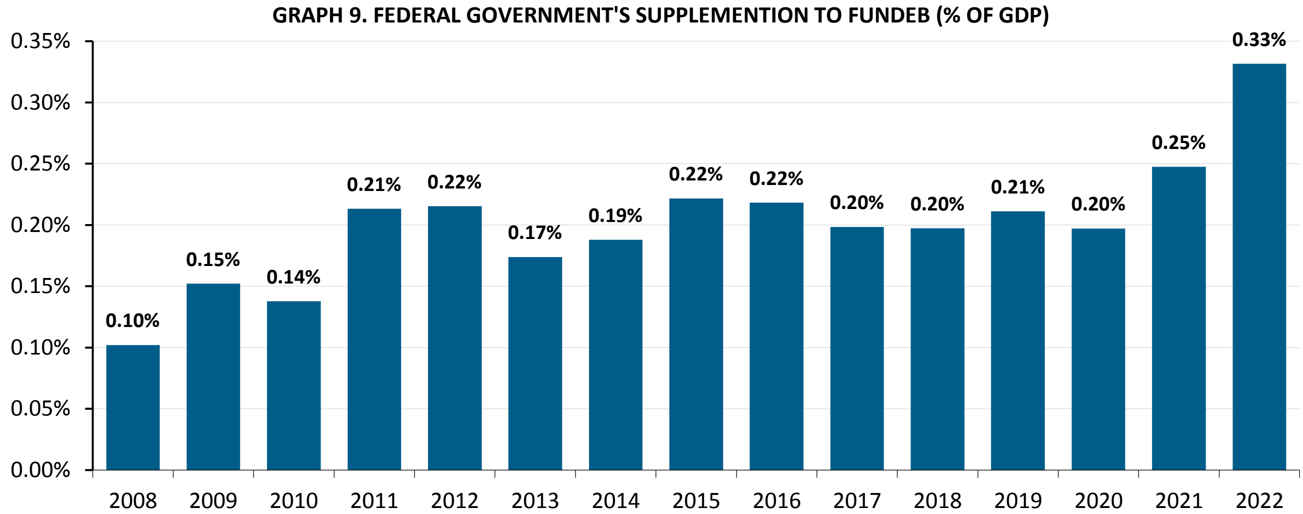
A fourth scenario could be thought of, that is, when real revenues grow at a 0.9% real rate, causing the expenditure to grow by 0.6% (floor). In this case, this impact of R$ 24 billion would be reduced to R$ 3.1 billion, which indicates the unreality of scenario (i).

(ii) Federal Government's Supplement to Fundeb

The Fund for Maintenance and Development of Basic Education and Education Professionals (Fundeb, in the original acronym) is an accounting fund and one of the main sources of education funding in Brazil. The fund guarantees resources so that states and municipalities fulfill their constitutional duties to invest in education.

The Federal Government contributed 10% of the funds to Fundeb until 2019 when Constitutional Amendment No. 108 established the gradual increase of such a percentage over the years until it reaches 23% in 2026. The new rules prescribe the following Fundeb percentages: 12% in 2021; 15% in 2022; 17% in 2023; 19% in 2024; 21% in 2025; and 23% in 2026. In 2022, the Federal Government supplemented R$ 38.9 billion to the fund. The effects of such a change can be observed in the 2021 and 2022 implementation in Graph 9, which presents the Federal Government's supplementation to Fundeb as a GDP ratio.

The fact that the Federal Government's supplementation to Fundeb is or is not subject to the primary expenditure limits established by the new framework will not affect transfers to the fund since a potential change in this direction would have to be made through a constitutional amendment.



Source: STN. Elaboration: IFI.

V – Concluding Remarks

This technical note tried to discuss the main elements present in the proposal for the new fiscal framework submitted by the Government in April, as well as the most significant changes made to the text during its processing in the Chamber of Deputies.

The approval of a new fiscal framework is important for the conduct of the Federal Government's fiscal policy in the years to come. The successive changes made to the previous expenditure ceiling rule affected its credibility, posing uncertainties in consolidating the country's macroeconomic stability. Therefore, a new rule is made necessary to support expectations and reduce uncertainties, broadening the planning horizon for households and companies. A new fiscal rule is also important to make forecasts possible regarding the dynamics of public spending in the years to come, making it easier for the Central Bank to conduct the monetary policy.

In broad terms, the proposed fiscal rule is complex, although the issue has not been discussed in this note. The new framework is more flexible than the previous rule (expenditure ceiling), although it also establishes a ceiling for the evolution of primary expenditure, which will be conditioned to the performance of revenues. It is an improvement compared to the country's previous fiscal rules.

The point of greatest uncertainty about the new rule lies precisely in the realization of the revenues necessary to meet the primary balance target set in the budget guidelines. As discussed in the presentation of the main topics of PLP No. 93, 2023, the framework makes the budget implementation stricter by introducing a floor for expenditures. And the lack of flexibility to reduce discretionary expenditures in the budget impacts revenues performance.

Over the last 25 years, the federal government's collection has been greatly influenced by the behavior of commodity prices, both by direct and indirect effects. The boom noticed in the 2000s generated impressive collection gains and, therefore, led to the achievement of continued primary surpluses, even with the real growth in expenditure. This march was interrupted from 2014 onwards, when revenues decelerated and registered a behavior more in line with that of the GDP.

In this sense, the excessive burden on revenues to meet the primary balance targets may affect the credibility of the new fiscal framework. A new commodities cycle is not expected to happen in the coming years, with the Brazilian economy's real growth converging to 2.0% per year in the medium term, according to the latest revision of macroeconomic and fiscal scenarios published by the IFI.

In the absence of positive external shocks, the increase in the economy's average growth rate will require productivity increases, which will depend, in turn, on structural reforms capable of improving the business environment for companies and promoting income increases for households. IFI expects potential productivity gains from the possible approval of a tax reform capable of making the Brazilian tax system simpler.

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