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Tax Reform on Consumption in Brazil: The Need for Change

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Abstract

This article provides a brief analysis of the reasons that led Brazil to pursue tax reform on consumption, highlighting the peculiarities of the Brazilian tax system through: i) the high complexity of complying with tax legislation; ii) extensive tax litigation; and iii) tax competition among the federated entities seeking to attract private investment and increase revenue. The methodological approach adopted combines pragmatic and zetetic research, drawing upon Brazilian and foreign legal scholarship and analyzing precedents from the Brazilian Supreme Federal Court. The development of this study necessarily entails questioning and criticizing classical tax law dogmatics in order to adapt it to the new challenges and demands to which it is constantly exposed. By situating the Brazilian experience, the article also offers insights into the broader international debate on VAT reforms and federal systems.

Keywords

Tax Reform on Consumption, Complexity of Rules, Extensive Tax Litigation, Tax Competition

1. Introduction

Why did Brazil undertake tax reform on consumption? What objectives does it seek to achieve? How might this reform contribute to international tax law? These are the central questions, admittedly complex, that this article seeks to address without claiming to exhaust such a multifaceted issue.

Beyond responding to these questions, the article also aims to provide foreign legal scholars with an understanding of the Brazilian tax system, whose challenges may resemble those of other countries but manifest under different circumstances and invite distinct legal solutions (Mössner, 2008).

Naturally, any comparative discussion must account for the peculiarities of le-

gal systems shaped by different histories, contexts, and legal cultures (Garbarino, 2010). For this reason, the article begins by outlining the minimum requirements for "law" to be recognized as "law," before turning to the peculiarities of the Brazilian tax system.

This article proceeds in four parts. Chapter 1 discusses the peculiarities of Brazilian federalism; Chapter 2 examines the complexity and interpretative challenges in Brazilian tax law; Chapter 3 explores tax litigation; and Chapter 4 analyzes the fiscal war and the reform's potential.

2. Peculiarities of the Brazilian Tax System

Brazil adopts a federal system, redistributing its political power among i) the Federal Union, ii) the States, and iii) the Municipalities and the Federal District, guaranteeing each federated entity its respective independence and autonomy. This federal structure of Brazil constitutes an entrenched clause and thus cannot be altered even by constitutional amendment (Costa, 2023), as determined by Article 60, §4, I, of the Brazilian Federal Constitution[1]. In other words, only a new Federal Constitution could abolish the Brazilian federative system.

The concept of federalism leads us to consider at least two levels of government, each exercising authority over the same territory and the same population, with a guarantee of a certain degree of autonomy for each government to act in one or more areas. Federalism also presupposes the coexistence of partial legal orders, represented by the constituent states, alongside the national legal order, from which emanate legal norms applicable throughout the entire national territory, such as Brazil's supplementary laws and the Federal Constitution (Lewandowski, 1994).

Thus, what distinguishes federalism from a unitary state is precisely the collaboration and solidarity among the entities that compose the federation in the pursuit of a common ideal of justice (Maneira & Lima, 2019).

The Brazilian state conceived by the 1988 Constitution is not neutral (Schoueri, 2005). It expressly establishes the following fundamental objectives to be achieved: i) "to build a free, just, and solidary society"; ii) "to ensure national development"; iii) "to eradicate poverty and reduce existing social and regional inequalities"; and iv) "to promote the well-being of all, without prejudice based on origin, race, sex, color, age, or any other form of discrimination."

To achieve these objectives, particularly that of promoting national development and reducing existing social and regional inequalities, Brazilian consumption taxation represents an important mechanism to be employed in this effort.

In general terms, the current system of taxation on the consumption of goods and services in Brazil is widely recognized as both complex and regressive, overburdening the productive sector and, consequently, undermining the competi-

[1]Federal Constitution of Brazil of 1988: "Art. 60. The Constitution may be amended by proposal: (…) § 4 No proposal of amendment shall be considered if it tends to abolish: I—the federal form of State".

tiveness of Brazilian producers in global markets. For this reason, as will be explained further below, reform is necessary.

To give a brief sense of the overall complexity of the Brazilian tax system, from the enactment of the Federal Constitution of 1988 until 2024, approximately 517,388 tax norms have been created in Brazil: i) 45,814 enacted by the Federal Union; ii) 170,758 enacted by the States; and iii) 300,816 enacted by the Municipalities, according to a study conducted by the Brazilian Institute of Tax Planning and Research[2]. In other words, in approximately thirty-six years, more than half a million norms have been enacted in Brazil solely in the field of taxation.

This immense proliferation of norms renders the Brazilian tax system highly complex and, in many cases, inefficient. As a result, it is not uncommon for taxpayers and the tax authorities to adopt divergent interpretations of tax legislation, which leads to judicial disputes. These interpretative divergences—combined with inefficiencies in the collection of tax debts—make Brazil the country with the highest level of tax litigation in the world.

In addition to the vast complexity of its tax legislation and the extraordinarily high rate of tax litigation, Brazil also faces profound social and economic inequality across its territory. By way of example, the Southeast region of Brazil (comprising only four states) accounts for 53% of the country's Gross Domestic Product, whereas the North and Northeast regions (together comprising sixteen states) account for only 19.5%, according to a study published in November 2024 by the Brazilian Institute of Geography and Statistics[3]. Therefore, it is necessary to adopt measures that promote equality and create opportunities for all regions of the country.

A useful comparative reference may be found in the Canadian Goods and Services Tax ("GST") and the Harmonized Sales Tax ("HST"), which exemplify a model of cooperation in a federal system (Canada Revenue Agency, 2023). While the federal government levies the GST, several provinces have chosen to harmonize their sales taxes with the federal regime, creating the HST. This mechanism illustrates how federated entities can maintain financial autonomy while also pursuing harmonization and efficiency through intergovernmental agreements. The Canadian experience demonstrates that revenue-sharing arrangements, rather than the mere allocation of taxing powers, are crucial to reconciling federalism with an efficient consumption tax system.

In this context, since the 1988 Constitution, Brazilian states have used the ICMS

[2]Brazilian Institute of Tax Planning and Research, 2024, accessed on November 1, 2025: https://ibpt.org.br/quantidade-de-normas-editadas-no-brasil-30-anos-da-constituicao-federal-de-1988/.

[3]Brazilian Institute of Geography and Statistics, 2024, accessed on November 1, 2025: https://agenciadenoticias.ibge.gov.br/agencia-noticias/2012-agencia-de-noticias/noticias/41893-em-2022-pib-cresce-em-24-unidades-da-federacao#:~:text=Regi%C3%A3o%20Sudeste%20ganha%20participa%C3%A7%C3%A3o%20no%20PIB%20nacional&text=%2C6%20p.p.).-,J%C3%A1%20a%20Regi%C3%A3o%20Nordeste%20manteve%20sua%20participa%C3%A7%C3%A3o.,cada%2C%20entre%202021%20e%202022.

(Tax on the Circulation of Goods and Services) as an instrument for attracting investment and stimulating regional development[4]. It is precisely against the backdrop of these serious inequalities, and the granting of tax advantages by states and municipalities to attract greater private investment into their territories, that the so-called "tax war" emerged.

To attract private investment, states and municipalities began to unilaterally grant tax incentives—particularly reductions, exemptions, or deferrals of taxes levied on the sale of goods and the provision of services—often without the required authorization from the National Council for Fiscal Policy (an essential requirement for the validity of tax incentives in Brazil). This uncoordinated competition among federated entities generated significant distortions.

Companies frequently choose the location of their operations not for reasons of efficiency, logistics, or market potential, but rather because of the tax benefits offered by particular jurisdictions. In practice, economic decisions that should have been based on business criteria are determined by fiscal incentives.

A company would hardly choose to establish itself in the Northern Region of Brazil, for example, rather than in Rio de Janeiro or São Paulo (both located in the Southeast Region), unless it were offered an incentive in the form of a tax benefit. However, the wealthier states were equally unwilling to forgo part of their revenue.

By analogy with a commercial context, the states began to view one another as "competitors", granting benefits to taxpayers—such as deferrals of tax payments and/or reductions in the tax burden—in order to attract them and secure them as "clients". Yet this fiscal war among the states did nothing to reduce Brazil's social inequalities. Instead, it generated considerable legal uncertainty and further intensified the already excessive level of tax litigation.

To curb this fiscal war, it was established that the states should be subject to a collegiate body—the National Council for Fiscal Policy[5]—which represents the federation as a whole. Thus, for any state to grant a tax benefit, it must obtain the unanimous approval of that collegiate body. However, this mechanism did not produce the expected effects, as states continued to unilaterally grant tax benefits as a means of attracting further investment.

Therefore, more effective mechanisms were required in order to i) reduce the complexity of tax legislation; ii) diminish tax litigation in Brazil; and iii) curb and ultimately extinguish the fiscal war among the states.

With the enactment of Complementary Law No. 214 on 16 January 2025, Brazil took a decisive step toward restructuring national taxation on the consumption of

[4]The municipalities also began granting tax benefits to reduce the ISS (Tax on Services) burden as an instrument for attracting investment.

[5]The National Council for Fiscal Policy in Brazil is the collegiate body composed of the Secretaries of Finance, Treasury, or Taxation of the States and of the Federal District, with its meetings chaired by the Minister of Finance. Its primary function is to enter into agreements for the granting or revocation of exemptions, incentives, and fiscal and financial benefits related to the Tax on the Circulation of Goods and on the Provision of Interstate, Intermunicipal, and Communication Services ("ICMS"), pursuant to the Constitution, Article 155, item II and § 2, item XII, subitem g, and Complementary Law No. 24 of 7 January 1975.

goods and services by instituting the "dual VAT system" (*IVA-Dual*), composed of i) the Goods and Services Tax (IBS), under the jurisdiction of the States and Municipalities; and ii) the Contribution on Goods and Services (CBS), under the jurisdiction of the Federal Union. These two taxes will operate as "twins", subject to the same set of rules.

In essence, the tax reform replaces six existing taxes (PIS, COFINS, IOF-Insurance, IPI, ICMS, and ISS) with two IBS and CBS. Approved by the National Congress, this reform was introduced with the promise of addressing part of the current problems and fostering a more efficient business environment, by means of the imposition of consumption taxes under a broad non-cumulative regime, with uniform application across the entire national territory, with the minimum possible tax incentives, and with collection taking place exclusively at the place of destination.

The implementation of this new taxation model in Brazil is only feasible due to technological advances that enable the issuance of electronic invoices and the adoption of the split payment system. Under this mechanism, at the moment of payment for the acquisition of a good or service, the portion corresponding to the tax is automatically allocated to settle the tax obligation (Teixeira, 2022).

As a result, the seller receives only the net amount, with the tax already deducted and transferred to the tax authorities. If, at the end of a given period, the taxpayer holds more credits than debits, the immediate refund of the consumption taxes paid in advance must be guaranteed in their favor. In addition to preventing fraud related to the creation of fictitious tax credits, this system also allows the competent federative entity to benefit from significant cash flow anticipation (Maneira & Maia, 2025).

While the split payment mechanism has the potential to prevent fraud and improve cash flow management for tax authorities, its practical application requires careful consideration of comparative experiences. Lessons from other jurisdictions, particularly within the European Union, reveal both the strengths and the limitations of such a system. The European Union's VAT Committee concluded that the administrative and compliance costs imposed on both tax administrations and taxpayers through the use of split payment are potentially more burdensome than the benefits derived[6].

However, the fact that this mechanism has not been fully successful in other jurisdictions does not mean that it will necessarily fail in Brazil. There are two

[6]Given the importance of the topic, see below the exact terms used in the studies conducted by the European Union:

"The analysis carried out illustrated the potential benefits as well as significant challenges related to the use of split payment as an alternative VAT collection method. Although split payment has high potential to reduce the VAT gap (especially MTIC fraud and non-compliance), if applied broadly across the EU, the cost of it through increased complexity of the VAT system, high administrative burden and significant impact on businesses' cash flow may easily outweigh the benefits. Therefore, broad application of split payment is likely to be an unattractive policy tool, given the significant rise in costs for businesses and authorities. However, it has characteristics that are very effective in reducing certain types of fraud and therefore may be suited as a targeted measure with limited scope." (EUROPEAN COMMISSION. Analysis of the impact of the split payment mechanism as an alternative VAT collection method. Brussels: Deloitte, 2017).

peculiar features of the Brazilian context that provide some grounds for optimism. First, Brazil has a comparatively high level of tax evasion when contrasted with that of the European Union. Second, Brazil has a highly efficient and technologically advanced financial system, which allows for instant bank transfers. These characteristics may render the split payment mechanism effective in Brazil, to the extent that the benefits achieved outweigh the costs of its implementation.

3. Complexity and Interpretative Challenges in Brazilian Tax Law

Law reveals itself as an argumentative discipline (Maccormick, 2005), in which well-constructed reasoning can persuade an institution of the thesis advanced. Precisely because of the persuasive power of arguments, law may be regarded as an "art" or a "game", given its reliance on interpretation and argumentation (Scalia, 1997).

The act of interpretation involves not only acts of knowledge but also acts of will. In other words, interpretation entails the choice of one among the various meanings admitted by the text. The provisions constitute the object of interpretation, while the norms constitute the result of that interpretation. Therefore, law is not equivalent to written normative texts, whether enacted by the legislature (through statutes) or issued by the judiciary (through judicial decisions). The norm is not the object but rather the product of interpretation (Guastini, 2020).

Anyway, the will of the Democratic Rule of Law must coincide with and represent the will of the People. This is one of the fundamental principles of the Brazilian Republic, already set forth in the very first article of the Federal Constitution[7]. In the Rule of Law, rulers are subject to the authority of law, and not to their personal will. The formal structuring of law is a key element in ensuring the realization of legal certainty (Ávila, 2021b).

Law, as a source of general and abstract norms, promotes the stability of legal order, since it avoids the need to alter norms with every change of persons or circumstances. Precisely because norms are general, they are addressed to a "class of persons", and because they are also abstract, they are addressed to a "class of actions" (Bobbio, 2016). In other words, by being general, norms apply to all addressees falling within the hypothesis established by the normative instrument.

For example, when providing that owners of motor vehicles must pay the annual vehicle tax, the norm already identifies its addressees ("class of persons"). That is, regardless of who owns the vehicle—whether the wealthiest individual in the country or the poorest—he or she will be subject to the payment of the annual

[7]"Article 1. The Federative Republic of Brazil, formed by the indissoluble union of the States, the Municipalities, and the Federal District, constitutes a Democratic State governed by the rule of law and is founded upon the following principles:"
(...)
Sole paragraph. All power emanates from the people, who exercise it through elected representatives or directly, in accordance with this Constitution.

vehicle tax.

By being abstract, norms apply to a universality of actions, without specifically addressing each individual case. Returning to the example above, when establishing that the annual vehicle tax is levied on the ownership of motor vehicles, the norm defines its hypothesis of incidence ("class of actions"). Thus, whether the property is a Ferrari or a modest Volkswagen Beetle, because both are "motor vehicles", the annual vehicle tax will apply in either case.

Given that norms are general and abstract, the law is applicable to an indeterminate number of persons and situations under a "one-size-fits-all" or "average-size" approach, based on certain properties that the legislator deemed relevant while disregarding others that, at the time of application, may become significant depending on the perspective adopted (Ávila, 2021a).

In Brazil, the problem concerning the complexity of tax legislation is not the absence of fiscal norms. After all, if that were the case, how could one explain that, from the enactment of the Federal Constitution of 1988 until 2024, approximately 517,388 such norms were created in Brazil, and, even so, the problem has not yet been resolved?

In fact, the real problem lies in the excessive number of ancillary obligations and in the difficulty of interpreting such tax norms in a teleological and systematic manner.

According to the World Bank[8], in Brazil the time required to calculate, declare, and pay taxes is about ten times greater than that of member countries of the Organization for Economic Co-operation and Development (OECD). While companies in Brazil spend an average of 1500 hours per year to comply with ancillary tax obligations, the OECD average is only 164 hours per year. These numbers are striking and reveal a troubling reality in Brazil.

The more complex and burdensome the compliance with ancillary obligations becomes—requiring high compliance costs and exposing taxpayers to significant risks of penalties for errors—the less attractive the jurisdiction will be for investment. After all, who would invest in a country marked by high compliance costs, a complex tax system, and considerable political instability?

To offset such a "risk investment", the expected financial return must be considerably higher. This is how markets operate: the greater the investment risk, the greater the expected return. In Brazil, this expectation of high financial returns is indeed present, since, in addition to being one of the largest economies in the world and being geographically strategic (not subject to natural disasters such as tsunamis, hurricanes, or earthquakes), it also has a highly dynamic domestic consumer market, with more than 212 million inhabitants[9].

[8]WORLD BANK STUDY, accessed on November 1, 2025: https://archive.doingbusiness.org/pt/data/exploretopics/paying-taxes.

[9]BRAZILIAN GOVERNMENT DATA, accessed on November 1, 2025: https://www.gov.br/secom/pt-br/assuntos/noticias/2024/08/populacao-do-brasil-chega-a-212-6-milhoes-de-habitantes-aponta-ibge#:~:text=A%20popula%C3%A7%C3%A3o%20brasileira%20at%C3%A9%201%C2%BA,Uni%C3%A3o%2C%20por%20meio%20de%20portaria.

Nevertheless, there is still a need for greater maturity in tax law, particularly with respect to compliance with ancillary obligations[10].

Brazil currently has more than 5500 municipalities, according to data from the Brazilian Institute of Geography and Statistics. This means that Brazil has over five thousand five hundred distinct federated entities, each with competence to legislate and to impose specific ancillary obligations.

In this context, imagine a company operating in the retail e-commerce sector, selling goods to individual consumers across all regions of Brazil. It would be unreasonable to require such a company to monitor, study, and apply the tax legislation of more than 5500 federated entities in order to determine which ancillary obligations must be fulfilled. The obscurity of the norms and the sheer number of tax-related legal instruments can render the Brazilian tax system nearly impracticable (Costa, 2007). Taxpayers should not be penalized as a result of the political choice to maintain so many federated entities.

To avoid this scenario, one possible solution would be to unify the system of all federated entities (the Federal Union, the States, the Municipalities, and the Federal District) and to strictly limit the number of ancillary obligations, allowing taxpayers to submit centralized electronic filings.

A study conducted by Ernst & Young[11] demonstrates the advantages of such an approach: in the European Union, for example, harmonized Value-Added Tax ("VAT") reporting rules and the adoption of standardized electronic systems have reduced compliance costs and improved legal certainty across member states. Similarly, OECD countries have advanced digital platforms that centralize the fulfillment of tax obligations, minimizing duplication and promoting efficiency (OECD, 2025). Brazil could significantly benefit from adopting comparable measures, thereby enhancing its business environment and fostering greater competitiveness in the global market.

Moreover, Brazil currently faces a serious difficulty regarding the interpretation of tax norms. At this point, the provision of the normative text (the object of interpretation) must not be confused with the legal norm itself (the result of interpretation). Instead of adopting a teleological and systematic interpretation, the Public Treasury often resorts to a merely economic interpretation, with a clear revenue-oriented bias.

The interpretation of tax norms with the clear purpose of maximizing revenue to satisfy the needs of the State does not appear to be the most appropriate approach. After all, if this were the case, it would mean endorsing as correct any

[10]Brazilian Institute of Geography and Statistics, 2024, accessed on November 1, 2025: https://agenciadenoticias.ibge.gov.br/agencia-noticias/2012-agencia-de-noticias/noticias/41111-populacao-estimada-do-pais-chega-a-212-6-milhoes-de-habitantes-em-2024#:~:text=O%20IBGE%20divulga%20hoje%20(29,212%2C6%20milh%C3%B5es%20de%20habitantes.

[11]Ernst & Young studies, accessed on November 1, 2025: https://www.ey.com/en_lu/insights/tax/vida-and-the-future-of-vat-a-digital-revolution-in-european-tax-compliance.

interpretation that leads to the highest possible tax collection, which would clearly violate the principles of contributive capacity and tax justice (Lehner, 1998).

It is undisputed that normative provisions may potentially carry more than one meaning. In such cases, however, the interpreter cannot arbitrarily select any interpretation; rather, the analysis must remain within the minimum meanings incorporated into the ordinary or technical use of language. The interpretation of tax norms in Brazil often requires a critical re-examination of both doctrine and jurisprudence that have been consolidated over decades.

It is referred to as a re-examination rather than an abandonment because past reflections should not serve to bind present or future reasoning, but rather to inform and reveal what has previously been decided and, where compatible, to persuade the legal decision-maker either i) that the previously established position remains valid and coherent, or ii) that sufficiently compelling reasons exist to overcome the prior understanding, thereby creating a new norm, whether through legislation enacted by the Legislative Branch or through precedent established by the Judiciary (Schauer, 2009).

Therefore, the analysis of tax norms must—or at least should—be carried out in a neutral manner (without privileging either the Public Treasury or the taxpayer), adopting teleological and systematic interpretations. The Judiciary, being in theory a strictly legal (and not political) institution, should not resort to political or economic considerations as decisive criteria when adjudicating specific cases.

When called upon, the Judiciary must interpret the provisions contained in the normative instruments enacted by the legislator and apply the result of this legal interpretation to concrete cases. The executive branch, in turn, is primarily responsible for implementing what has been established by the legislature and for defining, within the limits set by law, public policies and its plan of government, while observing the public budget. The legislature, for its part, is primarily tasked with introducing the sources of law by enacting general, abstract, and prospective norms.

Therefore, the legality of a tax norm must be examined by the Judiciary from a technical perspective (and not a political one), assessing its compatibility or incompatibility with the national tax system. Accordingly, although the potential effects of a given decision on the public budget may influence the adjudicator to some extent, they should not constitute a decisive criterion for judicial decision-making.

Currently, less positivist approaches are directly influencing Brazilian tax law, which today is likely less legalistic and less balanced in the relationship between the Treasury and taxpayers than in the past. Indeed, there is currently no equilibrium in the Treasury-taxpayer relationship in Brazil; quite the opposite. There is, in fact, a certain tendency to adopt interpretations in favor of the Treasury under the pretext of privileging the "public budget" (Becho, 2014).

As an illustrative example, one may cite the decision of the Superior Court of

Justice in Special Appeal No. 1.120.295-SP[12], which—by expressly disregarding the rule set forth in Article 174, sole paragraph, item I, of the Brazilian National Tax Code[13]—adopted a new standard for interrupting the statute of limitations: the filing of the tax enforcement action, without any legal basis. In that decision, "law" was effectively created through a judicial decision, thereby expressly altering the positivized norm.

Another example may help to clarify the issue. Companies operating in Brazil are required to pay social security contributions on their gross revenues. In situations where a company has provided a service but has not received any payment from its client—who remains in default—must the company still pay social security contributions? In other words, can a taxpayer be required to pay a tax levied on revenue even when nothing has been received?

If the Brazilian tax system is analyzed systematically and teleologically, the answer to the above question would be negative. In cases where default is effectively confirmed, the taxpayer lacks contributive capacity and therefore should not (or, at least, should not reasonably) be burdened with the incidence of social security contributions. Moreover, if such taxes have been paid, the taxpayer may seek restitution from the Federal Treasury. This would be the logical outcome.

However, in addressing the aforementioned issue and adjudicating Extraordinary Appeal No. 586.482[14]—with general repercussion recognized (Theme 87)—the Federal Supreme Court held that defaulted sales must be subject to the payment of social security contributions[15], since they form part of the company's gross revenue. According to the *ratio decidendi* adopted in that judgment, nonpayment represents an event subsequent to the taxable event, meaning that the tax liabilities remain due. Moreover, default is considered an inherent part of any business activity, and thus, companies cannot shift to the government the risks that are intrinsic to taxpayers.

With due respect, this decision is misguided. After all, the presumption of contributive capacity in cases of the sale of goods or services was not effectively realized. It is not the provision of goods, services, or rights that reveals taxable wealth, but rather the remuneration received (Maneira & Maia, 2025). Brazilian tax law expressly determines that social contributions must be levied on the gross revenue earned by the company. Therefore, allowing social contributions to be imposed on unpaid amounts means permitting such a tax to be levied on assets (a situation

[12]Brazilian Superior Court of Justice in the judgment of Special Appeal No. 1.120.295-SP in 2010: https://processo.stj.jus.br/processo/pesquisa/?tipoPesquisa=tipoPesquisaNumeroRegistro&termo=200901139645.

[13]The Brazilian National Tax Code:

"Article 174. The action for the collection of tax credit is subject to a statute of limitations of five years, counted from the date of its definitive assessment.

Sole Paragraph. The limitation period is interrupted:

I—by the judge's order directing the summons in tax enforcement proceedings."

[14]Brazilian Federal Supreme Court in the judgment of Extraordinary Appeal No. 586.482 in 2011: https://portal.stf.jus.br/processos/detalhe.asp?incidente=2616815.

[15]PIS (Social Integration Program Contribution) and COFINS (Contribution for the Financing of Social Security).

entirely different from that provided for in the tax statute) instead of on gross revenue.

Tax norms cannot be interpreted with the purely economic objective of increasing revenue in favor of the federated entity. They must be interpreted teleologically and systematically, in accordance with the principles of tax justice and contributive capacity.

From an economic standpoint, the decision to uphold the taxation of defaulted sales also generates several distortive and regressive consequences that undermine both market efficiency and the constitutional principle of contributive capacity.

First, such taxation discourages credit-based transactions, as firms become reluctant to sell goods or services on deferred payment terms. In economies like Brazil's—where installment sales play a fundamental role in sustaining consumption—this effect may cause a contraction in aggregate demand, negatively impacting growth and employment. The most affected sectors are typically retail, manufacturing, and services, which rely heavily on credit sales.

Secondly, the decision introduces fiscal inefficiency and systemic risk. By taxing unpaid sales, the government encourages non-compliance with tax obligations (precisely to avoid paying taxes on revenue that was not received), which will inevitably increase tax assessments. This undermines the predictability and transparency of the tax system, essential factors for attracting investment and maintaining macroeconomic stability.

This decision also highlights the clear imbalance in the Treasury–taxpayer relationship, which currently reveals a notable trend of rulings in favor of the Treasury and a disregard for rules expressly established in the Brazilian legal system. The role of the judiciary is not to concern itself with the public budget, but rather with the constitutionality of the laws.

It is therefore expected that the ongoing tax reform in Brazil will change this scenario, making it possible to i) effectively reduce the existing complexity and ancillary tax obligations; and ii) promote a teleological and systematic interpretation of tax norms, instead of a merely economic interpretation with an overtly revenue-oriented bias.

4. Extensive Tax Litigation in Brazil

In their constant pursuit of increased revenue, tax authorities employ argumentative techniques to defend a more flexible interpretation of the concepts used in tax norms, so as to tax the greatest possible number of transactions carried out by taxpayers. From the perspective of the tax authorities, such an interpretation upholds the Democratic Rule of Law, insofar as it enables greater revenue collection to finance public services.

Taxpayers, in turn, also resort to argumentative techniques, maintaining that the private law institutions incorporated into tax legislation must be understood strictly within the limits established by the legal sources. From the taxpayer's standpoint, this interpretation promotes legal certainty and predictability regarding the tax burden that will affect business operations.

This argumentative divergence between the Treasury and taxpayers is neither new nor exclusive to Brazil. In fact, tax litigation exists throughout the world, to a greater or lesser extent. The problem is that, in Brazil, tax litigation is exceptionally high and—in certain matters—appears to be practically endless.

At this point, to better understand the relevance of tax litigation in Brazil, nothing is more illustrative than objective numbers.

According to an article published by FENACON in 2022[16], tax litigation in Brazil amounts to R$5.44 trillion (almost 1 trillion American dollars). This figure is larger than the combined GDP of Argentina (US$621.83 billion) and Colombia (US$363.84 billion) in 2023. These countries represent, respectively, the third and fourth largest economies in Latin America.

The data contained in the *Justice in Numbers* 2023 *Report* issued by the Brazilian National Council of Justice[17] further highlights the duration of cases under judicial review, with low success rates in the collection of tax debts. By way of example, tax enforcement actions remain a significant bottleneck in the Judiciary, accounting for 27.3 million (33.5%) of all cases pending, with the highest congestion rate in the Judiciary (88.4%). In State Courts, a tax enforcement case takes an average of 6 years and 3 months to be closed, whereas in Federal Courts it takes 8 years and 10 months. In 2022, the average duration of a tax enforcement proceeding was 6 years and 7 months.

Indeed, excessive prolongation of proceedings leads to the erosion of certain rights, which is why expeditious adjudication becomes particularly important. In this regard, the parties to the process must cooperate with one another in order to obtain, within a reasonable time, a fair and effective decision on the merits.

Although the concept of "reasonable duration of proceedings," set forth in article 5, item LXXVIII, of the Brazilian Federal Constitution, is highly indeterminate[18], this provision—applicable to both administrative and judicial proceedings—imposes upon the legislature the duty to adopt the necessary measures to make the exercise of this right feasible (Costa, 2023).

In the broader framework of human rights protection, the Inter-American Human Rights System plays a highly relevant role. Through the American Convention on Human Rights ("ACHR"), signed in San José, Costa Rica, on November 22, 1969, the most basic rights inherent to human dignity were elevated to the international level, among them the principle of reasonable duration of proceedings. This established the need to define minimum thresholds that, if observed, safeguard fundamental rights.

In this context, to mitigate the harmful effects caused by the accumulation of ineffective tax enforcement proceedings, one suggestion would be that, in Brazil,

[16]National Federation of Accounting Services Companies and Advisory, Expertise, Information and Research Companies ("FENACON"), accessed on November 1, 2025: https://fenacon.org.br/noticias/contencioso-chega-a-r-544-tri-no-brasil%EF%BF%BC/.

[17]National Council of Justice, accessed on November 1, 2025: https://www.cnj.jus.br/wp-content/uploads/2023/08/justica-em-numeros-2023.

[18]Indeterminacy arises when doubt or lack of clarity emerges regarding a relevant issue that requires an answer, for which a (more or less) determinate response is sought.

whenever the adjudicator requires a measure to be undertaken by the claimant (the Public Treasury), three opportunities should be granted for compliance with the legal order: i) the first order, to be fulfilled within sixty days; ii) the second, within thirty days; and iii) the third, within forty-eight hours. If these deadlines are disregarded, the tax enforcement proceeding should be dismissed, on the grounds of abandonment of the case by the claimant, in accordance with the Brazilian Code of Civil Procedure (Becho, 2011).

As long as no sanctions are applied in cases of violation of the principle of reasonable duration of proceedings—particularly in matters concerning tax enforcement—this principle will remain of limited effectiveness within the Brazilian legal system (Carrazza, 2023). It is likely that, if there were a more explicit and direct provision for sanctions, the reality would be quite different.

Although no sanctions have been adopted, the Ministry of Finance has expressly set out the following objectives of the tax reform on consumption: i) to make the tax system simpler, fairer, more efficient, and more transparent; ii) to employ technical and objective criteria in delimiting the exceptions to the general rule of the Contribution on Goods and Services (called in Brazil as "CBS") and the Tax on Goods and Services (called in Brazil as "IBS"); and iii) to ensure that the features of the CBS (with a projected rate of 8.8%) and the IBS (with a projected rate of 17.7%) correspond to an "international standard" Value-Added Tax ("VAT"), through the mechanism of non-cumulative, by which taxpayers may credit the IBS and CBS paid in prior transactions[19].

The proposed harmonization—including the unification of rules between CBS and IBS, the adoption of reference rates, the allowance of non-cumulative tax credits, and the prioritization of technical rules—is consistent with this global trend toward tax modernization[20].

In this context, with a view to mitigating Brazilian tax litigation, the National Congress also enacted §3 of Article 145 of the Brazilian Federal Constitution, expressly providing that the "*National Tax System must adhere to the principles of simplicity, transparency, and tax justice*."

It is true that such principles had already been implicitly embedded within the Brazilian legal framework; nevertheless, the expectation is that, by means of their

[19]However, the appropriation of tax credits is prohibited in relation to the acquisition of "goods for personal use and consumption" (for instance, jewelry, works of art, alcoholic beverages, tobacco, firearms, sports-related services, except when required for the taxpayer's operations), pursuant to Articles 47 and 57 of Complementary Law No. 214 of 2025.

[20]The non-cumulative nature of the VAT is a fundamental principle designed to prevent tax cascading. Under this system, each business in the production and distribution chain is entitled to deduct, as a credit, the VAT already paid on its inputs from the VAT charged on its outputs. As a result, the tax burden applies only to the "value added" at each stage of the chain, rather than compounding cumulatively throughout the production and distribution process. The objective is that, regardless of how many stages of production and distribution may exist, the VAT is designed to be transferred throughout the chain without burdening any of the intermediate agents. In other words, the actual taxpayer of the IBS and CBS will be the final consumer, who will ultimately bear the effective financial burden of these taxes. This ensures neutrality, efficiency, and fairness in taxation, preventing distortions in prices and investment decisions.

explicit constitutional enshrinement, these principles will acquire greater normative effectiveness.

The premises outlined above pursue two main objectives: first, to reduce the volume of Brazilian tax litigation; and second, to enhance the effectiveness of tax collection. Theoretically, if i) the system for enforcing tax liabilities operates efficiently and ii) tax rules are drafted in a simple and clear manner, disputes between the tax authorities and taxpayers will become less likely, which, as a matter of logic, tends to decrease tax litigation.

Nevertheless, despite representing an important advancement, it is not believed that such measures alone will suffice.

It is deemed essential, first, to define in concrete terms how the Brazilian tax system is to become more "simple," "transparent," and "fair." Subsequently, there must be an explicit provision establishing sanctions against any actor who renders the tax system more complex, opaque, or unjust, regardless of who the responsible party may be (whether the taxpayer[21], the tax authorities[22] or even a member of the judiciary, the Brazilian National Congress or the public administration[23]). The rule, in turn, should be applied universally.

5. Tax War among Federated Entities in Brazil

In today's globalized world, consumption is primarily taxed through the Value-Added Tax ("VAT"), which is levied on the sale and acquisition of goods and services. Consequently, given the intense competitiveness in the productive sector, companies seek to establish themselves in jurisdictions that offer the greatest financial and fiscal advantages.

In Brazil, consumption taxation is characterized by a federalist structure, under which the authority to levy taxes on consumption is shared among three levels of government: the Union, the States, and the Municipalities. The Union is responsible for the Tax on Industrialized Products (called in Brazil "IPI"), the States impose the Tax on the Circulation of Goods and Services (called in Brazil "ICMS"), and the Municipalities collect the Tax on Services of Any Kind (called in Brazil "ISSQN"). Although this division of competencies is expressly provided for in the Constitution, it has generated a range of problems and challenges.

In Brazil, 26 States and the Federal District possess the authority to legislate, establish, and collect the Tax on the Circulation of Goods and Services. In addition, more than 5000 municipalities hold the power to create and levy the Tax on Services of Any Kind. This framework creates a competitive environment among federative entities, as each seeks to attract investment through the granting of tax incentives, a practice that may produce distortions within the tax system.

[21]For example, sanctions could include fines, exclusion from simplified regimes, or temporary suspension of tax benefits.

[22]For example, sanctions could involve disciplinary proceedings, suspension, or in severe cases, dismissal from public office.

[23]For example, sanctions could involve fiscal responsibility audits and, depending on the legal case, disciplinary and financial penalties may be applied.

Indeed, this fragmentation of tax competence generates significant distortions in the national tax system. The fact that 26 States and the Federal District are empowered to establish the "ICMS"—a tax with an inherently national scope—creates a peculiar situation: although the levy is of national reach, it falls under state jurisdiction. This highlights the complexities and challenges of a tax system in which multiple federative entities act autonomously, yet without centralized coordination.

The Tax on the Circulation of Goods and Services (within the legislative competence of the States) constitutes an inexhaustible source of problems and an extraordinary degree of complexity. It is a consumption tax designed to operate on a non-cumulative basis. The implementation of non-cumulativity essentially follows two models: the financial credit model and the physical credit model.

Under the financial credit model, every acquisition made by a company that serves its business purposes—whether related to fixed assets, goods for use and consumption, raw materials, or intermediate products—grants the right to input tax credits. By contrast, under the physical credit model, only goods that are incorporated into the final product or those purchased for resale generate credit entitlement. Evidently, the adoption of the physical credit model renders the tax calculation process considerably more complex (Moreira, 2023).

What, then, is the problem with a tax of national scope falling under the jurisdiction of the States? The difficulty lies in the fact that a citizen purchasing goods in "State B" may, in practice, be financing "State A", which produced the goods through illegitimate tax incentives.

The explanation is as follows: because the Tax on the Circulation of Goods and Services is levied at the origin, goods leaving "State A" for "State B" are accompanied by a credit corresponding to the tax supposedly paid in the state of origin ("State A"). Consequently, when these goods are consumed in "State B", they generate less tax revenue for the state of consumption, owing to tax credits that were, in truth, never effectively paid (Maneira, 2019).

In this scenario, it is not uncommon for State B to disregard the tax benefit illegitimately granted by State A and to demand from the taxpayer the full amount of the tax due, thereby giving rise to tax litigation.

Tax competition arises when states grant tax exemptions and fiscal benefits to attract companies to their territories without the necessary approval of the National Council for Fiscal Policy, thereby generating unfair competition among them. To solve this problem, the reform proposes the harmonization of the taxation of the Tax on the Circulation of Goods and Services and Tax on Services of Any Kind across states, municipalities, and the Federal District through a shared-competence tax known as the Tax on Goods and Services.

According to the newly introduced Article 156-A of the Brazilian Constitution, the Tax on Goods and Services shall be guided by the principle of neutrality and must be governed by "*a single and uniform legislation throughout the national territory*."

The neutrality of VAT has been the subject of a series of recent OECD reports

(OECD, 2017), which have issued the following specific guidelines on the matter: i) value-added taxes should not be borne by legal taxpayers, except where the legislation expressly so provides; ii) taxpayers in comparable situations, engaging in similar transactions, should be subject to similar levels of taxation regardless of their location within a given country; and iii) VAT rules should not primarily influence business decisions.

These OECD guidelines on VAT neutrality directly resonate with the design of Brazil's dual VAT system, composed of the Contribution on Goods and Services (CBS) and the Tax on Goods and Services (IBS). Both taxes have been structured to follow the international standard of being non-cumulative, ensuring that taxpayers can credit input taxes at each stage of the supply chain. In this sense, the Brazilian reform aligns itself with the OECD International VAT/GST Guidelines, seeking to ensure that taxation does not distort business decisions and that taxpayers in comparable situations are treated consistently.

Furthermore, the IBS will be collected at the destination, that is, in the state where the goods or services are consumed, rather than in the state of origin. Consequently, states will no longer have an incentive to grant tax benefits in order to attract companies, since revenue will accrue to the jurisdiction where the products or services are actually used. This, at least in theory, will eliminate the practice of tax competition among the states.

This change makes the tax system fairer, as states with a higher concentration of consumers but lower levels of industrialization will receive a more proportional share of tax revenue. Moreover, the allocation of resources becomes more efficient, since business decisions will cease to be influenced by regional tax incentives and will instead be based on economic and market criteria.

In 2016, India introduced into its tax legislation a "dual VAT" system—the Goods and Services Tax (GST)—similar to the one established by Constitutional Amendment No. 132/23 in Brazil. Following its implementation, India experienced significant positive social and economic impacts, making it possible to affirm that the subsequent growth of its GDP was directly linked to the introduction of the dual VAT. In this context, the following outcomes were observed: i) a reduction in administrative and tax compliance costs; ii) an increase in the taxation of services, particularly within the digital economy; iii) a reduction in overlapping tax incidences; and iv) a reduction in tax incentives (Bal, 2016).

Nonetheless, several renowned Brazilian jurists[24] consider the tax reform unconstitutional. The principal argument against the national VAT is that the new tax would infringe on the federal principle by restricting the taxing powers of the states and municipalities. With due respect to this understanding, I submit that it does not adequately capture the issue. For the purposes of federalism, what mat-

[24]For example, one may cite Professors Roque Antonio Carrazza, Hamilton Dias de Souza, Humberto Ávila, and Ives Gandra da Silva Martins, as referenced in an article published in the newspaper Estadão: https://www.estadao.com.br/politica/blog-do-fausto-macedo/a-questao-federativa-nos-plps-68-e-108/?srsltid=AfmBOop_W6fs_Z9HsnLYH_B421kMSzZxOPlsdtecOEhzkUrNh4iSuinu.

ters most is that the federated entities possess financial autonomy, not necessarily broad taxing competence.

The concentration of legislative and taxing authority within the IBS Managing Committee does not, *a priori*, entail a violation of federalism. In Brazil, far too much attention has historically been paid to the power to create taxes, while the equally crucial matter of revenue sharing has received insufficient focus. The federal pact presupposes financial autonomy.

There is no question that Germany is a federal state composed of the Federation and 16 Länder. In Germany, the Länder (equivalent to the states in Brazil) are allocated the revenue from certain taxes, but not the legislative competence over them, which remains with the central legislature. In other words, although subnational entities cannot increase the taxes levied within their own territories, they possess financial autonomy to ensure the regular exercise of their functions.

Germany, therefore, presents a much more simplified structure: taxing competence—that is, the power to establish taxes—is concentrated in the Federation, accompanied by the allocation of administrative responsibilities and revenue sharing, aimed, among other objectives, at maintaining federal equilibrium (Maneira & Lima, 2019).

Again, by contrast, in Brazil, much emphasis is placed on the competence to create and increase taxes, while too little attention is devoted to the crucial issue of revenue distribution.

Thus, with the implementation of the tax reform on consumption, there is hope that the longstanding problem of tax competition among the federated entities may finally be resolved.

6. Conclusion

In international tax law, it is considered highly desirable that taxes be raised (revenue yield) in a way that treats individuals fairly (equity), minimizes interference in economic decisions (efficiency), and does not impose undue costs on taxpayers or tax administrators (simplicity) (Alm, 1996).

The tax reform on consumption in Brazil aims to introduce a new value-added taxation system through the levying of two taxes (CBS and IBS), both of which adopt a broad non-cumulative regime, with uniform application across the entire Brazilian territory, allowing for the fewest possible tax incentives, and concentrating all taxation in the place of destination. This new framework is expected to simplify the national tax system, reduce tax litigation, and eliminate the so-called "fiscal war".

However, whether tax reform in Brazil will be a success or a complete catastrophe, only time will tell.

Beyond its domestic relevance, the Brazilian reform may also serve as an international case study for federative systems grappling with the tension between fiscal autonomy and the need for harmonized consumption taxation. Other federations could face similar dilemmas, and Brazil's innovative dual VAT model pro-

vides valuable insights for comparative tax law.

By attempting to reconcile the imperatives of federalism with the efficiency and neutrality of a value-added tax, Brazil contributes not only to the modernization of its own tax system but also to the broader global discourse on the design of consumption taxes in complex federative structures. In this sense, the reform represents not merely a national endeavor but also a comparative case study of international relevance.

Ariano Suassuna, a renowned Brazilian writer and philosopher, often described himself as a "hopeful realist"[25], a perspective that also informs the outlook of this article. In his view, optimists are naive. Pessimists are bitter and boring. The writer called himself a hopeful realist, a man of hope. It is in the same way that I also see the tax reform on consumption in Brazil, being a hopeful realist, aware of the weaknesses of this new system, but with the hope that we will have better days in tax law.

This is definitely not the best tax reform on consumption in Brazil, but it was the possible tax reform, given the political, economic, and legal circumstances.

Conflicts of Interest

The author declares no conflicts of interest regarding the publication of this paper.

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[25]The way the writer approached the world was analyzed through the immersive exhibition about his life, held in the city of Recife, State of Pernambuco, in December 2024. Link below with more information: https://arianosuassunaimersivo.com.br/.

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