

MODERNIZING INDIRECT TAXATION TO ENSURE BRAZIL'S COMPETITIVENESS

- *The current tax system generates many distortions. Cumulative taxation, taxes on exports and investments and high complexity are the most serious problems of Brazil's indirect taxation system.*
- *Modernizing the current indirect taxation system by aligning it more closely with global standards is the way to ensure Brazil's competitiveness.*
- *The challenge lies in choosing the right strategy to promote necessary changes for taxation not to constitute an obstacle to Brazil's development any longer.*

Tax on goods and services in Brazil is one of the main constraints on the competitiveness of companies, on international inclusion, on investments and on economic growth. The current system generates a set of distortions and, therefore, requires urgent changes.

Cumulative taxation, taxes on exports and investments and the high complexity of the tax system, which increases compliance costs and legal disputes between the tax authority and taxpayers, are the most serious problems of Brazil's indirect taxation system.

The first three problems are mainly due to inefficiencies in the debit-credit system, such as delays in refunding tax credit balances and the tax credit concept, which restricts tax credit only on taxes paid on acquisitions used directly in the manufacturing process and for resale.

The complexity arises from the existence of several taxes levied on the same tax base - in this case, the circulation of goods and services. The list is long: Tax on the Circulation of Goods and Services (ICMS), contributions to the Social Integration Program (PIS) and the Public Service Employee Savings Program (PASEP), Social Security Financing Contribution (COFINS), Tax on Industrialized Products (IPI), Tax on Services (ISS),

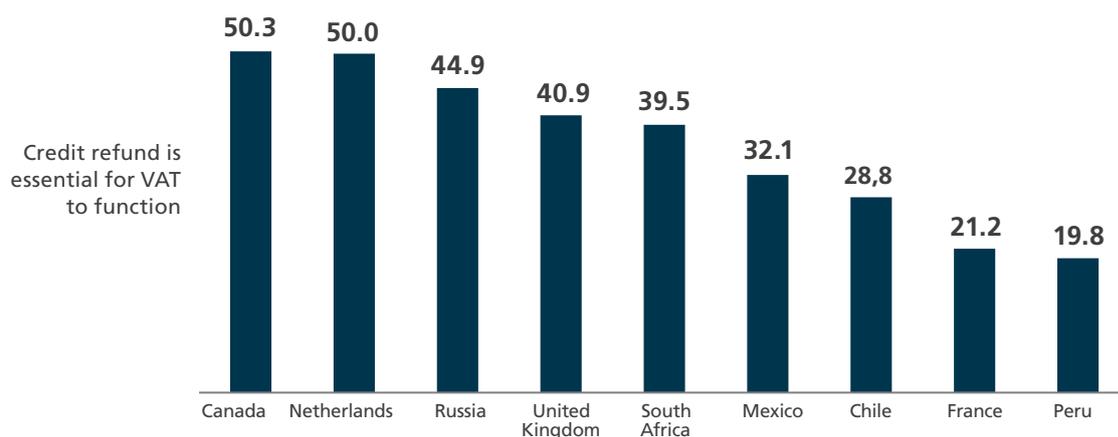
and Contribution for Intervention on the Economic Domain - Fuels (CIDE-Combustíveis).

In addition to being levied on the same tax base, these taxes are often levied on themselves and other taxes (tax on tax). Other elements found in indirect taxation add complexity to the system, such as doubts about the type of acquisition that gives right to tax credit, as a result of the application of the tax credit concept.

Having an efficient tax system is essential to a country's economic prosperity. The ideal tax policy is one that preserves market balance and competition, which is a prerequisite for establishing a competitive and attractive business environment, in order to allow the country to optimize the use of its skills and vocations.

In Brazil there are some possible paths for overcoming tax challenges and making our system more efficient. The most pragmatic path is based on correcting the distortions of the current system, such as adopting the broad tax credit concept without the need for a general reformulation. The disruptive path, in turn, requires a broad reform through which new foundations for the tax system are built by adopting, for example, new taxes to replace existing ones.

AMOUNT OF CREDIT REFUNDS AS A PERCENTAGE OF TOTAL VAT COLLECTION (%)



Source: FMI.
Note: Average 1998 - 2001.



Problems and solutions have been identified.

The challenge lies in choosing the right strategy to promote necessary changes for taxation not to constitute an obstacle to Brazil's development any longer.

Main recommendations

1 The concept of broad right to credit in federal and state-level indirect taxes should be adopted.

2 Taxation at the destination should be established in state indirect taxes.

3 The possibilities of federal and state tax credits compensation should be expanded.

4 The agile refund of credit balances should be guaranteed.

5 Investments should be tax exempt.

6 The amount of taxes payable should be assessed without including the tax on its own tax base.

7 The Tax on Services (ISS) should be incorporated into the state-level tax on the circulation of goods and services (ICMS).

8 The use of tax substitution system should be limited.

9 Excise tax on certain consumption should be adopted.

10 Centralized tax collection by company should be adopted in the ICMS.

11 ICMS legislation should be harmonized.

12 Payment periods for collection of federal and state indirect taxes should be increased.

13 Tax compliance should be reduced and simplified.



The full version of the document can be accessed through the QR code on the side or at: <http://www.cni.com.br/eleicoes2018/downloads/> This summary is part of the series Proposals of Industry for the 2018 Elections comprising 43 documents. The series, which is based on the *2018-2022 Strategy Map for Industry* is a CNI contribution to the new federal administration and presents analyses and proposals of priorities to increase Brazil's competitiveness. Any part of this publication may be copied, provided that the source is acknowledged. Brasília-DF, July 2018.

