

Progressive VAT in Practice: Designing Brazil's Cashback Mechanism and the Key Policy Lessons

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Key Topics Covered

- Overview of Brazil's VAT Reform
- Progressive VAT in Practice: Cashback Design
- Expected Economic and Social Impacts

VAT Reform: Overview

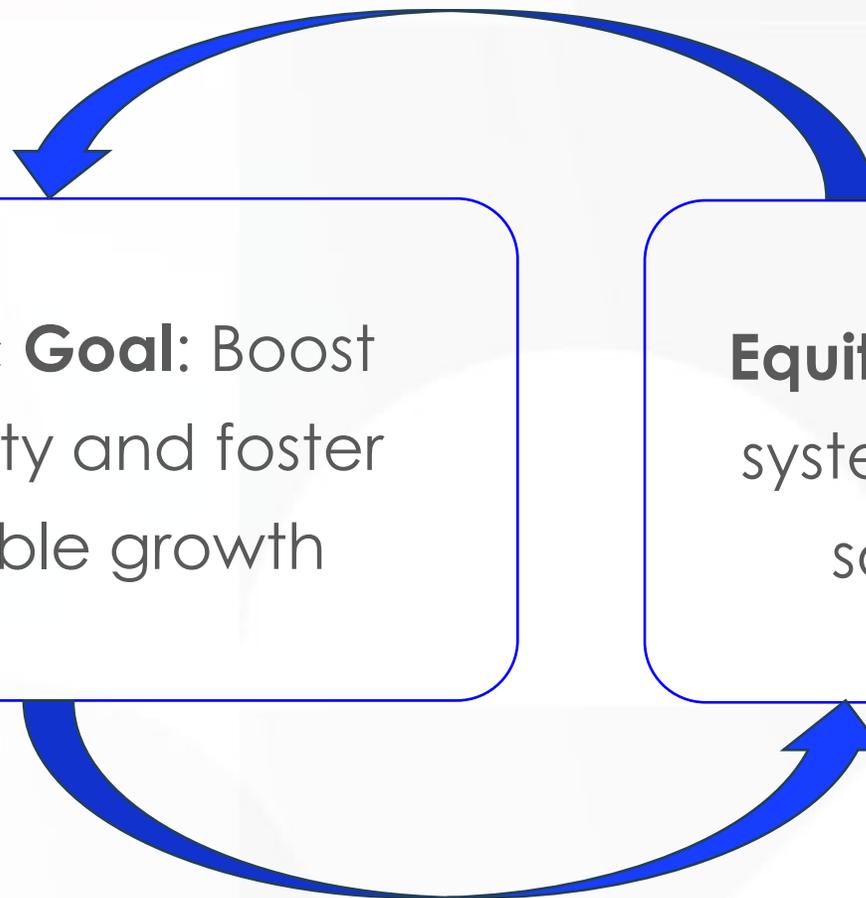
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Main objectives

Economic Goal: Boost productivity and foster sustainable growth

Equity Goal: Make the tax system fairer by reducing social and regional inequalities



VAT Reform | Overview

TODAY

Narrow tax base
(due to exemptions, reduced rates,
and special regimes)



Benefits
disproportionately
concentrated among
higher-income
households

AFTER VAT REFORM

Broader tax
base



Cashback
mechanism



Expanded benefits
for low-income
households

VAT Reform | Overview

Replacing inefficient and regressive taxes through a revenue-neutral reform.

Two-pillar system aligned with best practices:

- 1) Dual Modern VAT:** Broad base, full input crediting, destination-based, limited exceptions
- 2) Excise Tax:** Levied on goods and services harmful to health or the environment

TODAY

PIS

Cofins

IOF-
Insurance

IPI

ICMS

ISS

AFTER THE REFORM

Dual VAT

CBS
FEDERAL VAT

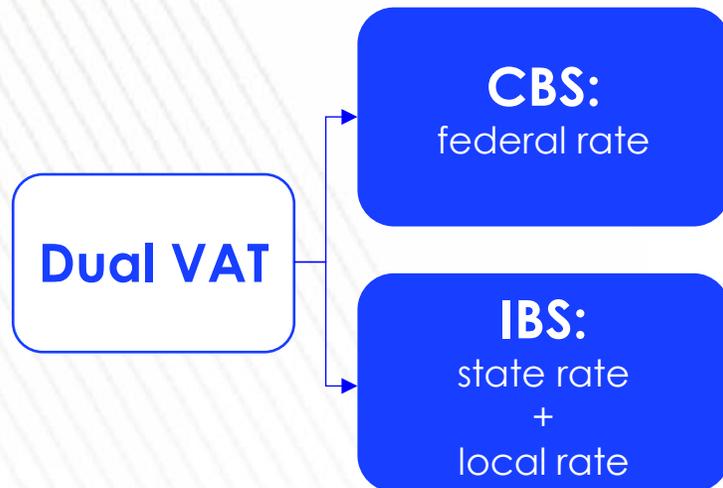
IBS
SUBNATIONAL VAT

Excise Tax



VAT Reform | Overview

AFTER THE REFORM



CBS and IBS will share the features of a modern VAT:

- **Harmonized broad base:** goods and services, tangible or intangible
- **Single national legislation:** special regimes, rules for compensation and refund of tax credits etc.
- **Unified taxpayer interface** operating “as a single tax administration”: integration between the Federal Revenue Office and the IBS Steering Committee (shared governance)
- **Technology-driven operational system:** electronic invoice, pre-filled tax returns, **cashback**, split payment etc.
- Uniform rule for setting the standard rate during the transition: reference rates will be established at levels necessary to ensure revenue neutrality

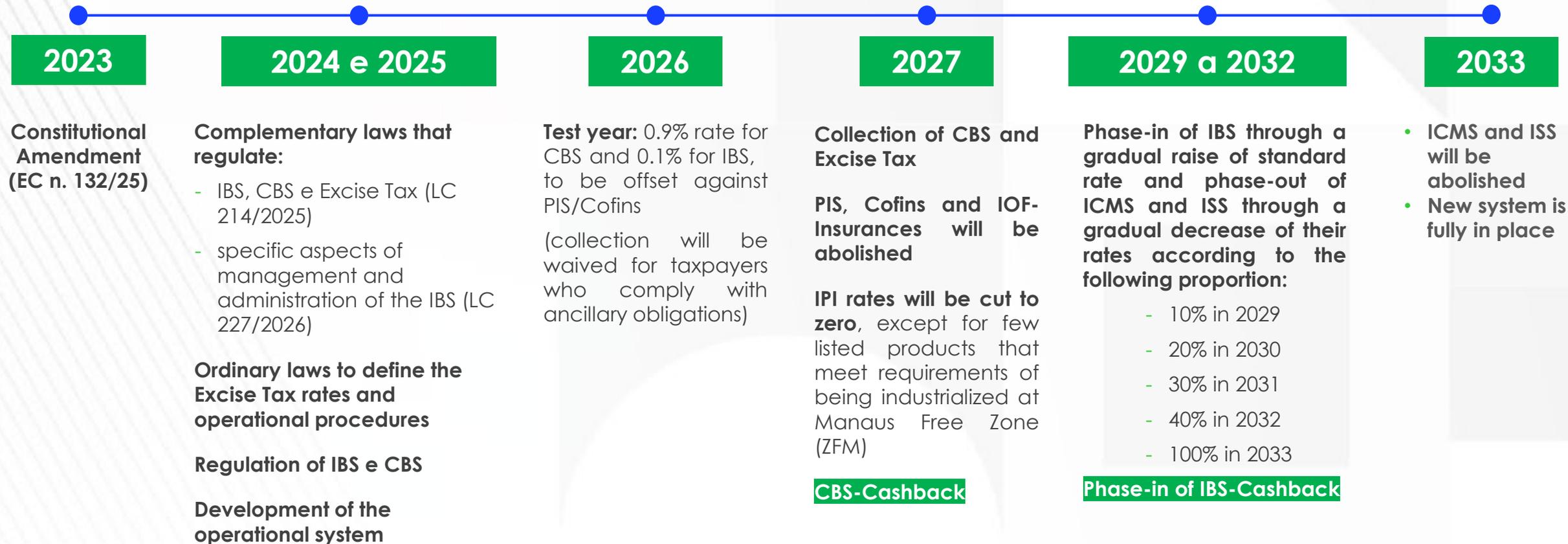
Exception: each federative entity retains **autonomy** to set its own **standard VAT rate and cashback refund rate** (specific law).

Brazil’s unique approach: modern VAT through cooperative federalism –

a shared tax base with autonomy for federative entities to set their own standard rates

VAT Reform | Overview

Implementation Timeline



Federative Transition: a 50-year period for State and Municipal public finances, featuring a gradual phase-out of compensation mechanisms



VAT Reform: Cashback

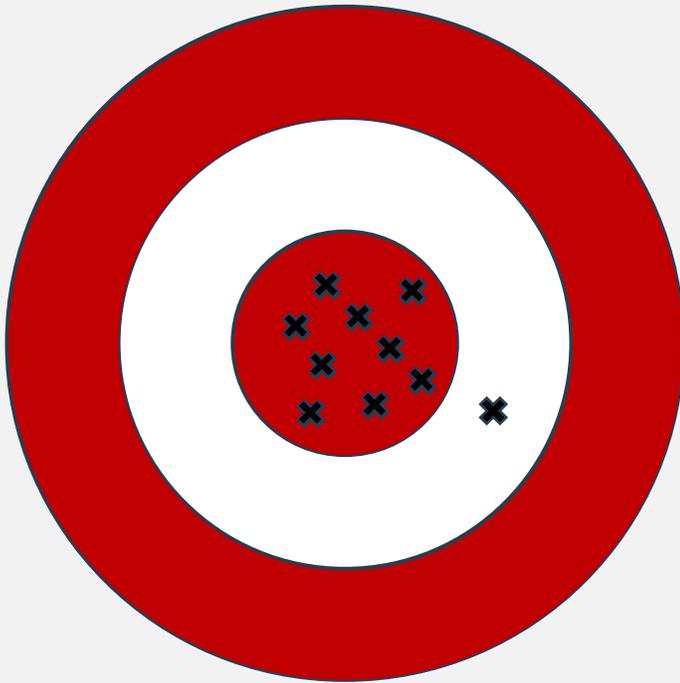
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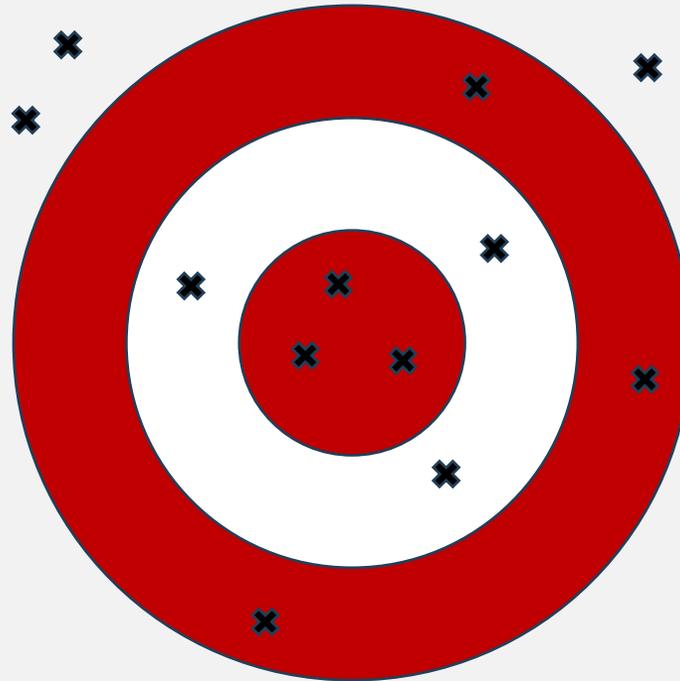
Rationale for Personalized Refunds for Low-Income Households (Cashback)

How to address the inherent regressivity of VAT?

Targeted refund:
Cashback

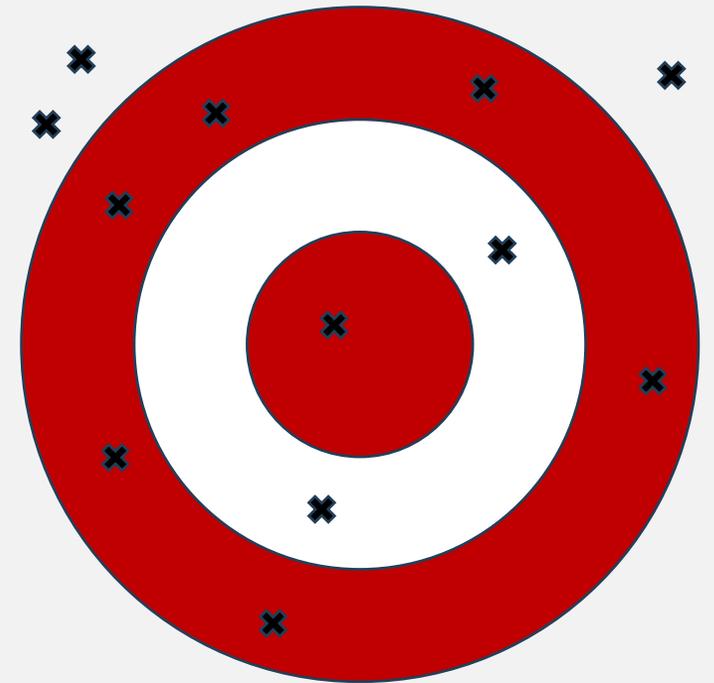


Traditional approach:
best-case scenario



Base exclusions for basic-needs goods

Traditional approach:
realistic scenario



Rationale for Personalized Refunds for Low-Income Households (**Cashback**)

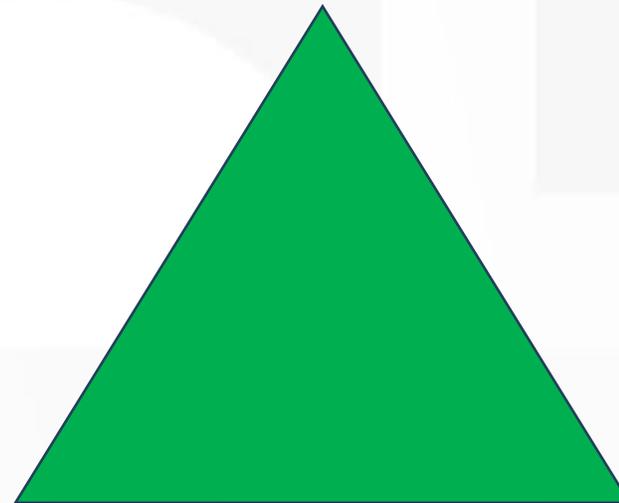
How to address the regressivity while preserving the core design of the Modern VAT?

Traditional approach: universal solution through base exclusions (exemptions and zero/reduced rates) ranging from low progressivity gains (best case scenario) to the opposite effect of increasing regressivity, and harmful to efficiency.

**Impossible
Trinity**

Address regressivity

Broad base



Single/limited rate

Rationale for Personalized Refund for Low-Income households (**Cashback**)

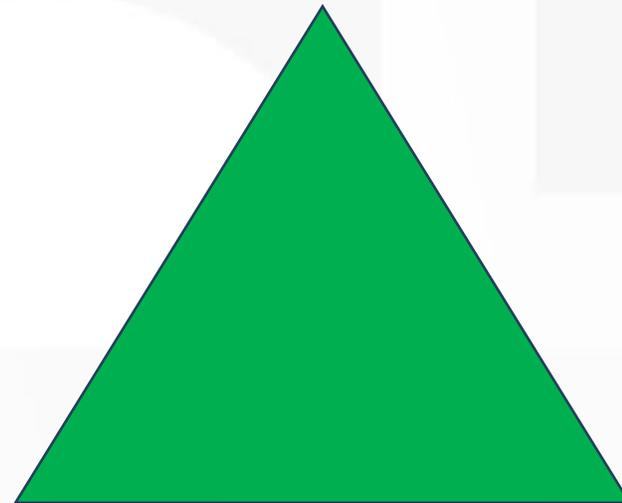
How to address the regressivity while preserving the core design of the Modern VAT?

Modern approach: external solutions to compensate the VAT (targeted transfers or progressive taxes), which often face political-economy constraints.

**Impossible
Trinity**

Address regressivity ☒

Broad base ☑



Single/limited rate ☑

Rationale for Personalized Refund for Low-Income households (**Cashback**)

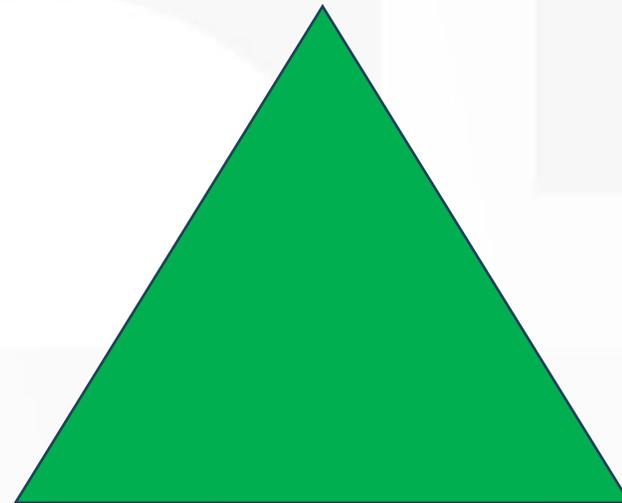
How to address the regressivity while preserving the core design of the Modern VAT?

New approach: Cashback (IVA-P) as a more effective internal solution compatible with the backbone of a Modern VAT – **achieving both equity and efficiency.**

**Solving the
Impossible
Trinity
(Barreix et al., 2011)**

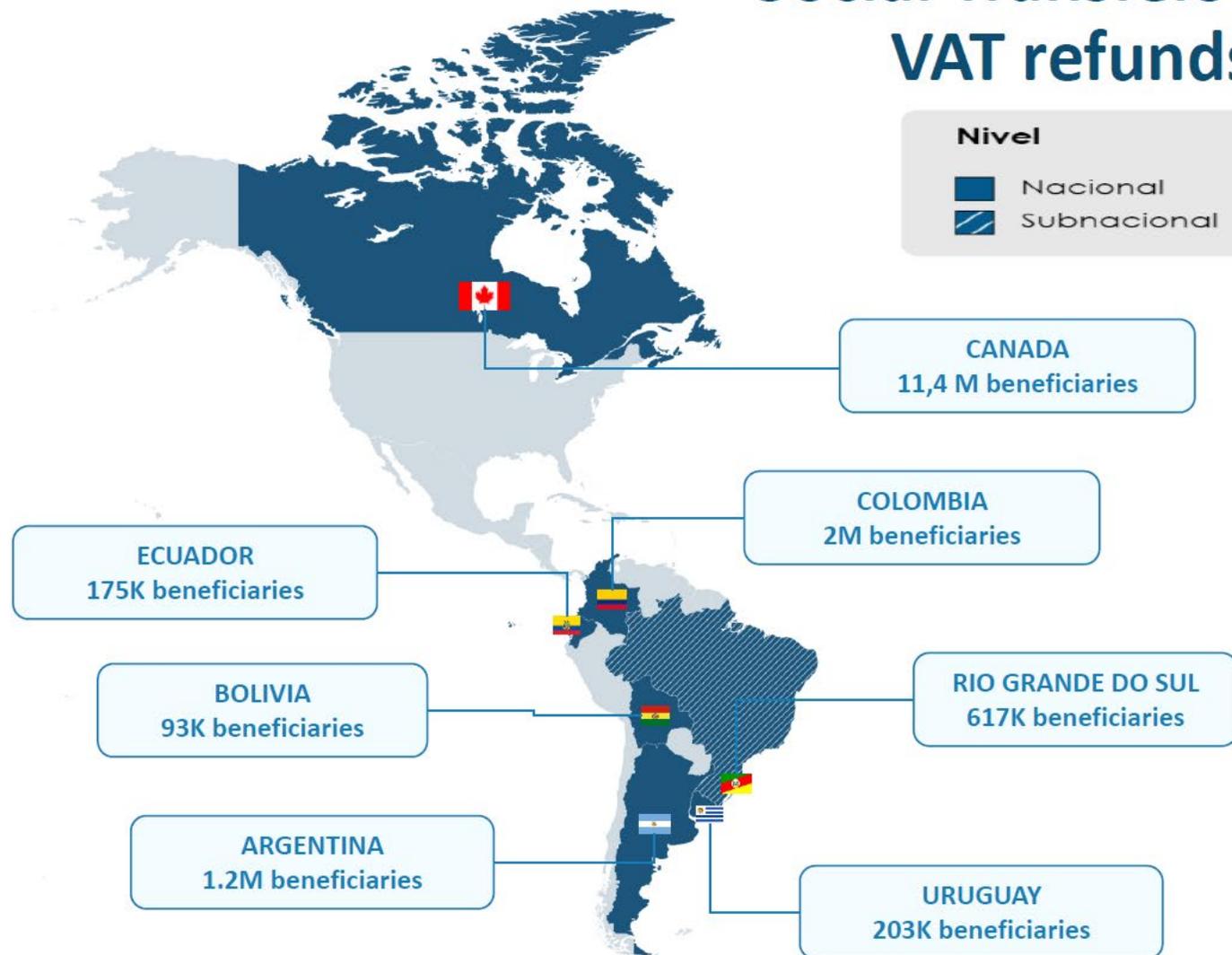
Address regressivity

Broad base



Single/limited rate

Social Transfers considering VAT refunds in LAC



Pioneering experiences in LAC

	Colombia 	Ecuador 	Rio Grande do Sul - Brazil 
Type of program	Compensation: Fixed amount (presumptive)	Refund: variable amount based on invoices issued with ID.	Hybrid approach: Fixed amount + Variable amount based on invoices issued with ID
Beneficiary	Low income households and older adults (beneficiaries of social programs)	Older adults (aged 65 and above) and individuals with disabilities.	Low income households (CadÚnico)
Eligible purchases	-	Basic goods and essential services	Goods and telecommunications, transportation, and electricity services
Amount of the benefit	US\$ 17.5 every two months	up to 100% of VAT paid, with a US\$ 145 monthly limit	Greater amount between US\$ 18.9 (fixed) or 50% of VAT paid (variable), with a rule to ensure compatibility with household income
Required processes	Amount directly deposited into both transfer programs (<i>Family in Action and Older Colombians</i>)	Upon refund request and now moving to automatic discount at purchase (VAT non-collection modality)	Amount directly deposited into a specific refund account (Devolve ICMS).
Pros	Simplicity	Incentives for formal consumption and its spillovers: promotes fiscal citizenship, tax compliance and formalization	Balance between both pros and cons

Pioneering experiences in LAC

Foundation: Two Major Developments in LAC Over the Past Three Decades:

- **New-generation of Targeted Social Policies.** (Barreix et al., 2011).
- **Technological Modernization of Tax Administration:** Widespread adoption of e-Invoicing and Programs promoting Tax Citizenship (Padilha da Silva, 2017).

Key Enabling Features

- **Robust social registries:** Reliable socioeconomic data on low-income households
- **Inclusive payment instruments:** Mechanisms that effectively reach vulnerable populations.
- **Consumer identification at Point of Sale:** powered by electronic invoicing systems.

Operational Simplicity

1. Electronic invoices capture consumer personal identification at purchase.
2. Invoice data is linked to social registries to identify eligible beneficiaries and calculate refundable tax amounts.
3. Refunds are transferred via payment instruments—potentially in real time in the future.

Operational Simplicity



What is it

It is a tax justice instrument that reduces the burden on low-income households

What it is not

It is not a social transfer, although refunds are delivered directly to households

Source: Giovanni Padilha da Silva, Public Hearing in the House of Representatives, May 2024

Pioneering experiences in LAC



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Pilot Program: Devolve ICMS – Rio Grande do Sul

Emissão	Número	Tipo Doc.	Chave de Acesso	Valor	Data Registro	Tipo Operação	Situação Docto
11/05/24	97912	Nota Fiscal de Consumidor Eletrônica	4324051461375700016565 0150000979121009793019	R\$86,90	30/05/24	Aquisição	Normal
05/05/24	867717	Nota Fiscal de Consumidor Eletrônica	4324059301500600194265 1130008677171880473972	R\$278,52	05/05/24	Aquisição	Normal
03/05/24	1015703	Nota Fiscal de Consumidor Eletrônica	4324059301500600194265 1020010157031731355884	R\$266,77	03/05/24	Aquisição	Normal
30/04/24	294027	Nota Fiscal de Consumidor Eletrônica	4324049301500600194265 1150002940271309106040	R\$195,00	30/04/24	Aquisição	Normal
26/04/24	768718	Nota Fiscal de Consumidor Eletrônica	4324049301500600194265 1040007687181989743296	R\$226,11	26/04/24	Aquisição	Normal
23/04/24	1012591	Nota Fiscal de Consumidor Eletrônica	4324049301500600194265 1020010125911372595704	R\$171,14	23/04/24	Aquisição	Normal
19/04/24	1381768	Nota Fiscal de Consumidor Eletrônica	4324049301500600194265 1030013817681308412104	R\$199,67	19/04/24	Aquisição	Normal
15/04/24	3473475	Nota Fiscal de Consumidor Eletrônica	4324049044770700013365 0060034734759747218127	R\$49,00	15/04/24	Aquisição	Normal
14/04/24	949388	Nota Fiscal de Consumidor Eletrônica	4324049301500600194265 1110009493881820112548	R\$275,53	14/04/24	Aquisição	Normal

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Minhas

Devoluç es por

VAT Reform | Design of the new CBS/IBS Cashback

- **Who is eligible?** Households with monthly income up to ½ MW (CadÚnico) – official criteria for social programs.
- **What is the refund amount?** Broad base of eligible products, either full (100%) or partial refund (≥20%)

Category	CBS	IBS
Utility services (electricity, water, gas and telecommunications)	100%	≥20%
Goods and services harmful to health or environment (Excise Tax)	0%	0%
Other goods and services	≥20%	≥20%

- **Federative entities** retain autonomy to set their refund rates by specific law (within national limits of 20%-100%), which may vary according to household income and among the two categories of eligible products.

VAT Reform | Design of the new CBS/IBS Cashback

General procedure:

- Refunds linked to formal consumption
- Households must request fiscal documents with their personal identification (e-invoice + CPF)
- Refund credited to a specific bank account, following the established payment schedule
- Payment schedule is expected to evolve toward real-time in the future
- Fraud prevention: rule per family/period to ensure compatibility with household income

Simplified procedures:

- **Direct discount** for bills with fixed periodicity (monthly), such as utility services
- **Safeguard clause:** estimated (presumptive) refunds may be used in areas with operational constraints.

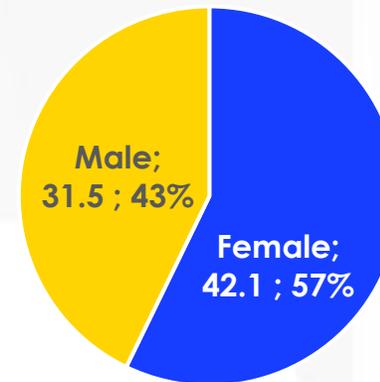
Integrated solution for unified refund of IBS and CBS

VAT Reform | Design of the new CBS/IBS Cashback

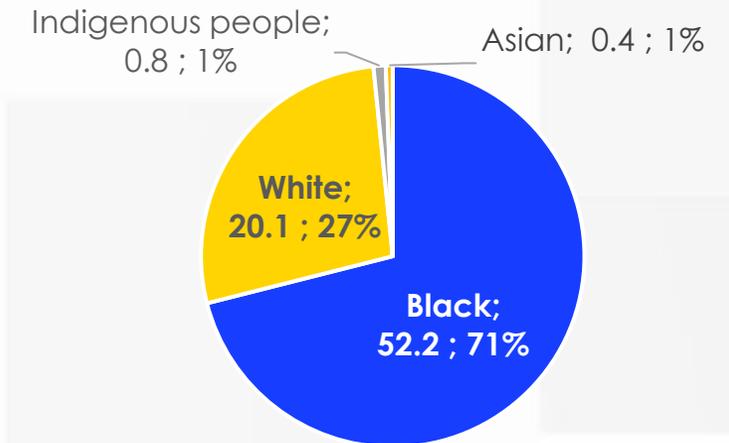
COVERAGE

	People (millions)	Share
Between 0 and 6 y.o.	11.2	55.2%
Between 7 and 17 y.o.	18.6	57.7%
Between 18 and 24 y.o.	8.8	39.9%
Older than 24 y.o.	34.9	24.4%
Total	73.5	33.8%

Gender
(millions) ; (%)



Race/Skin Color
(millions) ; (%)



One-third of the Brazilian population, including more than half of all children in early childhood

71% of the eligible beneficiaries are black and 57% are female

Concluding Remarks

- **Disclaimer:**
 - Brazilian solution: hybrid approach (Cashback + Traditional base exclusions) was necessary for political feasibility – an important first step.
 - Five-Year assessments: periodical mandatory reviews to reinforce the **track towards a Progressive VAT** (ultimate goal).
- **Cashback** in Brazil has the potential to become **one of the world's most ambitious VAT-equity instrument**.
- This represents not only a **major advancement in Brazil's tax structure**, but also a **paradigm shift** in global consumption taxation — setting a benchmark for countries seeking fairer and more efficient tax systems.



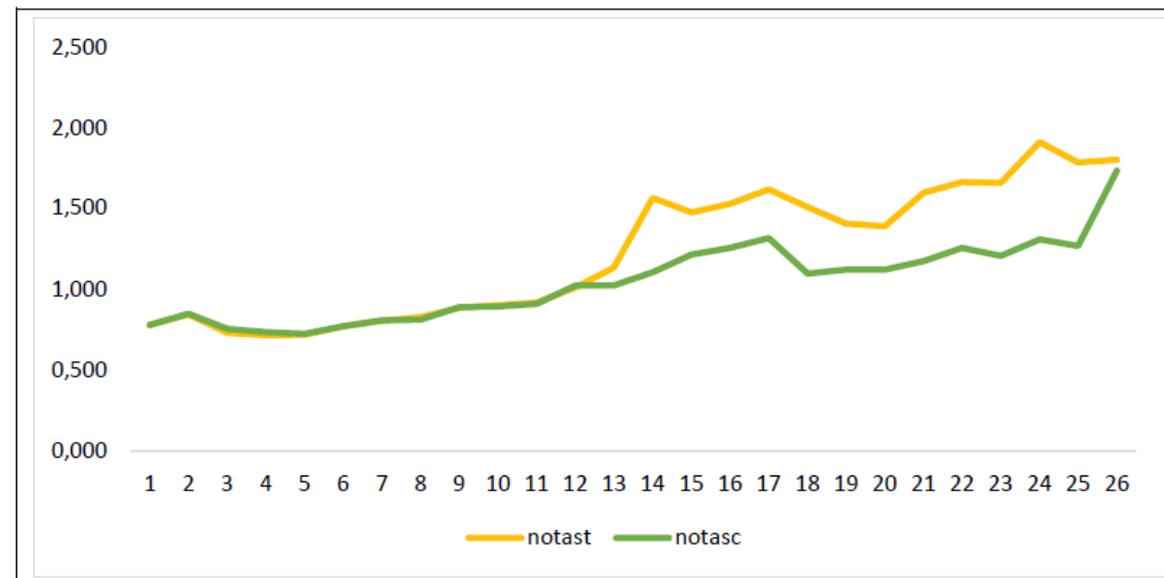
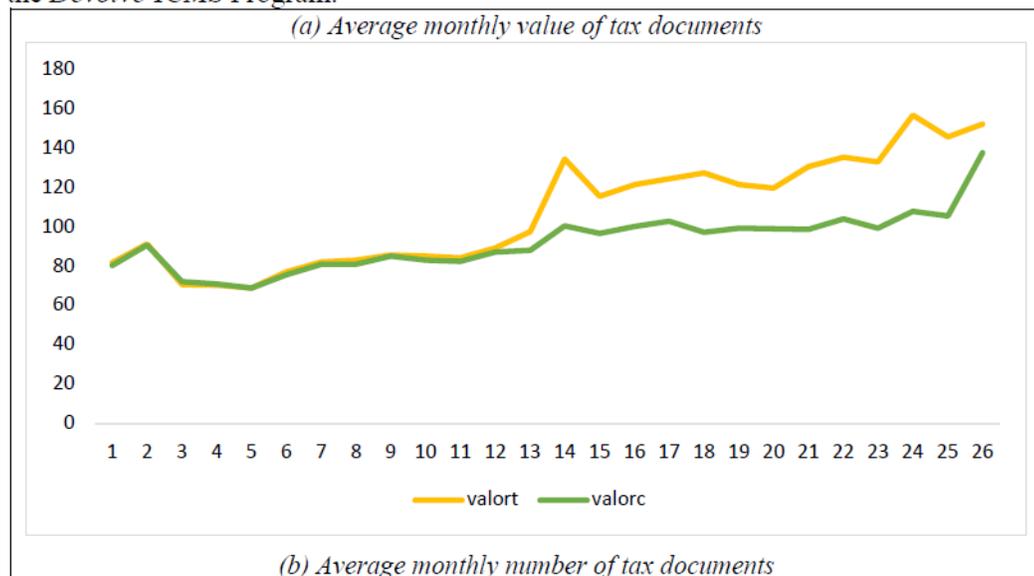
VAT Reform: Expected Economic and Social Impacts

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Effectiveness in reducing informality (DEVOLVE ICMS Program)

Graph 2. The behavior of the treatment and control groups before and after the implementation of the *Devolve-ICMS* Program.



Source: Prepared by the authors.

Notes: valort = monthly value for the treatment group; valorc = monthly value for the control group; notast = monthly number of tax records issued by CPF in the treatment group; and notasc = monthly number of tax records issued by CPF in the control group.

Refund of consumption tax to low-income people: impact assessment using differences in differences

Jorge L. Tonetto, Adelar Fochezatto and Giovanni P. Silva

SimVat tool – World Bank

Fiscalmente neutro: Sim

Alíquota base: ⓘ 28.05%

Alíquota simulada: **25.94%**

Proporção da renda

Proporção do consumo

Proporção das receitas

Progressivity gains:

cashback

+

tax base broadening (despite the hybrid approach)

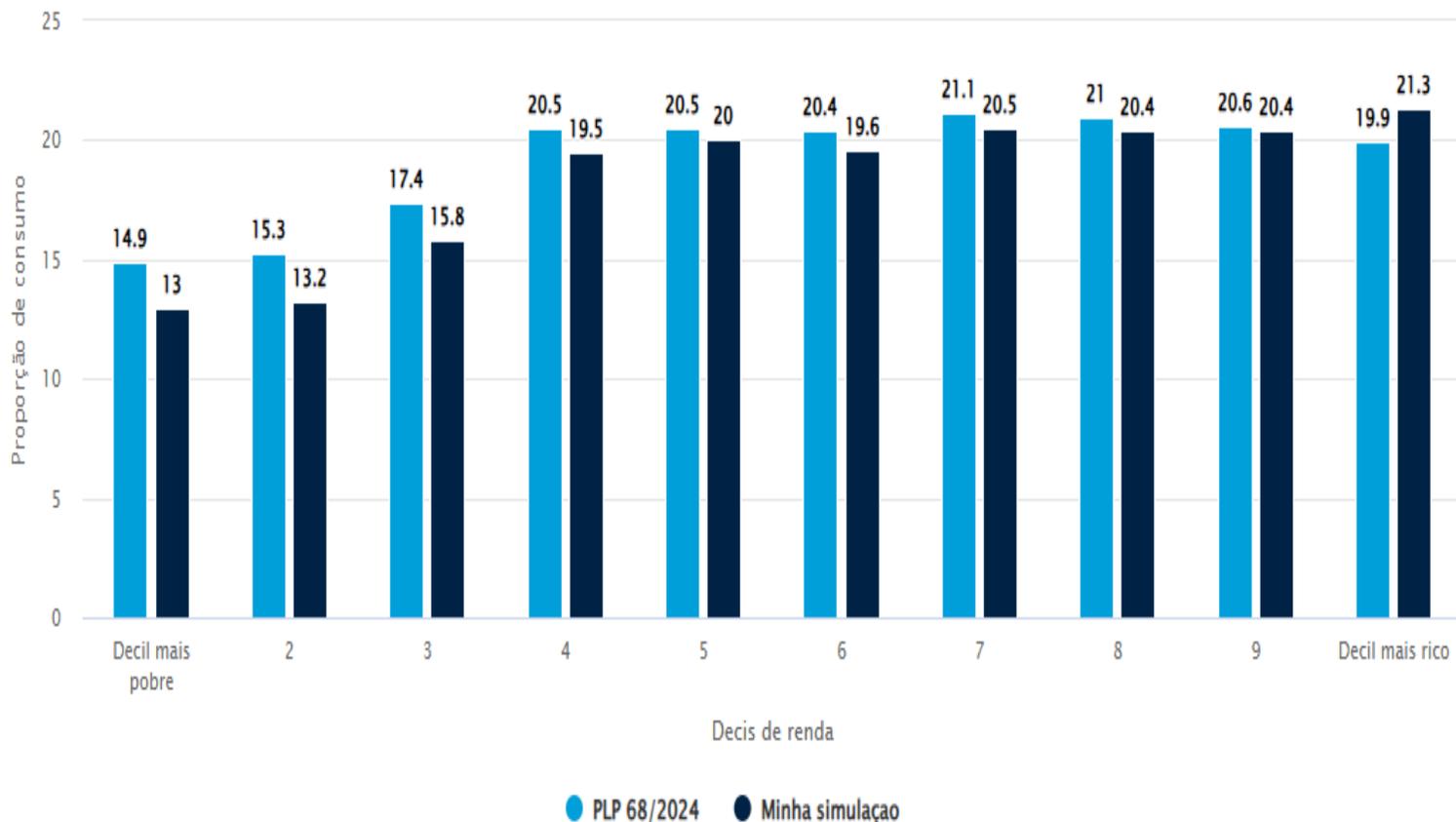
Enhancing redistributive impact:

periodical mandatory reviews (five-year assessments)

World Bank's SimVat tool:

<https://datanalytics.worldbank.org/simvat>

Participação na receita total por decil (%)



VAT Reform | Expected Economic and Social Impacts

Impact of VAT reform on economy

Variables		Conservative	Optimistic
GDP	var. % real	12.0	20.0
Consumption Families	var. % real	12.6	24.2
Investment	var. % real	20.3	25.0
Exports	var. % real	11.7	17.4
Imports	var. % real	9.5	15.6
Labor	var. % real	7.5	12.6

VAT reform is projected to deliver over 12% in additional GDP growth in the medium term

Source: Domingues and Cardoso (2021), based on Borges (2019).
Data corresponds to direct impact in 15 years.

VAT Reform | Expected Economic and Social Impacts

Impact of VAT reform on income

Income bracket	Conservative (A)	Optimistic (B)
0-1 MW	10.2%	17.5%
1-2 MW	10.1%	17.4%
2-3 MW	10.0%	17.4%
3-5 MW	9.8%	17.3%
5-6 MW	9.6%	17.1%
6-8 MW	9.4%	17.0%
8-10 MW	9.3%	16.9%
10-15 MW	9.0%	16.7%
15-20 MW	8.5%	16.2%
20-30 MW	8.4%	16.3%
>30 MW	8.1%	16.1%

Purchasing power increases for families across all income brackets, with the strongest gains among lower-income households

Source: Domingues and Cardoso (2021)

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