ABILITY TO PAY AND INDIRECT TAXES: AN ECONOMIC ANALYSIS OF THE REGRESSION ON BRAZILIAN TAX SYSTEM.

Edson Antônio Sousa Pinto
Professor at Catholic University of Rondônia - Brazil.

ABSTRACT

The Brazilian Constitution establishes that whenever possible, taxes shall have an individual character and shall be graded according to the economic capacity of the taxpayer. It is, in other words, the realization of materially equal treatment to determine that those who have greater wealth and/or ability to pay contribute more than others who are not in the same condition. The principle of ability to pay aims to ensure that the tax amounts due increase according with the growth of the greatness achieved by the tax, so that the greater the capacity, the greater the impact of taxation to be borne by the citizen-taxpayer. In Brazil, however, the indirect tax incidence (e.g. on consumption) harms the assets of the taxpayer, because it reduces their ability to use the product of their income and work, diminishing therefore their consumption basket. This study aims to demonstrate, based on the systematic and economic analysis, that the indirect taxes levied are inversely proportional to income, treating extremely unequal social classes, since its impact worsens as the ability to pay decreases characterizing a regressive tax system.

KEYWORDS: TAX SYSTEM, INDIRECT TAXES, PROGRESSIVE TAXES, REGRESSIVE TAXES.

I. INTRODUCTION: ABILITY TO PAY IN BRAZIL

Taxation is the primary way to finance state activities; it's, therefore, by definition, the materialization of the burden to fund state structure of all that live in a organized society, with powers and established Institutions. That is, as the famous phrase of The Supreme Court Justice Oliver Wendell Holmes Jr. placed in the entrance of Internal Revenue Service (IRS): “Taxes are what we pay for a civilized society”.

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1 That inscription is in the IRS headquarters, situated at the address: 1111 Constitution Avenue Northwest, Washington, DC, USA.
The taxing power of the state, and the corresponding duty to pay taxes by the citizen-taxpayers, define not only the economic and financial structure of society, but also its political structure, and delimit the subject criteria for the constitutional powers established, determining the protection of taxpayers against this power and duty of the State.

All citizens assume, then, the obligation to pay the State, but not as a protection to the State as a collective goal, but in defense of their own freedom, so that the tax function in the State of the XXI century is to ensure the funding of basic state activities, but to justify the incidence of tax exactions without damaging the exercise of freedom and citizenship by taxpayers-citizens who come to take on tasks before exclusive of public officials and agencies.

From this premise, it is then defined that the tax, in its primary effect, means the removal of portion of the individual wealth, transferring it to the State so that this funds essential activities while living in society.²

But all taxpayers can and must contribute equally to state funding?

The Brazilian Constitution states in Paragraph 1 of Article 145: "Whenever possible, taxes shall have an individual character and shall be graded according to the economic capacity of the taxpayer, provided the tax administration, particularly to give effect to these objectives, identify, respected individual rights and under the law, estate, income and economic activities of the taxpayer."

In other words, it means the implementation of materially equal treatment to determine that those who have greater wealth and/or possibility to pay, contribute more than others who are not in the same condition.

Such constitutional dictum called the ability to pay principle, which ensures that the amounts due to pay the tax rise in line with the growth of the greatness achieved by the tax³, so that the greater capacity (e.g. income,

assets and other), the greater the incidence of taxation to be endured by the citizen-taxpayer. 

So the Brazilian Constitution determines materially a taxation limit, a protective strip of minimum conditions necessary for the taxpayer to avoid that fundamental rights are violated by the Taxing Power of the State.

Thus, the ability to pay becomes a different treatment criteria among those who are not in a similar situation, considering, therefore, an analysis of the factual situation of taxpayers, guaranteeing therefore an approximation to equity in taxation, therefore, will not only take into account the condition of citizen-taxpayers, but also their economic ability to pay for the State funding.

Accentuates this sense Sevillano Sandra Chavez:

“Thus, the ability to pay is the basic rule, although it may not be the only one in the division or distribution of the tax burden among all those who are called to finance the state. To the extent that the payment of taxes will be in connection with the economic capability of individuals, tax equality is to treat equally those with similar ability to pay and unequally those with different capacity to contribute.”

This principle derives from the republican structure of the Brazilian State and, consequently, of the values that emanate from it, among which stands out equality.

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4 Similarly it's worth mentioning the concepts of German tax doctrine that describes this principle (Leistungsfähigkeitsprinzip) as the duty to pay taxes in accordance with the size of their income, and provided that such imposition reaches a greater magnitude than the minimum existential (Existenzminimum) of the taxpayer, and that such amount need not be used for urgent private needs. (TIPKE, Klaus. Besteuerungsmoral und Steuermoral. Wiesbaden/Alemanha: Westdeutscher Verlag, 2000. p. 18).


Equality in a republican system is an intrinsic presuppose to guarantee State’s own structure, in such a way that it can be said that without equality there is no Republic.\(^8\)

After all, in a Republican State there are no differences or privileges among citizens because, in the words of the Brazilian Constitution, "all are equal before the law" (article 5, caput), and this is the basic postulate of the creation of the republican regime.

That is the teaching of Geraldo Ataliba.\(^9\)

"Isonomy needs to express in all State manifestations, which, mostly translate concretely in acts of law enforcement, or its unfolding. No act or form of expression of the state can escape or evade the requirements of equality. (...) Isonomy imposes on the rights system facing the opportunities that the state offers, either to the enjoyment of public services, either in the use of their assets, whether in relation to the police power, or other administrative events, or costs that the State may require of citizens - such as the power to expropriate, to demand etc. - Either in relation to tax events, disciplinary or others. "\(^{10}\)

Thereupon, it is stated categorically that the constitutional structure of ability to pay is rooted, in this sense, on a higher principle, which is the principle of equality, because, in the words of Marcelo Martins (2011, p 193.), "It's understood to be necessary, based on the higher principle of equality, that the welfare loss is, if not identical, at least equivalent between the various groups obliged in a given society."

It is worth noting the distinction between equality before the law (formal) and equality in law (material), for the realization of ability to pay orders not just a uniform application of the law\(^{11}\), but also the compliance with the economic differences of each citizen-taxpayer in the task to fund the State activity. Therefore, to consider only formal equality does not fulfill all normative content

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\(^{10}\) According to Roque Carrazza: “The principle of ability to pay hosts up in the folds of the principle of equality and helps to realize in the tax field republican ideals. (...) Who has more wealth should, in proportional terms, pay more tax than those who have less wealth. In other words, should contribute more to the maintenance of public affairs." (Free translation from: Curso de Direito Constitucional Tributário, 23° Ed., São Paulo: Malheiros Editores, 2007. p. 87).

of the constitutional principle of equality, after all, in the words of Hans Kelsen\textsuperscript{12} equality before the law is not equality, but a mere application of the rule (Gleichheit vor dem Gesetz ist somit gar nicht Gleichheit, sondern Normgemäßheit), and thus it must be sought an equality de facto, as material equality, as Norberto Bobbio says:

“of the principle of equality before the law and that equality of opportunity it's distinguished the requirement or the ideal of real or substantive equality or, as we read in the Italian Constitution, ‘de facto’. What generally mean by ‘de facto equality’ is very clear: it means equality in respect to material goods, or economic equality”\textsuperscript{13}

Equality is a constitutional postulate with values that spreads throughout the tax system, to ensure that the contribution to the State is proportional, and guarantee to the taxpayers the same sacrifice, proportionally measured.\textsuperscript{14}

However, the tax equality will not be achieved in a tax system in which the legal structure of taxes is fixed or proportional only to the tax base, object of the taxation.

It is necessary that the tax base be the object of a progressive and variable taxation according to its amount, that is, the tax burden should be proportional not only numerical but also materially, under penalty of not respecting the tax equality described in the Brazilian Constitution.

Therefore, the national tax system brings in Article 153, Paragraph 2, Section I of the Federal Constitution, progressivity as a technical (or subprinciple)\textsuperscript{15} of taxation that determines the application of increasing rates in

\textsuperscript{12} KELSEN, Hans. Reine Rechtslehre. 2\textsuperscript{a} Auflage. Wien/Austria: Franz Deuticke, 1960. p. 396/397.
\textsuperscript{14} We are not here to argue that everyone should have the same amount of money. But all should be taxed proportionally according to the greatness of its equity, ensuring all the vital minimum (bare minimum). We agree with Harry Frankfurt: “Economic equality is not, as such, of any particular moral importance; and by the same token, economic inequality is not in itself morally objectionable. From the point of view of morality, it is not important that everyone should have the same. What is morally important is that each should have enough. If everyone had enough money, it would be of no special or deliberate concern whether some people had more money than others. I shall call this alternative to egalitarianism the ‘doctrine of sufficiency’—that is, the doctrine that what is morally important with regard to money is that everyone should have enough.” (FRANKFURT, Harry G. On Inequality. Princeton University Press, 2015.)
\textsuperscript{15} It is worth mentioning that the jurist Elizabeth Nazar Carrazza says that tax progressivity is not a tax technique, but a subprinciple the principle of Contributory capacity (CARRAZZA,
progression to the increase for a given tax base. That is, the larger the calculation base, the larger the rate, always progressively.

Progressivity means the feature in a tax system in which as the taxpayer’s wealth manifestation increases, grows at the same rate or higher, the contribution to the State funding.

It’s aimed with such technique to adjust the tax to the economic capacity of the taxpayer according to the principle of variable proportionality, by which the tax burden should be directly proportional to the wealth of the taxpayer,\(^{16}\) treating equally the equal and the unequal unequally, to the extent of their inequality, in respect to the constitutional principle of equality (Article 5, CF).

So, materially progressivity ensures equal treatment in the measure that it will impute a greater economic burden to those who can bear it, and less to those who have less capacity to contribute. As teaches Fernando Pérez Royo: “Those who have more contribute in proportion higher than those who have less”\(^{17}\)

In Brazil, for example, the Federal Constitution (Article 153, Paragraph 2, Section I) provides that the income tax will be informed by the principle of progressivity, so the rates of this direct tax are progressive due to income levels as shown:

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The ability to pay, therefore, is a concept that must be interpreted so as to ensure the fulfillment of the principle of equality, thus, the taxes may fall over a number of statements of economic capacity, such as, income, assets, inheritance, consumption, among others\textsuperscript{18}, so that the analysis of this capacity must take into account the different signs of wealth.

Furthermore, a tax system should seek equality to also ensure their own safety and existence of state institutions, avoiding thus taxpayers to evade the duty to pay taxes, and therefore, that few eventually support the spending of many. This is the understanding of the argentine jurist Osvaldo H. Soler:

"In addition to an ethical reason, fairness in a tax system seeks to solve the practical necessity that the taxes are not rejected by those who must pay them. Unfair taxes may cause the phenomenon of tax resistance, which can translate into tax evasion and even revolution as history teaches us as to explain the origins of the American and French revolutions."\textsuperscript{19}

Based on such contextual and conceptual considerations, it needs to be said that the ability to pay should be analyzed according to the espoused legal criteria, but should also be seen under an economic focus, given that


economic theory seeks to bring the foundations of ability to pay in several theoretical lines.

The Brazilian Constitution adopted the *faculty theory* of ability to pay, to justify that an equal sacrifice should mean that, proportionally, the taxation must consider individually the ability of citizens to contribute to public burden, respecting every single capability to pay taxes.\(^{20}\)

That is the only interpretation that suits with the equality principle described above.

But the problem arises when we consider that the indirect taxation distances the tax treatment of different material situations of taxpayers, bringing an increase in the tax burden to those who have less ability to pay, disregarding the ability to pay and, consequently, the constitutional tax equality.

**II. INDIRECT TAXES IN BRAZIL**

The Brazilian tax doctrine brings the classification of direct and indirect taxes to determine the impact on estate, income, or consumption expressions.

Direct taxes are those where the legal incidence falls on the taxpayer that is at the same time legally qualified taxpayer (*de jure*), and responsible for paying the tax (*de facto*). As an example, the Income Tax (*Imposto de Renda* – *IR*), and the Tax on Land and Urban Land Property (*Imposto sobre propriedade predial e territorial urbana* – *IPTU*), who are increased by tax progressivity.

When the taxes impact on the price of objects (consumption) to various third parties that are not part of the tax legal relation (taxpayer/State), they are

\(^{20}\)“Equal sacrifice is thus merely a rough way of expressing the idea of ‘proportional’ sacrifice. In assuming that ‘equal sacrifice’ necessarily implies that ‘the intensity of the wants that remain unsatisfied because of the tax’ must be equal, these objectors really confound equal sacrifice with arithmetical equality. All that is implied in the doctrine of equal sacrifice is that the pressure must be relatively proportional, not that it must be identically the same” (SELGIMAN, Edwin. Progressive Taxation in Theory and Practice. Princeton University Press, 1908. p. 214)
indirect, given that the law qualifies the taxpayer (de jure), but passes on the economic impact to others (de facto).\textsuperscript{21}

Economically, and corroborating the legal classification, in direct taxes the incidence of taxation is in direct taxpayer to assume the financial burden and bear the economic consequences of the tax. On the other hand, in indirect taxes, even though the law obliges the payment by the taxpayer, the economic and financial reflection of the tax will be passed on to another person, which, in fact, will ultimately suffer the consequences of tax incidence.

Brazil focus its revenues in indirect taxes, such that the presence of these taxes in the total State revenue characterizes as a tax system dependent on consumption, since the origin of resources in these operations is relevant and indispensable to the treasury, as shown:\textsuperscript{22}

\begin{table}[h]
\centering
\begin{tabular}{|c|c|}
\hline
\textbf{2004 Brazilian Taxation - (BRL Billion)} & \\
\hline
R$ 270,00 & \\
R$ 265,00 & \\
R$ 260,00 & \\
R$ 255,00 & \\
R$ 250,00 & \\
R$ 245,00 & \\
R$ 240,00 & \\
R$ 235,00 & \\
R$ 230,00 & \\
R$ 225,00 & \\
R$ 220,00 & \\
R$ 215,00 & \\
\hline
\end{tabular}
\end{table}

\begin{itemize}
\item Income Taxes
\item Consumption Taxes
\end{itemize}

\textsuperscript{21} To Renato Becho, “to say that a tax is direct or an indirect tax is has as a referential its economic impact, i.e. whether or not the economic cost of the tax can be passed on to another person other than the taxpayer. Direct taxes are those in which the taxpayer has to absorb the impact of the tax on its assets, while as indirect taxes are classifiable those in which the taxpayer transfers the cost of the tax to another person, through various mechanisms, such as a contract or, more commonly, by the insertion of its value within the cost of a product or service.” (Lições de Direito Tributário..., p. 239).

Such characteristic can be justified by what Tino Sanandaji e Björn Wallace call *Fiscal Illusion*, that is, “the premise is that the tax system design could lead to underestimation of the costs of public expenditure, with the public not being fully informed of the total costs of taxation.”

The taxpayer cannot scale the size of the tax burden, so the payment of the tax is silent, but powerful. We do not know what taxes, how and when they are paid, feeling only its effect on the price of the products you buy.

The *tax carnival* of laws, rules and amounts of taxes, in the words of Alfredo Augusto Becker, make it so that the taxpayer cannot predict or plan himself on the tax that falls over consumption. Even though there is in Brazil a federal law (Law n. 12,741 / 2012), stating that "shall include, in tax or equivalent documents, information corresponding the approximated value of all federal, state and municipal taxes, whose incidence influences the formation of their selling price."

Access to this information is quite difficult, since it requires of the taxpayer knowledge of legal science and tax law, to determine the actual incidence of all taxes which increase consumption, such as ICMS (sales); ISS (services); IPI (industrialized product); PIS and COFINS (social contributions); CIDE (economic intervention contribution).

In a study by the Economic Research Institute Foundation (*Fundação Instituto de Pesquisas Econômicas – FIPE*), under the coordination of Maria Helena Zuckon found that in 2004 more than 40% (forty percent) of the tax burden is indirect, incident on consumption in a scenario where the tax burden is more than 36% (thirty-six percent) of the national GDP.

Furthermore, in 2014, despite the downturn in the sector of commerce and industry at 1.8%, indirect taxation has remained close to 40% of all taxes,
and the taxation represented 33.74% of GDP, according to a study of Brazil's Federal Revenue Service.\textsuperscript{26}

Therefore, it's noted that the indirect tax burden is higher than the direct taxes on income and on the property, and it outlines the characteristics of a tax system that taxes equally, the unequal, because it does not take into account the individual ability to pay, imposing an identical tax burden on consumption.

The indirect tax removes the personal characteristics of the taxpayer \textit{de facto}, excluding specifically its economic and financial situation, assuming absolutely their ability to contribute by the purchase of a product.

Two indirect taxes in Brazil, ICMS and IPI, are graduated according to the essentiality of the product object of taxation because the Federal Constitution, Article 153, Paragraph 3, Section I, and Article 155, Section III, determines that State prioritize lower rates to more essential goods.

Both the ICMS as the IPI are indirect taxes on the chain of production and consumption, which ultimately are passed on the price to consumers, regardless of what and who they are.

In other words, these two indirect taxes should be graded in inverse proportion to the need and importance of products: the higher its essentiality, the lower the tax burden; the lower its essentiality, the greater the tax burden.

Thus, the Brazilian constitutional legislator sought to prioritize the most essential products in the lower and middle class Brazilian market basket, avoiding excessive taxation of the minimal necessary goods for survival.

However, an average of such products, even if essential, is taxed by rates exceeding 15% of the cost of the product, demonstrating the severity of such taxation on the possibility of consumption of those with smaller economic capacity.

It is noteworthy that in 2014, these two taxes were responsible for 23.45% of all tax revenues in the country.

However, the lack of progressivity in taxes on consumption, bringing the same treatment, with identical rates for all, without distinction, makes the national tax system regressive: *taxing more severely those who have less ability to pay*.

### III. THE REGRESSIVITY OF BRAZIL’S TAX SYSTEM

The progressivity is, as shown, a tax technique that will increase the tax rate according to the wealth growth that will be taxed. Thus, it differs from proportionality and regressivity, because while in proportionality there’s a individualized increasing tax base without the direct increase of the rate, in regressivity there is a disproportion between fiscal capacity and tax incidence.

The regressivity is characterized, therefore, by disregarding the effective taxpayer’s ability to bear the tax obligation so that the tax burden is inversely proportional to their wealth, and, thus, taxpayers with greater wealth will pay less taxes compared with one that has a lower capacity.

In other words, regressivity is the worsening of economic and financial situation of those who have less ability to pay.

Analyzing the Brazilian tax system, based again on the research conducted by Maria Helena Zuckon, it shows that the analysis of the total tax burden on Brazilian families regresses according to the increase of the income.\(^{27}\)

In 2004 the tax burden of direct taxes was 3.1% for families that earned up to two minimum wages, and 9.9% for households receiving over 30 minimum wages, demonstrating, thus, the progressive character of direct taxes.

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However, with regard to indirect taxes families that received up to two minimum wages were taxed with a 45.8% rate, as for families receiving over 30 minimum wages this indirect taxation was 16.4%, *ergo*, inversely proportional to the ability to pay of taxpayers.

Verifying jointly the two tax burdens, it is concluded that the families that received up to two minimum wages were taxed with a 48.8% charge, as for families receiving over 30 minimum wages that burden is much lower, reaching 26.3% or 46.10% lower than the burden of families with lower income.

The following graphs easily demonstrate this great divergence:

**2004 Direct Taxation**

<table>
<thead>
<tr>
<th>MW</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to 2 MW</td>
<td>3.1</td>
</tr>
<tr>
<td>2 to 3 MW</td>
<td>3.5</td>
</tr>
<tr>
<td>3 to 5 MW</td>
<td>3.7</td>
</tr>
<tr>
<td>5 to 6 MW</td>
<td>4.1</td>
</tr>
<tr>
<td>6 to 8 MW</td>
<td>5.2</td>
</tr>
<tr>
<td>8 to 10 MW</td>
<td>5.9</td>
</tr>
<tr>
<td>10 to 15 MW</td>
<td>6.8</td>
</tr>
<tr>
<td>15 to 20 MW</td>
<td>6.9</td>
</tr>
<tr>
<td>20 to 30 MW</td>
<td>8.6</td>
</tr>
<tr>
<td>Above 30 MW</td>
<td>9.9</td>
</tr>
</tbody>
</table>

MW = Minimum wages
With data collected by the Brazilian Internal Revenue Service in 2014, indirect taxation has remained close to 40% of the tax burden even with the downturn in the sector of commerce and industry at 1.8%.\textsuperscript{28}

The situation of citizens with lower income remains the same: an indirect tax burden that exacerbates their situation and makes it impossible to exercise basic consumption, or save their income to ensure in possible cases of economic and financial crisis.

In other words, excessive incidence of indirect taxes, especially for those who have less ability to pay, brings a worsening of the economic possibilities of consumption of those taxpayers who, with a smaller share of their income, decrease the amount of purchased products in your market basket.

To demonstrate such a situation, we will describe the basic lines of the economic theory about the allocative efficiency of supply and demand.29

In an efficient market, equilibrium of prices in economic transactions reflects the possibility of maximizing consumers and suppliers welfare, on a point of Pareto-efficient, so that the balance of the market will bring the best solution ($p^0$-$q^0$) for economic agents.

In the chart analysis below, we see that the efficiency point ($p^0$-$q^0$) shows that there is a necessary balance between supply ($P_S$) and demand ($P_D$), given that with a higher production $q^0$, prices would be higher than $p^0$. However, with a price greater than $p^0$, buyers would buy a smaller amount $q^0$.

On the other hand, if the price is lower than $p^0$, buyers would take a larger quantity $q^0$, however, producers would not produce the amount required for consumption demanded.

So, in both cases the incompatibility between prices (for) products (q) demonstrate the lack of balance and inefficiency of the scenarios that are positioned outside of the point ($p^0$-$q^0$).

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Thus, the price of goods traded in an efficient market is the result of a balance between the welfare sought by buyers and sellers, after all, "free markets produce the quantity of goods that maximizes the sum of consumer and producer surplus"\(^{30}\) allocating the supply of goods to buyers and sellers, increasing economic welfare.

In this dynamic, the inclusion of a tax creates distortions in an economic price system, influencing the supply and demand curves, and thus bringing an inefficiency in the allocation of resources, and so an increase of social cost.

That is what the economic theory called the *deadweight loss* of taxation, or the tax cost that reduces the social welfare.

Looking at the chart below\(^{31}\), we see that with the incidence of the tax \((t)\), there is a decrease in supply (from \(q^0\) to \(q^1\)), due to the increase in the price of the product to the buyer \((P_D)\), and the consequent reduction of the profit for the seller \((P_s)\).

Taxation brings then a decrease in consumer surplus, reducing their capacity to consume for \(a\), but, before tax, consumers could acquire \(a + b + c\). Similarly, the tax reduced the production surplus for \(f\), given that, before taxes, he could offer \(d + e + f\).

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Likewise, the tax revenue (TR) is $b + d$, and the remaining elements $c + e$ represent the deadweight loss (DL), which is precisely the lost fraction, which now do not mean supply or demand, generating consequently less wealth and welfare for society.

Taxation generates distortions and allocative inefficiencies in the economic system of any country, so that an excessive indirect taxation on consumption ultimately reduces the consumption possibilities by those who have less ability to pay, and therefore less economic output for producers, who, on the other side of the relationship, cease to transact goods produced, reducing thus the generation of wealth.

Indirect taxation, in this context, does not give concreteness to the principle of tax equality described.

The indirect taxation should be seen, therefore, as one of the causes of social inequalities in Brazil, since it removes the redistributive potential of taxation, while worsening the situation of consumers with lower consumption
potential and contribution capacity in much higher proportion than the one applied to taxpayers with higher economic and financial capacities.\textsuperscript{32}

The regressivity of the tax system with a huge indirect tax burden, does not reach the income earned by citizens, but their income consumed, decreasing their chances of consumption, property or savings.

Even if there is in Brazil the principle of tax essentiality, it just reaches a few products, and even so, the rates are still aggressive to the reality of many Brazilians, not being a mitigation for regressivity of taxes on consumption.

In conclusion, taxation cannot be a factor of social inequality, as the Constitution requires, as a fundamental right, a tax equality according to the material capacity of each citizen and should thus the tax system determine a progressive tax burden, or in the worst cases an equal one, but never regressive - as currently occurs in the structure of direct and indirect taxes, jointly considered.

Only in this way can be achieved the objectives of the Federative Republic of Brazil (Article 3), in particular the construction of a free, just and solidary society (section I) and eradication of poverty and marginalization and reduction of social and regional inequalities (section II).

\textbf{IV. CONCLUSION}

Aristotelian equality\textsuperscript{33}, affirmed also by the celebrated Brazilian jurist Rui Barbosa\textsuperscript{34}, determines that equals should be treated equally and unequals must be treated unequally, in the extent of its inequality.

\textsuperscript{32} That is the conclusion of Cristiano Carvalho in his work Teoria da Decisão Tributária (The Theory of Tax Decision): “what you want, from the point of view of economic efficiency is the basis of assessment at a point that does not inhibit private activity only wealth generator for society”. p. 155.

\textsuperscript{33} Further, this is clear from what accords with merit, for all agree that what is just in distributions ought to accord with a certain merit.”. Nicomachean Ethics. Chicago: Chicago University Press, 2011. p. 95.

The principle of tax equality on Brazilian Constitution means the achievement of a materially equal treatment to taxpayers who are in the same situation, and unequal treatment for taxpayers in different situations.

It is determined, therefore, that those who have greater wealth and/or ability to pay, contribute more than others who are not in the same economic and financial condition. Such constitutional dictum is called the *ability to pay principle*, which is an expression of constitutional material equality.

According to this principle, the amounts due are raised according to the growth of the base achieved by the tax, so that the greater the capacity, the greater the incidence of taxation to be support by the citizen-taxpayer.

To achieve this goal, the Constitution places the progressivity as a taxation technique, whereby as the taxpayer's wealth manifestation increases, the rates grow at the same rate or higher. That way the contribution to the State is adjusted in order to bring the tax to the economic capacity of the taxpayer as determined by the constitutional principle of material equality (and its derivation: the ability to pay principle).

However, indirect taxes levied on consumption, passed on the prices of goods and services to consumers, do not respect the ability to pay, reaching more seriously equity and income precisely of those who have less condition to contribute to the state - in true demonstration of tax regressivity.

To say that the tax system is regressive requires the analysis of the total tax burden levied on the Brazilian families, in order to measure how much each income group contributes proportionately to the Treasury.

As shown in this article, Brazilian families are taxed progressively by direct taxes such as income tax, with increasing rates according to income earned. On the other hand, they are taxed regressively by indirect taxes, because, even though everyone pays the same tax embedded in the price of products, indirect taxation is a larger share of income of taxpayers with less ability to pay (45.8% for poorest and 16.4% for the richest, compared 2 to 30 minimum wages).
This situation worsens when we see that the consumed income of the poorest households is all they have after direct taxation, so that the incidence of indirect taxes in large volume makes it impossible for them to save part of their earned income.

Thus, the regressivity of the Brazilian tax system is a patent characteristic, and the reduction of indirect taxation is imperative, in which the Constitution requires material equality as a guiding principle and primary objective of the State, without which one cannot say of fair taxation.

Given the difficulty of creating progressive indirect taxes, and in accordance with the individual characteristics of each taxpayer, we believe that the solution would be create a single federal tax on consumption (a Brazilian Value-Added Tax - VAT), whose revenue would be divided proportionally between the Federated States, with a smaller impact on consumption than the current reality, with an added increase of direct taxes, which are graduated by progressivity and respect individual ability to pay.

As said by Edwin Seligman: “Justice indeed demands that the state should do nothing consciously and purposely to increase inequality of wealth; but we clearly transcend the claims of justice when we demand that the state should do away with all inequalities of wealth. Justice, in the sense of equality, may indeed demand changes in the existing forms of taxation.”

V. REFERENCES


