THE PRINCIPLE OF TAX NEUTRALITY AND EXTRAFISCALITY IN THE BRAZILIAN TAX REFORM

O PRINCÍPIO DA NEUTRALIDADE E A EXTRAFISCALIDADE NA REFORMA TRIBUTÁRIA BRASILEIRA

EL PRINCIPIO DE NEUTRALIDAD Y LA EXTRAFISCALIDAD EN LA REFORMA TRIBUTARIA BRASILEÑA

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Danielle Uessler[1], Arthur Sandro Golombieski Ferreira[2], Mariana Matias Ribeiro Ramos[3]

ABSTRACT

This paper aims to analyze whether the principle of neutrality, one of the pillars of the Consumption Tax Reform, is compatible with the extrafiscal function of the tax system, in order to assess whether there is harmony within the context of the new consumption taxation framework introduced by Constitutional Amendment No. 132/2023. The issue arises from the contrast between neutrality, which seeks to avoid economic distortions and ensure a balanced competitive environment, and extrafiscality, expressed mainly through the Selective Tax, which retains the function of influencing behavior through taxation. The research finds that, although the Reform sought to establish a functional separation between the principle of neutrality and the extrafiscal function, relevant risks remain, such as the reduction of space for promotional policies, the rigid crystallization of essentiality, and political pressures for sector-specific benefits. Using the hypothetico-deductive method, it is concluded that neutrality and extrafiscality are not mutually exclusive, but require harmonization through clear criteria to ensure simplicity, economic efficiency, and social justice.

Keywords: Tax Neutrality. Extrafiscality. Tax Reform.

RESUMO

O presente trabalho tem como objetivo analisar se o princípio da neutralidade, um dos pilares da Reforma Tributária sobre o consumo, é compatível com a função extrafiscal do sistema tributário, a fim de verificar se há harmonia no contexto da nova arquitetura da tributação sobre o consumo, introduzida pela Emenda Constitucional n.º 132/2023. A problemática decorre do contraste entre a neutralidade, que busca evitar distorções econômicas e assegurar um ambiente concorrencial equilibrado, e a extrafiscalidade, expressa sobretudo

[1] Master's student in Law. Pontifícia Universidade Católica do Paraná (PUCPR).
E-mail: danielleuessler@hotmail.com Orcid: https://orcid.org/0000-0001-5514-5096
Lattes: http://lattes.cnpq.br/8763626921178215
[2] Master's student in Law. Pontifícia Universidade Católica do Paraná (PUCPR). E-mail: asgfarthur@gmail.com
Lattes: http://lattes.cnpq.br/4260959798547687
[3] Master's student in Law. Pontifícia Universidade Católica do Paraná (PUCPR).
E-mail: marimatiasramos@hotmail.com Lattes: http://lattes.cnpq.br/4688944690272548

no Imposto Seletivo, que mantém a função de induzir comportamentos por meio da tributação. A pesquisa constata que, embora a Reforma tenha buscado estabelecer uma divisão funcional entre o princípio da neutralidade e a função extrafiscal, permanecem riscos relevantes, como a redução do espaço para políticas promocionais, a cristalização da essencialidade em moldes rígidos e as pressões políticas por benefícios setoriais. Mediante a metodologia hipotético-dedutiva, conclui-se que neutralidade e extrafiscalidade não são excludentes, mas exigem compatibilização por critérios claros, de forma a assegurar simplicidade, eficiência econômica e justiça social.

Palavras-chave: Tax Neutrality. Extrafiscality. Tax Reform.

RESUMEN

El presente trabajo tiene como objetivo analizar si el principio de neutralidad, uno de los pilares de la Reforma Tributaria sobre el consumo, es compatible con la función extrafiscal del sistema tributario, con el fin de verificar si existe armonía en el contexto de la nueva arquitectura de la tributación sobre el consumo, introducida por la Enmienda Constitucional n.º 132/2023. La problemática surge del contraste entre la neutralidad, que busca evitar distorsiones económicas y asegurar un entorno competitivo equilibrado, y la extrafiscalidad, expresada principalmente en el Impuesto Selectivo, que mantiene la función de inducir comportamientos mediante la tributación. La investigación constata que, aunque la Reforma haya buscado establecer una división funcional entre el principio de neutralidad y la función extrafiscal, persisten riesgos relevantes, tales como la reducción del espacio para políticas promocionales, la cristalización de la esencialidad en modelos rígidos y las presiones políticas por beneficios sectoriales. Mediante la metodología hipotético-deductiva, se concluye que la neutralidad y la extrafiscalidad no son excluyentes, sino que exigen compatibilización a través de criterios claros, con el fin de asegurar simplicidad, eficiencia económica y justicia social.

Palabras clave: Neutralidad Tributaria. Extrafiscalidad. Reforma Tributaria.

1 INTRODUCTION

The Consumption Tax Reform, implemented by Constitutional Amendment No. 132/2023, inserted in article 156-A, paragraph 1, of the Federal Constitution, the determination that the Tax on Goods and Services (IBS) and the Contribution on Goods and Services (CBS) will be governed by the principle of neutrality. This principle seeks to minimize tax distortions in economic choices, ensuring greater predictability and allocative efficiency.

However, the tradition of the Brazilian tax system reveals that taxes are not limited to a collection function, as they also play an extra-fiscal role, and can influence social and economic behavior. The Tax Reform preserved this regulatory dimension through the Selective Tax, aimed at discouraging conducts that cause negative externalities to promote constitutional values, such as the protection of health and the environment.

Although conceived as complementary, neutrality and extra-taxation can come into tension. The first seeks uniformity and simplicity in taxation, in order to reduce the interference of taxation in economic choices, while the second, on the contrary, operates through selective differentiations, using the tax as an instrument to induce behavior in favor of tax policy purposes.

The Reform sought to mitigate the tension between neutrality and extra-taxation through functional specialization: neutral taxes for broad and uniform collection purposes, and extra-fiscal taxes for specific regulatory purposes. This division, however, does not eliminate the challenges of its implementation, such as the risk of a "rigid essentiality", the reduction of space for promotional policies and the pressure for sectoral benefits that can weaken neutrality.

In this context, the problem of the compatibility between neutrality and extra-fiscal policy emerges, since would neutrality, chosen as one of the structuring guidelines of the new system of taxation on consumption, be compatible with the permanence of extra-fiscal instruments? From this, through the hypothetical-deductive methodology, this article aims to analyze whether the principle of neutrality is compatible with the extrafiscal nature of the system, in order to verify whether there is a harmonious or antagonistic coexistence in the context of the new architecture of taxation on consumption.

2 THE PRINCIPLE OF NEUTRALITY IN THE TAX REFORM ON CONSUMPTION

Tax neutrality is one of the pillars of an efficient tax system, alongside principles such as equity, simplicity and ability to pay. As conceptualized by Zilveti[4], this rule gravitates around

[4] ZILVETI, Fernando Aurélio. Variations on the principle of neutrality in international tax law. **Revista Direito Tributário Atual,** v. 19, p. 30.

the principle of tax equality, and the system that is structured in such a way as not to compromise the efficient allocation of the means of production is neutral, avoiding distortions that may unbalance the market.

It is the requirement that taxation interfere as little as possible in the economic decisions of individuals and companies, avoiding distortions that may favor certain sectors or forms of organization to the detriment of others. In essence, it means that economically equivalent activities or operations must receive equivalent tax treatment, so that the tax does not become a determining factor in the choice between business or consumption alternatives.

Tax neutrality has its origin in the economic tradition[5], maintaining that the tax system should interfere in a minimal way in the choices of economic agents, avoiding distortions that compromise the efficient allocation of resources. The starting point of this thought is Adam Smith, who in his book The Wealth of Nations (1776), formulated principles of equality, certainty, convenience and efficiency, which, although they did not expressly use the term neutrality, indicated the need to avoid artificial barriers to production and trade.

In Brazil, the doctrine assimilated these economic bases, resulting in the debate about the theory of optimal taxation[6], which defends broad systems, with uniform rates and few exceptions. The logic is that similar activities receive the same tax treatment, avoiding distortions that affect competition and ensuring that the choices of economic agents are based on real preferences, and not on artificial incentives created by the State.

This conception is connected to the notion of "fiscal wedge",[7] understood as the difference between the amount paid by the consumer and the amount actually received by the producer due to taxation. When poorly designed, taxes widen this difference, discouraging consumption, production and investment, with negative effects on the allocation of resources and economic competitiveness.

In this sense, Moreira[8] systematizes neutrality in two dimensions: horizontal and vertical. Horizontal neutrality requires equal treatment for economically equivalent situations, avoiding arbitrary distinctions between products, services or sectors. Vertical neutrality, on the other hand, is related to the technique of non-cumulativeness, which ensures that the tax

[5] KOCH, Mariana Porto. **Theory of tax neutrality**. 2023. Thesis (Doctorate in Law) – Faculty of Law, Federal University of Rio Grande do Sul, Porto Alegre, 2023.
[6] COSTA, C. F. de C., & Vieira, J. de C. (2021). Theory of optimal taxation: Contributions to the Brazilian reality. Journal of Contemporary Administration.
[7] For the OECD, the term used is called "*Tax wedge*" and is understood as "*the ratio between the amount of taxes paid by an average single worker (a single person with 100% of the average income) without children and the corresponding total labor cost for the employer*. [Free translation]". Available at: https://www.oecd.org/en/data/indicators/tax-wedge.html.
[8] MOREIRA, André Mendes. **Neutrality, added value and taxation**. Belo Horizonte: Forum, 2019, p. 211.

is levied only on the value added at each stage of the production chain, eliminating cascading taxation.

On the other hand, Schoueri[9] warns of the limits of this conception. For him, there is no absolutely neutral tax: every tax incidence interferes in some way with the economy. What should be required, therefore, is that this interference be justified, proportional, and guided by constitutional purposes, so as not to generate undue competitive imbalances. In other words, neutrality is not the absence of impact, but the limitation of distortions.

Thus, the classical economic concept of neutrality provides the initial framework, but its application to positive law demands adjustments that recognize the tensions between ideal and normative reality. It is precisely at this point that the principle gains more defined technical and constitutional contours, especially with the adoption of non-cumulativeness.

However, it is important to emphasize that neutrality should not be confused with the absence of economic effects. Every tax changes, to a greater or lesser extent, the behavior of the agents. The aim is to ensure that such changes are not arbitrary or disproportionate. In this context, non-cumulativeness emerges as a fundamental technique to ensure vertical neutrality, preserving the efficiency of the system.

By allowing the taxpayer to credit the tax paid in the previous stages of the chain, non-cumulativeness ensures that the tax is levied only on the value added in each transaction. This structure prevents the so-called "cascade taxation", which generates serious distortions, such as the artificial increase in prices, the loss of competitiveness, and the induction of business decisions guided by the accumulated tax burden, and not by criteria of economic efficiency.

Moreira[10], in a comparative law study on European VAT, points out that any undue restriction on the right to credit weakens neutrality. For him, non-cumulativeness must be broad, automatic and objective, so as not to compromise competitive equality.

This perspective was incorporated by Constitutional Amendment No. 132/2023, which enshrined full non-cumulativeness in the new model of Tax on Goods and Services (IBS) and Contribution on Goods and Services (CBS), replacing the old criterion of "physical credit" applied to ICMS and IPI with a more comprehensive financial credit model. Thus, the IBS and CBS must be guided by this principle[11].

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[9] SCHOUERI, Luís Eduardo. Taxation and economic induction: the economic effects of a tax as a criterion for its constitutionality. *In:* Roberto Ferraz. (Org.). **Principles and Limits of Taxation 2 – The principles of the economic order and taxation**. São Paulo: Quartier Latin, v. 2, 2009.

[10] MOREIRA, André Mendes. The right to credit in European VAT: notes on the principle of tax neutrality. **Current Tax Law Journal**, n. 42, p. 47, 2019.

[11] SCHOUERI, Luís Eduardo; GALDINO, Guilherme. The Neutrality of the Transitory Rules in the IBS and CBS: the Case of Capital Goods. **Current Tax Law Journal**, v. 59, 2025.

The technique of non-cumulativeness is directly connected to vertical neutrality: a tax is neutral when it does not accumulate along the production chain. Horizontal neutrality, on the other hand, as seen, requires a broad and uniform base, avoiding artificial distinctions. Both dimensions are indispensable for building a more efficient and fair tax system.

This normative framework represents an advance, as it inserts neutrality among the constitutional limitations on the power to tax, transforming it into a parameter of constitutionality and interpretative guide for legislators, regulators and courts. From an economic point of view, neutrality seeks to promote allocative efficiency, as resources should flow to the most productive activities according to market criteria and not as a result of tax incentives or penalties.

Failure to comply with this principle can generate relevant costs to the economy, such as loss of international competitiveness, artificial favoring of certain sectors, administrative complexity and increased tax litigation, in addition to business verticalization. In other words, distorting taxes reduce productivity and compromise sustainable development.

The constitutional incorporation of neutrality does not, however, eliminate the possibility of using taxation for extra-fiscal purposes. Public policies can use taxation to encourage desirable behaviors, such as technological innovation or environmentally responsible practices, and discourage harmful behaviors, such as the consumption of cigarettes and alcoholic beverages.

This tension between neutrality and extra-taxation requires the legislator to establish clear and proportional criteria for interventions, preventing exceptions from converting the principle into mere rhetoric.

The practical implementation of neutrality in Brazil faces significant challenges. Although Complementary Law No. 214/2025 regulated the IBS and CBS, reproducing the constitutional text and defining neutrality as a legislative guideline, the legal diploma included exceptions that reduce the scope of the principle. This situation creates risks of judicialization, especially in the face of provisions that may restrict the scope of a constitutional guarantee.

Another challenge is the very nature of consumption taxation, which is inherently distorting. The burden falls on goods and services[12], affecting relative prices and influencing consumption decisions. Neutrality, in this context, works as a regulatory goal: it seeks to reduce undesirable effects to a minimum, but they will hardly be completely eliminated.

[12] ZILVETI, Fernando Aurélio. Variations on the principle of neutrality in international tax law. **Revista direito tributário atual,** v. 19, 2005.

In addition, there is a risk that political interests and sectoral pressures will weaken the application of the principle. Comparative experience[13] shows that highly fragmented Value Added Tax (VAT) systems, with multiple exceptions, special regimes and benefits, end up sacrificing neutrality and amplifying distortions[14].

This is what happens in countries such as India, whose GST (*Goods and Services Tax*) maintains numerous different rates, and also in pre-reform Brazil, with the multiplicity of ICMS, ISS and PIS/COFINS regimes.

Nevertheless, it is important to highlight that neutrality does not oppose tax justice, but complements it. While progressivity and the ability to pay seek to distribute the tax burden equitably, neutrality ensures that this burden is not manipulated in a way that favors specific groups. A neutral system tends to be more transparent, predictable, and reliable, which are essential factors for attracting investments and consolidating legal certainty.

In this sense, the doctrine points out that neutrality must be interpreted systemically, in articulation with other constitutional tax principles. It is not an absolute ideal, but a guideline whose observance strengthens the rationality of the system, increases economic efficiency and contributes to the democratic legitimacy of taxation.

Thus, if neutrality seeks to reduce distortions, extra-taxation reveals precisely the possibility of the State intentionally using them to pursue legitimate ends. It is at this point of balance between economic efficiency and normative intervention that the debate on the extrafiscal function of taxation opens.

3 EXTRA-TAXATION IN THE TAX REFORM ON CONSUMPTION

Throughout history, taxation has never been limited to the function of raising funds to fund state activities. The tax has also been used as a tool for economic and social intervention, capable of encouraging certain conducts, discouraging others and guiding the actions of private agents in line with broader constitutional objectives. This phenomenon, known as extrafiscality, expresses the political dimension of the tax system and reinforces its condition as an instrument for the implementation of public policies.

Adamy, in exploring the theoretical origins of extrataxation, elucidates that Adolph Wagner, a German author of the late nineteenth century, was the one who began to conceive the tax phenomenon "in a differentiated way, thinking of it beyond the mere instrument of

[13] ABSWOUDE, Kevin van. *The principle of fiscal neutrality and economic reality in EU VAT: two peas in a pod?*element. **Lund University**, Sweden, 2022.
[14] MOREIRA, André Mendes. The right to credit in European VAT: notes on the principle of tax neutrality. **Current Tax Law Journal**, n. 42, 2019.

state financing",[15] having revolutionized the central concept of tax. The author explains that it was Wagner who established the theoretical bases of the discussion on non-collection tax purposes, "demonstrating that tax law can have political and social purposes distinct from mere collection".[16]

Vieira elucidates that extra-taxation is a central concept in tax law, which transcends the mere collection function, positioning it as a fundamental instrument for the implementation of public policies[17]. This is because, for the author, tax law should not be conceived only as a means of state financing, but also as a mechanism for implementing policies in several areas[18].

It is in this sense that Adamy maintains that the law is not an end in itself, but also an instrument for the achievement of state purposes[19]. The author defines the instrumentalization of law as "the right being used as an instrument, as a means, as a tool"[20] for the induction of behaviors, according to the purpose of the State. Still, Adamy points out that in the tax context, this instrumentalization is manifested in the ability to influence conduct, whether granting incentives or disincentives[21].

Unlike tax taxes, as Folloni explains, whose main function is to sustain state expenditures based on the ability to pay, the foundation of extrafiscal taxes "is not the sustenance of public expenditures in general, but the internalization of negative externalities".[22] Because of this, extra-taxation justifies the adoption of different differentiation criteria for the ability to pay, allowing taxation to be guided by public policy purposes. Thus, selectivity, the granting of exemptions, the setting of increased or reduced rates and the institution of special regimes are not explained only by the economic aptitude of the taxpayer, but by the search for desired effects in the social or economic reality.

With this, Leão emphasizes the importance of defining the "extrafiscal purpose aimed at in the law"[23] for the control over the instrumental use of Tax Law. For the author, the

[15] ADAMY, Pedro. Theoretical Origins of Extrafiscality. **Current Tax Law Journal**, No. 39, 2021, p. 353.
[16] Ibid.
[17] VIEIRA, Andreia Costa. The Precautionary Principle and Extrataxation in Environmental Taxation. **Current Tax Law Journal**, nº 32, 2014, p. 37.
[18] Ibid., p. 38.
[19] ADAMY, Pedro. Instrumentalization of Tax Law. *In*: ÁVILA, Humberto (ed.). **Fundamentals of Tax Law**. Rio de Janeiro: Marcial Poins, 2012, p. 305.
[20] Ibid., p. 302.
[21] Ibid., p. 307.
[22] FOLLONI, André. Tax Competence of the Selective Tax: the text and its contexts. **Current Tax Law Journal**, v. 57, 2024, p. 637.
[23] LEÃO, Martha. Contribution to the study of Extrafiscality: the importance of purpose in the identification of extrafiscal tax rules. Revista Direito Tributário Atual, nº 34, 2015, p. 314.

extrafiscal purpose is not the intention of the 'historical legislator', so that it must be embodied in the will itself objectified in the law and not in the subjective will of the legislator[24].

The will of the law, as Guastini points out, is the "reason, the motive, the end, the practical result, by which a certain norm has been edited"[25] and to verify it "it is necessary to pay attention not (or at least not so much) to the preparatory work, but to the text of the law as such, in addition to the social and political circumstances in which it was edited".[26]

It is in this sense that extra-taxation is seen as a facet that allows the State to induce behavior through taxes, so that "taxation can also act as an instrument to induce social and economic behaviors".[27] This would be, for Santos and Scabora, the essence of the extrafiscal function of taxation, which does not have as its main purpose to supply the public budget, but rather the "attempt to increase economic or social well-being".[28]

In this sense, Schoueri observes that extra-taxation transforms the tax into a true instrument for inducing behavior, [29]acting as an indirect regulatory mechanism in sensitive areas, such as health, environment, regional development or incentive to technological innovation. The tax, therefore, ceases to be an end in itself – the collection – and starts to assume an instrumental function, to shape individual and collective choices in order to bring them closer to constitutional values and state policy objectives.

Thus, within this context of conduct induction, extrataxation is used to correct "externalities", whose notion, extracted from economic law, refers to costs and gains from private activities borne or enjoyed by the community due to market failures[30]. Externalities can be positive, when they generate benefits, or negative, when they generate costs/harms.

Economist Arthur Cecil Pigou has already suggested the institution of a tax to correct negative externalities and the payment of a subsidy to compensate for the positive externalities practiced by companies[31]. In this sense, extra-taxation would not aim to prevent an activity, but rather to condition the freedom of choice of the economic agent through the graduation of the tax burden according to specific purposes[32].

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[24] Ibid., p. 309-310.
[25] GUASTINI, Riccardo. *Apud* LEÃO, Martha. Contribution to the study of Extrafiscality: the importance of purpose in the identification of extrafiscal tax rules. **Revista Direito Tributário Atual**, nº 34, 2015, p. 311.
[26] Ibid.
[27] SANTOS, Flávio Felipe Pereira Vieira; SCABORA, Filipe Casellato. Environmental taxation and Extrataxation in Brazil: tax incentives and regressivity of green taxation. **Revista Direito Tributário Atual**, nº 52, year 40, São Paulo: IBDT, 3rd quarter 2022, p. 146.
[28] Ibid.
[29] SCHOUERI, Luís Eduardo. Inductive Tax Rules in Environmental Matters. *In:* TÔRRES, Heleno Taveira (ed.). **Environmental Tax Law**. São Paulo: Malheiros Editores, 2005, p. 235.
[30] Ibid., p. 236.
[31] BALTHAZAR. Ubaldo Cesar. **Taxes and the Environment**. Espaço Jurídico, Joaçaba, v. 12, n. 2, jul./dez. 2011, p. 238.
[32] DOMINGUES, José Marcos. **Tax Law and the Environment**. Rio de Janeiro: Forense, 2007, p. 49-50.

Schoueri explains that, in the case of pollution, for example, which generates environmental damage that is not borne by the perpetrators, state action seeks to internalize costs, so that the prices of products or services reflect the environmental damage caused by polluters[33]. For positive externalities, the author suggests that the State should, through economic advantages, increase the gains of those who generate environmental benefits, allowing these advantages to be accounted for[34].

In this scenario, it is clear that extra-taxation is not just a possibility, but a reality intrinsic to the very logic of the tax system's operation. If taxes can be shaped to internalize externalities and induce behaviors, it is natural that the Brazilian normative architecture, especially in the Reform process, seeks specific mechanisms to enhance this function.

In the context of the Consumption Tax Reform, this role was expressly assigned to the Selective Tax, provided for in Constitutional Amendment No. 132/2023 and regulated by Complementary Law No. 214/2025. Unlike the IBS and the CBS, conceived under the logic of neutrality and the fiscal purpose of collection, the Selective Tax assumes a predominantly extra-fiscal function, aimed at burdening goods and services considered harmful to health or the environment.

This tax, clearly of extrafiscal inspiration, is not connected to the idea of tax reinforcement, but rather to the regulatory function of the State, in line with what Pigou and contemporary doctrine have already outlined as essential for the correction of negative externalities. Thus, the Selective Tax emerges as the manifestation that extra-taxation continues to play a structuring role in the Brazilian tax system, even in a context in which neutrality is elected as a guiding principle of the Reform.

In this context of the Tax Reform, extra-taxation is manifested through selectivity, which allows the identification of the negative characteristics of goods and services, associating them with the damage they cause to the environment and health. The logic of extra-taxation used in the Selective Tax of the Reform is different from that applied to the Tax on Industrialized Products (IPI), in which the rates are selective according to the essentiality of the product.

Matschulat and Amaral explain that in the case of IPI, extrataxation is a "secondary consequence of taxation"[35] and not an "effect deliberately intended by the legislator", [36]as in

[33] SCHOUERI, Luís Eduardo. Environmental Law, Op. cit., p. 236.
[34] Ibid., p. 237.
[35] MATSCHULAT, Leonardo; AMARAL, Luiz Bernardo Kämpf Amaral. The perspective for the implementation of the Selective Tax as a tax type in Brazil. **Res Severa Verum Gaudium**, v. 6, n. 2, 2022, p. 297.
[36] Ibid.

the Selective Tax. Returning to Leão, the authors state that for a tax to be considered for an extra-fiscal purpose, "this purpose must be unequivocally demonstrated by the legislator".[37]

Thus, it can be stated that, while the IPI operates under a logic of selectivity by essentiality, being a tax with extrafiscal effects, the Selective Tax is structured on a logic of extrafiscal selectivity, aimed at the internalization of social and environmental costs and protectionist purposes. When applied to harmful goods or services, its function is not to distinguish the superfluous from the essential, but rather to graduate taxation according to the adverse impact generated on the community and the environment.

Because of this, although Constitutional Amendment No. 132/2023 did not expressly insert in article 153, paragraph 6, the expression 'will have an extrafiscal purpose', Folloni maintains that such an omission does not mischaracterize its nature, which is precisely extrafiscal[38]. For the author, the only interpretation compatible with the principles of equality, ability to pay and with the stony clauses is to recognize the extra-fiscal function of the Selective Tax, because, otherwise, its very insertion in the Constitution would represent an affront to such principles[39].

On the other hand, Adamy says that the Tax Reform represented a break with the traditional role of extra-taxation in Brazilian tax law[40]. For him, the Reform subverted the foundations of extrataxation[41], by prioritizing the sanctioning function and restricting, almost completely, the promotional dimension of taxation. This is because extrataxation is not only used to discourage harmful conduct, but also to promote benefits, using the tax as a negative or positive instrument of induction[42].

In this scenario, the author identifies three central foundations of this subversion: the broad prohibition on the granting of tax incentives in the IBS and CBS, the creation of a Selective Tax with an exclusively sanctioning function and restricted to certain matters, and the adoption of a "rigid essentiality", which crystallizes in a constitutional context a closed list of goods and services considered deserving of favored treatment[43].

Adamy points out that such changes remove from the tax system its flexibility and its ability to serve as a tool for promoting public policies[44]. When commenting on the broad prohibition of benefits, he states that "by establishing this broad prohibition, the constitutional

[37] Ibid.
[38] FOLLONI, Op., op., p. 627.
[39] Ibid.
[40] ADAMY, Pedro. Extrafiscality in the Tax Reform: rigid essentiality and the end of the promotional function of Tax Law. **Revista Direito Tributário Atual,** v. 58. year 42, São Paulo: IBDT, 3rd quarter 2024, p. 427.
[41] Ibid., p. 412.
[42] Ibid., p. 411.
[43] Ibid., p. 417-429.
[44] Ibid., p. 412.

text disregards the promotional or positive function of tax law, which has historically been used as an instrument of implementation and promotion".[45]

In the case of the Selective Tax, Adamy observes that it was conceived in a 'doubly limited' way, because on the one hand it only has a sanctioning function, aimed at burdening harmful operations and, on the other hand, because it is restricted exclusively to goods and services harmful to health and the environment, removing the possibility of levying harmful practices in other equally relevant [46]sectors. For the author, this restriction implies an impoverished understanding of extra-taxation, which reduces its scope to a merely repressive instrument[47].

These criticisms are directly connected to the following discussion about the relationship between neutrality and extra-taxation in consumption taxation. Neutrality, understood as a guiding principle of the Tax Reform, seeks to avoid economic distortions and ensure uniform treatment between sectors.

However, when taken to the extreme, it can collide with the extra-fiscal function, which requires flexibility and differentiation to promote constitutional objectives. Thus, the dilemma of a system that has accentuated rigidity and eliminated the space for promotion makes it necessary to analyze the tension between these two principles: neutrality and extra-taxation.

4 ANALYSIS OF THE OPPOSITION OR COEXISTENCE BETWEEN EXTRA-TAXATION AND NEUTRALITY

On the one hand, as seen, neutrality advocates that taxation should not distort consumption decisions and the organization of economic activity, keeping away from private choices and ensuring that the tax system does not cause an environment of competitive imbalance. On the other hand, extra-taxation seeks to influence the behavior of economic agents, either to discourage practices considered harmful or to promote socially desirable conduct. The apparent contradiction between tax neutrality and extra-taxation deserves further analysis, especially in view of the transformations introduced by the Brazilian Tax Reform.

The first relevant observation is that the tension between neutrality and extra-taxation does not derive from a conceptual incompatibility, but rather from specific tax *design* choices. When collection, economic neutrality and behavioral induction functions are concentrated in the same tax, conflicts and distortions are inevitably created.

[45] Ibid., p. 419.
[46] Ibid., p. 421.
[47] Ibid., p. 422.

The Brazilian pre-reform tax system exemplified this problematic overlap: the ICMS, originally conceived as a tax on consumption, accumulated collection, extra-fiscal and regional policy functions, resulting in excessive complexity, tax war and significant economic distortions.

International experience shows, however, that neutrality and extra-taxation can coexist harmoniously when there is a clear functional division between taxes. Mature tax systems often combine broad-based neutral taxes (such as European VAT) with specific non-fiscal taxes (such as the so-called *sugar tax* in the UK – *Soft Drinks Industry Levy – SDIL*)[48]. This specialization allows each tax instrument to fulfill its specific function without compromising the effectiveness of the others.

The Brazilian Tax Reform adopted precisely this logic of functional division. The constitutional design establishes a tax architecture in which different taxes assume specialized roles, so that the IBS and CBS must operate under the principle of neutrality, while the Selective Tax concentrates the extrafiscal function.

In addition, other taxes that are known to be extra-fiscal maintain their roles, such as the IOF and the Import Tax, as well as other taxes that, although primarily fiscal, are often used for behavioral induction purposes (such as the zero IPVA rate for electric cars adopted by some states).

This functional division is expressly enshrined in the constitutional text and in infra-constitutional legislation. Article 156-A, § 1, item X, of the Federal Constitution, prohibits the granting of tax incentives and benefits related to the IBS (also applicable to the CBS, according to article 195, item V, § 16), "*except in the cases provided for in this Constitution*". This provision, regulated by article 2 of Complementary Law No. 214/2025, establishes that "*the IBS and the CBS are informed by the principle of neutrality, according to which these taxes must avoid distorting consumption decisions and the organization of economic activity*".

At the same time, the extra-fiscal nature of consumption taxes was not abolished from the system, but directed to specific instruments. As Folloni observes[49], the Selective Tax, provided for in article 153, VIII, of the Federal Constitution, assumes an extra-fiscal function when it is levied on goods and services that are harmful to health or the environment. The author argues that this competence cannot be understood as relating to a simple collection tax, because, if it were, it would violate the principles of ability to pay and tax equality, and should be interpreted as a genuinely extra-fiscal and selective tax[50].

[48] It is a tax with an ad rem rate for beverages with high sugar content.
[49] FOLLONI, Op. Cit., p. 624.
[50] Ibid.

The Tax Reform, therefore, did not eliminate extra-taxation, but promoted its systemic reorganization, concentrating the extra-fiscal function in the Selective Tax and preserving other tax instruments for promotional purposes. This coexistence, through functional specialization, has obvious advantages.

First, it provides greater clarity to the objectives of each tax, facilitating both application and jurisdictional control. Second, it reduces the complexity of the consumption tax system, eliminating the multiple rates, special regimes and exceptions that characterized, for example, the ICMS. Complementary Law No. 214/2025 operationalizes this simplification through a system of reference rates (article 18) and specific regimes. Third, it enhances the end or reduction of the tax war between federated entities (in line with the principle of destiny[51]), which used tax benefits as instruments of competition for investments, compromising federative harmony. The neutrality of the IBS and the CBS, established in article 2 of the aforementioned complementary law, eliminates this possibility by prohibiting differential treatment not provided for in the constitution.

The neutrality of the IBS and CBS also contributes to greater economic efficiency. By eliminating tax distortions in consumption and business organization decisions, these taxes allow the allocation of resources to be determined by economic efficiency criteria, not by tax considerations. This represents a significant advance towards a tax system that is less distortive and more compatible with economic development, especially when considering that the Tax Reform promises full non-cumulativeness (article 156-A, § 1, VIII, of the Federal Constitution), with a broad financial credit system, effectively eliminating the cascade effect, which characterized the previous system.

However, this coexistence architecture is not without important limitations. The main criticism formulated by Adamy, already pointed out previously and deepened here, is directed at the loss of the promotional function in the taxation of consumption. The author observes that "the Tax Reform on consumption taxation, by changing the constitutional tax system, modified and, to a large extent, subverted the foundations of extrataxation".[52]

According to Adamy, the Selective Tax has a strictly sanctioning nature, aimed at discouraging harmful practices (especially related to the environment and health), but without the ability to promote beneficial behaviors[53]. This limitation contrasts with the previous system, in which differentiated rates and tax benefits could be used to encourage sustainable practices, support strategic sectors, or promote social policies.

[51] The collection will pass from production to consumption, that is, to the States and Municipalities in which the consumers of the product or service are located.
[52] ADAMY, Pedro. Extrafiscality in Tax Reform. Op. Cit., p. 410.
[53] Ibid.

In addition, the Reform institutes what this author calls "*rigid essentiality*" or "*closed essentiality*", with a list of goods, services, activities and sectors that will have different treatment, to the exclusion of any others, no matter how relevant they may be. This rigidity can compromise the ability of the tax system to adapt to changes in social demands and public policy priorities[54].

The author also argues that "by instituting a rigid or closed essentiality, with an exhaustive enumeration of the goods, services, activities and sectors that will have the most beneficial treatment, to the exclusion of all others, however essential they may be considered", the Reform drastically limited the promotional function of tax law, overemphasizing the sanctioning function of extra-taxation[55].

The express prohibition on tax benefits in the IBS and CBS may also generate future tensions. Political pressures for differential treatment of certain regions, sectors or activities are predictable, especially in a country with the regional inequalities of Brazil and whose Federal Constitution, in its article 3, III, establishes that one of the fundamental objectives of the Federative Republic of Brazil is the reduction of regional inequalities. The maintenance of the neutrality of these taxes will depend on the ability of institutions – especially the Supreme Court – to preserve the constitutional architecture against attempts at erosion through extensive or creative interpretations.

Another challenge is related to the effectiveness of tax neutrality itself. Although the Tax Reform has inserted the principle in a much more emphatic way than in the previous regime, the fact is that, until now, "tax neutrality has been understood at its minimum level by the Federal Supreme Court", [56]and the application of this principle by the Judiciary[57] to declare the unconstitutionality of a certain tax benefit is absent, characterizing, until then, as a theoretical ideal.

The sustainability of systems based on the functional division between neutral and extra-fiscal taxes depends on institutional and political factors. The Tax Reform represents a bet on the ability of institutions to maintain systemic coherence in the face of pressure from interest groups. The success of this architecture will depend on the ability to channel demands for sectoral public policies to other instruments – tax or not – without compromising the neutrality of taxes on consumption.

Finally, it is important to recognize that the coexistence between neutrality and extra-taxation through functional specialization represents a choice that implies trade-offs: one

[54] ADAMY, Pedro. Extrafiscality in Tax Reform. Op. cit., p. 412 and 428.
[55] Ibid, p. 429
[56] MOREIRA, André Mendes. **Neutrality, added value and taxation**. Belo Horizonte: Forum, 2019. p. 211.
[57] KOCH, Mariana Porto, Op. cit., p. 83.

gains in simplicity and efficiency, but loses in flexibility for public policies. As Adamy summarizes, "in the case of extrafiscality, the (constitutional) amendment came out worse than the sonnet",[58] indicating that, despite these aforementioned gains, the promotional function of extrafiscal is lost.

This tension reflects political choices. The Brazilian Tax Reform, at first, chose to privilege economic efficiency and operational simplicity to the detriment of flexibility for sectoral public policies, concentrating the extrafiscal function on consumption taxation in the Selective Tax and tax neutrality in the IBS and CBS.

5 CONCLUSION

The conclusion that emerges from the analysis of the present study is that tax neutrality and extra-taxation are not necessarily antagonistic norms, but can coexist harmoniously when there is a clear division of functions between different taxes. The Tax Reform operationalized this coexistence in an innovative way, establishing a system in which neutral taxes (IBS and CBS) coexist with specific extrafiscal instruments (Selective Tax).

The success of this architecture, as seen, will depend on the ability of institutions, especially the Federal Supreme Court, to preserve the functional specialization of taxes, resisting pressure from interest groups for exceptions that may compromise systemic coherence.

Although this solution has limitations in terms of flexibility for public policies, it represents a significant advance towards a more efficient, simple, and less distortive tax system. The ability to adapt to new social demands will be conditioned to the use of other tax instruments or to the eventual constitutional revision of the exhaustive lists established by Constitutional Amendment No. 132/2023.

It is noted that neutrality, as a constitutional principle, should not be understood as state indifference, but as a guarantee of equal treatment and economic efficiency. Extrataxation, even if delimited, continues to play an essential role in the correction of externalities. The coexistence between both norms requires institutional safeguards: (i) clear and justified exceptions; (ii) periodic review mechanisms; (iii) transparency in political choices; and (iv) jurisdictional firmness to contain interpretative erosions.

Thus, in summary, the study demonstrated that the Brazilian Tax Reform promoted a reconfiguration of the relationship between neutrality and extra-taxation. By reserving neutrality for broad-based taxes (IBS and CBS) and concentrating extra-taxation in the Selective Tax, the legislator sought to eliminate historical distortions, reduce litigation and end

[58] ADAMY, Pedro. Extrafiscality in Tax Reform. Op. cit., p. 430.

the tax war. However, this design reduced the flexibility for the promotion of public policies, limiting extra-taxation to a predominantly sanctioning function.

The Brazilian Tax Reform, therefore, did not eliminate the tension between neutrality and extra-taxation, but reorganized it systemically, creating a model adequate to the needs of a modern and complex economy, although at the cost of greater rigidity in the implementation of sectoral public policies through taxation on consumption.

Thus, the central conclusion is that neutrality and extra-taxation are not antagonistic norms, but complementary dimensions of the same system. When articulated in a balanced way, they can ensure simplicity and efficiency without abdicating the social function of the tax, making Brazilian taxation on consumption more rational, predictable and fair.

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