

COMMENTS

Fiscal Federalism and Intergovernmental Distribution of VAT in BRICS Countries

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<https://doi.org/10.21684/2412-2343-2026-13-2-208-231>

Received: September 10, 2025

Reviewed: November 5, 2025

Accepted: March 6, 2026

Abstract. The article suggests a comparative analysis of the legal framework for the distribution of value added tax between different levels of the budget in the BRICS states—Brazil, Russia, India, China, and the Republic of South Africa. The aim of the study is to identify general patterns and unique national models that have developed in the context of federal or decentralized state structures. Drawing on an analysis of the constitutional norms and the tax and budget legislation of these countries, the author identifies three main approaches. China demonstrates a centralized model where equal sharing of VAT revenues is combined with a system of strictly targeted redistribution of funds for the implementation of economic development plans. India exemplifies a cooperative model based on joint decision-making by the centre and the states through a special council and an independent commission that set out detailed distribution formulas. Brazil and South Africa can be seen as opposite poles. The Brazilian system, owing to the detailed constitutional entrenchment of state rights, is characterized by internal contradictions and stagnation, whereas the South African system is marked by strong centralization and the passive dependence of provinces on grants. The article emphasizes that, despite the differences, all countries face similar problems: the need to bridge the gap between regional revenues and expenditures, reduce territorial inequality, and create effective incentives for the development of the local economy. The author using the comparative analysis makes contribution to the Russian model, i.e., to avoid extreme models, develop a system that combines stable regional revenues with nationwide oversight, and gradually

transform financial assistance to territories into an instrument for stimulating specific socio-economic development. The scientific contribution of the research lies in a comprehensive comparison of the legal frameworks for VAT distribution in the largest developing economies of the BRICS group, which makes it possible to identify strategic guidelines for improving intergovernmental fiscal relations.

Keywords: fiscal federalism; VAT; GST; legal regulation; BRICS; taxation; budgetary; equalization.

To cite: Bachurin, D. (2026). Fiscal federalism and intergovernmental distribution of VAT in BRICS countries. *BRICS Law Journal*, 13(2), 208–231.

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Introduction

Comparative experience indicates that, in the contemporary period, the federal form of state organization exhibits the most consistent trend of development among alternative territorial models. In this regard, the American political scientist D. Elazar introduced the “federalist revolution” concept, stating that one of the main dominants of the modern society development is the process of federalization of unitary states, which makes it possible to reconcile a unified framework of governance with a sufficient degree of self-government for constituent units.

Daniel Elazar’s concept of federalism, which views it as a principle of balance between unity and self-government, can be used as a key analytical framework for studying VAT distribution models in BRICS countries. The specific mechanisms for crediting VAT to budgets of different levels in each of these countries reflect their unique search for an optimal balance between centralized revenues and regional autonomy in conditions of economic diversity and integration processes.

The legal regulation of the intergovernmental distribution of VAT directly reflects the state of the balance Elazar wrote about. On the other hand, the procedure for crediting or sharing this revenue between levels of government (entirely to the central budget, in fixed shares to regional budgets, or at the place of origin) determines the degree of financial autonomy of the regions.

The latter delegate to the federal center that volume of political, economic, financial and managerial functions that cannot be effectively performed, creating “checks and balances” against the dangers of excessive centralization and decentralization, bureaucratic dictatorship and universal anarchy.

It is important, however, to consider the fact that federal and decentralized structure by itself does not guarantee either social harmony or budgetary efficiency. A federal system of VAT distribution can create opportunities for greater accountability and consideration of regional specifics, but it can also give rise to problems of “vertical” and “horizontal” imbalances in budgetary distribution, conflicts over the tax base, the creation of regional “enclaves,” or, conversely, excessive financial dependence of regions on the center.

Attention should be paid to the conclusions of Ebrill, Keen, Bodin and Summers, who suggest that, in general, “the center shares the additional revenues associated with VAT with lower levels of government by canceling other taxes.”¹ In their opinion, “VAT has managed to become such a powerful tool precisely because its introduction largely determined the model of functioning of the tax-distribution system as a whole,” and “understanding the distributive function of VAT, taken separately, should be part of an overall strategy aimed at reducing poverty.”²

A comparative analysis of VAT distribution in BRICS states reveals how different political systems solve the common task of ensuring an acceptable balance between fiscal centralization and regional autonomy, using tax-budget federalism as a financial management tool to ensure economic development.

The complexity of this objective lies primarily in the fact that it is very difficult to analyze all aspects of existing models of fiscal federalism. Every model of fiscal federalism has its own specific features, determined by the specifics of historical, political, economic, and cultural development of the country. Comparing, in particular, fiscal federalism in individual BRICS states reveals both similarities and significant differences.

Accordingly, this study focuses on the legal regulation of the intergovernmental distribution of value-added tax revenues, which constitutes one of the key dimensions of fiscal federalism in all BRICS countries. Placing this issue in the context of the historical development of each country’s federal system and its constitutional entrenchment in the state’s basic law helps generate insights needed to further improve the legal framework for intergovernmental revenue allocation. The analysis

¹ Ebrill, L., et al. (2003). *Modern VAT* (p. 46). Ves Mir. (In Russian).

² Ebrill et al., 2003, p. 129.

also takes into account not only the tax legislation and the structure of value-added taxation, but also the basic and additional elements of the tax. The author gives particular attention to informal norms, conditioned by the national specifics of relations in the super-system “human-society-power,” sociocultural values and practices existing in the BRICS states.

1. Centralized Model of Intergovernmental VAT Distribution in the People’s Republic of China

Historically, China has carried out territorial-administrative differentiation, when each dynasty practiced the division of provinces and territories according to various factors and standards, such as the area of governance, population size, the amount of taxes and the complexity of administrative issues: the Qin and Han dynasties classified territories by their size; the Tang and Song dynasties mainly divided counties into “Chi, Ji, Wang, upper, middle and lower” depending on political status and economic power; during the Ming dynasty, both traditional and simplified methods of division into prefectures and counties were applied; the Qing dynasty revised the standards for territorial division, applying a comprehensive approach.

Since each new division of the country was accompanied by almost universal reassignment of bureaucracy, the rulers of China tried to announce the reasons for the ongoing administrative-territorial transformations. In particular, Emperor Muzong of the Ming Dynasty noted in a corresponding decree that “the complexity and simplicity of prefectures and counties vary and the difficulties are different.”

The current Chinese leadership also seeks to strengthen bureaucratic incentives by reforming cadre evaluation systems and by publicly defining and disseminating the country’s development objectives. Authors note that the reforms that began in China in the early 1980s were efficient due to the empowerment of local authorities and the encouragement of local experiments. In this period, the origins of federalism can be traced in the gradual differentiation of powers between central and regional authorities. In institutional terms, an important foundation of the China’s successful economic reform has been “federalism, Chinese style”—a form of market-preserving federalism that supports the development of market relations.³

The advancement of tax-sharing reform exemplifies a power of ‘fiscal federalism’ that promotes economic development.⁴ Intergovernmental tax sharing and subnational

³ Montinola, G., Qian, Y., & Weingast, B. R. (1996). Federalism, Chinese style: The political basis for economic success. *World Politics*, 48(1), 50–81; Qian, Y., & Weingast, B. R. (1997). Federalism as a commitment to preserving market incentives. *Journal of Economic Perspectives*, 11(4), 83–92; Cai, H., & Treisman, D. (2006). Did government decentralization cause China’s economic miracle? *World Politics*, 58(4), 505–535.

⁴ Lin, J. Y., & Liu, Z. (2000). Fiscal decentralization and economic growth in China. *Economic Development and Cultural Change*, 49(1), 1–21.

fiscal systems become critical elements of governance that are consistently enshrined in policy documents of central authorities, reflecting a systematic approach to solve the dilemma between centralizing financial resources to implement national priorities and the need to ensure fiscal decentralization to stimulate regional development.

The State Council's Decision "Implementation of Comprehensive Financial Measures at the Local Level," adopted in 1988, is aimed at stabilizing financial relations between the central government and local authorities. In 1993, the State Council of the PRC adopted the Decision "Introduction of a Financial Management System with Tax Sharing," the main goal of which is to promote the country's long-term stability and sustainable economic development.

In 2013, at the third plenary session of the 18th Central Committee of the Communist Party of China, it was proposed to deepen the reform of the tax system and improve the local tax system. After increasing the share of VAT in local budgets, this tax became the main source of income for local authorities.

Issues of further improvement of distribution relations between the center and local authorities reflect the guiding ideology of tax distribution issued by the State Council in 2016, when the share of local revenues from value-added tax is appropriately increased, which helps mobilize financial resources locally and improve the current economic situation.

In the Chinese system of intergovernmental fiscal relations, the basic element of the distribution of tax potential becomes the principle of equal proportional (50/50) sharing of VAT revenues between the central and consolidated regional budgets. This principle performs not only a fiscal-distributive but also a crucial motivational function, integrating the interests of the center and the provinces. It was legislatively confirmed in 2019 during the VAT reform with a reduction in the tax burden. At the same time, the strategic task is to enhance the stimulating role of the tax by strengthening the link between the economic efforts of the regions and the revenue base of their budgets. However, the need to direct funds to support underdeveloped regions did not allow this task to be fully realized.

For this reason, the established principle was implemented through a complex, multi-stage redistribution system established by the financial and tax authorities of the Peoples Republic of China (PRC).⁵ The share of VAT (50%) assigned to the regional level of government is divided according to the rule of joint use, when 15% of the total VAT amount is directly credited to the budget of the administrative entity at the place of registration of the taxpayer, and the remaining 35% is subject to secondary redistribution by the Ministry of Finance of the PRC among provincial budgets.

⁵ "Notice on Adjusting and Improving the Local Mechanism for Sharing Value-Added Tax Revenue and Related Budget Management Issues," issued by the Ministry of Finance, the State Taxation Administration, and the People's Bank of China, which came into effect on September 1, 2019, stipulates that the 50% share of value-added tax revenue allocated to the local budget is to be distributed according to the rules of shared use.

The final calculation is made taking into account tax refunds to taxpayers. This approach, being derived from the complex VAT administration system involving significant and often deferred refunds, creates an additional level of conditionality in the formation of regional revenues. The actual volume of financial resources at the disposal of local authorities turns out to be dependent not only on economic activity in their territory but also on the results of national fiscal policy and the efficiency of the tax apparatus in processing VAT refund applications.

The created model objectively forms less favorable conditions for individual economically successful regions, since a significant part of the fiscal result they generate is redistributed in favor of less developed territories. However, from a macroeconomic and strategic point of view, such a system ensures more balanced development in the country.

It combines two key elements: first, preserving a direct financial interest for regions in building up their own tax base through a direct link between part of their income and local economic activity, and second, retaining powerful levers of centralized budget regulation. These levers allow the central government to concentrate resources on priority areas of spatial development, equalize basic conditions in lagging regions, and implement large-scale national projects, which would be impossible under conditions of full fiscal autonomy of the territories. Thus, the effectiveness of the model is assessed not from the standpoint of maximizing the income of an individual region, but from the point of view of achieving long-term national goals.

The instrument of this policy is special financial transfers, which perform not so much a compensatory as a stimulating function. They are formalized as development contracts between the center and provinces, where funding is linked to the achievement of specific indicators of economic growth, infrastructure development and increased tax potential. The transfer acts as start-up capital, creating a direct interest for regional authorities in fulfilling the conditions as soon as possible to receive the next stage of investment support.

The most important feature of the Chinese model is the combination of vertical and horizontal mechanisms for resource redistribution. In addition to a developed system of targeted transfers from the center, China actively encourages direct investment and cooperation projects between developed eastern and developing western provinces. Such practice creates additional channels for the flow of capital and technology without excessive centralization of financial flows and forms sustainable networks of mutual economic interest.

This stands in contrast to the Russian system, in which intergovernmental relations are structured predominantly along a vertical 'power-vertical' hierarchy, with only limited horizontal interaction among regions. The potential for horizontal equalization is not utilized, for example, through the tax deductions for interregional investments or joint infrastructure projects, where part of the tax generated as a result of joint projects could remain in the budgets of partner regions.

Particular attention should be paid to the Chinese experience in creating experimental zones with special budgetary and tax powers (for example: Shenzhen, Chongqing, Hainan, Hong Kong, Zhuhai), which were delegated the right to test their own models of tax and budget regulation. This made it possible to develop effective mechanisms for stimulating investments and administering a mobile tax base, the main part of which was added value, with subsequent scaling of successful practices at the national level.

Russian analogues in the form of territories of advanced development (TAD) or special economic zones (SEZ) are, as a rule, point-based and fragmented in nature, focused on providing an individual set of benefits without transferring real fiscal prerogatives and without applying their results in the systemic budgetary policy of the state.

In summary, the thirty-year history of improving the intergovernmental distribution of value-added tax revenues has a significant positive impact on the goals of increasing created value added (GDP) and investments. Unlike non-equivalent subsidiary encouragement, the tax incentive system represented by flexible tax distribution is a significant motivation for local authorities to promote economic growth. Analysis of empirical data indicates that tax incentives account for 17.98% of local economic growth and 31.63% of growth in local investment.⁶

These institutional changes are aimed at creating a stable and predictable system of intergovernmental relations capable of adapting to the requirements of a dynamic market economy and global economic competition.

The described features of intergovernmental VAT regulation reflect the logic of China's industrial economy. The advancement of digital technologies creates the basis for the transition to a fundamentally different tax-budget distribution of value added. The emerging digital architecture opens up opportunities for moving from complex multi-stage VAT redistribution rules to systems of direct, transparent and adaptive fiscal regulation based on big data analysis in near real-time.

Turning to the Chinese experience in organizing intergovernmental relations opens up strategic guidelines for creating a Russian model for distributing value-added tax revenues between levels of the budget system. Although Russia and China, within the BRICS framework, have similar macroeconomic targets of spatial development, their approaches to budget regulation demonstrate fundamental differences. The Chinese model evolved from uniform subsidization of territories to creating targeted growth poles based on the principle of temporary support for a future leap.

The main feature of the Chinese system is its focus on results and the presence of feedback. The model is built on the principle of development through responsibility,

⁶ Lu, B., & Chen, Y. (2022). Fiscal incentive system and promotion: An institutional debate on the driving forces of growth. *China Industrial Economics*, 2022(6), 25–43. (In Chinese).

where failures in program implementation lead not to their termination or automatic increase in funding, but to a revision of methods, tighter control, or adjustment of contract terms.

As strategic conclusions for the Russian system, the following directions for adapting Chinese principles can be proposed.

First, it is necessary to abandon the paternalistic tradition and transition to a partnership concept of intergovernmental relations, implying that the center and regions are jointly responsible for achieving measurable results of spatial development.

Second, a reform of the legal regulation of the intergovernmental distribution of VAT is required, providing for the introduction of targeted “development” transfers, part of which can be financed from the centralized share of VAT, with clear key performance indicators and conditions for their phased reduction as goals are achieved.

Third, institutional development should include the creation of full-fledged experimental regimes with expanded budgetary and tax powers, focused on improving and subsequently replicating new models.

Fourth, it is important to stimulate horizontal links through tax and budgetary instruments that encourage interregional investment projects.

Thus, the strategic lesson from China is that effective budgetary equalization is not an end in itself but part of a comprehensive spatial development strategy based on tax-budget incentives, mutual responsibility, and continuous institutional experimentation.

2. Cooperative Model of Intergovernmental VAT Distribution in the Republic of India

The Indian model of legal regulation of the intergovernmental distribution of the Goods and Services Tax (GST), which replaced cascading taxes, is a unique example of cooperative federalism in conditions of regional diversity. Unlike the hierarchical Chinese system, its core is an institution of constant negotiation between the center and the states.

An example of the negotiated overcoming of contradictions between different levels of government is the adoption of the new model of legal regulation of value-added taxation in the form of the Goods and Services Tax (GST) during the midnight session of both houses of parliament on June 30–July 1, 2017. The bill was boycotted by the opposition for a long time due to alleged problems for middle- and lower-class Indians. The tax was opposed by members of the Indian National Congress, Trinamool Congress, Communist parties of India and the Dravida Munnetra

Kazhagam,⁷ who argued that the introduced tax would increase rates on everyday goods while lowering rates on luxury items.⁸

As a result of the agreements reached, the Goods and Services Tax (GST) is a legal construction of double taxation combined with consolidated decision-making at the federal level. The legislator subdivides commercial transactions into intra-state and inter-state. Intra-state transactions are taxed by two parallel taxes: Central GST (CGST), the revenues from which are fully credited to the Union budget, and State (SGST), which goes entirely to the budget of the respective state.

Thus, for an intra-state transaction, the total tax burden is divided equally between the center and the region. For transactions extending beyond the borders of one state, including imports, an Integrated Tax (IGST) is introduced, administered exclusively by the central government. The legal distinction of IGST is the subsequent mechanism of intergovernmental splitting: the collected funds are ultimately also distributed equally between the center and the consuming state (the destination of the goods/services), which legally enshrines the principle of taxation at the place of consumption, not production.

The main body of legal regulation in this system is the GST Council, constitutionally established under Article 279A. Its composition, including 33 members (2 representatives of the center and 31 representatives from states and union territories), formally reflects the principle of broad regional representation. However, the voting formula enshrined in the Constitution of India creates a paradoxical legal situation. Although the states collectively possess two-thirds of the votes, and the center only one-third, the approval of any decision requires a three-quarters majority. This mathematical construction ensures the central government's *de facto* veto power, since its share of 33.3% of the votes exceeds the threshold of 25% needed to block a decision. Thus, even with a consolidated position of all states, the center alone can reject any proposal to change rates, administration rules, or revenue distribution. This creates an asymmetry in legal regulation. The formal cooperative dialogue in the Council exists within a rigidly structured legal scheme guaranteeing the fiscal control of the center, yet it provides a balance of interests and sufficient legitimacy for the decisions.

The legal principles for distributing GST tax revenues among states are formulated by the Finance Commission, which develops its recommendations every five years. The formula enshrined in its decisions takes into account various criteria: demographics (15%), territory (15%), tax efforts of states (14%), and, what is particularly noteworthy,

⁷ Hindustan Times. (2017, June 30). *GST launch: Times when the Parliament convened for a session at midnight*. <https://www.hindustantimes.com/india-news/gst-launch-times-when-the-parliament-convened-for-a-session-at-midnight/story-c55g94ewrOMefUvQJVFSEO.html>

⁸ NDTV. (2017, June 29). *Congress to boycott GST launch, Arun Jaitley suggests broader shoulders*. <https://www.ndtv.com/india-news/manmohan-singh-will-not-be-on-stage-at-midnight-goods-and-services-tax-gst-launch-1718417>

the level of forest cover (2.5%) as an environmental parameter that has no direct analogues in the legal systems of other BRICS countries. The greatest weight (47.5%) in the formula is given to equalizing budgetary capacity.

An important transitional legal institution is the GST Compensation Cess Fund, created for the first five years of the reform (2017–2022) to guarantee compensation to states for potential revenue losses. Sharp political and legal discussions about its extension in 2022 led not only to the decision to establish a new transitional period until 2026 but also provoked resistance from the power elites of the states, which finds support in the judiciary.

On May 19, 2022, the Supreme Court of India upheld the verdict of the Gujarat State Court that the government cannot levy IGST on imports of sea cargo. In its decision, upholding the importance of ‘cooperative federalism’ for the well-being of democracy, the court ruled that the Union and state legislatures possess equal, simultaneous and unique powers to make laws on the Goods and Services Tax (GST), and the recommendations of the GST Council are not binding on them.

The bench headed by Justice D.Y. Chandrachud stated that the recommendations of the GST Council are the result of a collaborative dialogue involving the Union and the States and are recommendatory in nature. The recommendations have only persuasive value. To regard them as binding would disrupt fiscal federalism, where both the Union and the States are conferred equal power to legislate on GST.

The court emphasized that Article 246A of the Constitution of India, which gives states the power to enact laws on GST, treats the Union and states as equal units, and although in certain cases the Center may possess a greater share of power to prevent chaos and ensure security, states still possess power.⁹

The decision creates a serious precedent that clearly allows for the correction of the GST Council’s policy and expands the scope of judicial control over its provisions.

Current legal challenges in the sphere of intergovernmental VAT distribution are directly related to the digital transformation of the Indian economy and the need to adapt fiscal federalism to new realities. The rapid growth of the digital services sector has exacerbated the problem of determining the place of taxation for a mobile tax base. Leading IT states (Karnataka, Telangana) insist on revising the VAT distribution rules, arguing that the current norms do not account for their contribution to creating value added in the digital ecosystem, which is consumed throughout the country. In response, the possibility of introducing special digital levies or adjusting the GST distribution formula is being discussed.

Simultaneously, the legal regulation of GST is evolving to address environmental issues. Experimental initiatives by individual states regarding ‘green transfers’, where

⁹ Rajagopal, K. (2022, May 20). *Supreme Court says Centre, States have equal powers to make GST-related laws*. The Hindu. <https://www.thehindu.com/business/Economy/recommendations-of-gst-council-not-binding-on-centre-states-supreme-court/article65429432.ece>

the volume of financial assistance to local authorities is linked to achieving target environmental indicators, may form the basis for future pan-federal legal norms.

An important aspect of the legal regulation of GST has been the institutionalization of adaptation mechanisms to crises. The COVID-19 pandemic revealed the limitations of existing norms when a sharp drop in state revenues amid growing expenditure obligations required emergency fiscal solutions. The response was not so much a point-based legal adjustment of the distribution formula as an increasing role of the center in providing targeted emergency transfers and a temporary easing of budgetary rules for states. This experience indicates that the legal system for distributing tax revenues, even as detailed as the Indian one, must contain built-in tools for operational response to shocks while preserving the basic foundations of the federal structure.

The Indian model offers a unique legal precedent for the public coordination of interests of heterogeneous federal subjects through a permanent negotiating body (the GST Council) with clearly defined decision-making rules. For Russia, where dialogue between the center and regions on tax issues is often more informal and consultative, the Indian experience could be useful for creating a comparable public-law institution for tax governance.

India's legal innovations in accounting for environmental criteria (share of forest cover) and experiments with "green transfers" are of conceptual interest to all countries seeking to integrate wildlife conservation goals into their intergovernmental regulation system.

Prospects for the development of legal regulation in India are seen in further digitalization, which inspires new legal norms. The introduction of the e-invoicing system and the development of the GST Network platform create a technological basis for a possible transition to more complex legal models of revenue distribution, for example, based on tracking value chains in real time. This could lead to the evolution of rules based on aggregated macroeconomic indicators towards more precise and dynamic legal distribution principles that resolve disputes about the place of origin of the tax liability.

Simultaneously, legal regulation is forced to respond to challenges generated by digitalization. The creation of a centralized technological platform (GST Network) led to the emergence of a vast array of data on the financial and economic operations of GST payers. Access to aggregated transaction data in real time becomes a powerful tool, changing the balance of power.

The center, having exclusive access to this information, gains unprecedented opportunities for analysis and control, allowing it to influence the negotiating positions of states. Therefore, the next stage of legal development may be the formulation of exact norms regulating data rights, their confidentiality, and the procedure for their use for intergovernmental settlement purposes, so that technological superiority does not turn into a tool of the center's fiscal dictate.

Ultimately, the legal evolution of the Indian model of intergovernmental GST distribution demonstrates that for the sustainability of fiscal federalism, it is necessary to create adaptive legal institutions. These institutions must perform three functions: (1) to ensure continuous dialogue between levels of government (GST Council), (2) to offer expert-based and fair distribution principles (Finance Commission), and (3) to possess legal tools for integrating new priorities, like ecology or digitalization. They balance between the need to maintain a single tax space through the development of consensus decisions by the GST Council and the trend toward flexible, multi-factor equalization through the recommendations of the Finance Commission.

India's case confirms that there is no perfectly completed model of intergovernmental VAT distribution. What we observe instead is an ongoing process of legislative adjustment designed to ensure that the fiscal system functions as an instrument of development rather than a source of conflict, in the context of an increasingly diverse and dynamic economic environment.

For other BRICS countries, including Russia, India's intergovernmental GST distribution is an interesting example of building a complex system of legitimate and constantly adapting dialogue between the center and regions, as well as a laboratory for searching non-standard solutions made under new factors (ecology, digital economy) within the logic of budgetary equalization.

3. Legal Frameworks of Intergovernmental VAT Distribution in the Federative Republic of Brazil

Brazil is a three-level federation consisting of 24 states, two federal territories, a federal district, and 4,300 municipalities. The evolutionary path of Brazilian federalism can be clearly divided into several stages depending on the model of competence distribution between the federal center and the provinces. A defining feature of this process is the confrontation between centrifugal and centripetal trends. Among the significant factors that have transformed the models of Brazilian federalism are the processes of centralization and decentralization, as well as the activities of the state's highest judicial bodies, authorized to interpret constitutional norms and review existing legislation for compliance with them.

The legal regulation of value-added taxation in Brazil is an example of constitutionally enshrined, yet extremely complex and fragmented fiscal federalism. The country's federal structure, comprising the union, states, federal districts, and thousands of municipalities, is directly reflected in a tax system where the authority to levy and administer indirect taxes is divided among all levels of government. The 1988 Constitution, which granted subnational units broad autonomy, meticulously regulates both the list of taxes and the principles of their distribution, creating legal barriers to unconstitutional changes in the sphere of intergovernmental VAT distribution.

These features have resulted in a specific form of federalism, typical for Brazil. It combines aspects of American federalism, with its principles of territorial separation of power between the federal center and federation subjects possessing significant authority and financial resources, and a well-established mechanism for regulating conflicts between levels of government. Its foundation is formed by structures of intergovernmental coordination, which include a historically developed network of institutions for reconciling mutually acceptable decisions for the federal center and the provinces. In the sphere of taxation, the body aimed at achieving mutual compromise is the Council of States (CONFAZ), which adjusts tax rates and specific rules for defining the tax base for the value-added tax (ICMS—Imposto sobre Circulação de Mercadorias e Serviços).

The problems were mainly related to sales taxes, as municipalities are independent from the states in their collection and are equated to them. The tax bases for the federal Tax on Industrialized Products (IPI) at the manufacturer level and the state-level value-added tax (ICMS) partially overlapped but were managed separately by these two levels. Similarly, the tax bases for ICMS and the municipal Service Tax (ISS) overlapped and were managed in an uncoordinated manner.

The constitutional rules governing the intergovernmental distribution of revenue from these taxes display a clear bias in favour of subnational governments, sharply distinguishing the Brazilian model from more centralized federations. Constitutional guarantees ensure significant shares of tax revenues for states and municipalities. For instance, 25% of ICMS collections are automatically transferred to municipalities. Furthermore, a complex system of participation funds (FPE and FPM) operates, according to which states and municipalities receive 47% of the revenues from federal income taxes and IPI.

Until 2025, states possessed one of the most dynamic revenue bases (ICMS), and municipalities were guaranteed a significant share of federal and state revenues. Unlike municipal authorities, the revenues of the federal center and state governments significantly lag behind their expenditure needs. Despite having one of the highest tax burdens among developing countries, reaching 32.3% of GDP in 2009 and 2016 and further increasing to 32.9% in 2021,¹⁰ Brazil cannot solve the problem of horizontal fiscal imbalance. Interregional differences in the socio-economic development of various parts of the country are excessively large. Per capita income in the state of Rondônia is only 12% of that in the richest state of the Union, São Paulo.

As a result, distribution analysis shows that provinces and municipalities accumulate the main mass of fiscal resources from consumption taxes, whereas the share of the federal center remains limited.

¹⁰ Ranking of countries by share of taxes in GDP. (n.d.). svspb.net. <https://svspb.net/danmark/nalogov-vvp-stran.php>. (In Russian).

Historically entrenched problems of Brazilian fiscal federalism¹¹ directly influence the modern reform of value-added taxation, the foundation of which was laid by Complementary Law No. 214, which came into force on January 16, 2025. The adoption of this law is the result of long political and expert debates aimed at overcoming the deep structural crisis of Brazil's indirect taxation system.

The substantive essence of Law No. 214 is the implementation of a constitutionally sanctioned replacement of five existing consumption taxes (federal PIS and COFINS, regional ICMS, municipal ISS, and federal IPI) with a single, unified two-tier value-added tax model. This reform aims to eliminate an archaic and extremely burdensome multiplicity of taxes, whose bases historically overlapped, creating a cascading effect, high transaction costs, and 'tax wars' between states. The law meticulously regulates the architecture of the new system, introducing from January 1, 2026, a federal Goods and Services Contribution (CBS—Contribuição sobre Bens e Serviços) and a State and Municipal Goods and Services Tax (IBS—Imposto sobre Bens e Serviços), as well as a selective tax (IS—Imposto Seletivo) on harmful goods.

While preserving the constitutional principle of dividing tax revenues between levels of government, the law fundamentally changes the very procedure of this division. A gradual transition is being made from a model of parallel and often conflicting administration of several taxes to a center-coordinated collection and distribution of revenues from unified CBS and IBS tax bases. This represents an attempt to overcome the key paradox of Brazilian fiscal federalism, which lay in the contradiction between the formal autonomy of subnational units and the need to ensure the country's economic unity. The success of implementing this fiscal project will depend not only on technical administration but also on the ability of all levels of government to engage in constant dialogue and coordination within the new institutional framework created by the law.

The law also establishes the legal framework for applying the Brazilian tax system to the digital economy. It introduces clear obligations for foreign suppliers of digital services without tax residency in Brazil to register with tax authorities, calculate, and pay VAT on transactions made for the benefit of Brazilian consumers. This norm, known as the "digital VAT" rule, aims to level the playing field between local and international companies. The law establishes the institution of joint and several liability, imposing additional control functions on payment system operators and electronic platforms, creating a multi-level mechanism for tax compliance.

Imposing control functions in the sphere of VAT collection on payment system operators and establishing corresponding tax obligations for foreign suppliers is aimed at creating an integrated legal ecosystem adapted to new economic realities. This resonates with similar efforts by other countries seeking to preserve

¹¹ Bachurin, D. G. (2020). The current state of legal regulation of VAT in the Federative Republic of Brazil: On the threshold of tax reform. *International Public and Private Law*, 4, 30–35. (In Russian).

fiscal sovereignty in conditions of capital and digital asset mobility. The Brazilian specificity lies in the fact that these new rules are being integrated into the process of internal tax transformation, creating additional potential for synergy in value-added taxation.

Particular attention should be paid to the regulation of the transition period up to 2033, which establishes a complex system of compensatory mechanisms and temporary tax credits intended to cushion the financial impact on states and municipalities as their revenues from traditional taxes (ICMS, ISS) are gradually replaced by receipts from the IBS. Simultaneously, the law introduces a moratorium on creating new tax incentives and exemptions at the subnational level, aimed at preventing “tax wars” during the transition period and preserving the integrity of the reform.

Thus, Complementary Law No. 214 represents a comprehensive legal instrument attempting to resolve the contradiction between federalism and fiscal efficiency by creating a new model of cooperative management of tax flows. If the old system relied on maximum fiscal autonomy for regions, which in practice led to chaos and “tax wars,” the new model preserves a significant share of total tax revenues for subnational authorities but fundamentally changes the mechanism of its formation, making it dependent on unified administrative rules and a unified tax base. Thus, the reform aims to create legal conditions under which the financial interests of states and municipalities begin to coincide with the task of strengthening the integrity of the national market, rather than contradicting it. In this way, legal regulation moves away from entrenching separateness and instead provides a platform for developing common rules governing intergovernmental VAT distribution.

In this sense, the Brazilian reform moves in the same logic as other BRICS countries but with its own reinterpretation of federal principles. This fits into the broader picture of the BRICS countries’ search for an optimal model of intergovernmental relations, in which each state, shaped by its own political history and economic structure, seeks to balance fiscal efficiency and territorial justice.

While India employs a complex but legitimate mechanism of constant negotiation between the center and states, and China ensures the unconditional priority of centralized strategic planning with elements of contractual responsibility of regions, Brazil is attempting to overcome the legacy of conflictual decentralization by creating unified rules of the game. The basic element here becomes a fundamental redistribution of roles in tax administration, where regions do not lose their revenue rights but are deprived of the ability to independently and uncontrollably determine the parameters of the tax base.

The Brazilian approach can be characterized as a model of coordinated revenue sharing, where the autonomy of subnational levels is ensured not by the right to establish their own taxes but by a guaranteed share in the receipts from a single tax, administered within strict federal standards. The extended transition period provided by the law is of particular importance. This legal measure reflects an understanding of the

need for gradual adaptation of the institutional environment that has developed over decades, the budgetary systems of states, and business practices, which is a critically important condition for maintaining stability during such a large-scale restructuring.

Comparative analysis shows that each of the large federal economies of BRICS is searching for its own path to balance between the poles of decentralization and centralization. The Brazilian reform represents a bold experiment to escape the trap of constitutional stagnation towards a more flexible and functional model of fiscal federalism. Its success will be judged by the stability of a system of incentives in which both the center and the regions will be objectively interested in the growth of the overall economy, not in individual benefits from redistributing limited resources. This case is important for Russia as a demonstration that even deeply entrenched institutional problems are amenable to solution through legal redesign. This path requires political will, careful elaboration of transitional mechanisms, and readiness for consistent implementation.

4. Russian Case of Intergovernmental VAT Distribution in 1992–2000

Debates on the efficient territorial organization of the state often point to an intermediate model that seeks to harmoniously combine federal and unitary principles of state-building. The most preferable form of government for Russia in the future may be a unitary state based on broad legislative autonomy for its regions. In Russian political and legal discourse, this intermediate model is frequently presented as one toward which the country has historically gravitated and as best reflecting the perceived essence and traditions of Russian statehood. It does not conflict with the fundamental principle of the state—sovereignty—and equally protects the state from the extremes of both federalism and hypertrophied centralism.

General global development trends create a tense-negative backdrop for the existence of the Russian Federation which will remain the main trend in the near future. It is jeopardized by the accelerated depletion of natural resources and environmental degradation, which in turn intensify international competition and heighten the risk of territorial disputes. These threats tend to displace integration in favour of coercive forms of rivalry. Under such conditions, the primary goal of Russia's policy and law is to ensure its survival and existence as a state.

Addressing such challenges is invariably difficult: it tends to push governance toward a more militarised paradigm and to require the central government to concentrate as much tax revenue as possible. In this context, the constitution should resolve the contradiction between the obligation to guarantee human and civil rights and freedoms and the need to ensure national security.¹² At the same time, there are substantial arguments against excessive centralization of tax revenues.

¹² Zorkin, V. (2009, April 10). Crisis of trust and the state. *Rossiyskaya gazeta*. (In Russian).

First, along with external threats, Russia faces a challenge to create a new model of a social state. What is critically important here is the capacity to sustain planned, balanced economic dynamics without overburdening society and the national economy, together with the country's regional particularities, which inevitably brings to the fore issues of fiscal federalism and the optimal allocation of the VAT base across levels of government.

Second, the main social functions (providing primary and secondary education, healthcare, social protection) in federal states are most effectively solved at the regional level, primarily from their own sources of funding. In solving social tasks, the federal center can only be an ideological inspirer, legislatively defining rules and standards. In practice, there have been repeated signs of resistance to initiatives implemented through "manual control" by the federal centre, and the difficulties with the so-called "national projects" are only one example of the limited effectiveness of such instruments.

Third, granting regional and local budgets their own tax sources of funding allows the nation not only to survive but also to carry out its expanded social, cultural, and scientific-technical reproduction, this way the federal center receives a sufficient stream of new achievements that contribute to strengthening the economy, the defense capability, and the spiritual uplift of the country. Conversely, remaining at a low level of well-being is fraught with the degradation of society, the worsening of its development conditions, and threatens the instability of the power. Until the early 1970s, under conditions of ideological monopoly, this instability was contained primarily through coercive methods. In the postmodern era, under conditions of ideological pluralism and militant tolerance, the instability of power is skillfully used by the opposition and foreign political forces interested in changing the ruling clan.

In this regard, the organization of the optimal distribution of the stable financial resource in the form of VAT between the federal, regional, and local budgets is not only closely related to the legal regulation of value-added taxation itself but also becomes one of the most important issues of state governance.

Historically, the Russian system has been structured around a logic of addressing regional underdevelopment, with federal transfers focused mainly on equalizing budgetary capacity and tending to take on an indefinite, dependency-creating character.

Crisis processes reveal the need to create self-sufficient regions of the Russian Federation, where economic independence and self-reliance are achieved through a transition from receiving external sources of sufficiency from the federal center to using internal resources.

As a basis for strengthening regional tax self-sufficiency within the existing tax system, the author can propose an intergovernmental VAT-sharing mechanism that operates through a split of the tax rate between levels of government. The legal regulation of the methodological support for such redistribution must be regulated

by stable laws,¹³ including legislative regulation of the rules for intergovernmental redistribution of VAT based on equal distribution of VAT between the federal center and the regions.

This is convincingly evidenced by the results of calculations for 83 subjects of the Russian Federation (excluding the Republic of Crimea and the city of Sevastopol), showing that over the period 2007–2018, with VAT shared in this way, there were 33 subsidized regions in 2007, 40 in 2013, 41 in 2016, and 45 in 2018.

The analysis results indicate that of the 18 financially self-sufficient regions not receiving federal subsidies in 2007, none remained by 2018; from 2007–2013, the number of regions with a negative VAT receipt balance increased and stabilized at a high level—in 12 regions in 2013, 9 regions in 2016, and 10 regions in 2018, the amount of VAT refund exceeded the amount of VAT payable to the budget.

The relatively successful experience of VAT sharing between the federal centre and the constituent entities of the Russian Federation in 1992–2000 also provides empirical support for this proposed approach. Unfortunately, it was complicated by the federal center restraining the initiatives of regional elites and limiting their funding sources. The dynamics of increasing financial constraint are reflected in the legislative change of proportions in VAT distribution between federal and regional levels of government.

Thus, during 1992–1993, six regulatory acts were adopted establishing standards for VAT deductions to regional budgets. Five of them were adopted by the Supreme Soviet of the Russian Federation, and only one act implements the powers of the Government of the Russian Federation to clarify deduction standards for individual regions in the III–IV quarters of 1992. During this period, parliament actively changed the standards for VAT deductions to the budgets of the regions of the Russian Federation, thereby exercising differentiated socio-economic management of territories. It is important to note that during 1993, parliamentarians found the ‘golden section’ in splitting VAT rates and established a predominantly equal distribution of VAT receipts for the federal center and most regions of the Russian Federation (57 subjects).

The Decree of the President of the Russian Federation of December 22, 1993, No. 2268 “The Formation of the Republican Budget of the Russian Federation and Relations with the Budgets of the Subjects of the Russian Federation in 1994” effectively removed parliament from the position of the main distributor of budget VAT receipts, ceased individual regulation, and introduced a single standard for VAT deductions of 25% (reduced to 15% in 1999–2000). In 2001, the intergovernmental distribution of VAT ceased, and a centralized regime of 100% crediting of tax receipts to the federal budget was established.

¹³ Bachurin, D. G. (2016). The impact of political and socio-economic factors on the formation of theoretical and methodological approaches to the legal regulation of the distribution of VAT revenues. *Innovative Development of the Economy*, 3(33), 155–160. (In Russian).

As a result, each region of the Russian Federation actually developed individual conditions for sharing fiscal revenues, the proportions of which depend on the ability of local elites to defend the interests of the territories and their own interests. When the upper echelons of the Russian state apparatus become closely intertwined with private capital, this tends to produce a highly centralized system that severely constrains local government initiatives. Currently, the regions of the Russian Federation cannot independently provide the minimum established volume of budget services that they must provide to the population regardless of the amount of their own tax revenues and need financial transfers from the federal center. As of 2025, all regions of the Russian Federation became the recipients of federal transfers.

5. Model of Fiscal Centralization in the Republic of South Africa

The process of forming the fiscal system in South Africa is an example of a political compromise that determined its current decentralized unitary model. After the fall of the apartheid regime, during the development of the Interim Constitution of 1993, the issue of the political-territorial structure became a subject of acute debate.

While right-wing and ethno-nationalist forces (white parties, the Freedom Front) advocated for federalism as a tool for preserving regional influence and isolation,¹⁴ the African National Congress (ANC) insisted on a unitary state with a strong center,¹⁵ capable of redistributing resources in favor of previously oppressed groups.

As a result of complex discussions, a decision was made on a predominantly unitary state structure and the formation of future provinces within new borders. The political compromise was implemented in Article 6 of the Constitution of South Africa, according to which provinces can independently determine their policy on the use of official languages on their territory. The authors note that under conditions of territorial concentration of ethnic groups, this decision ensures the development of regional languages and promotes the development of self-government of ethnic communities.¹⁶

The Constitutional Assembly in October 1996 approved a new Constitution of South Africa, which came into force on February 4, 1997. As a result, each of the 9 new provinces receives the right to its own constitution, an executive authority, a head of government, and a legislative body elected by universal suffrage based on proportional representation. However, in the tax-budget sphere, the rights of the provinces were significantly limited.

¹⁴ Simeon, R. (1998). Considerations on the design of federations: The South African Constitution in comparative context. *Southern African Public Law*, 13(1), 49–67.

¹⁵ Berman, B., Eyoh, D., & Kymlicka, W. J. C. (Eds.). (2004). *Ethnicity and democracy in Africa* (p. 281). Ohio University Press.

¹⁶ Fessha, Y. T. (2010). *Ethnic diversity and federalism: Constitution-making in South Africa and Ethiopia* (p. 104). Ashgate.

A study of the legal regulation of value-added taxation in South Africa reveals that the conditions for levying, distributing,¹⁷ and spending VAT in South Africa in its main aspects are comparable to the corresponding model of the Russian Federation. The initial collection of VAT into the central budget is conducted without deductions to provincial and municipal budgets, followed by centralized distribution of grants and subsidies.

In the tax-budget sphere, South Africa demonstrates a highly centralized model, similar to the Russian one. Value Added Tax (VAT) is fully credited to the central budget without direct payments to provinces or municipalities. This makes VAT a tool for consolidating financial resources at the national level. In the 2021/22 fiscal year, VAT receipts amounted to 390.7 billion rand (25% of all tax revenues), second only to personal income tax.

The redistribution of funds is carried out through a system of grants and subsidies from the national government to subnational levels of government. It is supposed to compensate for deep territorial imbalances, as a third of South Africa's GDP is provided by three regions: Gauteng (34.1%) with the city of Johannesburg and the capital Pretoria, KwaZulu-Natal (16.0%) with the city of Durban, and the Western Cape province (13.6%) with the city of Cape Town. However, the effectiveness of this model of intergovernmental relations is undermined by several structural weaknesses.

First, a high level of corruption and financial violations, and extreme inefficiency of budget expenditure, is manifested in the dispersal of funds among numerous municipalities (257 units), which complicates the financing of large infrastructure projects.

Second, the policy of the center is focused on direct financing, rather than on creating institutional conditions for developing their own revenue base and managing investments at the subnational level, which limits the financial responsibility and initiative of the regions.

Third, there remains a persistent practice of holding sizeable government cash balances in accounts at the South African Reserve Bank, even as local public needs are chronically underfunded.

The large-scale system of grants, designed to mitigate regional inequality, can further generate serious negative effects: a chronic dependent position of subnational authorities; erosion of their financial responsibility; creation of extensive space for corruption and misuse of funds.

The fiscal system operates in complex socio-economic conditions, which complicate the tasks of equalization and development. The South African economy is characterized by a high share of the financial sector (asset management over \$1.4 trillion) and resource dependence (60% of exports is mineral raw materials). At the same time, the informal sector is estimated at 28% of GDP, and the official

¹⁷ Bachurin, D. G. (2021). Legal regulation of VAT in the Republic of South Africa: A comparative study. *International Public and Private Law*, 2, 35–39. (In Russian).

unemployment rate reaches critical levels (only 41% of the working-age population is employed). These factors, along with high illegal migration and the world's highest level of inequality (Gini coefficient of 0.69), create a vicious circle where the centralized fiscal system, although collecting significant revenues (25% of GDP), is unable to transform them into inclusive growth and effective provision of public services throughout the country.

The ability of VAT as a stable source of income to finance equalizing transfers faces its limited effectiveness in taxing the informal sector and in stimulating the diversification of the regional economy.

The experience of South Africa illustrates the challenges faced by decentralized unitary states with high territorial and social polarization. The model based on the full centralization of VAT and subsequent redistribution through grants proves vulnerable to problems of public finance management, corruption, and insufficient subnational responsibility.

The centralization of fiscal resources, including VAT, with subsequent redistribution through transfers, contrasts with the decentralized models of Brazil and India, where states have significant powers to set rates and bases for individual taxes and also receive a direct share of VAT. China, formally a unitary state, in practice implements a complex system of dividing tax revenues, where provinces retain a substantial share of VAT receipts after its 2016 reform, stimulating regional competition. Thus, the spectrum of models within BRICS varies from centralized redistribution (South Africa, Russia) to contractual sharing systems (China) and constitutionally enshrined division of tax powers (Brazil, India).

The example of South Africa shows that this system of intergovernmental transfers has serious risks: creating dependent attitudes in regions, reducing the financial responsibility of subnational authorities, administrative complexities, and high corruption potential. Similar problems can be observed in the Russian Federation, including the dependence of regions on federal subsidies and the accumulation of idle public funds in budgetary accounts and the Federative Republic of Brazil (a complex and often politically motivated system of funds).

The South African crisis of public finance management points to the problem of institutional quality, extending beyond the legal framework of fiscal federalism. Regardless of whether the model is based on centralization (South Africa) or decentralization (Brazil), its success is determined by the state's ability to ensure transparency, combat corruption, and build a system of accountability of authorities at all levels. In this regard, Russia and South Africa face similar challenges of low expenditure efficiency, while India and Brazil demonstrate more active involvement of civil society and judicial bodies in fiscal control, confirming Elazar's thesis about federalism as a dynamic search for balance. This search takes place between, on the one hand, the need to consolidate resources for national projects and safeguard macroeconomic stability and, on the other, the requirement to give regions sufficient incentives and autonomy for development.

The comparative analysis confirms that the choice of a centralized or decentralized model of VAT distribution by itself is not a guarantee of success. This choice must be deeply linked with the institutional development and political culture of a particular country.

Conclusion

A comparative legal analysis of VAT distribution systems in the BRICS countries reveals two fundamental, but ultimately dysfunctional, extremes in the organization of intergovernmental fiscal relations. On the one hand, a decentralized model, exemplified for a long time by Brazil, constitutionally entrenches fragmented tax rights for states, impeding necessary nationwide reforms and fragmenting the economic space. On the other hand, a fiscally centralized model, as in South Africa where VAT is fully consolidated in the national budget, generates systemic regional dependence, a chronic mismatch between subnational expenditure responsibilities and revenue sources, and low effectiveness of equalization grants. Although formally opposed, these approaches produce similar institutional outcomes: weakened state capacity to perform core public functions, stagnation in public financial management, and the persistence of territorial inequality.

The Indian model, by contrast, is based on the principle of cooperative interaction: key decisions on the Goods and Services Tax (GST) are taken by a joint body with guaranteed state representation, while an independent Finance Commission sets out detailed formulas for the redistribution of budgetary resources.

The strategic implication is the need for a balanced model that avoids both extremes. Such a model should combine moderate regional tax autonomy (for example, through the right to levy limited surtaxes) with federal rules that guarantee the unity of the national tax space. A key element is a shift from simple equalization to performance-oriented development contracts, following the Chinese example, which fosters partnership between the centre and the regions, mutual accountability, and a shared interest in expanding the common tax base.

Despite their differences, all BRICS systems face similar challenges. The first is to strike a fair balance between the tax capacities and expenditure responsibilities of the various levels of government. The second is to overcome deep disparities between more developed and lagging regions. The third is to design effective legal incentives that make regional authorities genuinely interested in developing their own economic base and in using the resources they receive responsibly. The fourth common problem is the limited flexibility of tax–budget institutions, which hampers their adaptation to new crisis conditions, in which the legal framework for intergovernmental VAT sharing becomes a key instrument of economic security and sovereignty.

The crisis resilience of an intergovernmental VAT-sharing model depends on its ability to provide, at the legal level, economic incentives for territories, fiscal

flexibility, and effective digital control tools. This, in turn, allows both the national economy and individual regions to adapt promptly to external shocks and changing conditions.

For the Russian Federation, which is simultaneously pursuing spatial development and budget equalization objectives, the comparative analysis of intergovernmental VAT-sharing regimes in BRICS countries suggests several important directions. First, it is essential to avoid the extremes of both excessive decentralization and full centralization of tax powers, as each undermines both overall steerability and local initiative. Second, policy should move toward a model that combines regions' own revenue bases with unified national rules for tax collection and oversight. Third, the system of financial assistance to regions should gradually evolve from straightforward subsidization into an incentive-based instrument, with the volume of support linked to demonstrable results in economic growth and improvements in quality of life. Fourth, there is a need to develop durable formats for continuous dialogue between the federal centre and the constituent entities of the Federation on tax and budget policy, in order to strengthen the transparency and perceived legitimacy of decisions.

All of this points to the necessity of enshrining clear public-law rules for intergovernmental fiscal relations at the legislative level, applicable in both normal and exceptional economic conditions. A balanced set of such norms should preserve the unity of the country's economic space, ensure fair equalization of citizens' social conditions, and create regions' direct interest and responsibility for their own economic development. The cases of the BRICS countries show that achieving this balance is not an easy solution but a continuous process of adjustment, requiring sensitivity to national specificities and a sustained commitment to improving the legal institutions that govern fiscal distribution.

Acknowledgements

The study was supported by a grant from the Russian Science Foundation No. 25-28-00172, project: "The Concept of Legal Regulation of Intergovernmental Distribution of VAT in the Russian Federation," <https://rscf.ru/project/25-28-00172/>.

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