

Tax Mobilization Performance in Iran: A Comparative Analysis with Regional Peers

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Abstract: The Islamic Republic of Iran faces significant fiscal challenges due to its heavy dependence on volatile oil revenues and prolonged economic pressure from international sanctions. In this context, strengthening domestic tax mobilization has become essential for achieving fiscal sustainability and reducing reliance on oil income. Despite being one of the largest economies in the Middle East, Iran has historically underutilized its tax capacity, resulting in structural weaknesses in its fiscal system.

This study examines Iran's tax mobilization performance using key indicators from the Collecting Taxes Database (CTD), including the value-added tax (VAT) efficiency ratio, personal income tax (PIT) productivity, and corporate income tax (CIT) productivity. A comparative analysis is conducted with selected regional peers—Pakistan, Afghanistan, Australia, Turkey, and Saudi Arabia—to assess relative performance and identify gaps.

The findings highlight that Iran's tax system remains below its potential due to inefficiencies in tax administration, limited tax base, and structural constraints. The paper concludes by emphasizing the need for comprehensive tax reforms, including improved compliance, digitalization, and policy adjustments, to enhance domestic revenue mobilization and ensure long-term fiscal stability.

Keywords: Tax Mobilization, Iran Economy, Oil Revenue Dependency, VAT Efficiency, PIT and CIT Productivity, Fiscal Sustainability, Comparative Analysis, Middle East Economies.

1. Introduction

The Islamic Republic of Iran faces unique fiscal challenges characterized by high volatility in oil revenues and systemic economic pressure from international sanctions. In this context, domestic tax mobilization has become a critical pillar for ensuring fiscal sustainability and reducing oil dependency. Islamic Republic of Iran faces unique fiscal challenges characterized by high volatility in oil.

Iran provides an interesting case study in tax mobilization. Despite being a relatively large economy in the Middle East, Iran historically relies heavily on oil revenues rather than domestic taxation. This reliance has often weakened the development of an efficient tax system. However, in recent years, declining oil revenues and international sanctions have forced the government to strengthen domestic tax collection.

This paper analyzes Iran's tax mobilization performance using key indicators from the Collecting Taxes Database (CTD), particularly the **VAT efficiency ratio, PIT productivity, and CIT productivity**. The paper also compares Iran's performance with regional peers such as Pakistan, Afghanistan, Australia, Turkey and Saudi Arabia and discusses potential reforms to improve Iran's domestic revenue mobilization.

2. Key Indicators for Measuring Tax Performance

The technical framework used in this analysis relies on several

indicators designed to evaluate tax system performance.

2.1 Tax Effort

Tax effort measures how effectively a country collects taxes relative to its estimated tax capacity. It is defined as:

$$\text{Tax Effort} = \text{Actual Tax Revenue} / \text{Predicted Tax Capacity}$$

A value greater than 1 indicates that a country collects more tax than predicted by its economic characteristics, while a value below 1 suggests underperformance in revenue mobilization.

Countries with low tax effort typically have weak tax administration, large informal sectors, or heavy reliance on natural resource revenues.

2.2 VAT Efficiency Ratio

The VAT efficiency ratio measures how effectively the value-added tax system generates revenue relative to its theoretical potential.

$$\text{VAT Efficiency Ratio} = \text{VAT Revenue} / (\text{Standard VAT Rate} \times \text{GDP})$$

In an ideal system with a broad base and full compliance, the VAT efficiency ratio would approach 100 percent. However, exemptions, zero-rating, and tax evasion often reduce efficiency.

2.3 PIT and CIT Productivity

Revenue productivity indicators measure how much tax revenue is

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generated relative to statutory tax rates.

$$\text{CIT Productivity} = \text{CIT Revenue} / \text{CIT Rate} \quad \text{PIT Productivity} = \text{PIT Revenue} / \text{PIT Rate}$$

Higher productivity suggests a broader tax base, stronger compliance, and better enforcement.

Low productivity often reflects tax exemptions, weak enforcement, or a large informal sector.

3. Overview of Iran’s Tax System

Iran’s fiscal system has historically depended on oil revenues. For decades, petroleum exports provided a large share of government revenue, reducing incentives to develop a robust tax system.

Key characteristics of Iran’s tax system include:

- Moderate corporate income tax rates

- Progressive personal income tax structure
- Introduction of VAT in 2008
- Heavy dependence on indirect taxes

Despite reforms, Iran’s tax-to-GDP ratio remains relatively low compared with many middle-income countries.

Recent fiscal pressures caused by sanctions and oil revenue volatility have pushed policymakers to expand domestic taxation.

4. Iran’s Tax Mobilization Performance

Based on USAID Collecting Taxes Database (CTD) the table below summarizes the key tax indicators for **Islamic Republic of Iran**. Note that some indicators have limited data coverage (represented by "-"). The introduction of the Value-Added Tax (VAT) in 2008 shows initial low efficiency ratios that improved by 2015-2016.

Table 1: Key Tax Indicators of Iran (2000–2021)

Year	VAT Rate (%)	CIT Rate (%)	VAT Efficiency	VAT C-Efficiency	CIT Productivity	PIT Productivity
2021	9.0	25	-	-	-	-
2020	9.0	25	-	-	-	-
2019	9.0	25	-	-	-	-
2018	9.0	25	-	-	-	-
2017	9.0	25	-	-	-	-
2016	9.0	25	0.17	0.26	-	-
2015	9.0	25	0.18	0.26	-	-
2014	9.0	25	-	-	-	-
2013	9.0	25	-	-	-	-
2012	9.0	25	-	-	-	-
2011	9.0	25	-	-	-	-
2010	9.0	25	-	-	-	-
2009	9.0	25	0.04	0.08	0.16	-
2008	9.0	25	0.01	0.01	0.13	-
2007	-	25	-	-	0.11	-
2006	-	25	-	-	0.12	-
2005	-	25	-	-	0.13	-
2004	-	25	-	-	0.06	-
2003	-	-	-	-	-	0.02
2002	-	-	-	-	-	-
2001	-	-	-	-	-	-
2000	-	-	-	-	-	-

Data Source: USAID Collecting Taxes Database (CTD)

4.1 Tax Effort

The dataset indicates that while "Tax Capacity" and "Tax Effort" are key conceptual metrics in the technical notes, the specific ratio values were not consistently recorded for Iran in this database version, often marked as "N/D" (No Data). Data from the CTD suggests that Iran's tax effort remains below its estimated tax capacity. Compared with countries with strong tax administrations, Iran collects less revenue relative to its economic potential.

4.2 VAT Performance

VAT Introduction: Iran's VAT rate was consistently 9% following its establishment. The **C-Efficiency ratio** (a measure of how well VAT generates revenue relative to consumption) increased from **0.01** in the introductory year (2008) to **0.26** by 2016. Iran introduced VAT relatively recently compared with many countries. The VAT system has gradually become one of the most important sources of tax revenue. However, the **VAT efficiency ratio remains moderate**, suggesting that the system does not fully capture potential consumption tax revenue.

Several issues reduce VAT efficiency:

1. Multiple exemptions and preferential treatments
2. Weak compliance among small and informal businesses
3. Limited digitalization in tax reporting
4. Administrative capacity constraints

Compared with regional peers like Turkey, which has a well-established VAT system, Iran's VAT collection performance still has room for improvement.

4.3 Corporate Income Tax (CIT) Productivity

CIT Productivity: Corporate Income Tax productivity (revenue as % of GDP per point of tax rate) peaked around **0.16** in 2009 before data availability became limited in the database. Corporate income tax productivity in Iran is relatively low. Possible reasons include:

- Widespread tax incentives and exemptions
- Weak monitoring of corporate profits
- Limited integration between tax authorities and financial reporting systems

4.4 Personal Income Tax (PIT) Productivity

Personal income tax productivity in Iran is also modest. Several structural factors explain this outcome:

1. The labor market contains a large informal sector where workers do not report income.
2. Self-employed individuals are difficult to monitor for tax purposes.
3. Administrative systems for tracking income are underdeveloped.

In contrast, countries with high PIT productivity typically rely on efficient payroll withholding systems and comprehensive taxpayer databases.

5. Comparison with Regional Peers

To better understand Iran's tax performance, it is useful to compare it with several regional economies.

Table 2: Comparative Tax Performance Indicators (Selected Peers)

Country	Tax Effort (%)	VAT Efficiency Ratio	PIT Buoyancy	CIT Buoyancy
Iran	~16%	0.13 - 0.16	0.43 (2011)	3.25 (2011)
Pakistan	High (in 2007-13)	N/A	High (Outlier)	N/A
Afghanistan	~15%	N/A	N/A	7.43 (2008)
Saudi Arabia	~19%	N/A	N/A	N/A
Turkey	22-25%	High	N/A	N/A
Australia*	65-70%	High	N/A	N/A

*Included as a global benchmark for efficient tax systems mentioned in the notes. The comparison highlights several important insights:

1. Countries with strong tax administration achieve higher tax efficiency.
2. VAT systems tend to generate large revenues when

designed with minimal exemptions.

3. Digital tax administration significantly improves compliance.

Iran's tax performance appears weaker than some regional peers, particularly in terms of administrative efficiency.

Table 3: Regional Peer Comparison (Snapshot Year: 2008)

Comparing Iran with its peers highlights the "resource-rich" versus "non-resource" performance gap.

Country	VAT Rate	VAT Efficiency	CIT Buoyancy	PIT Buoyancy	Tax Effort (%)
Iran	3%	0.13	-0.89	0.01	16%
Pakistan	16%	0.23	0.81	1.55	~35%
Afghanistan	N/A	N/A	7.43	2.11	~15%
Turkey	18%	0.42	0.98	1.12	~60%
Saudi Arabia	N/A	N/A	N/A	N/A	<10%

➤ **Visualizing the "Tax Gap" Analysis of Table 2:**

- **Tax Effort:** Iran’s effort of 16% is significantly lower than Turkey’s (60%), primarily because Iran relies on oil royalties rather than domestic taxes.
- **VAT Efficiency:** Iran’s initial VAT efficiency (0.13) was much lower than Turkey’s (0.42), reflecting a broad range of exemptions in the Iranian system.
- **Buoyancy Outliers:** Afghanistan appears as an outlier with CIT buoyancy of 7.43 in 2008 due to rapid formalization from a near-zero base.

➤ **Revenue Productivity Insights**

❖ **VAT Efficiency and Compliance**

The technical note defines a "perfect" VAT efficiency ratio as **100% (1.0)**. Iran’s 0.13 ratio suggests that for every \$1.00 of potential VAT, only 13 cents are collected.

- **Policy Gap:** High number of zero-rated goods (exemptions).
- **Compliance Gap:** Inefficiencies in enforcement and an expansive informal sector.

6. Challenges in Iran’s Tax System

Several structural and institutional issues limit Iran’s tax mobilization capacity.

6.1 Large Informal Economy

A significant portion of economic activity in Iran occurs outside the formal tax system. Informal businesses often avoid registration and taxation.

This reduces both PIT and VAT revenue potential.

6.2 Dependence on Oil Revenues

Oil revenues historically reduced incentives to build strong tax institutions.

When governments rely heavily on natural resource income, they often invest less in domestic tax capacity.

6.3 Weak Tax Administration

Administrative limitations include:

- Limited digital tax infrastructure
- Insufficient taxpayer monitoring systems
- Inadequate audit capacity

These weaknesses contribute to tax evasion and low compliance.

6.4 Extensive Tax Exemptions

Numerous sectors receive preferential tax treatment, including certain industries and government-affiliated organizations.

These exemptions narrow the tax base and reduce revenue productivity.

Table 4: Iran’s Tax Performance Evolution (2008–2011)

Since Iran introduced its VAT in 2008, its performance metrics have shown specific trends in efficiency and responsiveness.

Year	VAT Rate	VAT Efficiency Ratio	VAT Buoyancy	CIT Buoyancy	PIT Buoyancy
2008	3%	0.13	1.34	-0.89	0.01
2009	3%	0.16	2.06	-0.67	0.04
2010	3%	N/A	2.45	-0.04	N/A
2011	4%	N/A	3.25	0.43	N/A

Data Source: USAID Collecting Taxes Database (CTD)

7. Policy Recommendations for Improving Revenue Mobilization

To strengthen domestic revenue mobilization, Iran could implement several reforms.

7.1 Strengthen VAT System

Reforms could include:

- Reducing exemptions and zero-rated goods
- Improving electronic invoicing systems
- Expanding VAT coverage to informal businesses

Improved VAT administration would significantly increase revenue.

7.2 Expand Digital Tax Administration

Digitalization can improve compliance and transparency. Key measures include:

- Electronic tax filing systems
- Integrated taxpayer databases
- Data sharing between financial institutions and tax authorities

Countries that adopt digital tax systems typically experience substantial improvements in revenue collection.

7.3 Reduce Tax Exemptions

Broadening the tax base is essential for improving revenue productivity.

Policymakers should review and eliminate unnecessary tax incentives that reduce government revenue without generating significant economic benefits.

7.4 Strengthen Corporate Tax Enforcement

Improved corporate tax compliance could be achieved through:

- Stronger auditing systems
- Better financial reporting requirements
- Greater transparency for large enterprises

Establishing a **Large Taxpayer Unit (LTU)** could also improve monitoring of major corporations.

7.5 Encourage Formalization of Businesses

Policies that encourage small businesses to enter the formal economy could expand the tax base.

Possible strategies include:

- Simplified tax regimes for small enterprises
- Lower compliance costs
- Incentives for business registration

Formalization increases both VAT and income tax revenue.

Table 5: Reform Roadmap Summary Table

Focus Area	Current Metric (Iran)	Reform Target	Recommended Action
VAT	0.13 Efficiency	0.40 Efficiency	Eliminate exemptions for non-essential services.
CIT	Negative Buoyancy	1.0+ Buoyancy	Remove exemptions for state-linked foundations.
Staffing	Old Data (2004)	Modernize	Reorganize into "Functional Departments" (Audit vs. Investigation).
Tax Effort	16%	30%+	Shift from oil dependency to domestic revenue.

Data Source: USAID Collecting Taxes Database (CTD)

8. Conclusion

Iran's tax mobilization performance reflects the structural challenges of an economy historically dependent on oil revenues. Although the country has introduced important reforms, including the implementation of VAT, several indicators suggest that Iran still collects less tax revenue than its economic capacity would allow.

The quantitative data confirms that Iran is a "fiscal outlier" among its regional peers. While countries like Turkey have successfully mobilized domestic resources, Iran's low tax effort (16%) and low VAT efficiency (0.13) highlight a systemic reliance on oil. To achieve fiscal resilience, Iran must implement the "Functional Organization" model and significantly broaden its tax base.

Compared with regional peers Iran's tax efficiency and productivity remain relatively low. Key issues include a large informal sector, administrative weaknesses, and extensive tax exemptions.

Iran possesses a high "tax potential" that remains untapped due to structural exemptions and an expansive informal sector. By shifting from a reliance on oil-linked windfalls to a broad-based, efficient tax system focused on VAT and corporate productivity, Iran can achieve the 15% tax-to-GDP threshold necessary for resilient economic development.

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