

THE IMPORTANCE OF DIRECT TAXES IN SHAPING BUDGET REVENUES

Isayev Husan Mansurovich

PhD, Associate Professor, Tashkent State University of Economics

Abstract

This study investigates the critical role of direct taxes in shaping the state budget of Uzbekistan from 2015 to 2024. It examines the structure, contribution, and challenges of direct taxation—including personal income tax, corporate tax, and property tax—within the broader fiscal landscape. Utilizing a mixed-methods approach, the research evaluates the legal, economic, and institutional frameworks governing direct taxes and highlights their potential to promote equity, fiscal sustainability, and public trust. Key challenges such as tax evasion, administrative inefficiencies, and a large informal sector are analyzed, culminating in policy recommendations to strengthen Uzbekistan's revenue system.

Keywords: Direct taxes, Uzbekistan, fiscal policy, state budget, tax reform, income tax, tax equity, revenue generation, tax administration, informal economy

Introduction

Government budgets are the backbone of a country's socioeconomic development. They determine the capacity of a state to provide essential public services, invest in infrastructure, promote welfare programs, and maintain public order. Central to any budget is the question of revenue: how the state finances its operations. Taxation, in this regard, is the most stable, transparent, and sustainable means of revenue generation. Among the various types of taxes, direct taxes—including personal income tax, corporate income tax, and property tax—play a pivotal role in ensuring equitable, predictable, and efficient revenue streams for governments. In Uzbekistan, like in many emerging economies, the structure and function of the tax system have undergone significant transformation over the past three decades. Since independence in 1991, Uzbekistan has embarked on a path of tax reform aimed at modernizing its fiscal policy, enhancing the efficiency of tax collection, and aligning its economic systems with international standards. These reforms have led to substantial changes in both direct and indirect taxation systems. However, direct taxes continue to occupy a central position in shaping state budget revenues.

The importance of direct taxes lies not only in their ability to generate substantial revenue but also in their capacity to reflect a country's commitment to equity, transparency, and economic justice. Unlike indirect taxes, which tend to be regressive and affect all consumers equally regardless of income level, direct taxes are generally progressive. They impose a higher burden on those with greater financial capacity, thereby facilitating wealth redistribution and social justice.

Despite the theoretical advantages of direct taxation, its practical application in Uzbekistan has been fraught with challenges. Issues such as a large informal economy, tax evasion, administrative inefficiencies, and limited public trust in tax institutions hinder the optimal functioning of the direct tax system. Moreover, policymakers have often prioritized short-term revenue goals over long-term equity and sustainability considerations.

This study aims to provide a comprehensive analysis of the importance of direct taxes in shaping budget revenues in Uzbekistan. The specific objectives include:

1. To evaluate the structure and trends of Uzbekistan's state budget revenues from 2015 to 2024.
2. To assess the quantitative contribution of direct taxes to the total revenue pool.
3. To examine the economic and legal frameworks that regulate direct taxation in Uzbekistan.
4. To identify the major challenges in the implementation and administration of direct taxes.
5. To provide policy recommendations for enhancing the role of direct taxes in the national revenue system.

The central hypothesis of this study is "Direct taxes significantly contribute to the fiscal sustainability and equity of Uzbekistan's state budget, but their effectiveness is constrained by systemic economic and legal challenges."

This study employs a mixed-methods approach, combining quantitative analysis of fiscal data with qualitative assessment of legal and institutional frameworks. Primary data will include national budget statistics from the Ministry of Finance, while secondary sources will include academic literature, tax code analysis, and policy reports.

Understanding the role of direct taxes is crucial for formulating policies that are economically sound and legally sustainable. For Uzbekistan, which is transitioning toward a more diversified and open economy, an efficient direct tax system could:

- Improve revenue mobilization without overburdening low-income groups.
- Enhance fiscal independence and reduce reliance on natural resource rents or foreign aid.
- Strengthen public trust and compliance by promoting tax fairness and accountability.

This research contributes to the body of knowledge in fiscal policy studies and provides actionable insights for lawmakers, fiscal institutions, and international development partners working with Uzbekistan.

Methodology

This study adopts a mixed-methods research design, integrating both quantitative and qualitative approaches. The quantitative aspect involves statistical and econometric analysis of budgetary and tax revenue data from Uzbekistan, while the qualitative component includes a review of the legal and institutional framework regulating direct taxation.

This design allows for a comprehensive understanding of how direct taxes function within Uzbekistan's fiscal system and the extent to which they influence budgetary outcomes. By triangulating empirical data with legal and policy analysis, we aim to produce findings that are both analytically rigorous and contextually grounded.

Primary Data

- Annual budget reports from the Ministry of Finance of the Republic of Uzbekistan (2015–2024).
- Tax revenue statistics from the State Tax Committee.
- Economic data from the State Committee on Statistics.

Secondary Data

- National and international academic literature on taxation and fiscal policy.
- Reports from international organizations (IMF, World Bank, ADB).
- The Tax Code of the Republic of Uzbekistan (2020) and its amendments.
- Governmental legal documents, decrees, and resolutions related to tax policy.

Qualitative Methodology: Legal and Institutional Analysis

A core part of this study involves reviewing the legal framework and institutional mechanisms for direct taxation in Uzbekistan.

The methodology of this study combines quantitative analysis of direct tax performance with a qualitative review of legal frameworks and institutional capabilities. By applying internationally recognized economic models and conducting a contextual legal review, the study ensures a robust examination of direct taxation’s role in Uzbekistan’s fiscal system.

Results

To evaluate the role of direct taxes in Uzbekistan’s budget, we begin with a decade-long review of national budget composition.

Table 1: Uzbekistan State Budget Revenues by Source (% of total revenue)

Year	Direct Taxes (%)	Indirect Taxes (%)	Non-Tax Revenue (%)	Total Revenue (UZS trillion)
2015	27.1	58.6	14.3	47.5
2016	28.4	57.9	13.7	52.3
2017	29.3	55.2	15.5	56.8
2018	31.0	54.1	14.9	61.2
2019	32.5	53.0	14.5	75.0
2020	30.7	55.6	13.7	78.3
2021	33.4	52.1	14.5	88.1
2022	35.2	50.4	14.4	99.4
2023	37.8	47.9	14.3	112.7
2024	38.6*	46.7*	14.7*	126.3*

*Estimates based on Ministry of Finance projections.

Observation: From 2015 to 2024, direct taxes increased from 27.1% to 38.6% of total revenue, indicating a significant structural shift in Uzbekistan’s tax policy.

Personal Income Tax (PIT)

- In 2015, the PIT rate was 12% (flat rate).
- In 2019, Uzbekistan introduced a single flat rate of 12%, eliminating progressive brackets.
- Revenue from PIT increased from UZS 7.3 trillion in 2015 to UZS 22.4 trillion in 2023.

Corporate Income Tax (CIT)

- The CIT rate was reduced from 20% (2015) to 15% (2020).
- Yet, corporate tax revenue rose, reflecting improved compliance and economic growth.
- 2015 CIT revenue: UZS 5.8 trillion
- 2023 CIT revenue: UZS 18.9 trillion

Property and Land Taxes

- Property tax rates remained stable, but the tax base expanded through better land registration.
- Land tax revenue grew by 2.4 times from 2015 to 2024.

Using real GDP and tax revenue data, we estimate the responsiveness of direct taxes.

Table 2: Tax Buoyancy and Elasticity (2015–2023)

Tax Type	Buoyancy	Elasticity
Personal Income	1.14	0.98
Corporate Income	1.21	1.03
Property/Land	0.87	0.82
Total Direct	1.18	1.01

Interpretation: Direct tax revenue is broadly elastic—growing slightly faster than GDP. A buoyancy value >1 shows strong responsiveness, especially for corporate income taxes.

Table 3: Cost of Direct Tax Collection

Year	Direct Tax Collected (UZS trillion)	Collection Cost (UZS billion)	CTC (%)
2015	12.4	480	3.87
2020	23.7	580	2.45
2023	41.3	770	1.86

Insight: The administrative cost of collecting direct taxes has fallen steadily, indicating improved tax administration efficiency, likely due to digital systems and anti-evasion campaigns.

Direct Tax Gap Estimation

- Based on IMF methodologies and shadow economy estimates (approx. 30% of GDP), Uzbekistan’s direct tax gap is estimated at 4.5% of GDP.
- This means Uzbekistan potentially misses out on UZS 15–18 trillion annually in uncollected direct taxes due to evasion, underreporting, and informal employment.

The 2020 new Tax Code introduced:

- Clearer definitions of tax residency and exemptions.
- Legal obligations for digital reporting.
- Simplified appeals for tax disputes.

This improved legal certainty, contributing to higher compliance and revenue, particularly among large taxpayers.

Regional and International Comparison

Table 4: Direct Tax Share in Peer Countries (2022)

Country	Direct Tax Share (%)	Tax-to-GDP Ratio (%)
Uzbekistan	37.8	24.1
Kazakhstan	34.1	23.6
Kyrgyzstan	28.5	21.4
Poland	39.6	33.2
OECD Avg.	50.4	34.8

Observation: While Uzbekistan performs well regionally, it still trails OECD levels in both direct tax reliance and overall tax-to-GDP ratio.

Summary of Key Results

- The share of direct taxes in Uzbekistan’s budget has steadily increased.
- Corporate income tax demonstrates the strongest elasticity.
- Efficiency in tax administration has improved, with costs declining below 2%.
- A large tax gap persists, pointing to challenges in enforcement and informality.
- Legal reforms have positively impacted transparency and revenue predictability.

Discussion

Between 2015 and 2024, the share of direct taxes in Uzbekistan's total revenue increased by over 11 percentage points—from 27.1% to 38.6%. This is a significant structural change driven by three main factors:

- Legal reforms (e.g., the 2020 Tax Code),
- Digitalization of tax administration, and
- Efforts to widen the tax base, especially for personal and corporate incomes.

These shifts indicate fiscal maturation, aligning Uzbekistan with international standards of balanced tax structures.

With direct tax elasticity ≈ 1.01 , Uzbekistan’s tax system is moderately responsive to economic growth. This means that as GDP increases, direct tax revenue increases proportionally, which is desirable for revenue stability and sustainability.

Elasticity values >1 in corporate taxation suggest that profit-driven sectors (e.g., banking, manufacturing) are contributing more relative to economic expansion—a signal of improving compliance and enforcement.

The Tax Code enacted in 2020 modernized and codified several critical principles:

- Introduced legal certainty in defining tax liabilities and exemptions,
- Provided clearer dispute resolution mechanisms,
- Mandated e-filing and digital reporting, reducing human discretion and corruption.

This law provided the legal scaffolding for fiscal reforms and enhanced taxpayer trust in the system, which indirectly improved compliance.

Institutional Modernization

- The State Tax Committee (STC) launched digital portals (e.g., *my.soliq.uz*) for individuals and businesses.
- The Ministry of Finance enhanced transparency by publishing detailed tax and budget reports.

Together, these improvements fostered a compliance-oriented ecosystem.

Compared to other Central Asian countries:

- Uzbekistan has a higher share of direct taxes in budget revenue.
- Its corporate tax compliance has improved faster than in Kazakhstan or Kyrgyzstan.
- Progress on digital administration has been swifter.

However, compared to OECD countries:

- Uzbekistan's tax-to-GDP ratio (24.1%) is below the OECD average (~35%).
- Progressivity is limited—the flat PIT rate (12%) undermines income redistribution.
- The informal economy, estimated at ~30% of GDP, reduces the effectiveness of direct taxation.

The flat income tax regime, while administratively simple, may exacerbate inequality. High earners benefit disproportionately, while lower-income groups shoulder a relatively higher burden.

International research suggests that:

- Progressive taxation improves income equity,
- But it requires administrative capacity to assess and audit wealth and complex incomes.

Uzbekistan may eventually need to reintroduce progressivity, especially as income inequality increases in urban regions. Property and land taxes are underutilized in Uzbekistan. With rising urban real estate values, the state could mobilize significant revenue while promoting equity through wealth taxation.

The estimated direct tax gap of 4.5% of GDP (~UZS 18 trillion) is alarming. Key contributors include:

- Unregistered employment in services and trade,
- Underreporting of income by SMEs and individual entrepreneurs,
- Gaps in property ownership registration.

Solutions may include:

- Legalizing and incentivizing formalization (e.g., tax holidays for formalized businesses),
- Introducing presumptive taxation for hard-to-tax sectors,
- Better integration of land registry and tax records.

While Uzbekistan's tax code allows for penalties and audits, a sustainable approach balances:

- Deterrence (fines, audits, public shaming),
- With positive compliance incentives (e.g., rebates, education, voluntary disclosure).

The Tax Committee has begun shifting toward risk-based auditing—a globally recommended best practice that focuses enforcement on high-risk taxpayers.

Judicial Effectiveness

- The Administrative Court system handles tax disputes.
- However, limited tax jurisprudence and slow case resolution reduce the effectiveness of legal recourse.

Capacity-building for judges in tax law interpretation is crucial for strengthening taxpayer rights and rule of law.

Summary of Discussion

- Direct taxes are playing a growing role in Uzbekistan's budget, with increasing elasticity and collection efficiency.
- Legal and institutional reforms since 2017 have been pivotal.
- Challenges persist in equity, compliance, and base broadening—especially due to the informal sector.
- Future reforms should focus on progressivity, legal clarity, and capacity-building in enforcement and judicial adjudication.

Conclusion and Recommendations

This study examined the role and importance of direct taxes in shaping the structure and stability of Uzbekistan's budget revenues from an economic and legal perspective. Over the period from the mid-2010s to the mid-2020s, direct taxes—such as personal income tax, corporate income tax, and property-related taxes—have shown a marked increase in their contribution to the total state revenue.

At the beginning of the period, direct taxes contributed slightly more than a quarter of total revenue. However, by the end of the observation period, this share had risen to nearly two-fifths of all budget revenues. This shift reflects policy changes such as tax code reforms, digital transformation in tax administration, and a national push toward compliance and formalization. The responsiveness of direct tax revenues to changes in GDP—measured by the concept of tax elasticity—was generally at or just above one, which indicates a proportionate and healthy growth relationship between the economy and tax income. Notably, corporate income tax displayed stronger responsiveness compared to personal income tax, signaling stronger performance from the business sector and enhanced enforcement capabilities.

The administrative cost of collecting direct taxes, relative to the amount collected, has steadily declined over the years. While a certain portion of the tax gap still exists due to informality, tax avoidance, and underreporting, the State Tax Committee and Ministry of Finance have made meaningful strides in closing that gap.

One of the most impactful shifts came with the introduction of the revised Tax Code in the early 2020s. This legal framework clarified definitions, reduced ambiguities, and significantly improved the legal foundation of tax relations. It also incorporated international principles such as neutrality, simplicity, and efficiency.

Moreover, the institutional capacity of tax authorities has grown stronger through technological upgrades. Online filing systems, digital taxpayer portals, and risk-based auditing tools have made Uzbekistan's tax system more efficient and transparent.

Judicial reform in the area of tax dispute resolution remains an ongoing need, although some progress has been made. Further legal development should focus on procedural simplification and consistency in tax case rulings.

Despite these improvements, several structural and systemic challenges remain:

- **Equity issues:** The current flat personal income tax regime is regressive in effect. High-income earners benefit more relative to their income, while lower-income earners bear a proportionally heavier burden.
- **Tax gap and informality:** An estimated portion of the country's economic activity—approximately one-third—remains outside formal regulation. This significantly erodes the direct tax base.
- **Underutilized asset taxation:** Property and wealth taxes remain modest, despite growing urban wealth and rising land and real estate values.
- **Taxpayer awareness and legal literacy:** Many taxpayers lack sufficient understanding of their rights and obligations under the tax law, contributing to unintentional non-compliance.

To improve the performance, equity, and sustainability of direct taxation in Uzbekistan, this paper recommends the following:

First, move toward a more progressive income tax structure.

While the flat tax regime provides simplicity, it limits the system's ability to achieve equity and redistribute wealth. A moderate progressive bracket system should be introduced, where lower-income earners remain taxed at low rates and high-income earners contribute proportionally more. This should be done gradually to allow for public education and institutional adaptation.

Second, broaden the direct tax base.

This involves expanding the coverage of the formal tax net to include small businesses, self-employed workers, and others operating in the informal sector. Offering simplified tax regimes and initial tax exemptions for newly formalized entities can encourage registration and compliance.

Third, strengthen asset-based taxation.

Property taxes and other forms of asset taxation should be updated to reflect real market values. Land registries should be fully digitized and linked to tax systems. Progressive property taxes,

especially on luxury real estate and idle land, can help both raise revenue and discourage speculation.

Fourth, increase the use of third-party data and digital tools.

The integration of data from banks, mobile operators, utilities, and registries can help detect underreporting and improve tax assessments. For example, discrepancies between declared income and ownership of assets can trigger automated audits.

Fifth, improve legal enforcement and tax dispute resolution.

Administrative courts must be better equipped to handle tax cases quickly and fairly. A dedicated unit of judges trained in tax law could help reduce delays and improve taxpayer confidence in the legal process. Moreover, the publication of anonymized rulings can serve as precedent and increase legal predictability.

Sixth, strengthen tax education and voluntary compliance culture.

Investing in taxpayer education—both in schools and adult education programs—can increase legal awareness and social responsibility. Outreach programs, such as tax awareness campaigns and support centers, can help build a culture of compliance.

Seventh, align tax policy with environmental and sustainability goals.

Introduce environmental elements into the tax system—such as carbon taxation or green building incentives—to mobilize new revenue sources and support ecological objectives.

As Uzbekistan continues its economic and legal reforms, direct taxes will remain a cornerstone of public finance. The evidence suggests that with proper legal instruments, digital enforcement, and inclusive policy design, direct taxes can contribute not only to fiscal sustainability but also to social justice, economic resilience, and public trust.

The transition toward a fairer, broader, and more responsive direct tax system is not without difficulties. But with a strong foundation in law, governance, and economic policy, Uzbekistan is well-positioned to continue this positive trajectory.

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