Analysis and Assessment of the Modern State of the Tax Base in Azerbaijan

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Abstract. The article examines the current state of Azerbaijan's tax base for 2024–2025, analyzing its structure, efficiency, and challenges. Using a mixed-method approach that combines quantitative data from official and international sources with qualitative policy analysis, the study finds that Azerbaijan has made significant progress in tax administration, diversification of revenue sources, and increasing registered taxpayers. In 2024, total tax revenues reached $12.98 billion, though the tax-to-GDP ratio slightly decreased from 17.9% to 17.5%. The tax base remains heavily reliant on income tax and VAT, while a substantial share is categorized as "Other Taxes." Efforts to diversify into non-oil sectors have been supported by targeted tax incentives, such as reduced branch profits tax and exemptions for agriculture, renewable energy, and technology sectors. However, challenges persist, including the large informal economy, limited non-oil sector contributions, and the need to improve collection efficiency. Projections for 2025 indicate continued revenue growth, driven by diversification policies, but with potential risks from expiring tax exemptions. The study recommends enhancing compliance through digitization, expanding taxable activities, and reassessing the impact of incentives to ensure fiscal sustainability and economic resilience.

Keywords: *Azerbaijan, tax base, fiscal sustainability, economic diversification, tax policy*

INTRODUCTION

The tax system is one of the fundamental pillars of a country's economic structure, ensuring fiscal stability, financing public services, and fostering sustainable economic advancement. Tax base, which is basically the totality of assets, income, and economic activity subject to taxation, allows for government revenue generation. A properly structured and diversified tax base is necessary for fiscal balancing, avoiding excessive dependence on individual sectors, and enhancing the ability of public finances to withstand economic impacts.

In Azerbaijan, the tax system has undergone significant adaptations in recent years, mainly because the country is engaged in diversifying its economy away from the concentration on oil-gas activity. Despite reforms, major challenges surrounding the existence of a good, broad, and sustainable tax base remain with respect to the tax base whose composition, sectoral contributions, regional

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disparities, and compliance levels are all key indicators towards the review of the efficiency of the tax system and the investigation into areas for improvement.

The main objective of this paper is to do a thorough analysis and evaluation of the Azerbaijani tax base. It first looks into the generic makeup of the tax system, then studies the recent trends in tax collection, and finally considers the efficiency and sustainability of the tax base. The research further pinpoints challenges and potential opportunities to broaden and strengthen the tax base, thus offering insight with practical value to policymaking and economic development.

The study utilizes a mixed-method approach, relying on quantitative data produced by official bodies like the State Tax Service of Azerbaijan, the Ministry of Economy, and international organizations, and pairs that information with the qualitative assessments found in recent academic research and policy analyses. The analysis not only reviews the state of the tax base but also stresses the strategic aspects for fiscal sustainability and economic diversification in Azerbaijan.

2. LITERATURE REVIEW

The tax base of the country is a determinant of fiscal health; within such a framework, it determines the capacity of the government to provide public services and to invest in economic development. On the contrary, in Azerbaijan, the tax system has dramatically evolved through major changes to increase efficiency, broaden the tax base, and reduce dependence on the oil and gas sector.

History and Structural Reforms. Being heavily transformed post-independence, Azerbaijan's tax system has moved away from a post-Soviet type to one of more advanced and flexible types. Early reforms had attempted to make taxation legal and institutional. As time went on, as in the case of programs like the "State Program for Improving Tax Administration" (2005–2007) and the "Tax System Development Strategy" (2013–2020), the focus has shifted toward modernizing tax legislation, administration, and ways to enlarge the tax base.

Growth in the non-oil sector and efforts to diversify. Because the government wants to diversify the economy, it has started programs that focus on the non-oil sector. The International Monetary Fund (IMF) says that Azerbaijan has made progress in broadening its tax base by improving tax collection and lowering the non-oil primary deficit, which means that tax revenues from the non-oil sector are stronger. This change shows that there is a plan to rely less on oil revenues.

Tax Breaks and Contributions from Different Sectors. To encourage growth in important areas, tax breaks have been put in place for certain sectors. For example, farmers don't have to pay profit tax, VAT, or property tax for 13 years starting in 2014. Also, the renewable energy sector has seen tax breaks on income, VAT, and customs duties for projects that are part of public-private partnerships. These breaks are meant to encourage the growth of sustainable energy.

Problems and Things That Need to Be Better. Even with these improvements, it is still hard to expand the tax base. The informal economy is still a big problem; estimates say that a large part of economic activity happens outside of the formal tax system. There are still efforts to make these

activities more official, with programs aimed at lowering the shadow economy and improving compliance.

Global Acknowledgement and Guidance. International recognition has been given to Azerbaijan's tax reform advancements. The nation demonstrated its leadership in international tax administration and policy by serving as the Intra-European Organisation of Tax Administrations (IOTA) president in 2024–2025.

3. METHODOLOGY

In order to provide a thorough grasp of the structure, efficacy, and difficulties of the tax system, this study uses a mixed-method approach to analyse and evaluate the current state of the tax base in Azerbaijan. This includes both quantitative data analysis and qualitative evaluation.

3.1. Data sources

The analysis is based on current, trustworthy data from national and international sources, such as:

- Annual reports and statistical bulletins on tax collection, sectoral contributions, and compliance rates are published by the State Tax Service of Azerbaijan.
- Azerbaijan's Ministry of Economy: Sectoral performance data and economic indicators.
- International Organisations: Reports from the World Bank, IMF, and OECD offer comparative information and analysis on tax base assessment and fiscal performance.
- Academic and Policy Studies: 2020–2025 research articles and policy papers that look at Azerbaijan's efforts at diversification, revenue structure, and tax reform.

3.2. Research method

The following techniques are used in the study to guarantee a thorough and organised analysis:

1. Descriptive statistical analysis: To look at recent trends in tax collection, sectoral contributions, and the makeup of tax revenues.
2. Comparative Analysis: To assess how the current tax base structure compares to earlier time periods (2020–2025) and to comparable economies in the region, like those of Georgia and Kazakhstan.
3. Efficiency assessment is the process of determining the efficacy and sustainability of the tax base using metrics like the revenue-to-GDP ratio, compliance rate, and sectoral distribution.
4. Using policy documents and expert evaluations, qualitative analysis will be used to pinpoint structural issues, policy gaps, and chances to expand the tax base.

3.3. Analytical framework

The research employs a multifaceted framework to assess the tax base, which comprises:

- The variety of taxed industries and revenue streams represents the breadth of the tax base.
- Stability and Resilience: Tax revenues' susceptibility to changes in the economy, especially in the oil and non-oil sectors.

- Efficiency and Compliance: The degree to which tax laws are followed and the effectiveness of tax collection.
- Impact on Policy: The efficiency of tax breaks and reforms in generating income and promoting economic expansion.
- This methodology, which combines quantitative and qualitative approaches, enables a comprehensive evaluation of Azerbaijan's tax base, highlighting both its advantages and shortcomings. The findings are intended to give policymakers practical advice on how to improve fiscal stability and encourage economic diversification.

3.4. Current State of the Tax Base in Azerbaijan (2024–2025)

Total amount of tax revenue. From 12.978 billion USD in 2023 to 12.979 billion USD in 2024, Azerbaijan's total tax revenue increased marginally. This shows how far the nation has come in improving its tax collection methods over the past few decades, as it is a substantial increase from the 261.6 million USD recorded in 1995.

Ratio of taxes to GDP. In 2024, Azerbaijan's tax-to-GDP ratio was 17.5%, a minor decline from 17.9% in 2023. This shows that although tax revenues have grown in absolute terms, their growth rate has not kept up with the expansion of the economy as a whole.

Distribution of Tax Revenues by Sector. The following is the breakdown of tax revenues by category for 2024:

Table 1: Distribution of Tax Revenues in Azerbaijan by Category, 2024

Tax Category	Revenue (Billion AZN)	Percentage of Total Revenue
Income Tax	6.79	18.30%
Value Added Tax (VAT)	8.89	23.90%
Excise Tax	1.56	4.20%
Other Taxes	19.92	53.60%

This distribution shows a significant reliance on income taxes and VAT, while other taxes account for a sizable amount of revenue. The sizeable portion of "Other Taxes" indicates a varied tax base, but it also highlights the necessity of a thorough examination to comprehend the elements that make up this category.

Taxpayer Demographics. Azerbaijan had 1,556,028 taxpayers as of July 1, 2024, a 6.5% increase over the previous year. This increase suggests better compliance and a growing tax base. Making sure that this increase results in proportionate revenue growth, especially from non-oil sectors, is still a challenge.

Projected Tax Revenue for 2025. Forecasts for 2025 indicate that tax revenues will continue to rise, with both the overall revenue and the proportion of contributions from non-oil sectors expected to

rise. In the upcoming years, it is anticipated that the government's initiatives to diversify the economy and lessen reliance on oil earnings will be successful. Revenue streams could be impacted, though, if some tax exemptions expire by the end of 2025.

Tax incentives and policy reforms. Azerbaijan lowered the branch profits tax rate from 10% to 5% in December 2024 by amending its Tax Code. This policy seeks to boost economic expansion and draw in foreign investment. The government has also put in place a number of tax breaks to encourage industries like technology, renewable energy, and agriculture. Although sectoral growth has been aided by these incentives, more research is needed to determine how they will affect the tax base as a whole.

Challenges and Opportunities. Even with the encouraging developments, there are still obstacles to tax base expansion. According to estimates, a sizable amount of economic activity takes place outside of the official tax system, making the informal economy a major obstacle. Initiatives to increase compliance and lessen the shadow economy are part of the continuous efforts to formalise these activities.

Enhancing tax compliance through digitisation, increasing the scope of taxable activities, and evaluating the efficacy of current tax incentives are some opportunities to broaden the tax base. A more robust and varied tax system may result from these actions.

4. DISCUSSION

Based on the previously provided data, this section explores the analysis of Azerbaijan's tax base for 2024 and forecasts for 2025. To give a thorough grasp of the situation as it stands today and its prospects for the future, the conversation is arranged under a number of important headings.

4.1. Total Tax Revenue and GDP Ratio

Azerbaijan's total tax revenue in 2024 was $12.98 billion USD, which was a considerable rise over prior years. The tax-to-GDP ratio, however, dropped marginally from 17.9% in 2023 to 17.5% in 2024. This shows that although tax revenues have increased in absolute terms, their growth rate has not kept up with the expansion of the economy as a whole.

4.2. Sectoral Distribution of Tax Revenues

The distribution of tax revenues by category is as follows:

Table 2: Sectoral Distribution of Tax Revenues

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Source: https://www.azernews.az/business/238233.html

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4.4. Projected Tax Revenue for 2025

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4.5. Policy Implications and Recommendations

The analysis emphasises how crucial it is to increase the tax base in order to maintain fiscal sustainability. Among the suggestions are:

- Improving Tax Compliance: Putting policies in place to lessen the informal economy and increase the effectiveness of tax collection.
- Increasing the variety of taxable activities, especially in non-oil industries, is known as diversifying tax sources.
- Examining Tax Incentives: Making sure that current tax exemptions and incentives are in line with long-term financial objectives by evaluating their effects.
- Investing in technology and training to increase the efficacy and efficiency of tax authorities is one way to strengthen tax administration.

CONCLUSION

The examination of Azerbaijan's tax base as of 2024–2025 shows both advancements and enduring difficulties in the growth of the national budget. Azerbaijan has improved tax administration, raised the number of registered taxpayers, and greatly increased total tax revenues over the last ten years. A more resilient and balanced tax base has resulted from the government's initiatives to diversify the economy, lessen reliance on oil earnings, and implement targeted tax incentives.

The study also identifies structural problems that need ongoing care. While the potential of non-oil sectors has not yet been fully realised, the tax base is still comparatively concentrated in some sectors, especially in activities related to oil and VAT. The growth of revenue and the equity of the tax system are still at risk from the shadow economy. In addition, the tax-to-GDP ratio has fluctuated slightly, suggesting that tax collection efficiency needs to be increased in relation to economic growth.

A progressive strategy for drawing in investment and advancing sustainable industries is indicated by policy changes in 2024, such as the lowering of the branch profits tax and the implementation of incentives for green projects. However, to make sure that these actions don't eventually weaken the tax base, they must be supported by efficient monitoring.

Azerbaijan should prioritise increasing sectoral diversification, expanding the tax base through digitalisation, and reevaluating the extent of current tax exemptions in order to improve fiscal sustainability. By addressing these priorities, the nation's larger development objectives will be supported, stable public revenues will be secured, and economic vulnerability will be decreased.

The study's conclusions ultimately highlight the significance of a thorough, empirically supported approach to tax policy—one that strikes a balance between generating revenue and long-term growth, social equity, and economic competitiveness.

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