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Assessment of the Role of Inequality and Income Distribution Factors in the Third Economic Development Plan (with Emphasis on Direct Taxes)

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Abstract

In this paper the Auto Regressive Distributed Lag(ARDL) model has been utilized in order to study the long-terun relations among the elements of direct taxes on the income distribution within the years 1971-2004 and during the third Five-Year Economic Development Plan. Long-terun relations imply that during the hird Five-Year Economic Development Plan only the tax on property has been able to lower the Gini coefficient, while income and corporate taxes have only served to worsen income distribution. Also, improvement of the efficiency of the labor force as well as the income from oil and gas and the extent of openness of the economy in the long run have led to the improvement of income distribution and decrease of inequality. However, increase in the unemployment rate during the above- mentioned period has increased income inequality.

Keywords: Income distribution; Taxes; Direct Taxes; Gini Index; RDL Model.

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1- Introduction

Providing for the welfare of the different classes of societies through the careful study of income & property distribution has been one of the central issues in economics during the two recent centuries. One of the important goals of any type of economic planning is to improve the general welfare, particularly the welfare of the low- income classes. In studying the conditions of the under-developed countries, we find that income inequality is one of the most striking characteristics of such countries. Therefore, influencing income distribution has become one of the economic & social functions of the government. In order to decrease inequality, the income distribution function requires the government to first study the changes of the income levels and then take measures to improve it. The important question is how and by which means can the government realize these objectives?

It is accepted that development should improve economic welfare. However, in many developing countries that suffer from widespread poverty due to inequitable distribution of property, consumption & income and high inflation and lack of investment, one of the best ways to remove inequality and direct financial resources towards a better distribution of Income is to apply appropriate tax policies[1]. Taxes, due to their impact on distribution of wealth, have always been regarded as one of the most important factors in the government's economic policies and also as a means to change the patterns of national income distribution.

Meanwhile, regarding the government's policies, direct taxes are of higher importance. These taxes which are obtained from the individuals' income and property have some advantages; they are just and fair, economical definite, etc[2]. Unfortunately, in most of the developing countries (such as Iran), due to lack of adequate information and inefficiency of the taxing systems, most high- income occupations evade taxes and in this way a great amount of potential government income is not realized[3]. Moreover, the open income distribution system is ineffective in such countries[4]. The

1- Gary S Fields, 1989.
2- Gustav F Papanec,1986.
3-Pazhoian, jamshid,2005 .
4- Hollis Chenery,1974.

important point is that without appropriate macro-economic policies in the field of income distribution, it is difficult to reform the economy and manage the economic system properly. In recent years financial reform policies (particularly in the field of changing tax patterns) have been opposed and rejected by some social and economic groups who benefit from tax exemptions and governmental subsidies. Having no knowledge of optional taxes, lack of a useful strategy in directing subsides towards a definite goal and the barriers in the way of reform policies have been the factors that have made government plans in economic release, clarification of exchange rate, improving the subsidy system, creating monetary and financial discipline and particularly in reducing economic inequality face failure. Now, regarding the points mentioned above and considering the fact that taxes are among the required means to achieve economic growth, investment, control inflation and, more importantly, to fairly distribute income and property, it is vital to create a definite frame for direct taxes and study their roles in redistribution of income, optimal assigning of resources, reformation and distribution of income. This has been attempted during the Third Five-Year Economic Development Plan and its success or failure will be reviewed in this report.

2- Theoretical and Experimental foundations

Although the theory of income distribution has been one of the main topics of economic theories since the time of Adam Smith[1] and even before him, the first classic work in the field of income distribution changes was developed by Kuzenets[2] which is known as "Upside- down U' and applied to developing countries. Most of the studies about income distribution are based upon his theory.

Paukert (1973), Ram (1988) and Ogwang (1994) have tested and verified the theory by using some temporal data about developing countries. Other economists have studied the impacts of some macroeconomic indices on income distribution. Schaltz (1989), in his experimental work, considers unemployment as the most important factor in the unfairness of income distribution. Li (2002), by the use of panel data of the countries, has come to

1- Adam Smith,1776.
2- Kuzenets ,1955.

the conclusion that inflation worsens income distribution and lowers the rate of economic growth by increasing the income of the rich classes of the society. Many domestic studies on income distribution have been carried out in Iran. Some of them are: Oshima (1970), Loni(1975), Darvishi (1375), Parvin (1375), Tajaddin (1370), Abancnri (1376), Gorji (1376), Parvin (1380).

Gorji (1376), in studying the impact of financial policies on income distribution within the years 1974-1980, has measured Gini indices before and after applying those policies. In most regions, the indices have been continuously on the rise. It means that the tax pressure has had the largest impact on the lower class, then on the middle class and finally on the upper class. In the field of the impact of taxes and financial policies on income distribution, various researchers have studied the relationship between different taxes (direct or indirect) and financial policies with income distribution indices. Pim (1995) has studied the impact of financial policies and direct taxes on the inequality level in some developed countries. The results obtained show that directs taxes have had positive impacts on welfare and reduction of inequality in these countries. Kruger and Kahneman (2006), in their research about the desirable taxing system, have concluded that a taxing system in which direct taxes have the main part and are designed on an increasing rate is able to change the income distribution in the favor of low-income groups. Defina and Thanawala (2002) have studied the relationship between direct taxes and their transmission impacts on the poverty indices in 17 countries between the years 1969-1997. The results show that with the increase of direct taxes (particularly Tax on aggregate income) the national income is considerably redistributed to the benefit of poor classes.

Ke- young, Hamid Davoali and Sanjee Gupta, in their research, conclude that income distribution in developing countries is not more efficient and Gini index changes are not considerable before and after applying the taxing policies. Their results show that the developing countries (compared to the developed countries) are less able to use direct taxes (particularly tax on property) to reduce income and property inequality. Adel (1979), Milanovich (1994), Redmond (1997), Choi (1997), Sirk(1997), and others have studied the impact of direct and indirect taxes on the Gini index before and after applying taxing policies. In all of the studies, taxes (direct

and indirect) did not have any considerable impact on lowering the Gini index.

With reviewing the subject literature, research methodology: in the field of the impact of macro indices on the income distribution can be divided into three groups: parametric, sub- parametric and non- parametric. In the present paper, a parametric method has often been used. In this method, the impact of variables (e.g. direct taxes), as a descriptive variable, on the income distribution is measured[1].

3- Model variables and conclusions

3-1- Variables

In order to explore the impact of economic development on income distribution patterns during the Third Five-Year Economic Development Plan (1999-2003), the relationship between the quantitative variables affecting income distribution and the Gini index, as one of the most trusted indices of income inequality is carried out by use of the Auto Regressive Distributed Lag method (ARDL). The dependant variable is the Gini inequality index[2] and the independent variables are unemployment rate, income tax, property (wealth) tax, corporate tax, and inflation rate, incomes from oil and gas, openness, labor force efficiency and economic growth which will be explained.

3-1-1- Unemployment Rate

The first variable which considerably affects income distribution is the unemployment rate. Theoretical foundations of inequality and experimental observations related to the performance of many countries indicate that unemployment growth damages income distribution in the long run particularly in developing countries[3].

3-1-2- Inflation Rate

The inflation rate due to its impact on the resources assignment and distribution, affects the welfare of societies various income groups.

1- Abunouri,ismail , & tajdin, ali, 2005.
2- Refer to naji,1997,P24.
3- Blinder ,Alan & Howard ,Esaki,1978.

Theoretically, it is expected that there should be a positive and meaningful relationship between inflation growth rate and income inequality index[1].

3-1-3- Degree of Economic openness

The impacts of free trade policies on income distribution are not known. The degree of underdevelopment, elasticity of export domain, technological production factors, trade policies, etc can all play an active role in the income distribution process. However, it could be expected that by making proper trade policies, improvement of technology in production, estimating the country's capacity and producing according to that, elevating the capacities of efficient production, and faster economic growth income distribution improves in the long run[2].

3-1-4- Labor Force Efficiency

Efficiency improvement is the main cause of salary growth and lifestyle improvement. Moreover, efficiency improvement is an anti-inflation force which can absorb increases in nominal incomes. Lower efficiency level, particularly among low- income classes, makes them lose their jobs. Therefore, elevating labor-force efficiency (through training and specialization of production) leads to more economic growth and consequently improves welfare and reduces inequality in the long run[3].

3-1-5- Incomes from Oil and Gas

An increase in incomes from natural resources such as oil and gas leads to an increase in the government's ability to absorb the costs of consumption as well as its investment. If the government's general cost is limited to relieving side effects, removing privileges and producing general goods, it can enforce economic growth and encourage productive employment. Above factors could lead to a fairer income distribution and lower economic inequality[4].

1- Paul Schultz,1989.
2- Atkinson ,A ,1999.
3- David Richardson ,1995.
4- Saint , Paul & Verdier.T , 1996.

3-1-6- Property (wealth) tax

According to the tax literature related to the principle of paying ability, rich people should pay more tax. Equal property distribution is one of the main problems of both developed and developing countries. Principally, by recognizing and estimating the increase of property value and applying optional policies (with different rates according to the type of property), we can improve income distribution in the long run[1].

3-1-7 Corporate Taxes

In tax literature, corporate tax is known as a means to control and improve income distribution and production efficiency. In cases where applying corporate tax is carried out on the basis of a net-profit tax (if it has no negative effect on optimal assigning of resources), it can be effective on income distribution2. On the other hand, applying corporate tax in order to encourage investment and change the investment patterns can bring about economic growth and improve income distribution in the long run[3]. The impact of corporate tax with regard to the income distribution, will be seen in the reduction of gross investment return and consequently in the reduction of investors' or shareholders income. This impact is more dependent on the stock distribution and classification of investors.

3-1-8- Income Tax

Income tax is known as the most important means to reach a better distribution of income. If they are applied according to an individual's ability to pay, they can reduce income inequality. On the other hand, the impact of income tax can be viewed from the labour supply function view. If it leads to a reduction in labor- force offering, it may have negative impacts on income distribution. However, applying income tax can change income distribution patterns on the favor of in investor[4].

1- Barro , J ,1991.
2- Pazhoian, jamshid,2005.
3- Pazhoian, jamshid,2005.
4- Robin Boadway, Maurice Marchand ,1994.

3-2- Testing model and offering Results

3-2-1- Model Introduction

The mathematical model has been designed and defined on the basis of experimental and theoretical foundations of income distribution and with an explanation of independent variables effective on income distribution. So the desired mathematical model to survey the factors effecting income distribution during the 3rd socio-economic development plan can be presented like this:

$$G = F\,(UN\ , INF\ , RGDO\ , RLP\ , OPEN\ , OILR\ , TAXW\ , TAXJN\ , TAXCO\ , DUM_1\ , DUM_2\ , DUM_3\ )$$

In this model, "G" stands for Gini index, "UN" for unemployment rate, "INF" for inflation rate, "RGDP" for economic growth rate, "RLP" for labor-force efficiency rate, "OPEN" for degree of economic openness, "OILR" for oil and gas income, "TAXW" for wealth tax, "TAXIN" for income tax, "TAXCO" for corporate tax; "DUM" an unreal variable to show variables effect (Particularly direct taxes) on income distribution (index) during the Third Five-Year Economic Development Plan; "DUM2" an unreal variable related to the outcomes of "Imposed War"; and "DUM3" an unreal variable related to the outcomes of Islamic Revolution' of Iran.

Since there are numerous descriptive variables and few observations regarding the high number of variables, Johansson method and self-explaining model could not produce the desired results. To resolve the problem, an experimental methodological approach, an Auto Regressive Distributed Lag method (ARDL), was selected by the use of Microfit software. Moreover, to reduce the size of the model, only one tax variables is studied at each iteration.

Inference and analysis in ARDL method includes three equations Dynamic, Long - run, Error- Correction. Results of the estimations indicate that since coefficient of RGDP and INF variables were not statistically meaningful, a descriptive test for them revealed that elimination of these variables would not have a considerable impact on model efficiency. It should be mentioned that a Schwarz Bayesian scale was used to determine the optimum duration of the pauses for variables.

In order to exactly explore the effective factors on income distribution, particularly the effect of the elements of direct taxes on income distribution by comparing the situations before and after applying the tax, for a 33- year period (1350-1383), we first considered the variable of income tax as the direct tax to explore the effect of macro-variables change on the income distribution. At the second step, in order to carefully determine the impact of direct taxes on income distribution, wealth tax variable is inserted into the model. Finally, at the third step, by adding the corporate tax variable, the factors effective on income distribution during the Third Five-Year Economic Development Plan are determined.

In all these three equations, after calculating the dynamic equation, the Banerjee test should be applied to ensure a long-run relationship and co-integration. To do the test, we should subtract the coefficient of the dependant variable from '1' and then divide it by its variance. This test is carried out to test for a long-time relationship for income tax variable.

Its estimated T statistic is -7.85 which IS more than Banerjee and Dolado tables figures in terms of absolute value. In other words, according to this test, the null hypothesis of not being a long – run relationship is rejected.

3-2-2- Result Related to Income Tax Effect on Income Distribution

After applying the co-integration test and ensuring a long-run relationship, it is possible to analyze the long- run coefficients. Table 1 shows the results of a long-run relationship for the case where income tax effect has been used to measure impact of direct taxes on the Gini coefficient. Results offered in Table 1 to 3 are analyzed as following:

The coefficient obtained for the income tax variable shows that, in the short term, an increase in the income tax for one percent leads to a 26 percent rise in the Gini coefficient. As it is observed, the coefficient obtained for taxes has been low. This indicates that taxes and tax policies have had only slight impact among other financial means of the government during the period studied.

In the long-run, too, the coefficient of LTAXIN is .048 which indicates a weak impact of taxes on government's financial means to improve income distribution. The coefficient obtained shows that, in the long – run, a one-

percent increase in income tax, leads to a 0.48- percent increase in the Gini coefficient.

It is concluded that taxes have led to more inequality in income distribution. (Although their impact has not been great and considerable). (Table 3)

The coefficient of labor- force efficiency growth rate, RLP, in the major ARDL model, showed a -5.74 figure in the long – run. This indicates that labor-force efficiency growth had a considerable impact on inequality reduction. In other words, in the long- run, a one – percent increase in labor-force efficiency, decrease Gini coefficient as much as 5.74 percent.

The unemployment rate coefficient, UNEMP, shows 0.03 percent in the long – run, which indicates that a negative impact of unemployment rate on inequality reduction. In other words, in the long – run, a one percent increase in unemployment rate leads to a 0.03 percent increase in the Gini coefficient.

Table1: Results of income tax on income distribution

Variables	Coefficient	T statistics
LTAXINC	0.026	2.26
OPEN(-2)	-0.49	-3.12
UNEMP(-1)	0.007	2.01
LOILR	-0.026	-2.05
RLP(-2)	-0.86	-2.56
DUM1	-	-
DUM2	-0.064	-2.64
Ecm(-1)	-0.54	-7.31

Table2: Results of Diagnostic Test

Serial Correlation	6.99(0.09)
Functional Form	0.150(0.698)
Normality	1.11(0.574)
Heteroscedasticity	0.54(0.460)
F statistics	30.27
Coefficients of determination	0.97
Benerji	-7.85
DW	2.67

The open economy coefficient, OPEN, shows -0.56, which implies that the variable has a positive effect on inequality reduction. In other words, in the long– run, a one percent increase in this variable decreases Gini coefficient as much as 0.56 percent. (Table 3)

The coefficient of oil and gas incomes, LOILR, shows – 0.49 in the long – run, which indicates its positive impact on inequality reduction. That

is to say, in the long – run, a one percent incense in oil and gas incomes leads to a 0.49 percent decrease in Gini coefficient.

Table3: Long-run Results

Variables	Coefficient	T statistics
LTAXINC	0.048	2.34
OPEN	-0.56	-2.44
UNEMP	0.03	8.37
LOILR	-0.049	-2.22
RLP	-5.74	-2.83
DUM2	-0.0118	-2.78

Among the unreal variables of the model, only DUM2, which is a variable for the imposed war, seems meaningful. Considering its short – run coefficient, -0.066, and its long – run coefficient, -0.012, it leaves a negative and meaningful impact on Gini coefficient. It is concluded that DUM2 shows that during the imposed war years income distribution has become more balanced. (Tables 1 & 3)

The most important estimated coefficient in the long-run is Error-Correction coefficient and statistic, ECM (-1). It is due to the fact that the collateral relationship between the variables is estimated through this element. The meaningfulness of ECM(-1) with a t statistic, -7.98, shows that the principle of long – run model description has been right and all the collateral relationships explained by descriptive variables have been directed towards the dependant variable. It is because the long- run relationship, by itself, does not show a cause – and – effect relationship and it merely means a collateral relationship between variables. However, meaningfulness of ECM(-1) shows that the assumed description has been true in the – long – run. The results obtained show that in each period some 54 percent of divergence in the Gini coefficient has been improved and approached its long – run process.(Table 1)

It should be mentioned that all the variables in the model are meaningful for 5 and 10 percents. On the other hand, through diagnostic check no self- integration, co – variance or normality was proved.

3-2-3- Results Related to Wealth Tax Impaction Income Distribution

In this section, we can analyze the long- run coefficients after applying co-integration test and ensuring a long- run relationship. Table 6 shows the results of being long- run relationship for the time when the impact of welter tax, as the variable of direct Taxes, on Gini coefficient, has been used. Results offered in Table 4-6 are analyzed as following:

Coefficient obtained for wealth Tax variable, LTAXW (-2), with two pauses in the short- run shows that a one – percent increase in income Tax decreases Gini coefficient as much as 0.012 percent during the two following periods. As it is seen, the coefficient obtained for wealth tax has been negative and it is the only Tax, among direct taxes, which has decreased Gini coefficient during the discussed period. It should be noted that only wealth Tax has had a meaningful during the Third Five-Year Economic Development Plan. (Table 4)

In the long – run, too, the coefficient of LTAXW is -0.036 percent and the results obtained show that wealth Tax, as financial means in the hands of government, has had a positive and meaningful impact on income distribution. The coefficient obtained shows that, in the long- run, a one percent increase in income tax leads to a 0.036 percent decrease in Gini coefficient. It is concluded that wealth tax has made income distribution more balanced during the discussed period.(Although there was not great and considerable),(Table 6)

Labor – force efficiency grow rate coefficient, RLP, shows -3.94 in the long –run. This indicates that labor- force efficiency growth has a considerable impact on inequality reduction. In other words, in the long – run, a one percent increase in labor- force efficiency could decrease Gini coefficient as much as 3.94 percent.

Unemployment Rate Coefficient, UNEMP, shows 0.025 in the long – run, which indicates a negative impact of the variable on inequality reduction. In other words, in the long- run, a one – percent increases in unemployment rate leads to a 0.025 percent increase in Gini coefficient.

The coefficient of open economy variable, OPEN, is -0.97 in the long – run, which indicates a positive impact of the variable on inequality reduction. In other words, a one – percent increase in this variable leads to a 0.97 percent decrease in Gini coefficient. (Table 6)

Table4: Results of wealth tax on income distribution

Variables	Coefficient	T statistics
LTAXW(-٢)	-0.12	-5.12
OPEN(-2)	-0.34	-2.61
UNEMP	0.01	7.69
LOILR	-0.03	-3.21
RLP(-2)	-0.75	-2.38
DUM1	0.029	2.3
DUM2	-0.1	-5.69
DUM3	0.061	2.76
Ecm(-1)	-0.52	-10.84

Table5: Results of Diognostic Test

Serial Correlation	3.37(0.096)
Functional Form	0.5(0.478)
Normality	1.13(0.568)
Heteroscedasticity	0.25(0.157)
F statistics	54.46
Coefficients of determination	0.97
Benerji	-7.9
DW	2.48

In this equation, too, among the unreal variables pf the model. DUM1, DUM2, DUM_2, DUM3 which are respectively, variables during the Third Five-Year Economic Development Plan, Imposed war period and the Islamic revolution, are meaningful. Considering the coefficient of DUM1 in the Short- run, 0.029, and its coefficient in the long-run, 0.055, it is concluded that it leaves a positive and meaningful impact on Gini coefficient. The short- runs coefficient of DUM2, -0.1, and its Long-run coefficient, -0.19, show that the variable has a negative and meaningful impact on Gini coefficient. Therefore, DUM2 shows that during the imposed war income distribution was more balanced. The DUM3 too has had a positive and meaningful impact on Gini coefficient. (That is wealth tax has worsened income distribution during the due period). (Tables 4&6)

Results obtained from Error Correction show that in each period some 52percent of unbalanced ness in Gini coefficient (income inequality) has been reformed and approach its long-run process. (Table 4)

Table6: Long-run Results(Wealth tax)

Variables	Coefficient	T statistics
LTAXW	-0.036	-2.69
OPEN	-0.97	-5.38
UNEMP	0.025	10.19
LOILR	-	-
RLP	-3.94	-2.56
DUM2	-0.19	-6.33
DUM1	0.055	2.41
DUM3	0.11	2.81

3-2-4-Results Related to Corporate Tax Impact on Income Distribution

In this section, too, we can analyze the long – run coefficients after applying co- integration test and ensuring a long- time relationship. Tables 7 and 9, respectively, show the short – run and long – run relationship for the time when the impact of corporate tax, as the variable for direct taxes, has been used on Gini coefficient.

The coefficient obtained for corporate tax variable show that, in the short- run, a one-percent increase in income tax increase Gini coefficient as much as 0.023percent. (Table7).

In the long – run, too the coefficient of LTAXCO is 0.047, which indicates that corporate tax, as a financial means in the hands of government, has a negative impact on income distribution. The coefficient shows that a one-percent increase in corporate tax in the long- run will increase Gini coefficient as much as 0.047 percent. (Table 9)

Labor – force efficiency growth rate, RLP, is -6.88 in the long – run, which indicates that a one-percent increase in labor – force efficiency in the long – run leads to a 6.88 percent decrease in Gini coefficient. (Table 9).

Table7: Results of corporate tax on income distribution

Variables	Coefficient	T statistics
LTAXCOOP	0.023	2.75
LOILR	-0.021	-2.28
OPEN(-2)	-0.61	-3.94
UNEMP(-1)	0.01	2.81
RLP(-2)	-0.66	-1.99
DUM1	-	-
DUM2	-0.071	-3.25
Ecm(-1)	-0.49	-7.61

Table8: Results of Diognostic Test

Serial Correlation	6.37(0.09)
Functional Form	0.05(0.820)
Normality	1.50(0.470)
Heteroscedasticity	0.57(0.447)
F statistics	34.98
Coefficients of determination	0.97
Benerji	-8.33
DW	2.60

Unemployment Rate coefficient, UNEMP, is 0.03 in the long – run, which indicates its negative impact on inequality reduction. In other words, a one-percent increase in unemployment rate in the long-run leads to a 0.03 percent increase in Gini coefficient.

Open Economy coefficient, OPEN, is -0.8 in the long – run, which indicates its positive impact on inequality reduction. In other words, a one-percent increase in this variable in the long – run leads to 0.08 percent decrease in coefficient. (Table 9)

The Coefficient of oil and gas incomes, LOILR, is -0.043 in the long – run, which indicates its positive impact on inequality reduction. In other words, a one-percent increase in oil and gas incomes in the long – run decreases Gini coefficient as much as 0.043 percent. (Table 9)

Among the unreal variables in the model, only DUN2, which is an unreal variable for imposed war period, is meaningful. Considering its short-run coefficient, -0.071, and its long- run coefficient, -0.14, it is concluded that it leave a negative and meaningful impact on Gini coefficient. Therefore, it shows that daring the imposed war income distribution has become more balanced.

Results obtained from Error- Correction model show that in each period some 49 percent of a unbalanced in Gini coefficient (income inequality) has been reformed and approached its long – run process.

Table9: Long-run Results(Corporate tax)

Variables	Coefficient	T statistics
LTAXCOOP	0.027	2.62
OPEN	-0.8	-4.7
UNEMP	0.03	8.19
LOILR	-0.043	-2.28
RLP	-6.88	-3.46
DUM2	-0.14	-3.64

4- Conclusions and Considerations

Generally, the results of the study may be stated as following:

Considering the long- run relationships between statistical variables affecting the Gini coefficient, it is concluded that during the years 1971-2004 and particularly during the Third Five-Year Economic Development Plan only wealth tax, among the forms of direct taxes (including income tax, corporate tax and wealth tax) has been able to make income distribution more balanced and the two others have had a considerable role in making income distribution more unequal. Therefore, keeping the effect of various tax systems in mind, it is understood that, during the Third Five-Year Economic Development Plan, no considerable impact of tax policies on the Gini coefficient was observed, in spite of the fact that some taxing rules particularly corporate tax rate decrease were reformed.

Considering the fact that Iranian economy is dependent on the incomes from raw oil, a large part of tax base of corporate (value added of economic sectors) is under the effect of oil income turbulences. Therefore, with the increase of currency exchange incomes from raw oil corporate tax increases after a one- years pause. These uncertainties create a barrier on the stable implementation of distributive policies of corporate tax.

Tax payers of the occupational sector have the smallest share in providing tax incomes despite their higher incomes. These occupations need less skill, have higher profits and can easily escape paying taxes and that's why they are becoming more and more popular. Due to loopholes in recognition system and the rare self- report in the occupational sector, the

possibility of tax escape has increased. This, in turn, has made difficult the implementation of distributive policies in this sector.

While tax exemptions were considerably becoming limited during the Third Five-Year Economic Development Plan, still a large part of Gross Domestic Product enjoys tax exemptions. Such exemptions decrease tax incomes.

In Iran, except for taxes set on wages and salaries, the rest of the taxes, (particularly the tax on occupations and the tax on governmental and non-governmental corporations), tax collection is not done systematically. The above largely explains the decrease in government's tax incomes during the recent decades.

A majority of governmental employees live beneath the poverty line. Considering a two-figure inflation rate which drastically affects their lives, tax encouragements have failed to be directed towards the improvement of income distribution in this section.

4-1- Suggestion & Solutions

Considering the problems discussed, practicing the following solutions and suggestions may lead to an improved taxing system, income distribution and higher social welfare in the long- run.

- Increasing tax base through eliminating unnecessary exemptions.
- Creating an appropriate information system to organize tax reception system.
- Recognizing new tax capacities.
- Setting an optimum tax rate for different tax compounds to reach a maximum tax income against the current inflation rate.
- Designing a conclusive system for tax exemptions, defining necessities and solutions in the field of exemptions and tax encouragements.
- Promoting tax exemptions for employees below the poverty line adjusted for inflation.
- Systemizing the orders, renewing the distribution system and eliminating the intermediates, preventing the creation of false occupations and controlling it by the help of responsible bodies such as municipalities, ….

- Organizing a conclusive social security system as complimentary policies and a long with reformation of taxing system are recommended.

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