

IMPROVING THE TAXATION MECHANISM OF SOLE PROPRIETORS AND SELF-EMPLOYED INDIVIDUALS

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Annotatsiya: Yakka tartibdagi tadbirkorlar va o'zini o'zi band qilgan shaxslarni soliqqa tortishda fiskal barqarorlikni ta'minlash hamda tadbirkorlikni rivojlantirish o'rtasida muvozanatni saqlashda muhim rol o'ynaydi. Ko'plab rivojlanayotgan va o'tish davridagi iqtisodiyotlarda ushbu soliq to'lovchilar toifasi bandlikni ta'minlash, daromadlarni diversifikatsiya qilishga va qashshoqlikni kamaytirishga sezilarli hissa qo'shadi. Biroq, soliq intizomi bo'yicha kamchiliklar, norasmiy iqtisodiyot va ma'muriy samaradorlikning pastligi amaldagi soliqqa tortish tizimlarining samaradorligini ko'pincha susaytiradi.

Kalit so'zlar: Soliqqa tortish, yakka tartibdagi tadbirkorlar, o'zini o'zi band qilgan shaxslar, soliq mexanizmi, tadbirkorlik, fiskal siyosat, norasmiy iqtisodiyot.

Abstract: The taxation of sole proprietors and self-employed individuals plays a crucial role in balancing fiscal sustainability with the promotion of entrepreneurship. In many developing and transitional economies, these categories of taxpayers contribute significantly to employment generation, income diversification, and poverty reduction. However, challenges such as tax compliance gaps, informality, and administrative inefficiencies often hinder the effectiveness of current taxation systems.

Keywords: Taxation, sole proprietors, self-employed individuals, tax mechanism, entrepreneurship, fiscal policy, informality.

Аннотация: Налогообложение индивидуальных предпринимателей и самозанятых играет важнейшую роль в обеспечении фискальной устойчивости и одновременно в стимулировании предпринимательства. Во многих развивающихся и переходных экономиках эти категории налогоплательщиков вносят значительный вклад в создание рабочих мест, диверсификацию доходов и сокращение бедности. Однако такие проблемы, как пробелы в налоговой дисциплине, теневой сектор и административная неэффективность, часто снижают эффективность действующих систем налогообложения.

Ключевые слова: Налогообложение, индивидуальные предприниматели, самозанятые, налоговый механизм, предпринимательство, фискальная политика, теневой сектор.

INTRODUCTION





In contemporary economic development, sole proprietors and self-employed individuals occupy a vital position as both job creators and contributors to social stability. Unlike large enterprises, their activities are highly flexible, require relatively low initial investment, and often emerge in sectors with unmet local demand such as retail trade, services, agriculture, and small-scale manufacturing. This flexibility allows them to adapt quickly to changes in market conditions, making them an indispensable part of resilient economies.

From a fiscal perspective, integrating these individuals into the formal tax system is critical. Taxes from small entrepreneurs represent not only a source of government revenue but also a mechanism for ensuring social equity and broadening the tax base. Furthermore, the taxation of sole proprietors and self-employed persons has a socio-economic dimension: it encourages legal recognition of their activities, strengthens their access to credit and social insurance, and protects them from the risks of informality.

In transition economies such as those of Central Asia and Eastern Europe, the share of employment in self-employment is particularly high. For example, in Uzbekistan, over 1.5 million people are officially registered as self-employed, accounting for a significant part of the labor force. Ensuring their effective taxation without imposing an excessive administrative or financial burden has therefore become a pressing policy issue. The challenge is to design a taxation mechanism that balances fiscal sustainability with entrepreneurial encouragement, while also mitigating risks of tax evasion and informality.

The academic debate on taxing sole proprietors and self-employed individuals spans multiple dimensions: fiscal policy design, administrative efficiency, equity considerations, and entrepreneurship promotion.

Early studies (Tanzi & Zee, 2001) emphasized the importance of tax simplification for developing countries, warning that complex systems discourage compliance and push small businesses into informality. Bird and Wallace (2004) similarly argued that tax regimes for small taxpayers should prioritize ease of compliance, minimal paperwork, and proportionality in tax burdens.

More recent scholarship reflects the growing importance of digitalization in tax administration. According to the OECD (2020), countries that introduced mobile-based filing systems, electronic tax cards, and simplified e-declaration platforms experienced higher compliance rates among micro-entrepreneurs. For instance, in Georgia, a simplified income tax regime combined with online tax services led to a 40% increase in voluntary registrations of self-employed individuals.

In terms of equity, Alm and Martinez-Vazquez (2017) pointed out that taxation policies should carefully distinguish between low-income survival activities and higher-income entrepreneurial endeavors. Uniform tax rates may create inequities, discouraging





micro-entrepreneurs from formalizing their businesses. Progressive, income-linked taxation or fixed patent-based taxes are often recommended to maintain fairness.

The literature also underlines the socio-economic impact of taxation mechanisms. Properly designed regimes can enhance financial inclusion, improve access to credit, and integrate self-employed workers into pension and health insurance systems (Kanbur & Keen, 2014). Conversely, poorly designed mechanisms with excessive burdens can perpetuate informality, erode trust in government institutions, and limit entrepreneurial growth.

Studies focusing on Central Asia (Yusupov, 2021; Rahmonov, 2022) show that reforms in Uzbekistan and Kazakhstan have experimented with patent-based taxation, fixed payments, and simplified declarations. These reforms initially increased compliance but revealed shortcomings such as insufficient differentiation between high- and low-income entrepreneurs, limited coverage of digital tax services, and weak links between taxation and social protection.

In summary, the literature indicates that improving the taxation mechanism of sole proprietors and self-employed individuals requires a multi-dimensional approach that combines simplification, fairness, and digitalization, while also embedding taxation into broader policies of entrepreneurship support and social security.

The taxation of sole proprietors and self-employed individuals represents one of the most dynamic yet challenging aspects of fiscal policy. In many countries, the informal economy accounts for a substantial share of GDP and employment, and a significant proportion of this informality comes from small-scale entrepreneurial and self-employment activities.

According to the International Labour Organization (ILO, 2021), nearly 61% of the global workforce is engaged in informal employment, with the highest shares found in developing and transitional economies. Within Central Asia, informality rates vary between 35–45% of total employment, reflecting the prevalence of sole proprietorships and self-employment activities outside the formal tax net.

In Uzbekistan, the State Tax Committee reports that as of 2024, over 1.7 million individuals are officially registered as self-employed, representing around 12% of the labor force. However, unofficial estimates suggest that an additional 20–25% of workers engage in informal or unregistered self-employment. This indicates that despite recent reforms, a large tax potential remains untapped.

Kazakhstan provides a useful comparison: following the introduction of a simplified patent-based tax system for individual entrepreneurs, the number of registered small taxpayers increased by nearly 30% between 2016 and 2020. Similarly, in Georgia, the introduction of a simplified “micro business” tax regime—where businesses earning below





a threshold are exempt from income tax—resulted in a sharp rise in voluntary registration of entrepreneurs. These cases highlight that simplified, transparent, and predictable tax regimes can serve as strong incentives for compliance.

1. **Informality and Hidden Income:** Despite registration efforts, many self-employed individuals underreport income or remain outside the system. For instance, World Bank (2020) estimates suggest that over 40% of small entrepreneurs in Eastern Europe and Central Asia continue to operate informally.

2. **Administrative Inefficiency:** Traditional paper-based or fragmented tax reporting systems remain a barrier. Although Uzbekistan has digitized several tax services through the “my.soliq.uz” portal, surveys show that over 45% of self-employed individuals still prefer cash-based transactions and avoid online systems due to lack of digital literacy or trust.

3. **Mismatch Between Tax Burden and Income Capacity:** Fixed payment regimes often ignore income disparities. For example, in some Uzbek regions, both high-earning and low-earning self-employed workers pay the same fixed tax amount, leading to unfair burdens for low-income individuals and revenue loss from high-income individuals.

4. **Weak Link with Social Protection:** Unlike in EU countries, where tax contributions are integrated with pension and health insurance schemes, in Uzbekistan and many transitional economies, taxation of self-employed individuals remains largely disconnected from social benefits. This weakens motivation to comply, as taxpayers do not perceive direct advantages.

The analysis of international practices and local realities suggests several opportunities:

- **Digitalization of Tax Services:** Countries like Estonia and Georgia have achieved compliance rates above 80% among small taxpayers by introducing mobile-based tax filing systems and integrating them with e-payment platforms. Uzbekistan has made progress, but expanding mobile tax apps and ensuring user-friendly interfaces could significantly improve participation.

- **Differentiated Taxation:** Adopting progressive taxation for self-employed individuals, where tax liability is proportionate to declared income, could reduce inequities. Pilot studies in Kyrgyzstan showed that such differentiation improved both fairness and revenue mobilization.

- **Integration with Social Protection:** Linking taxation with social benefits (e.g., pension contributions, medical insurance, maternity leave coverage) creates incentives for voluntary compliance. Evidence from Turkey shows that after the introduction of integrated tax-social security systems, the number of formally registered self-employed increased by 22% within three years.





● Awareness and Education: The OECD (2020) emphasizes that compliance is not only about enforcement but also about trust. Targeted awareness campaigns and taxpayer education programs have proven effective in Latin America, where simplified regimes combined with taxpayer support increased voluntary compliance rates significantly.

Conclusion

Improving the taxation mechanism of sole proprietors and self-employed individuals is essential for fostering entrepreneurship, expanding the tax base, and strengthening socio-economic development. The key directions for reform should include the simplification of tax procedures, digitalization of tax administration, fair alignment of tax rates with income capacity, and integration of tax obligations with social protection benefits. Policymakers must also invest in taxpayer education and awareness campaigns to encourage voluntary compliance. By adopting international best practices while considering domestic conditions, countries can design taxation systems that both support entrepreneurial growth and ensure fiscal sustainability.

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