

IRAN UNDER SANCTIONS



Iran's Government Expenditure
Priorities and Social Policy Burdens
During Sanctions

KEVAN HARRIS



ABOUT IRAN UNDER SANCTIONS

Iran's economy has been under sanctions in one form or another since the 1979 revolution. Yet little systematic knowledge exists on the short- and medium-term impacts of sanctions on the growth patterns of the Iranian economy, the general welfare of its people in the cities and rural areas, societal dynamics, civic space, and the country's environment. The focus has often been on a few metrics that flare up with tightening of sanctions: currency depreciation, inflation, and recession, which are then followed by increases in unemployment and poverty. But the more comprehensive picture is lost in political cacophony around the policy's merits. This is the gap that SAIS is filling with its Iran Under Sanctions project, which is a 360-degree in-depth view on the implications of sanctions on Iran. This first-of-its-kind research provides for an instructive case study on the use of sanctions as a tool of statecraft. For any questions or feedback on the project, please reach out to Ali Vaez at avaez2@jh.edu.

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EXECUTIVE SUMMARY

This paper examines social policy expenditures and coverage levels in Iran as it has experienced a renewed round of U.S.-led sanctions. At the macro-level, annual budgets over the past decade show that, even while overall government expenditures have decreased as a share of GDP, the relative shares spent on sectors linked to health, education and welfare have increased under the Hassan Rouhani administration (2013–present). In addition, annual budgets show a relative decrease in defense spending coupled with a relative rise in spending on domestic security and public order. At the micro-level, household survey data show stagnating coverage levels in the social insurance system and rising levels in the health system. As plans for upgrading and universalizing the social policy system have been hampered by sanctions-linked revenue shortfalls, Iran's overlapping yet fragmented welfare system may exacerbate inequality by providing higher levels of access to social protection across upper- and middle-income strata. While the COVID-19 pandemic provided an opportunity to fill large gaps in policy coverage of lower-income strata, it remains to be seen whether emergency aid measures implemented for poorer households and unemployed workers will be extended under future governments.

As plans for upgrading and universalizing the social policy system have been hampered by sanctions-linked revenue shortfalls, Iran's overlapping yet fragmented welfare system may exacerbate inequality by providing higher levels of access to social protection across upper- and middle-income strata.

I. IRAN'S SOCIAL POLICY SYSTEM: FRAGMENTED AND OVERLAPPING

Iran's social policy system, as in many developing countries, is both fragmented and overlapping. The social policy system is *fragmented* in that individuals and households remain excluded from social protection and social insurance programs, often even when eligible. For example, a recent audit of the rolls of anti-poverty programs found that three million families (approximately 12 per cent of the population) eligible for aid and services were never enrolled in any of the main aid organizations until the COVID-19 pandemic. At the same time, the audit assessed that some 200,000 ineligible individuals had been drawing monthly support from these organizations.¹

The system is *overlapping* in that multiple organizations often provide services and oversee beneficiaries within the same pol-

icy fields, with no comprehensive regulatory enforcement to coordinate distribution of social welfare aid and insurance. For instance, as a former health minister noted in 2019, while roughly 10 per cent of Iranians received free health insurance, and 6.9 per cent were uninsured by any health policy at all, 8 per cent were over-enrolled in at least two health insurance plans.² Households and individuals which benefit from this overlapping tend to be not in the poorest classes, but in the country's upper income strata.³

As a result, the post-revolutionary social welfare system, though rhetorically generous in its constitutional provisions, may in practice contribute to the exacerbation of inequality in certain policy spheres. Plans to integrate social policy schemes and universalize access for eligible individu-

als have regularly been discussed since the early 1990s.⁴ The additional burdens of U.S.-led sanctions, with their corollary reduction of state revenue and amplification of economic volatility, have been claimed as one, though not the only reason for slow progress of reforms proposed by President Rouhani's government.⁵ This report identifies key trends in the social policy sphere over this sanctions era, using official budget data and household survey data collected by the Statistical Center of Iran.

Findings:

1. Government expenditure data suggests a relative increase in budget priorities toward spending on health care, education and social insurance from 2014 onwards, albeit under fiscal constraints on overall spending.
2. Since 2018, the spending increases on internal security and policing have relatively outpaced those on external defense.
3. Following a proposed expansion and unification of health insurance coverage under Rouhani, both household survey and official data suggest that a long-term trend of increased health care coverage has continued.
4. Pension insurance coverage exhibited rising inequality across the same period, likely due to the fact that pension insurance – access to retirement payments, disability insurance and extended insurance for household dependents – is partly tied to occupational status. Household surveys show that while social insurance coverage for the top two income quintiles remained stable, coverage levels dropped for the lower three.
5. Since late 2019, two separate income grant policies have been in place, both implemented in response to reduced state subsidies on gasoline prices. A monthly cash transfer in place since 2010 is still received by 95 per cent of the population, though its real amount has diminished due to inflation. A Livelihood Assistance Program implemented in late 2019 is reportedly received by up to 70 per cent, with the amount based on household size and income level.

II. BUDGET EXPENDITURES ACROSS THE SANCTIONS PERIOD

Iran's government budget goes through an annual process of proposal, review, revision and eventual passage into law. Like any annual budget, actual government spending does not entirely match up with projected amounts. The Audit Court reports on actual as compared to projected spending, but as the [NGO IranBudget notes](#), budget reports are not comprehensive enough to accurately assess these differences in a systematic manner.⁶

Projected spending levels, however, can be used as a proxy for assessing state priorities and tradeoffs after protracted negotiations between the Islamic Republic's executive, legislative and supervisory branches. While budgets in the 1990s were

notoriously opaque, reforms in the 2000s led to a more transparent classification of budget priorities for public oversight. As a result, recent budget reports contain data series which group state expenditure by key categories. This makes it easier to compare projected spending priorities over time.

While the detail of spending by category has changed, it is possible to trace back spending categories prior to the Rouhani administration by scrutinizing the annual budget laws passed under President Ahmadinezhad. For the latter's final two budgets, aggregated spending data is available for comparison.

II. Budget Expenditures Across the Sanctions Period

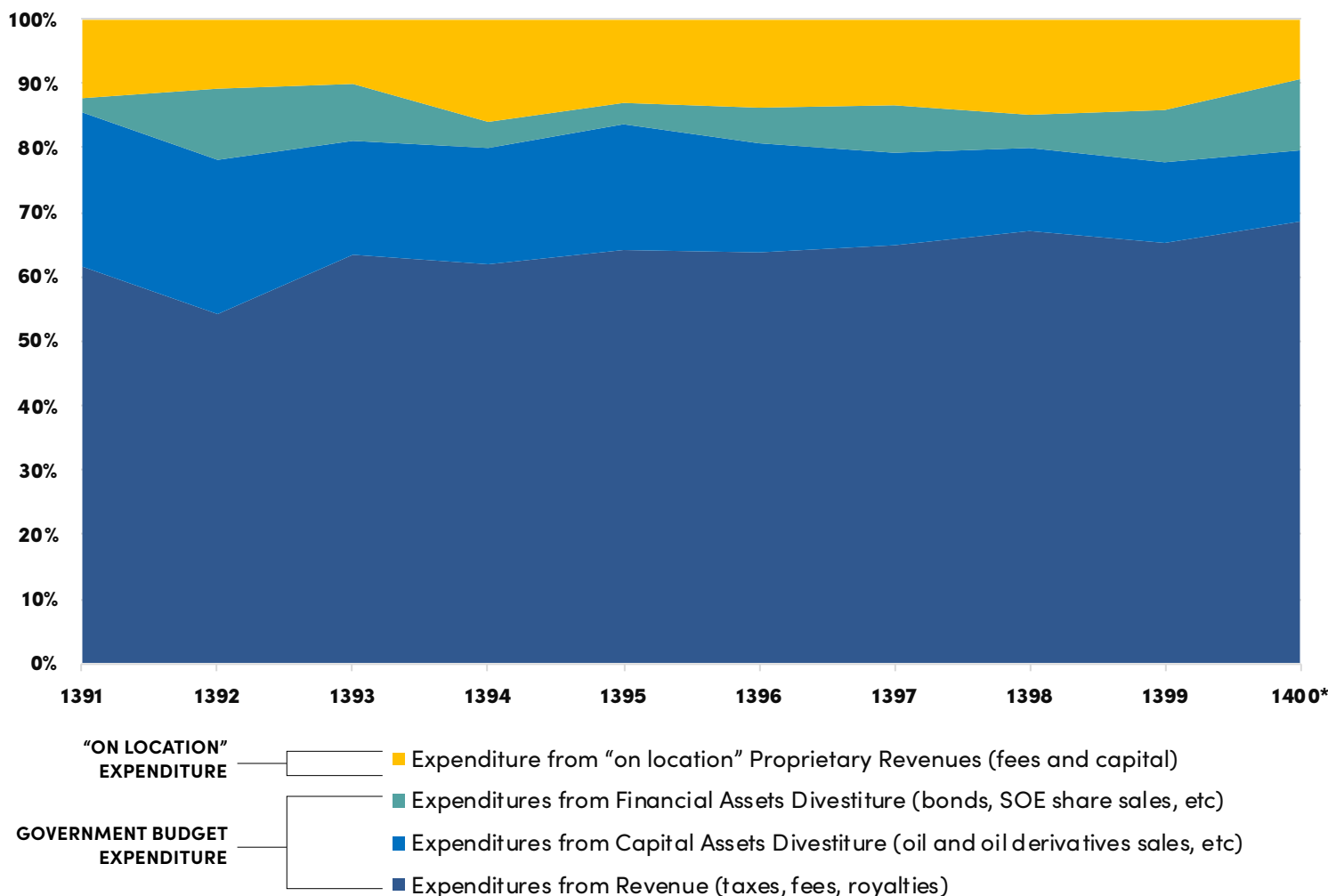
Government expenditures are grouped according to four accounting categories of revenue sources:

1. expenditures derived from income via taxes, fees and royalties (VAT, customs, etc.);
2. expenditures derived from sale of “capital assets” (oil and oil derivatives, etc.);
3. expenditures derived from sale of “financial assets” (bonds, shares of state-owned companies, public lands, etc.); and

4. expenditures derived from proprietary revenues earned “on location” by state organizations (hospital fees, university tuition, rent from ministry-owned buildings, services charged by state organizations, etc.).⁷

How did these four categories and overall government expenditure fare under the last decade of U.S.-led sanctions? Figure 1 reports these categories as a share of overall government spending from 1391 (2012-2013) to 1400 (2021-2022).

FIGURE 1 - REVENUE SOURCES FOR IRAN GOVERNMENT EXPENDITURES, 1391-1400 (2012/13-2021/22)



Source: Annual Budget Bills; budget for year 1400 (2021-22) has not yet been approved

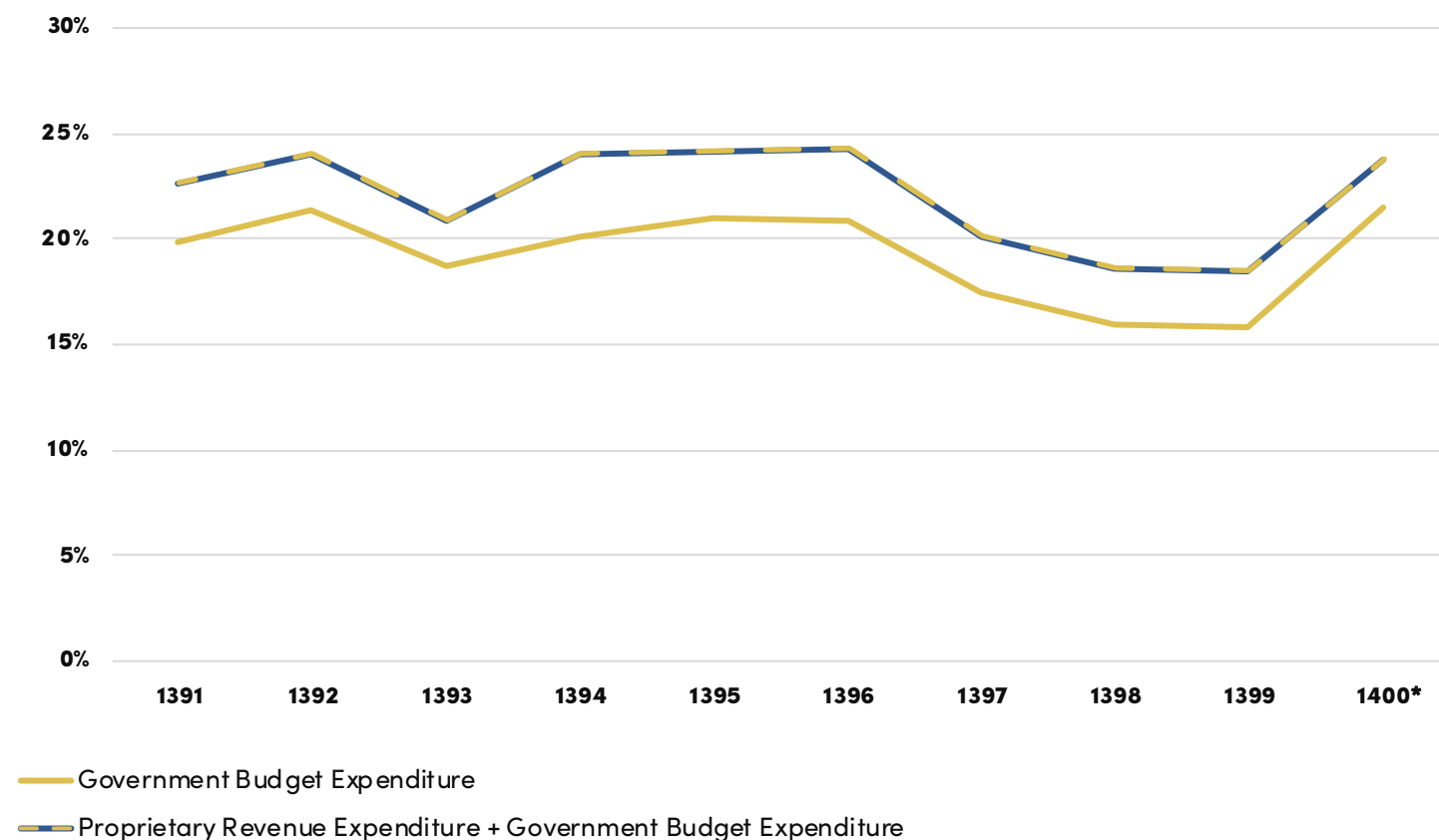
Visible in figure 1 is the relative rise in government expenditure funded by projected non-oil revenues, including from taxation and the sale of state-owned assets.⁸ The increase in the tax base, a main goal for the Rouhani government, has been partially realized, though revenue shortfalls have also been dealt with by increasing issuance of new debt and borrowing from the National Development Fund.⁹ The relative share of budget expenditure derived from revenues expected from oil and oil derivatives, conversely, has steadily declined.

[T]hese organization-specific income-generating activities are wide-ranging, not limited to military or parastatal organizations, and deserve future scrutiny in their own right.

Meanwhile, the somewhat obscure category of “on location” expenditures derived from proprietary revenues of state organizations seems to be the least volatile share of government spending. Often justified for the purpose of preventing “disruption” in essential government activities, such as reducing the reliance of higher educational instruction on direct fiscal appropriations, these organization-specific income-generating activities are wide-ranging, not limited to military or parastatal organizations, and deserve future scrutiny in their own right.¹⁰

At the aggregate level, the weight of government expenditure in the economy is shown in figure 2 as a share of GDP. The figure displays the relative size of government spending in the economy both with and without this proprietary “on location” expenditure stream. Here, trends in government spending track broadly with the imposition, relaxation and renewal of sanctions, reaching their lowest points from 2014–2015 and 2018–2020.

FIGURE 2
IRAN GOVERNMENT EXPENDITURE AS % SHARE OF GDP, 1391-1400 (2012/13-2021/22)



Source: Annual Budget Bills, National Accounts; budget for year 1400 (2021-22) has not yet been approved

In addition to overall government spending, we can examine the relative shares of each annual budget to gain a sense of whether spending priorities shifted. By relative expenditure size, the main categories listed in published annual budget documents are:

- welfare and social security;
- defense and internal security;
- education; and
- healthcare and sanitation

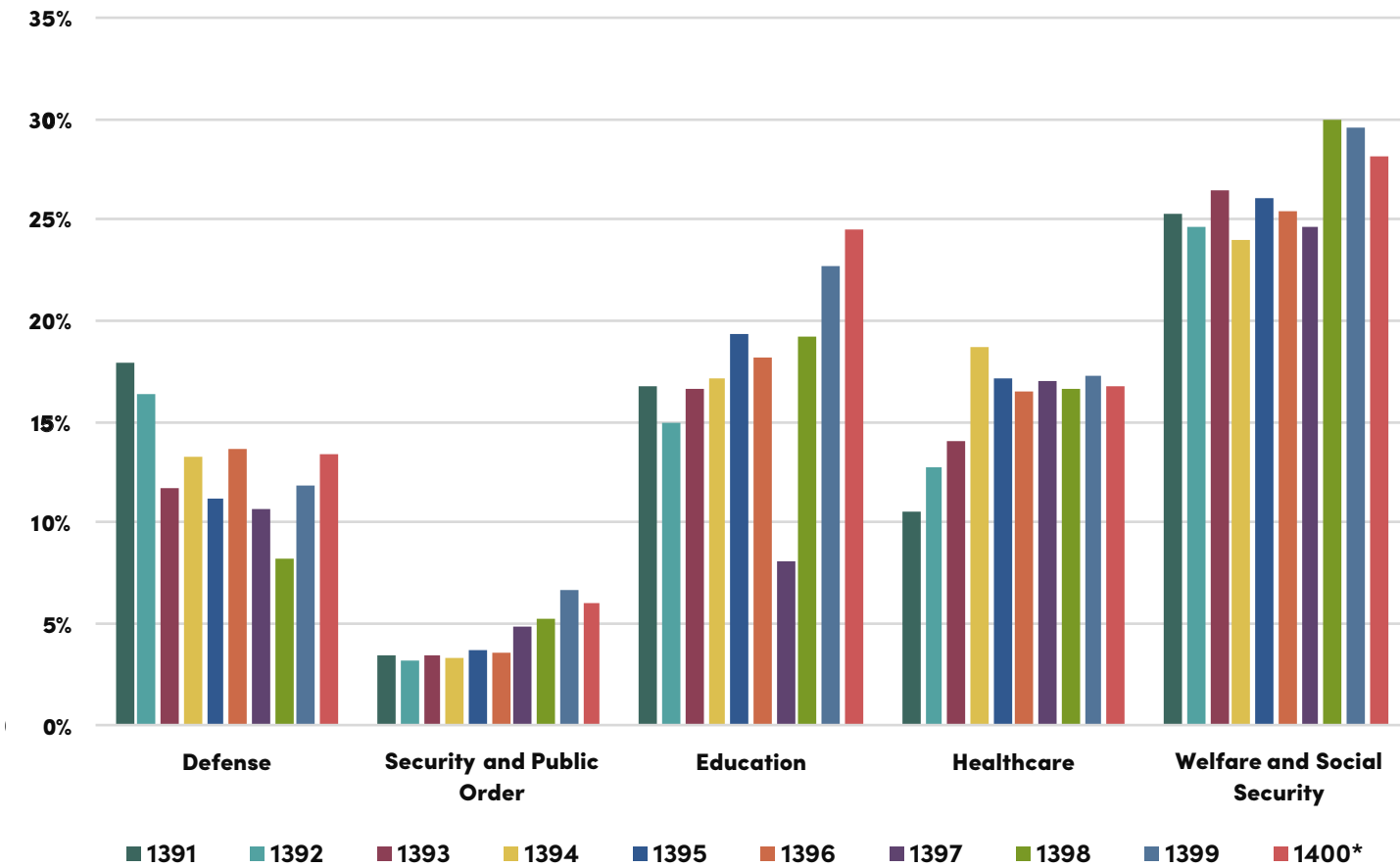
These do not include other spending types grouped in the budget under public affairs, economic affairs and cultural affairs. Those categories, however, make up far smaller shares of the budget than the above four.

For the purpose of visual comparison, changes in the relative shares of the top four spending categories in the overall budget from 2012/13 to 2021/22 are compared in both figure 3 and figure 4. Proposed spending on defense and internal security are divided into separate sub-categories.

II. Budget Expenditures Across the Sanctions Period

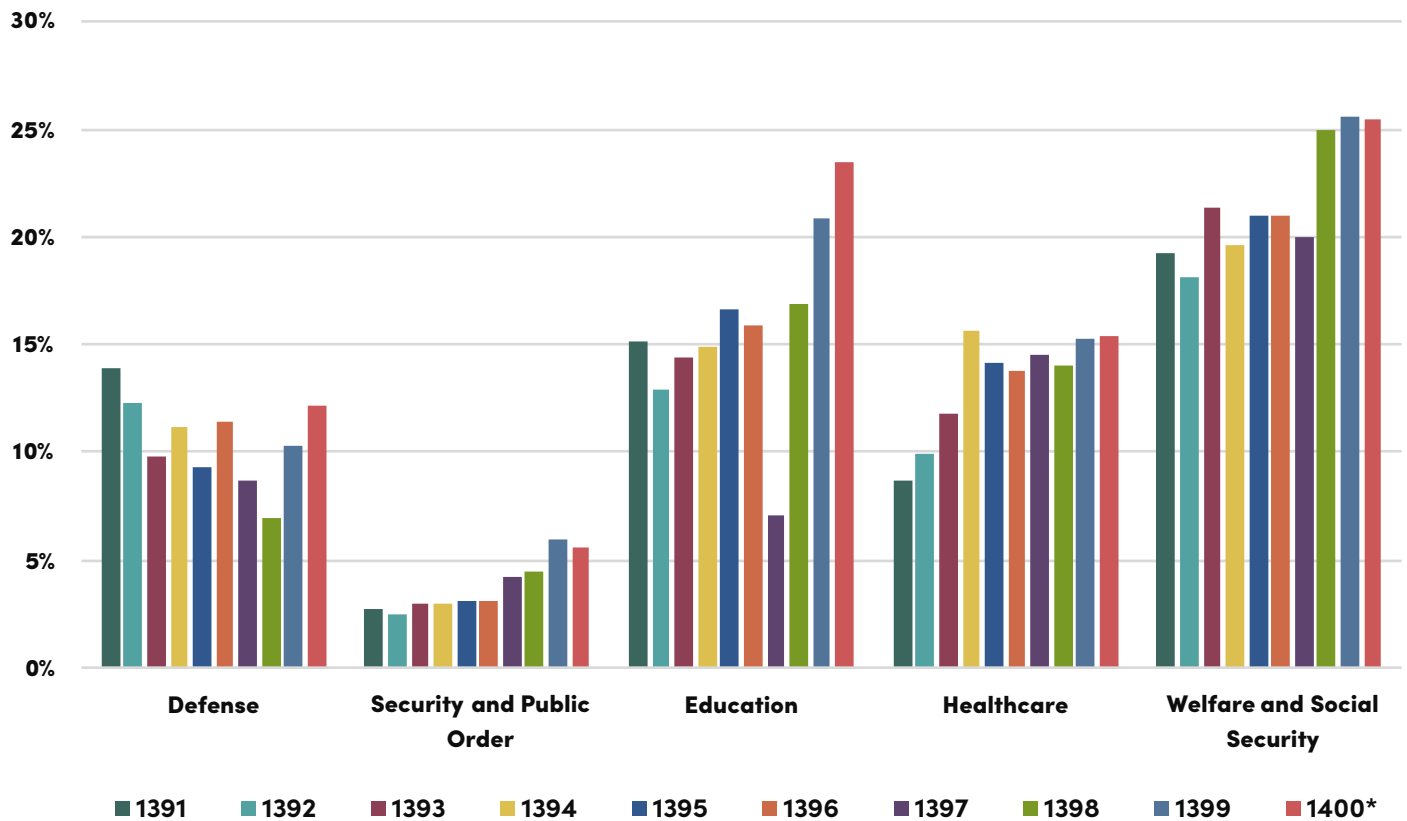
Figure 3 displays these trends using government budget expenditure data, while figure 4 displays them using the combined budget expenditure combined with proprietary spending data. This is done so as to examine whether including “self-generated” revenue by individual state organizations visibly alters trends in spending by category and over time.

FIGURE 3
BUDGETED GOVERNMENT EXPENDITURES BY CATEGORY, AS A SHARE OF TOTAL GOVERNMENT BUDGET EXPENDITURES, 1391-1400 (2012/13-2021/22)



Source: Annual Budget Bills; budget for fiscal year 1400 has not yet been approved

FIGURE 4
BUDGETED GOVERNMENT EXPENDITURES PLUS EXPECTED PROPRIETARY SPENDING
BY CATEGORY, AS A SHARE OF TOTAL GOVERNMENT BUDGET EXPENDITURES PLUS
EXPECTED PROPRIETARY SPENDING, 1391-1400 (2012/13-2021/2022)



Source: Annual Budget Bills; budget for fiscal year 1400 has not yet been approved

Trends across the two figures are roughly the same:

- First, the relative share of budget expenditures under education, healthcare and social welfare increases over time. This occurs over the years just prior to and during the nuclear agreement (JCPOA). (The dip in education spending in 1397 (2018-2019) is related to an aborted attempt at shifting revenues

and expenditures for higher education to the provincial level.¹¹⁾

- Secondly, the relative budget share under defense spending decreases from the final two Ahmadinezhad budgets (2012-2013), reaching a low point in 1398 (2019-2020). This stark cut in defense spending was noted in the Iranian press at the time.¹²⁾

II. Budget Expenditures Across the Sanctions Period

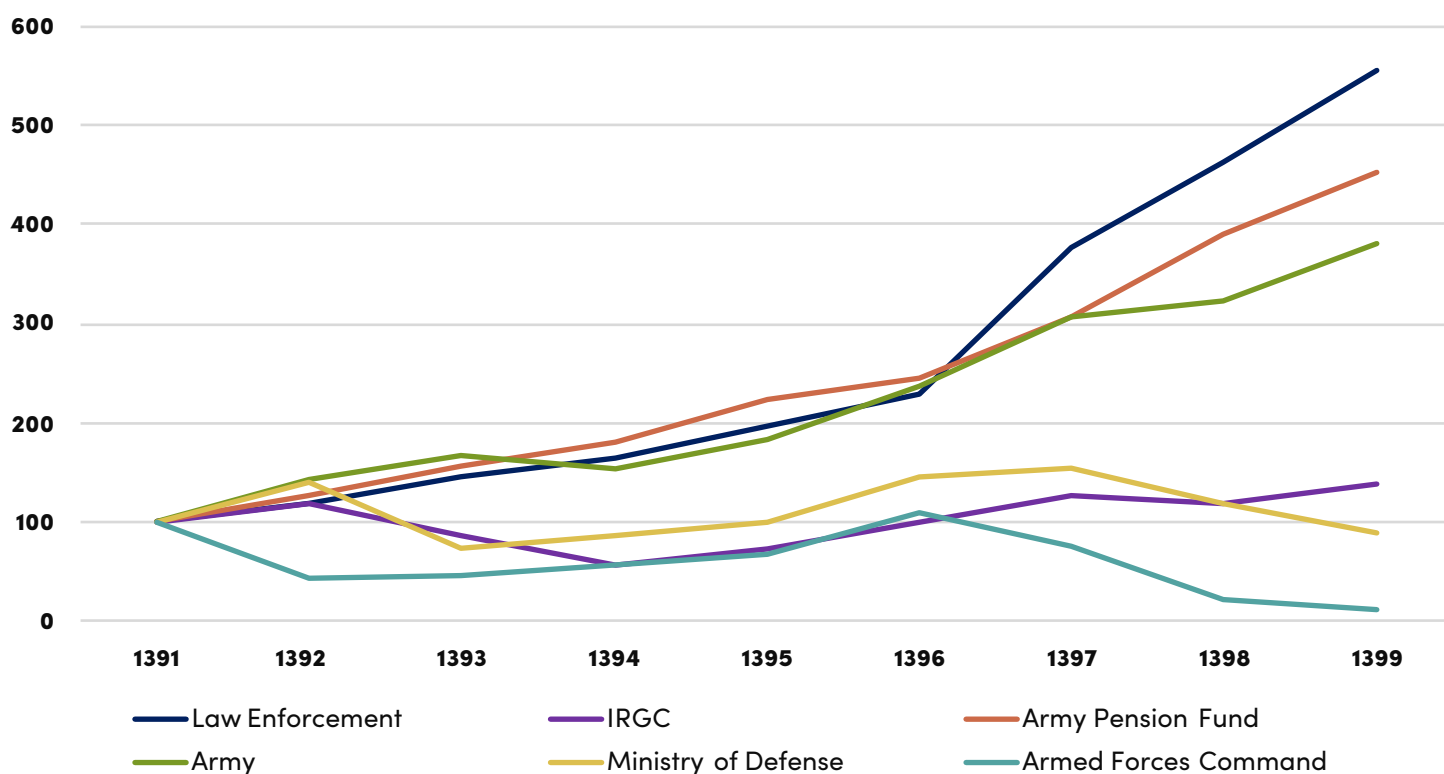
- Thirdly, the relative budget share under security and public order increases over this period, most notably for 1397-1399 (2018-2020).¹³ Whether this is partially attributable to the increase in social unrest and street protests across many cities from 2017-2019 requires further inquiry and cannot be assumed.

The relative decline in proposed defense spending can also be seen by examining expenditures over time for the six largest organizations in the defense and public security budget: Law Enforcement, Revo-

lutionary Guards (IRGC), the Armed Forces, The Army Pension Fund, The Ministry of Defence and the Armed Forces Command.

In figure 5 below, nominal increases in spending across these organizations are indexed to year 1391 (2012/13). The organization with the largest increase in relative spending over the period is Law Enforcement, followed by the Armed Forces Pension Fund and the Army. Proposed spending for the IRGC remains relatively flat in nominal terms.

FIGURE 5
CHANGE IN BUDGET EXPENDITURES (PROPOSED) AMONG SIX LARGEST ORGANIZATIONS IN DEFENSE AND SECURITY SECTORS IN IRAN, 1391-1399 (2012/13-2020/21) (INDEX 1391 = 100)



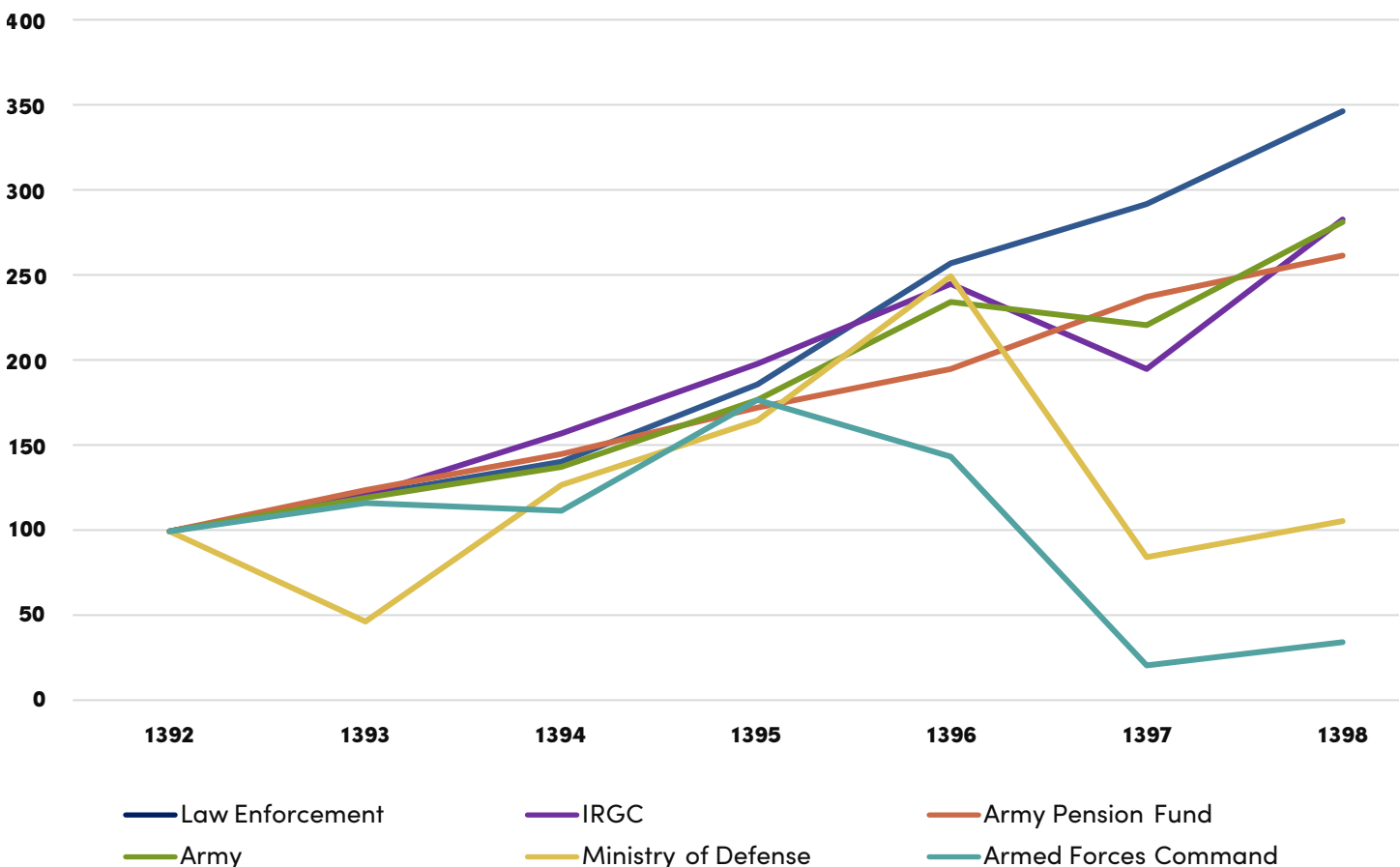
Source: Annual Budget Bills

II. Budget Expenditures Across the Sanctions Period

As noted above, proposed spending may diverge from actual spending, for which data is often less available. However, actual spending from 1392-1398 [2013/14-2019/20] is available in subsequent budget reports for these six defense and public security organizations. In figure 6, therefore, nominal increases in spending across these organizations are indexed to year 1392 (2013/14). Overall, the general trends are not too dissimilar from figure 5, though it appears that actual IRGC spend-

ing was slightly higher than proposed. Whether this is because of increased revenue from proprietary assets or additional government borrowing is unclear.¹⁴ Moreover, caution in interpreting these trends is warranted due to the likelihood that defense and security expenses may not be fully reported in public data. Nevertheless, line-item data on relative organizational expenditures by these large entities conforms broadly to the overall figures displayed above.

FIGURE 6
CHANGE IN BUDGET EXPENDITURES (ACTUAL) AMONG SIX LARGEST ORGANIZATIONS IN DEFENSE AND SECURITY SECTORS, 1392-1398 (2013/14 - 2019/20)
(INDEX 1392 = 100)



Source: Annual Budget Bills

III. SOCIAL POLICY PROFILES: HEALTH INSURANCE, SOCIAL INSURANCE, CASH TRANSFERS

Health

Key health insurance providers in Iran to-day include:

- the Health Insurance Organization (HIO, previously the Medical Services Insurance Organization), an umbrella entity that oversees additional funds for government employees, rural residents, the self-employed and dependents, the poor and other groups (e.g., university and seminary students and professional associations);
- the Social Security Insurance Organization, covering people employed in the formal private sector and their dependents;

- the Armed Forces Medical Services Insurance Organization;
- municipal funds for city employees;
- industry-specific funds (such as the National Iranian Oil Company); and
- private commercial secondary insurance companies (usually selling supplemental insurance).¹⁵

During the early 1990s, when the HIO's predecessor was created, health insurance coverage levels were estimated at around 40 per cent of the population.¹⁶ While access expanded over subsequent decades, continued fragmentation in the health care system produced two main challenges. First, numerous individuals

and households accessed care via “forum shopping” across multiple organizations, which tended to benefit middle- and upper-income households that more often possessed multiple linkages across the above organizations. Secondly, poorer households could usually obtain access to primary health care at a basic level, but more specialized or tertiary care was harder to obtain due to cost or other entry barriers. Nevertheless, health insurance coverage levels have continued to expand over the past two decades.

Social Insurance

Social insurance funds in Iran provide a range of benefits, such as pensions for retired workers, aid to dependents, supplemental health insurance and small loans. These funds include:

- Social Security Organization (SSO);
- Civil Servants Pension Fund (CSPF);
- Armed Forces Pension Fund;
- numerous sectoral pension funds by industry (steel, oil, gas, etc.);
- Imam Khomeini Relief Committee (monthly or ad hoc cash and in-kind distributions for poorer households, female-headed households, disabled citizens); and
- Social Welfare Agency (monthly or ad hoc cash and in-kind distributions for poorer households, female-headed households, disabled citizens).

The two largest social insurance organizations by coverage levels are the SSO and the CSPF. Insurance through the SSO is supplied by combined employer, employee and state contributions. Dependents of an insured person can usually be added to the policy. Coverage levels of these funds in 2017 are displayed in table 1.

TABLE 1: COVERAGE LEVELS BY MAIN SOCIAL INSURANCE AND AID FUNDS IN IRAN (2017)

	Total Popula- tion of Iran	Employed Population	SSO total insured	CSPF insured	Imam Relief Committee coverage (continuous and ad hoc)	Social Welfare Agency coverage (continuous and ad hoc)
2017 estimates	80.7 million	24 million	42 million	2.7 million	4.3 million	2.3 million

Source: Statistical Annuals of SSO, CSPF, IKRC, and SWO

Cash Transfers and Pandemic Aid

- Since 2010–2011, the government has delivered a bimonthly cash transfer of 45,500 tomans (\$20 at 2019 prices adjusted for purchasing power) per capita to the vast majority of the population (20 million households or 90 per cent of the population received this cash transfer in 2020).¹⁷
- Since November 2019, a separate program, the Livelihood Assistance Program, has delivered monthly cash transfers to 18 million households (60 million people) to partly compensate for increased gasoline prices. Cash aid was set at 55,000 tomans for one-person households, 103,000 tomans for two-person families, 138,000 tomans for three-person households, 172,000 tomans for four-person households and 205,000 tomans for those of five or more persons. Families and individuals registered under the Imam Khomeini Relief Committee or the State Welfare Organization (seven million people) receive an additional 50,000-toman cash transfer.¹⁸
- Unemployed insurance payments were widely expanded in 2020 to cushion economic dislocation from the pandemic. According to the Ministry of Welfare, out of 2.4 million unemployed in early 2021, 730,000 eligible had applied for unemployment insurance benefits. Prior to the pandemic, unemployment benefits had been distributed to a much narrower segment of the labor force (estimated at 12,500–13,500 individuals).¹⁹
- Along with unemployment benefits, retirement payments for 3.7 million pensioners are also coordinated through the Social Security Organization (SSO). As the largest social insurance organization in the country, the SSO has undergone severe financial strain during the period of sanctions, exacerbated by the pandemic. Even with around half the population covered by SSO social insurance, millions of workers in temporary contracts and informal jobs do not easily get access. Retirees have repeatedly protested to increase the level of pension payments after years of inflationary pressure.²⁰
- To compensate for pandemic-linked economic shutdowns, a variety of loans and grants were made available to workshops and firms which kept employees on payroll.²¹

Expanding Coverage in Health, Stagnation in Social Insurance

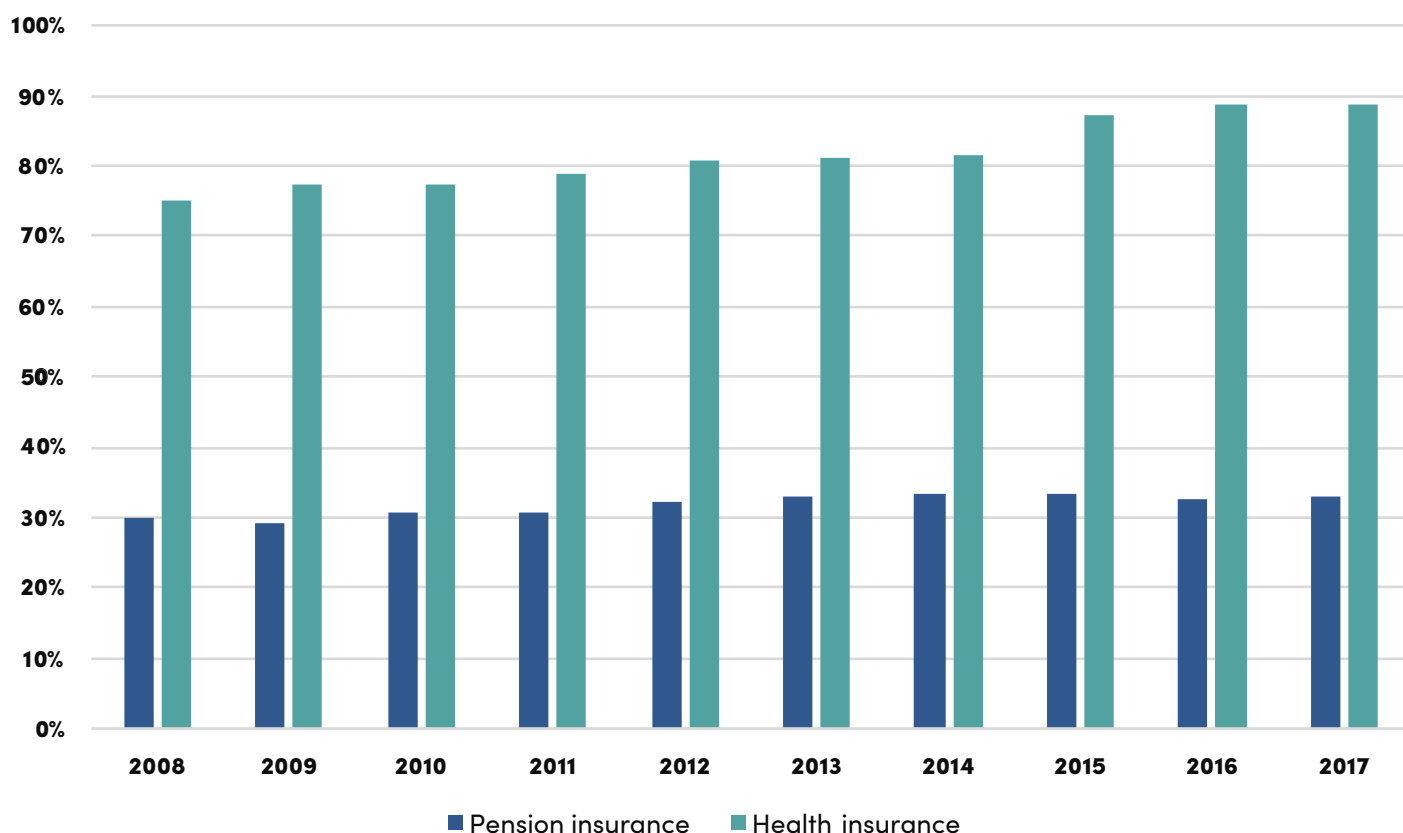
To estimate how coverage levels of health and social insurance of the above programs have changed over time, annual Household Expenditure and Income Surveys (HEIS) can be used. These are conducted annually and include several questions on coverage by various types of insurance. One advantage of the HEIS is that household-level data allows for the examination of coverage levels across income strata.

In figure 7, HEIS data on household coverage levels for health insurance and pension insurance, as measured by premiums paid for each insurance category, is displayed for 2008–2017. Two trends to note are:

- health insurance coverage reported by households steadily climbed. Under the Rouhani administration, a renewed push for expanded health insurance helped to increase coverage levels to just under 89 per cent by 2017; and

- pension insurance remained relatively stable at around a third of surveyed households (This does not include households enrolled in social insurance yet do not pay premiums.).

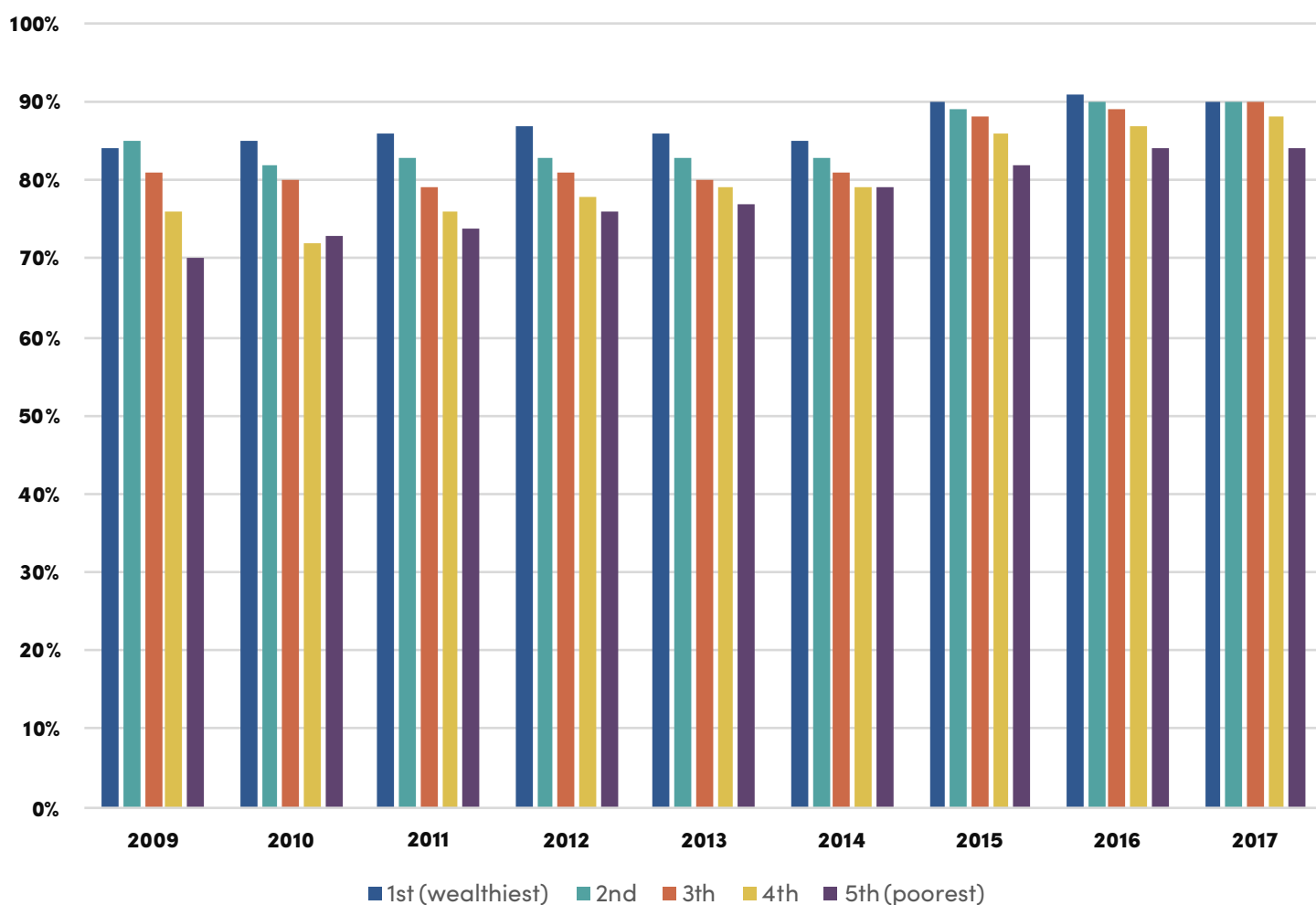
**FIGURE 7:
HOUSEHOLD COVERAGE LEVELS FOR PAID PENSION
INSURANCE AND HEALTH INSURANCE IN IRAN, 2008–2017**



Source: Household Income and Expenditure Surveys. Data was weighted to correct for likelihood of selection into the sample.

Insurance coverage levels, however, look quite different if households are separated out by income quintiles. Figure 8 displays health insurance coverage levels broken out by income quintiles for 2009–2017. HEIS data show that health coverage increased for all income groups, with health insurance becoming more universally accessible, at least in terms of coverage.

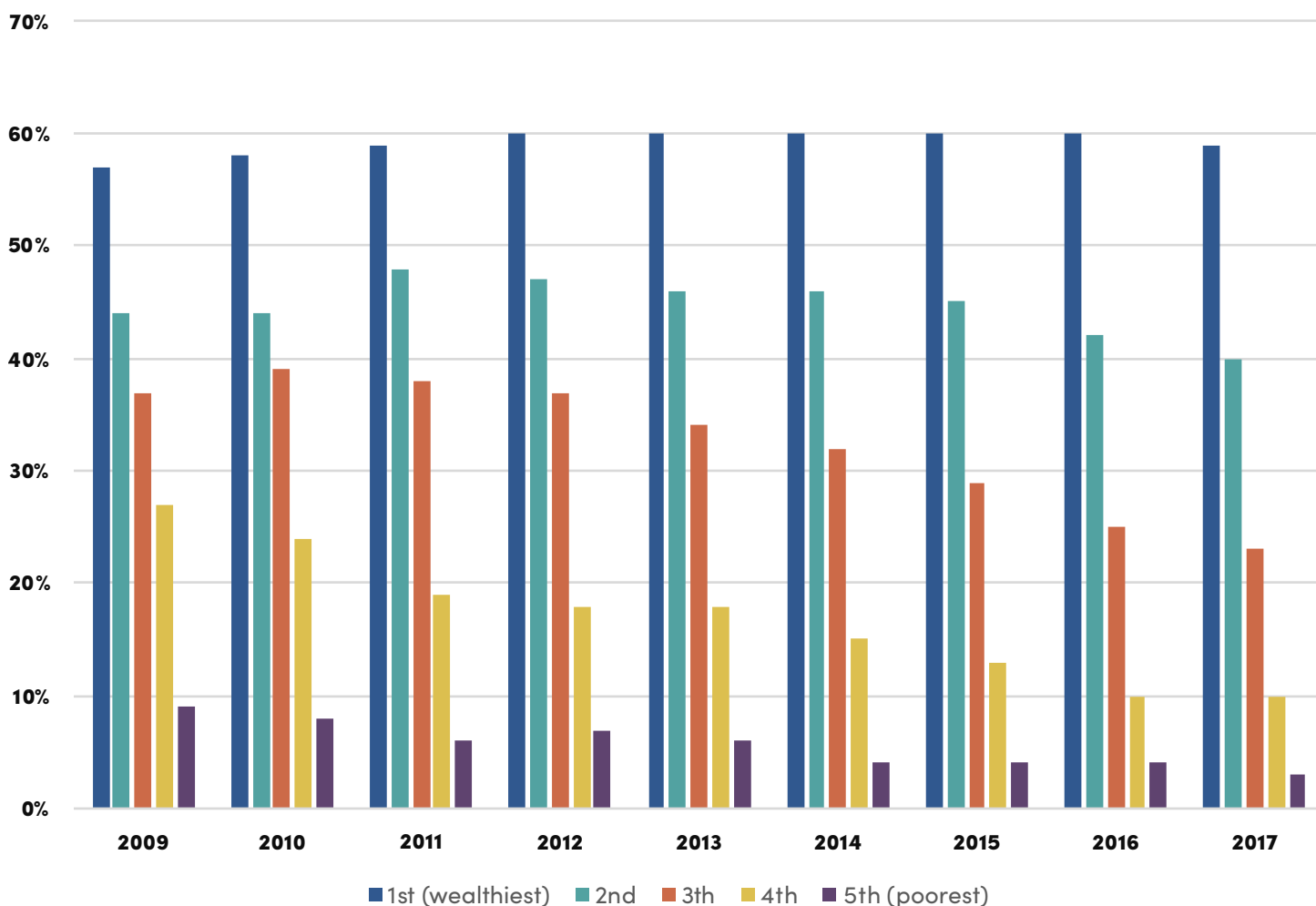
FIGURE 8:
HOUSEHOLD COVERAGE LEVELS FOR HEALTH INSURANCE
BY INCOME QUINTILES IN IRAN, 2009–2017



Source: Household Income and Expenditure Surveys. Data was weighted to correct for likelihood of selection into the sample.

This increasing equalization of access to health insurance across income groups is not mirrored in pension insurance coverage, however. Figure 9 below displays HEIS data on premiums paid for pension coverage by household income quintiles.

FIGURE 9
HOUSEHOLD COVERAGE LEVELS FOR PENSION INSURANCE
BY INCOME QUINTILES IN IRAN, 2009-2017



Source: Household Income and Expenditure Surveys. Data was weighted to correct for likelihood of selection into the sample.

Figure 9 shows that pension insurance coverage remained stable over 2009–2017 for the top two income quintiles, but the bottom three exhibited declining levels of coverage. One possible explanation for this increasing inequality is that pension insurance access in Iran is usually tied to employer and occupation across most of the large insurance programs. Another partial explanation is that the HEIS only displays data on households which pay premiums for social insurance, excluding those individuals who obtain free access to enrollment due to their occupation or income status.

What is more difficult to determine from HEIS data is the relative contribution of pension and health benefits to living standards, however measured. The numerous, albeit fragmented, linkages between state welfare organizations and households have provided one channel of support during the past two decades. However, the largest social insurance organizations face considerable funding challenges given low labor force participation and the aging of beneficiaries. According to the IMF, Iran's pension system debt is at least 2–3 per cent of GDP and faces a steep increase if future benefits, eligibility or state funding are not adjusted.²²

In summary:

- health insurance coverage has steadily increased during sanctions and relatively equally across income groups, as measured by household surveys;
- pension insurance coverage remained flat over the same period, with social welfare benefits accruing to pension insurance holders skewed towards the upper-middle and upper-income strata of the population; and
- the cash transfer system, albeit providing a dwindling level of income support due to inflation, is the social policy which covers the widest segment of the population; the government has also used additional cash transfers to provide supplemental income support during the COVID-19 crisis.

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