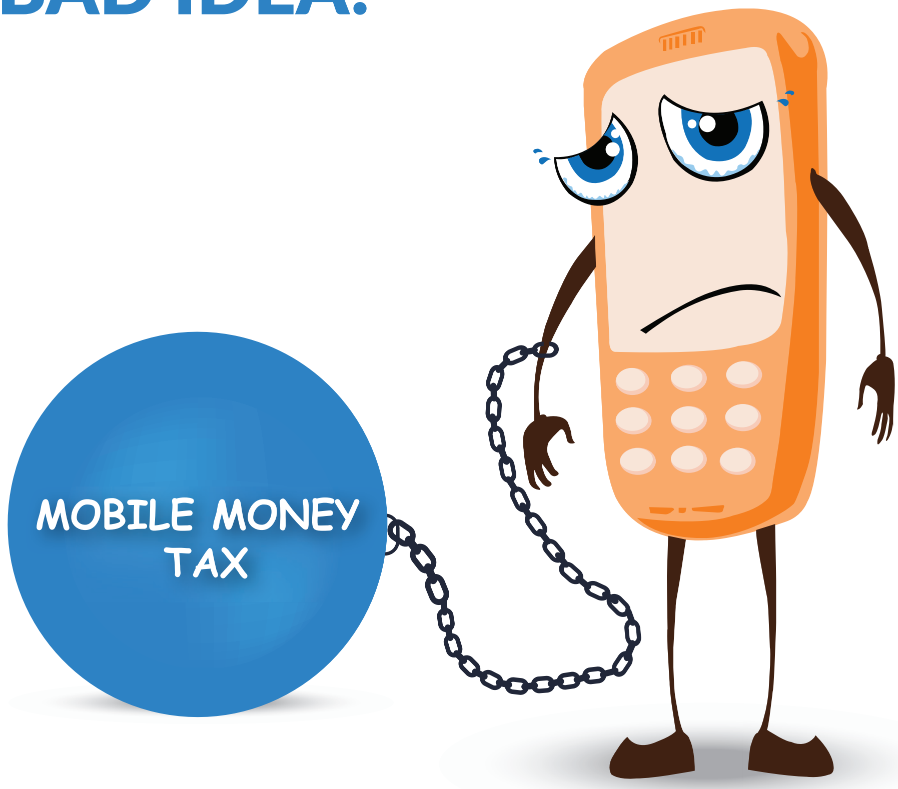
CSBAG

Budgeting for equity

Civil Society Budget Advocacy Group

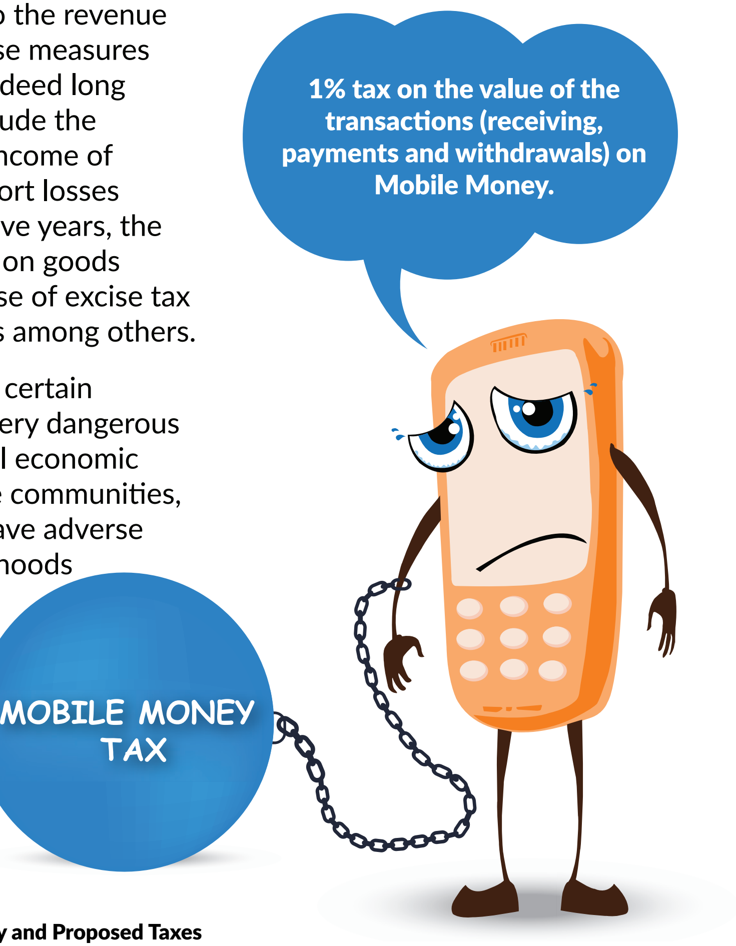
8 REASONS WHY TAXING TRANSACTION VALUE ON MOBILE MONEY IS A BAD IDEA!



EIGHT REASONS WHY TAXING TRANSACTION **VALUE** ON **MOBILE MONEY** IS **A BAD IDEA!**

In FY 2018/19 government has lined up several tax measures that will help add to the revenue purse. Some of these measures are welcome and indeed long overdue. These include the 0.5% tax on gross income of companies that report losses for seven consecutive years, the environmental levy on goods vehicles, the increase of excise tax on spirits and wines among others.

However, there are certain proposals we find very dangerous not only to the local economic development of the communities, but they will also have adverse effects on the livelihoods of vulnerable women and men. Specifically, the Finance Minister proposed in Clause 6 of the Excise Duty (Amendment) Bill 2018, to amend schedule 2 and substitute item 13 (f) to include 1% tax on the value of the transactions (receiving, payments and withdrawals) on Mobile Money (MM). Subsequently, CSBAG has detailed 8 reasons to demonstrate why taxing MM transactions in the proposed manner could be more harmful than the expected revenue of UGX 115bn and indicates two alternative sources of revenue.



1

Unnecessary reduction in disposable income

Taxing MM is in real effect going to reduce the amount of money available to cater for basic needs like health and education. This tax will increase the cost of sending and receiving money which will negatively affect value chains in agriculture, access to energy, utilities and trade services as illustrated in table 1 below.

Table 1: Impact of 1% Tax on Household income and Expenditure

Transaction type	Amount (UGX)	Service charge (UGX)	1% proposed tax on value	Total charge on amount	Acc Bal (UGX)
Deposit	50,000	0	500	500	49,500
Sending	49,500	1,000	495	1,495	48,005
Withdraw	48,005	1,500	480.05	1980.05	46,025
Cash received					46,025

Source: CSBAG Compilations and Computations

The additional impact of the tax on a transaction of UGX 50,000 is UGX 1,485. This is the market distortion that we find unnecessary yet significant enough to shock the MM growth trajectory into a retraction. The loss need not be examined only at the consumer level but also at the corporation level. When the volumes drop due to the tax shock on consumers, incomes reported by the industry players will also reduce and ultimately the return on corporation tax. In effect we could lose out at both consumer and institutional levels.

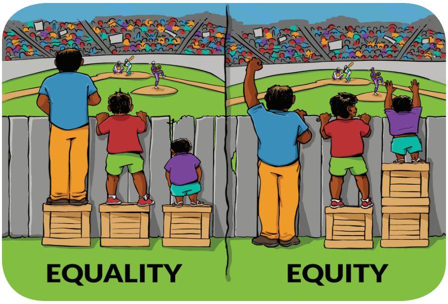
The sacrifice that citizens will have to bare because of the tax is not the same and as such the tax is regressive.

2 The tax is oblivious to the principle of equity.

Industry statistics have indicated that 61% of MM users transact less than UGX 45,000 per transaction. Although wealthier users may be able to absorb this additional cost, lower income users may struggle to do so. The sacrifice that citizens will have to bear because of the tax is not the same and as such the tax is regressive.

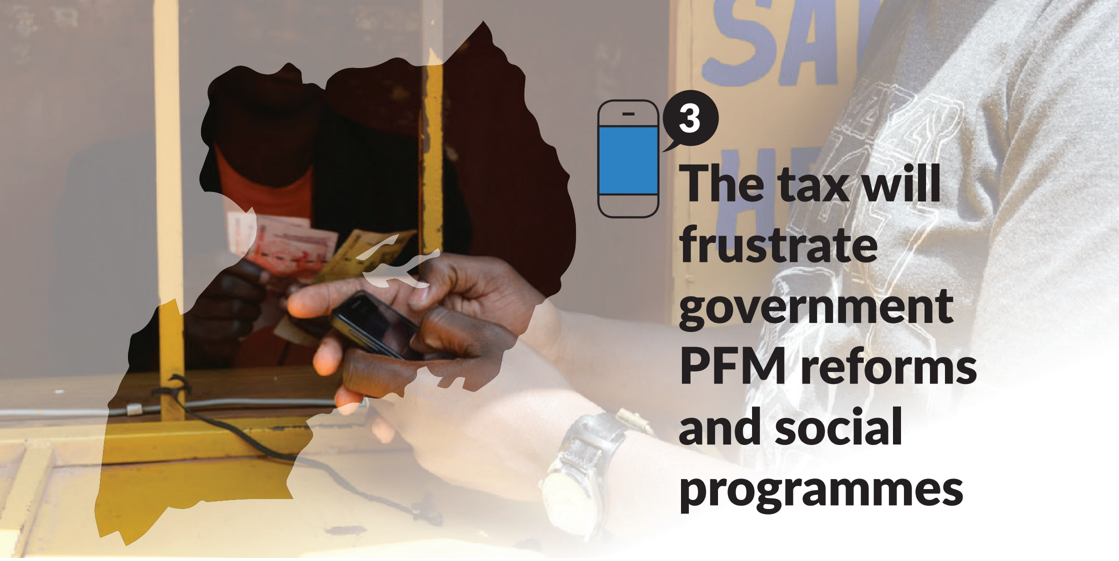
61% of MM users transact less than UGX **45,000** per transaction.

Figure 1: Illustration of equity and equality



Adam Smith argued that the taxes should be proportional to income, i.e., citizens should pay the taxes in proportion to the revenue which they respectively enjoy under the protection of the state.

However, with the imposition of a **1%** transaction value tax, if the rich and poor were all to with draw **UGX 50,000**, they would be impacted at the same rate; against the principle of equity



3 The tax will frustrate government PFM reforms and social programmes

Since FY 2015/16 the Government of Uganda has worked hard to institute public finance management (PFM) reforms to reduce cash transactions. For instance, since FY 2016/17, government ministries adopted MM as the means of payment for items like workshop allowances. With the imposition of the 1% transaction tax, the net balance received by participants as facilitation for meetings will be reduced. To accommodate the tax, there might arise a need to increase funds allocated for workshops and allowances. The flexibility that MM creates for real time expenditure like transport and accommodation should not be lost in the desperate search for money.

Similarly, plans by the government to use MM for payments to vulnerable groups like the elderly and refugees are likely to be affected; the tax will reduce the amount received by the beneficiaries of the Social Assistance Grant for the Elderly (SAGE) programme to below UGX 800 per day.

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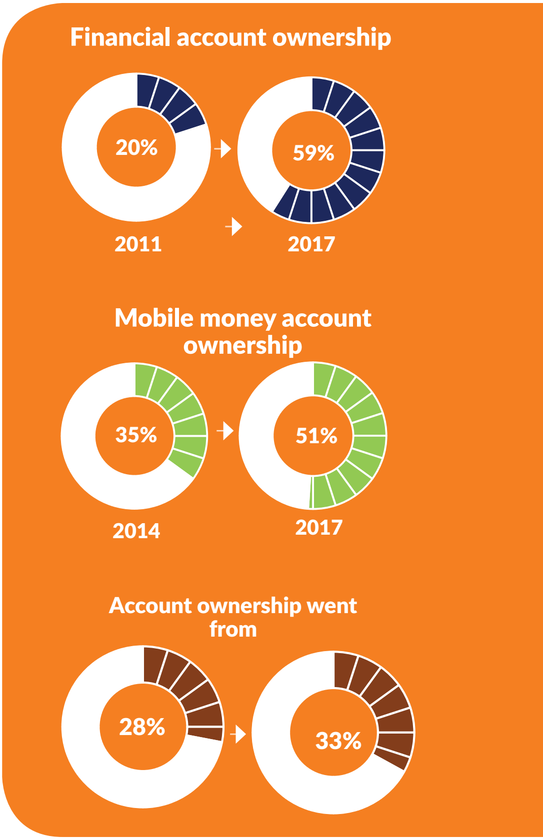
[1] Tax should be Levied on citizens equally. All citizens should pay a tax and it should be proportionate to their ability to pay

[2] http://interactioninstitute.org/illustrating-equality-vs-equity/

4 Reversal of gains on financial inclusion

According to the Findex Database 2017[3], Uganda is ranked second after Kenya in financial inclusion[1] in the East African Community. Financial account ownership jumped from **20% in 2011 to 59% in 2017** largely due to MM. MM account ownership jumped from 35% in 2014 to 51% in 2017, while financial institution account ownership went from 28% to 33%. More than 10 million Ugandans have been able to access formal financial services because of MM. According to CSBAG's analysis and projections, farmers currently use MM to facilitate 53.5% of their annual payments, however imposing the 1% transactional levy will see this number drop to just 5.9% primarily to buy airtime and transfer money to friends and relatives. Higher value services such as paying for school fees will become unaffordable.

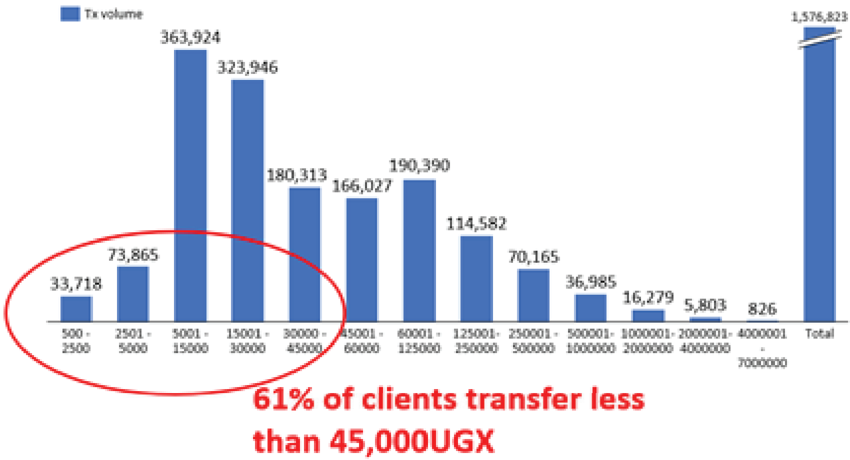
Through financial inclusion, MM has contributed to more efficient payments for goods and services, reduction in the informal economy, employment creation and financial



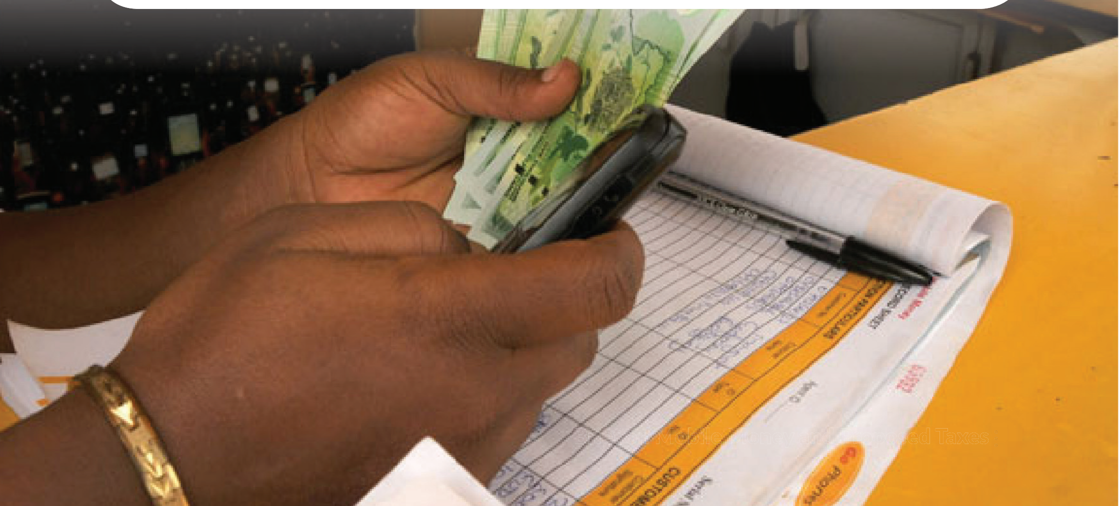
[1]The percentage of respondents who report having an account (by themselves or together with someone else) at a bank or another type of financial institution or report personally using a mobile money service in the past 12 months.

security for vulnerable segments of society. MM also facilitates social sectors, such as healthcare and education. In short, there are strong incentives for the state to support the growth of MM which are likely to be impeded by the proposed tax. Consequently, government's financial inclusion agenda which is heavily reliant on digital financial services to increase access and usage of financial services among Ugandans at the lowest possible cost will be negated.

Figure 2: Number of MM users per cash segment



Source: CSBAG computations



5 Risk of loss of revenue collection and business transaction efficiency

Uganda may incur huge losses from the potential increase in tax revenue if the money collected from the 1% tax cannot compensate for the revenue realized from efficiency gains arising from the use of MM which makes it simple, easy and quick for a taxpayer to settle their obligations. According to government's own report, the use of MM was expected to at least collect an **additional USD 25 million in taxes every month in 2016**.

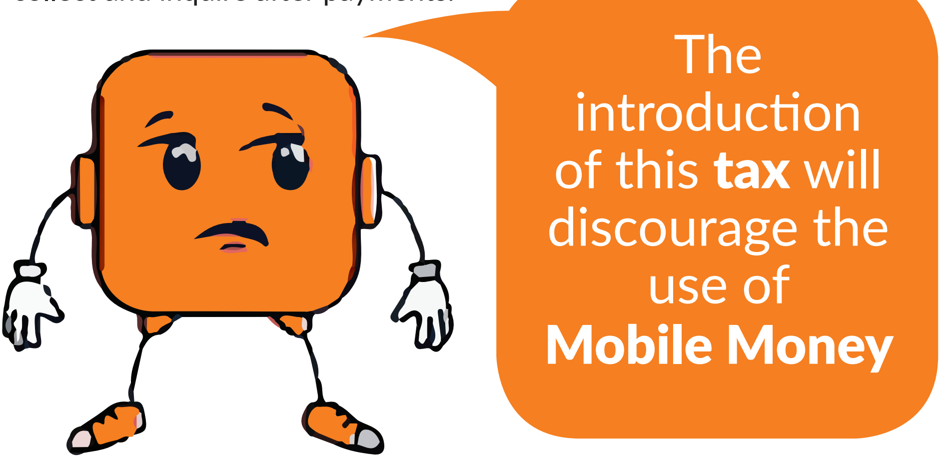
Similarly, the introduction of this tax will discourage the use of MM for utilities payments. MM has increased transaction speeds and reduced outstanding credit times, minimizing the time it takes to collect and inquire after payments.

According to the Bank of Uganda, the power company **UMEME reported a 99.1% revenue collection rate in 2014 compared to 94% in 2012**. The increased revenue collection rate was partly attributable to increased MM payments.

[3]The Global Findex database is the world's most comprehensive data set on how adults save, borrow, make payments, and manage risk. 2017 data was released just recently.

[4]The percentage of respondents who report having an account (by themselves or together with someone else) at a bank or another type of financial institution or report personally using a mobile money service in the past 12 months.

[5]UN briefing note on recent government effort to levy tax on mobile money, April 2018



6 There is a risk of increased youth unemployment

According the Uganda Bureau of Statistics Statistical Abstract 2017, Youth Unemployment increased from 13.2% in 2013 16.4% in the 2015. With MM account ownership growing from 35% in 2014 to 51% in 2017, and the fact that much of this growth has provided employment to the vulnerable youth, especially the women, the tax will make the business returns too little to attract labour and as such create voluntary or disguised unemployment amongst the youth in this trade. Taxing every MM transaction - sending, payment, receiving and withdrawing - as proposed in the tax may discourage growth in MM transactions and ultimately this is going to impact the business model on two fronts; i) with the reduced volumes of transactions the commission and hence revenue to the agents will reduce and ii) reduced commission from the increased withholding tax from 10% to 15%. This will negatively affect the profitability and long-term viability of the more than 60,000 MM agents in the country many of whom are youth.

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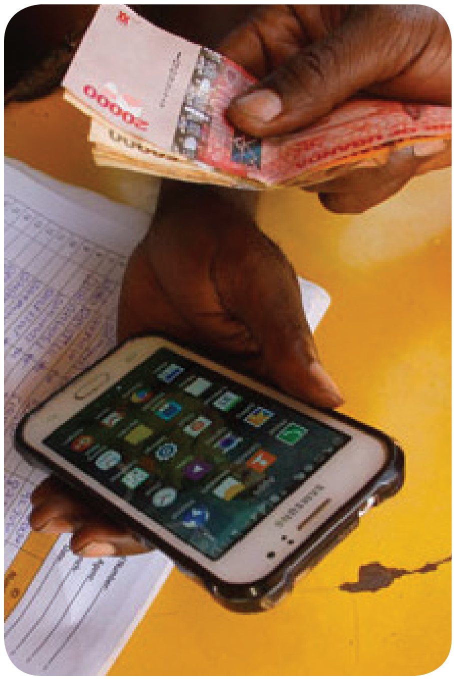
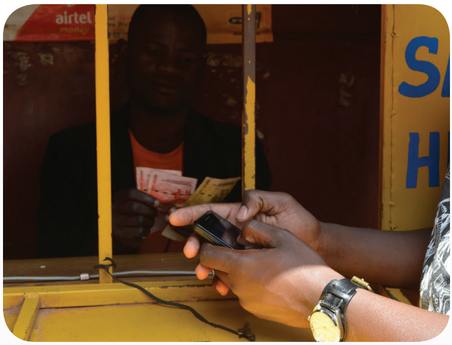


7 May limit usage of digital financial services

The proposed tax may curb the use of digital payment channels in effect impeding government transparency initiatives in revenue collection. The secretariat suggests that traceability of MM transactions significantly reduced reporting and other administrative costs of NGOs, government, businesses and other players. Another unintended consequence could be a slowdown in the development of the Ugandan financial technology sub-sector which is a driver of growth of digital financial services. Because financial technology firms rely on MM as a platform for innovation any increase in the cost of MM transactions will adversely affect innovation.



8 Risks promoting acts of money laundering

The tax could drive users off the MM platform and resort to insecure cash dealings increasing the risks associated with it. The requirement to provide identification at Sim-card registration had started to drive down fraud and money laundering through the financial systems.

By introducing the proposed tax, there is a risk that all these players could revert to using cash (because of the cost), thus increasing fraud incidences and supervision cost.

When all is said and done, Uganda needs tax revenue and as such we propose the following alternatives as more viable sources of revenue without the adverse effects discusses above.

REVENUE PROPOSALS FOR PARLIAMENT TO CONSIDER THAT WON'T HAMPER FINANCIAL INCLUSION

PROPOSAL 1

INCREASE EXCISE DUTY FROM 10% TO 17.5% ON WITHDRAW FEES:

Amend Sec 16 (f) to read in item 14, by substituting for "10% of the fees charged "appearing in the third column, with "17.5% of the withdrawal fees and 15% charged on all transactions fees".

This would generate **UGX 122bn** which is **33bn** below the expected revenue from the 1% transaction tax and the excise duty.

PROPOSAL 2

IMPLEMENT TIERED EXCISE DUTY ON TRANSACTION FEES:

Amend Sec 16 (e) item 13 (d) to read; In item 13, by substituting for "15% of the fees charged "appearing in the third column, with "Tiered excise tax on transaction fees as shown below.

This will raise UGX 86bn with minimum impact on the poor in comparison with the 1% transaction charge on Mobile Money.

Table 2: Proposed excise duty rate

Tiers	Proposed Excise Tax Rate
0-100,000 UGX	10%
100,001 – 1,000,000UGX	15%
1,000,001 UGX and more	20%

PROPOSAL 3

TAX INTEREST INCOME ON THE FLOAT MOBILE MONEY AGENTS DEPOSIT TO BANKS:

The total float mobile money agents deposited in commercial banks amounts to UGX 800bn. If Government of Uganda taxes the interest Commercial Banks earn from this float (escrow account), -in the worst-case scenario at a 3% Treasury Bill interest rate, it can collect UGX 5bn of the current UGX 800bn.

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OUR VISION

A Uganda with a people centered budget.

OUR MISSION

Working towards ensuring that budgets at local and national levels are financed, designed, implemented and monitored to promote prudent and transparent allocation of national resources for the benefit of marginalised groups.

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