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Taxing Mobile Money in Kenya: Impact on Financial Inclusion

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Summary of ICTD Working Paper 168

Financial inclusion – where individuals and businesses have access to useful and affordable financial products and services that meet their needs, delivered in a responsible and sustainable way – is a critical component of economic development. It is particularly important in sub-Saharan Africa (SSA), where there can be little traditional banking infrastructure. The success of M-PESA in Kenya shows that mobile money is helping financial inclusion in the region. Those in rural or underserved areas can use mobile money to access basic financial services – savings, payments, and credit – through their mobile phones. This is critical for impoverished households, helping them to manage their finances, build resilience, and participate more actively in the economy. Financial inclusion aligns with broader development goals, such as poverty reduction and gender equality, by empowering marginalised groups, including women and small-scale entrepreneurs. However, taxation policies can be a threat to the adoption of mobile money in Africa. This study assesses the short- and long-term impact of the Kenyan excise duty on the use of mobile money.

How can taxation be an obstacle to financial inclusion?

Governments often introduce taxes on digital financial services (DFS), including mobile money, to increase domestic revenue and formalise the informal economy – but they risk dampening the growth and accessibility of DFS. Taxes on mobile money transactions can increase costs for users, and may discourage the use of mobile money by vulnerable populations. It is important to assess the impact of DFS taxation on usage patterns, and consider revenue-raising strategies that do not undermine progress in financial inclusion.

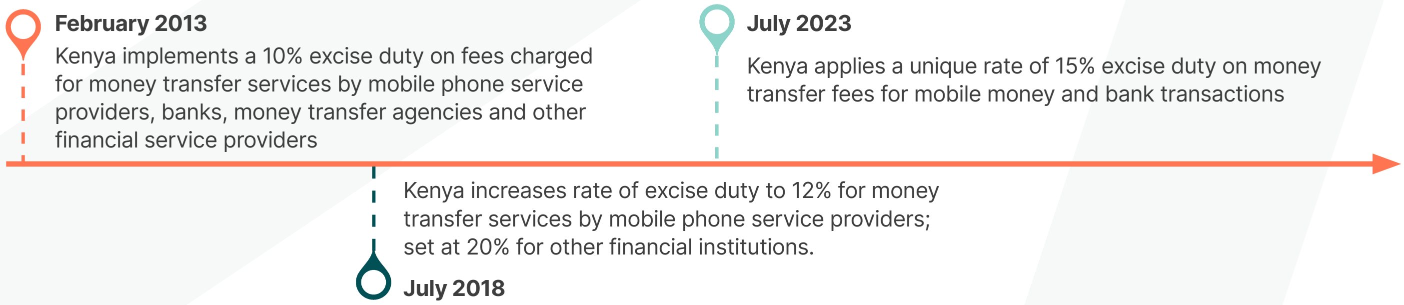
Kenyan excise duty on mobile money transactions

The Kenyan excise duty targets transaction fees associated with money transfers by banks and mobile money. Introduced at 10 per cent in 2013, the rate for mobile money transfers increased to 12 per cent in 2018 and 15 per cent in 2023. More information on the tax design is found at DFS TaxMap.

Research design and data

We use macro- and micro-economic data to assess the impact of the excise duty on mobile money transactions in Kenya. At the macro level, we use monthly data from the Central Bank of Kenya from January 2008 to November 2023, including information on mobile money transactions, agents, registered accounts, inflation, interest rates, exchange rates, monetary indicators, and COVID-19-related data. We construct a Composite Indicator of Economic Activity due to the absence of official monthly GDP data. At micro level, we use five rounds of nationally representative household survey data collected between 2008 and 2014. These surveys, administered to heads of households or their spouses, capture demographic information, household wealth, assets, dwelling characteristics, consumption, shocks, remittances, and

Figure 1. Changes to Kenya's excise duty on money transfers



Source: Adapted from *DFS TaxMap*

mobile phone ownership and usage patterns. Despite limitations, such as attrition rates and missing data on certain variables, these surveys provide valuable insights into individual mobile money usage. Through time series estimations and fixed effects regressions, we analyse short- and long-term effects of the excise duty on various aspects of mobile money usage at both national and individual levels.

Challenge for research: the lack of detailed data on transaction types and user behaviour, and difficulty in getting access to confidential data held by mobile network operators and financial institutions, can make it hard to assess the differential impact of taxation across segments of the population and types of transaction.

Main results

At macro level, using aggregated data on mobile money usage, our analysis indicates that introduction of the excise duty in 2013 had no significant short-term effect on transaction values, but a weakly significant negative impact on transaction volumes. At micro level, while the 2013 excise duty did not drastically reduce mobile money usage, it affected transaction types. The number of transactions that were not taxed, such as savings and bill payments, increased. The rate of growth slowed for transactions that were taxed, like sending and receiving money. The likelihood of using mobile money for household purposes decreased after introduction of the tax, particularly for larger and poorer households – exacerbating concern about equity. The study shows that mobile money services increased the range of bills that could be paid via a mobile money account after 2014.

Policy implications

- Policymakers should adopt a holistic approach, considering the broader implications of taxation on DFS and the unintended consequences of tax – such as increasing the financial burden and reducing access for marginalised groups. Achieving a balance between generating revenue and fostering financial inclusion remains paramount in crafting effective mobile money taxation policies.
- The design and timing of mobile money taxation policies can influence usage patterns. Policymakers should carefully consider which groups are relatively more affected by mobile money taxation, and which measures can prevent a decrease in use of DFS. Tailored rates for different types of digital financial transaction may help spread the burden of the taxation more equally, particularly when associated with the economic status of users. While this could benefit poorer populations, it creates an uneven playing field between banks and mobile money operators.
- Taxation for highly innovative sectors, such as DFS, require a flexible instrument that can adapt to continuous changes, and be designed to consider attitudes and perceptions of users.
- Future research should look further into understanding user attitudes and perceptions towards taxation, and the potential impact of taxation policies on other affected industries.

"The tax on money transfer fees had no significant impact on overall mobile money usage. Survey data shows that affected transactions grew more slowly after introduction of the tax."

Further reading

Diouf, A.; Carreras, M. and Santoro, F. (2023) ***Taxing Mobile Money in Kenya: Impact on Financial Inclusion***, ICTD Working Paper 168, Brighton: Institute of Development Studies, DOI: 10.19088/ICTD.2023.030

Abounabhan, M.; Diouf, A.; Santoro, F.; Sakyi-Nyarko, C. and Scarpini, C. (2024) ***Mobile Money Taxes: Knowledge, Perceptions and Politics. The Case of Ghana***, ICTD Working Paper 183, Brighton: Institute of Development Studies, DOI: 10.19088/ICTD.2024.008

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Credits

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