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EMERGING THREATS OF FINTECHS TO REVENUE MOBILIZATION IN UGANDA

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Uganda's fintech sector has seen an explosive rise over the past few years as witnessed by the disruptions it has caused to the traditional banking systems. From mobile money platforms like MTN Mobile Money and Airtel Money to digital lenders and cryptocurrency exchanges. The country has embraced financial technology in ways that are reshaping how Ugandans manage their financial transactions, investments, savings, credits and others.

However, this growth has also led to challenges in tax compliance. Tax evasion is a significant issue, threatening both the fintech sector's growth and the government's ability to collect revenue for public services.

In this article, we will explore how tax evasion happens in the fintech world, why it's such a big problem and how the government should suit up to combat the emerging threats.

Tax Evasion in the context of Fintechs in Uganda?

At its core, tax evasion is an illegal act where taxpayers deliberately reduce their tax liability by under-declaring, under-paying or non-declaring their appropriate financial positions to the tax body. It can take many forms, and in Uganda's growing fintech landscape, it's often difficult to detect them based on their dynamic state. For example; with the rise of digital wallets, online money lending platforms and cryptocurrency exchange systems, tax evasion is becoming a real concern for the Uganda Revenue Authority (URA) due to varying factors.

Some of the common tax evasion schemes that have been identified in the fintech industry by the financial investigation experts at URA, include [but are not limited] to the following;

- **Underreporting income**: Many fintech companies, especially those offering digital financial services in Uganda underreport the volume of their transactions or generated earnings. With so many transactions happening online, it's easier for companies to misreport their revenue or even hide it entirely with the help of highly sophisticated software. URA has identified this issue especially involving gaming and betting businesses in Uganda.

- **Non-disclosure of foreign income**: Many fintech companies in Uganda operate internationally, meaning they might have income coming from outside the country. Some businesses intentionally fail to report this income to avoid paying taxes on it.

- **Misclassifying transactions or services**: Some fintech platforms tend to misclassify their services to evade taxes. For example, some of those identified from the investigated schemes were observed to classify digital services in a way that minimizes or eliminates their VAT obligations. Also, to note further, some fintech companies that operate mobile payment platforms, were discovered to have categorized their transaction fees as "purely financial services" even though the fees charged for processing the payments fall under taxable services. This allows the company to avoid collecting VAT on the transactions among others.

- **Classifying workers as contractors**: Some fintech companies misclassify their employees as independent contractors to avoid paying social security and other taxes associated with formal employment such as PAYE. This can lead to significant tax losses for the government.

- **Cryptocurrencies**: While cryptocurrencies are still a new and somewhat controversial area, they present major challenges for URA. Fintech businesses that deal with digital currencies like Bitcoin or Ethereum can operate across borders, making it difficult for tax officers to track and tax transactions effectively due to their anonymous nature.

Why Is Tax Evasion a Growing Concern in Uganda's Fintech Sector?

As Uganda continues to embrace new fintech innovations, the ability to track and tax digital financial activities has lagged behind due to a number of factors that have continuously facilitated tax evasion within the Fintech Sector;

- **High volumes of transactions**: Many fintech platforms handle an enormous number of small transactions—whether it's mobile money transfers or peer-to-peer lending. With such high volumes, it's easy for companies to underreport or misreport earnings. This creates a huge risk for tax evasion, especially when transactions occur across multiple digital platforms.

- **Cross-border activities**: One of the unique features of fintech is that it often operates internationally. Money doesn't stay within borders anymore—platforms and users send funds across countries all the time. This complicates the process of taxation, as it's not always clear where the money is coming from or going to. Cryptocurrencies, for example, are completely decentralized, making it even harder for URA to track and tax them.

- **Complex business models**: facilitated by peer-to-peer lending platforms that connect lenders and borrowers directly, acting as intermediaries rather than providing the loan themselves. This can lead to confusion about how to tax the business, since they may not follow the same rules that apply to more conventional financial institutions.

- **Lack of clear regulations**: It is undisputed fact that Uganda's regulatory framework for fintech is still developing as indicated by various reports. However, whereas it is true that the government has made strides in regulating mobile money, other areas of fintech, such as cryptocurrency, remain less clear. The absence of well-defined tax rules can create confusion, which some businesses might exploit to avoid paying taxes.

The Impact of Tax Evasion on Uganda's Economy.

The consequences of tax evasion in the fintech sector go far beyond just the companies involved—it affects the entire Ugandan economy in far more ways that include;

- **Loss of tax revenue**: Tax evasion means that the government is not receiving the funds it needs to invest in critical areas like education, health, and infrastructure. In a country like Uganda, where public services are already underfunded, this loss of revenue has serious consequences for economic development.

- **Unfair competition**: Companies that evade taxes have an unfair advantage over those who comply with the law. For example, a fintech company that doesn't pay VAT or underreports its earnings can offer services at lower prices than competitors who are following the rules. This distorts the market and makes it harder for honest businesses to succeed.
- **Damage to public trust**: Continuous tax evasion can erode public confidence—not just in fintech companies, but also in the government's ability to regulate the sector. If consumers feel that businesses aren't being held accountable, they may lose trust in digital financial services altogether.

- **Reputation risks for Fintechs**: In addition to legal and financial consequences, fintech companies caught evading taxes risk significant reputational damage. For example; a company that is suspected to be engage in tax evasion, once placed investigation, may find it harder to attract investment or customers in the future. It is a public secret that nowadays that consumers, investors, and business partners are becoming more focused on ethical business practices.

What Can Be Done to Tackle Tax Evasion in Uganda's Fintech Industry?

As Uganda continues to develop its fintech industry, it's essential that both the government and businesses take steps to address tax evasion by ensuring:

- **Clearer regulatory frameworks** that specifically address the tax obligations of fintech companies. These regulations should cover everything from mobile money to cryptocurrencies, ensuring that businesses know exactly what they owe and how to comply.

- **Using technology to monitor transactions**: URA can leverage data analytics, artificial intelligence, and other modern technologies to track and monitor digital transactions. With the right tools, it's possible to detect suspicious activities and ensure businesses are paying the correct taxes.

- **Collaboration with fintech companies**: Instead of a purely adversarial relationship, URA and fintech companies can work together to ensure compliance. Regular audits, education on tax obligations, and incentives for voluntary compliance can go a long way in promoting good practices within the sector.

- **Penalties for non-compliance**: Businesses that intentionally evade taxes should face serious penalties. This could include fines, sanctions, or even the suspension of their operating licenses. Clear consequences for non-compliance can serve as a deterrent for others.

- **Consumer awareness**: Finally, educating consumers about the importance of supporting tax-compliant fintech platforms can help create pressure for businesses to follow the law. Informed consumers are more likely to choose services from companies that are transparent and compliant with tax regulations.

Therefore, it is important to note that tackling tax evasion in fintech is not just about securing government revenue, but it's rather about creating a level playing field where innovation can thrive while contributing to the country's overall development.

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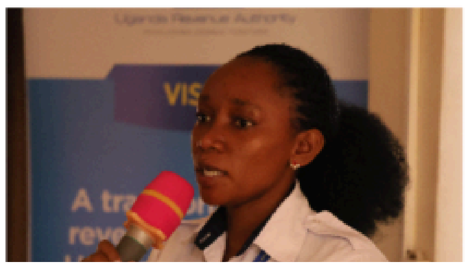


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