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Law School

The Regulatory Power of Taxes: Taxing to Control Betting in Kenya

Submitted in partial fulfilment of the requirements of the Bachelor of Laws Degree, Strathmore
University Law School

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March 2018


DECLARATION

I, **IANCHRIS WACHIRA MUCHANGI**, do hereby declare that this research is my original work and that to the best of my knowledge and belief, it has not been previously, in its entirety or in part, been submitted to any other university for a degree or diploma. Other works cited or referred to are accordingly acknowledged.

Signed: 

Date: 24/4/2018

This dissertation has been submitted for examination with my approval as University Supervisor.

Signed: 

Date: 24/4/2018

Ms Catherine Ngina Mutava

DEDICATION

I would like to dedicate this dissertation to my loving parents and younger siblings who have been with me through the journey, offering support and encouragement when the road was not easy. This work is an inspiration of hard work and determination which I trust will also inspire my younger siblings to scale greater heights.

ACKNOWLEDGEMENT

I thank the Lord Almighty for the energy, health and enthusiasm to pursue the LLB degree despite the ups and downs along the way. I am greatly indebted to my supervisor Mrs Catherine Ngina Mutava for her dedication, guidance, patience, invaluable contribution, effort and encouragement when reviewing and discussing the work and ensuring that the dissertation was well done despite her busy schedule. Once again, I thank her for her valuable time and thoughts in supervising this work and ensuring the correct spellings, grammar and sentencing. I would like to thank everyone who contributed directly and indirectly to the success of this dissertation. To my classmates and colleagues at school, I thank you for the support during the academic years at Strathmore Law School.

ABSTRACT

The activity of sports betting in Kenya has been on a steady rise despite efforts by the government to tame its prevalence. Ever since the first online sports betting company started business in Kenya, there has been an increase both in the number of people taking part in the activity and the number of companies operating in Kenya as bookmakers. The government has put in several policy directives and legislative measures in efforts to curb the dangerous rise in the number of citizens taking part in the activity. Key among them is the imposition of a surtax on the bookmakers' proceeds at the rate of 35% of their gross gaming revenue. This led to an uproar from the stakeholders mainly the bookmakers since they are set to lose a huge amount of their income through this surtax. The government on the other hand has turned a deaf ear to their pleas of revision of the 35% tax rate. Betting taxes have been used in various jurisdictions around the world to achieve regulation objectives. Kenya's problem is not unique. This research draws inspiration from jurisdictions that have levied taxes on betting as a means of bringing the sector under regulation. This is done by way of case studies. Legal theories that justify imposition of taxes in general also inform and guide this research. By drawing lessons from two contrasting jurisdictions, this paper makes a case for the retention of betting tax at 35% on the gross gaming revenue. Keywords: *gambling, betting, regulation, betting tax, gross gaming revenue, stakes.*

LIST OF ABBREVIATIONS AND ACRONYMS

ARJEL	Autorite de regulation des jeux en ligne
BCLB	Betting Control and Licensing Board
CSR	Corporate Social Responsibility
FDJ	Française des Jeux
GGR	Gross gaming revenue
HM Revenue & customs	Her Majesty's Revenue & customs
PMU	Pari-mutuel Urban
UK	United Kingdom

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1. CHAPTER ONE: INTRODUCTION TO THE RESEARCH

1.1. Background of the problem

Gambling has been practised around the world for thousands of years.¹ People have always placed wagers on the outcome of an event between two competitors.² Historically, in almost any human civilization across the centuries there were competition events and contests on whose outcome bets were placed.³ This goes as far back as in the Roman empire where many Roman emperors enjoyed gambling.⁴ For many years, it was only legal to place a bet in Rome at the circus or at the chariot races.⁵ Gambling has lived through the history of sports and competitions. As one tracks sporting events from the early Greece and Roman games up to the modern games such as football, there has always been a market for placing wagers.⁶

One key observation that can be made is that the number of people who could place bets on the outcome of one sporting event during the ancient times was relatively low. The way a wager is placed has changed over the years with advancement in technology causing changes in communication methods.⁷ In ancient times, bets were only made face to face with the two parties present.⁸ In modern times, the methods of betting have diversified leading to growth of the number of people who can place a bet on the outcome of one event.

In Kenya, this business has grown tremendously since 2013 when the first online sports betting operator was launched.⁹ Technological advancement has led to a steady rise of sports betting activities.¹⁰ This is evident from the steadily rising number of firms using the online platform and the number of people taking part in betting.¹¹ The advancement in technology provided room for this growth and more so boosted the speed at which it was happening.

¹ <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

² <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

³ <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

⁴ <http://www.historyinanhour.com/2012/10/22/the-ancient-ages-of-gambling/> on 26 January 2017.

⁵ <http://www.vroma.org/~bmcmanus/circus.html> on 26 January 2017.

⁶ http://www.jblearning.com/samples/0763749591/49591_ch03_mclean on 26 January 2016,

<http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

⁷ <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

⁸ <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

⁹ <http://www.najtion.co.ke/lifestyle/smartcompany/Why-KRA-cant-bet-on-gambling-tax-yet/1226-3030548-c173aqz/index.html> on 15 November 2016.

¹⁰ <http://www.najtion.co.ke/lifestyle/smartcompany/Why-KRA-cant-bet-on-gambling-tax-yet/1226-3030548-c173aqz/index.html> on 15 November 2016.

¹¹ <http://www.najtion.co.ke/lifestyle/smartcompany/Why-KRA-cant-bet-on-gambling-tax-yet/1226-3030548-c173aqz/index.html> on 15 November 2016.

This growth did not escape the government's eye and the public in almost equal measure. The expansion of the betting industry in this way alarmed some.¹² They felt that the government and the Betting Control and Licensing Board (BCLB) were not doing enough to protect the public from exploitation by betting firms and other adverse effects from engaging in the activity. On the other hand, some people were quite pleased to see the betting industry expand.¹³ Their view was that betting activities had led to some more money circulating in the country thus stimulating the economy.¹⁴ When the masses participating in the activity kept growing the government finally faced the challenge; to tame the growth of the betting industry. The challenge presented itself in many ways the most prominent and relevant to this research being choosing a regulatory tool.

The preferred means to address the social challenge of betting was introducing a surtax for the betting sector relative to other businesses, perceived to have less adverse effects to the society, carried out in the country. This was done in the year 2016 when betting tax was put in place.¹⁵ Betting tax is payable to the collector of betting tax by the licenced bookmakers. At the onset, the tax rates were capped at 7.5% of the gaming revenue.¹⁶ Gaming revenue in this case is the gross turnover less the amount paid out to customers as winnings.¹⁷

The government seemed dissatisfied with how things were going and less than a year later, in the budget statement dated 30th March 2017 delivered in parliament by the cabinet secretary for the national treasury, Henry Rotich, proposed to raise taxes for betting, lottery, gaming and competition from the rates of 7.5%, 5%, 12% and 15%, respectively, to a uniform tax rate of 50% for all categories.¹⁸ The proceeds, he said, would be put in the newly created National

¹² <https://www.standardmedia.co.ke/article/2000221452/parents-nightmare-as-gambling-and-betting-craze-grips-estates> on 22 January 2017. See <https://citizentv.co.ke/sports/sports-betting-craze-part-1-kenya-taken-by-storm-119772/> on 22 January 2017. See also <https://citizentv.co.ke/sports/sport-betting-craze-part-2-the-big-numbers-119849/> on 22 January 2017.

¹³ <http://www.nation.co.ke/sports/football/Betting-firms-cash-in-on-Kenyas-gambling-craze/1102-3067790-374h8f/index.html> on 2 January 2017.

¹⁴ <http://mobile.nation.co.ke/news/1950946-3788598-q0j9km/index.html> on 2 February 2017.

¹⁵ Section 29A, *Betting, Lotteries and Gaming Act* (Cap 131) and Section 80, *Finance Act* (Act No. 38 of 2016).

¹⁶ Section 29A, *Betting, Lotteries and Gaming Act* (Cap 131) and Section 80, *Finance Act* (Act No. 38 of 2016).

¹⁷ Section 2, *Betting, Lotteries and Gaming Act* (Cap 131) and Section 79, *Finance Act* (Act No. 38 of 2016).

¹⁸ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

Sports, Culture and Arts Fund to support development of sports, culture and arts in Kenya.¹⁹ The 50% proposal was rejected and parliament settled at a 35% uniform rate.²⁰

Implementation of the 35% rate has however been met with stiff opposition by the Association of Gaming Operators-Kenya (AGOK).²¹ In an open letter to the president, published both online and on print dailies, AGOK laid out its claim that the president had been ill-advised that the tax of such nature would achieve the desired results.²²

1.2.Statement of the problem

The law on betting in Kenya is primarily the Betting, Lotteries and Gaming Act (Cap 131).²³ Betting is licensed and regulated by the Betting Control and Licensing Board (BCLB) created under the Act.²⁴ Locally, the business of bookmaking is carried out in an array of media by a growing number of operators.²⁵ Some operators run betting shops, while others use the online platforms which include short message services.²⁶ The rise in prevalence of betting activities in Kenya, as pointed out in the background information of this research, led to concerns informed by the adverse effects betting activities could cause to the society and to individuals. In the Budget statement of March 2017, the cabinet secretary for the national treasury noted that betting and gaming had become widespread in our society in an environment that is inadequately regulated and that its expansion was beginning to have negative social effects, in particular on the young and vulnerable members of our society.²⁷

The typical response for Kenya to betting would have been to outlaw the activity of betting and deregister the companies who take part in the business of bookmaking. This was certainly not a feasible option due to the huge investment in the business of bookmaking by both local and

¹⁹ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

²⁰ Sections 29, 30, 31, 32, Finance Act 2017.

²¹ <http://www.businessdailyafrica.com/economy/Betting-firms-say-Uhuru-ill-advised-on-35pc-tax-rise/3946234-3983328-format-xhtml-um2y6az/index.html> on 30 August 2017.

²² <http://www.businessdailyafrica.com/economy/Betting-firms-say-Uhuru-ill-advised-on-35pc-tax-rise/3946234-3983328-format-xhtml-um2y6az/index.html> on 30 August 2017.

²³ *Betting, Lotteries and Gaming Act* (Cap 131).

²⁴ Section 2, *Betting, Lotteries and Gaming Act* (Cap 131).

²⁵ World Trade Organization committee on trade and development, *Electronic commerce, development and small, medium-sized enterprises*, 2013.

²⁶ ‘Lilian Ochieng’: Why KRA can't bet on gambling tax yet’ *eDaily Nation*, 12 January 2016

<http://www.nation.co.ke/lifestyle/smartcompany/Why-KRA-cant-bet-on-gambling-tax-yet/1226-3030548-c173aqz/index.html> on 15 November 2016.

²⁷ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

foreign companies.²⁸ Instead, the government introduced a surtax meant to curb the rapid growth of gambling which in its opinion hurts the young and vulnerable, and raise cash to fund sports, culture and the arts.²⁹

Taxes are certainly not new to the betting industry. Prior to the current regime, the Income Tax Act (Cap. 470) was amended to provide for a withholding tax on winnings from betting.³⁰ Punters had to pay a percentage of their winnings from bets placed in the country as tax to the state.³¹ The payment was made through the bookmakers withholding a percentage of the punter's winnings and remitting that to the collector of withholding tax.³² This applied for both residents and non-residents who placed bets in the country.³³ This provision has since been removed.³⁴ Levying withholding tax on the winnings proved to be inefficient both as a revenue collection means and regulation tool.³⁵

The bookmakers on the other hand were displeased by the surtax.³⁶ The Association of Gaming Operators-Kenya claimed that the tax would drive mainstream, legally established betting firms out of business and pave the way for underground, illegal players that would be difficult to regulate.³⁷

These two views of betting tax pose a policy question of the choice of taxation as the regulatory tool to tame growth of the betting sector.

1.3.Purpose of the study

The purpose of this research is to provide an independent review of Kenya's approach to taxing betting with the intention of achieving regulation. This research is an investigation of the use of tax as a regulatory tool for the rapidly growing betting sector in Kenya. The research also evaluates whether betting tax as a regulatory tool will achieve the desired results of reducing

²⁸ <http://www.businesslicense.or.ke/index.php/license/browse> accessed 25 March 2018.

²⁹ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

³⁰ Section 14, *Finance Act 2013*.

³¹ Section 14, *Finance Act 2013*.

³² Section 14, *Finance Act 2013*.

³³ Section 14, *Finance Act 2013*.

³⁴ Section 8 Finance Act (Act No. 38 of 2016).

³⁵ 'Lilian Ochieng': Why KRA can't bet on gambling tax yet' *eDaily Nation*, 12 January 2016 <http://www.nation.co.ke/lifestyle/smartcompany/Why-KRA-cant-bet-on-gambling-tax-yet/1226-3030548-cl73aqz/index.html> on 15 November 2016.

³⁶ <http://www.businessdailyafrica.com/economy/Betting-firms-say-Uhuru-ill-advised-on-35pc-tax-rise/3946234-3983328-format-xhtml-um2y6az/index.html> on 30 August 2017.

³⁷ <http://www.businessdailyafrica.com/economy/Betting-firms-say-Uhuru-ill-advised-on-35pc-tax-rise/3946234-3983328-format-xhtml-um2y6az/index.html> on 30 August 2017.

prevalence of betting activities in the country. There is need for the government to address the concerns of both the public and the private sector with regard to regulation of betting activities.

1.4.Scope of the study

The purpose of this research being to provide an independent review of Kenya's approach to taxing betting. It considers the merits of betting tax, which is a tax on gross gaming revenue, in terms of how it influences regulation of the Kenyan betting market and the tax revenue generated by the betting industry. Other taxes, including corporate tax, licenses and VAT, are not included in the focus of this study.

1.5.Research methodology

This research is conducted by drawing lessons from case studies of jurisdictions where betting tax has been levied to regulate the gambling sector. The findings of the case studies are then discussed to give answers to the research questions and conclusions are drawn. From the conclusions, recommendations will be made to the relevant stakeholders. This study is conducted through desktop review of pre-existing data.

1.6.Hypothesis

The following hypothesis will be tested in this research:

There is a significant regulatory role played by taxation in society and this can be utilised to curb the rise of the betting sector in Kenya to avert undesirable outcomes of overindulgence.

1.7.Research questions and specific objectives

The specific research objectives will be to:

- a. Determine whether tax can be used as a regulatory measure.
- b. Determine whether this regulatory power of taxes can be used to regulate betting in Kenya.
- c. Give recommendations on a suitable approach to regulate the betting sector using tax.

1.8.Research questions

To ensure that the objectives of this research are met, the questions to be asked are:

- a. Can tax be used to regulate social conduct?
- b. Should betting tax in Kenya be levied on the stakes or on gross gaming revenue?

- c. What is Kenya's chosen model of betting tax and why?

1.9. Justification of the study

People have been betting on sports for as long as sports have been played.³⁸ There is no reason to believe that this will change in the future. In modern times, the methods of betting have diversified, and this has come with an increase in the number of the people that participate in the activity. This strains the government as it tries to regulate the growing market for placing wagers on sports played within the country and over.

Despite the imposition of betting tax, the prevalence in sports betting activities has not died down.³⁹ As is expected, this activity has continued to impact on the productivity of the youths in the country.⁴⁰ This would be detrimental to the economy which is dependent upon other things such as agriculture. Overindulgence by the youth would leave these other sectors unattended and trigger a systemic effect bringing down the economy.

This research will therefore seek to show how betting tax will go a long way in achieving reduction of prevalence of betting activities in Kenya and avert the concerns of the government on productivity of the youths in Kenya.

1.10. Literature review

Clarkea and Demp wrote an article titled: "The feasibility of regulating gambling on the internet" in the *Managerial and Decision Economics Journal*.⁴¹ Their focus was on regulating internet gambling since it presented substantial and relatively new challenges to governments and regulatory agencies. They proceeded on the hypothesis that the then existing approaches to betting, lotteries and gaming were limited by the nature of internet technology and the international nature of the activity of internet betting. They considered particular aspects of internet gambling and reached the conclusion that prohibition is an ineffectual alternative and that licensing of gambling service providers was the appropriate approach. This work only

³⁸ <http://sportsgambling.about.com/od/sportsgambling101/a/sportsbettinghistory.htm> on 28 January 2017.

³⁹ <https://www.standardmedia.co.ke/business/article/2001265768/audit-firm-pwc-backs-betting-companies-in-protest-against-tax> on 25 March 2018.

⁴⁰ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

⁴¹ Clarkea R and Demp G, 'The feasibility of regulating gambling on the internet' 22 *The Managerial and Decision Economics Journal*, 1-3 (2001).

focused on licensing and prohibition as methods of regulating internet betting. The phenomena of internet betting, as it was then, is the basis on which online sports betting today is founded.

Paton, Siegel and Williams delved deeper into this issue. Their work was titled “A policy response to the e-commerce revolution: The case of betting taxation in the UK.”⁴² They discussed the impact of technological changes in the betting, lotteries and gaming sector. The fact was that there had been a lot of changes in the betting, lotteries and gaming sector in the UK coming with technological advancement in the 1990’s. The changes included the introduction of a national lottery and the rise of internet gambling. These fundamental changes induced the UK government to conduct a large-scale review of betting duty. As a result of this review, the government announced a significant reduction in betting taxes. The government also decided to replace the then current general betting duty, levied as a proportion of betting stakes, with a gross profits tax, based on the net revenue of bookmakers. The authors examined the economic rationale behind these decisions and demonstrated how these tax changes had broad implications regarding optimal levels of taxation for other sources of government revenue. They took an analytical approach where they sought to understand why the laws were being changed in the UK. It is from their explanations that this research gets its basic premises of the regulatory nature of a tax on betting activities.

This research seeks to go beyond Clarkea’s and Demp’s focus on licensing and prohibition as methods of regulating internet betting. The problem they tried to solve at that time has mutated into a more advanced social problem. The current trend of sports betting especially in online platforms needs to be looked at from a perspective that better regulates it. This is how imposition of a tax on the proceeds of both the bookmakers and the punters comes in as an attempt to regulate the betting sector.

1.11. Limitations of the study

A few challenges face the conduction of this research,

- a. There is not much literature on this topic.
- b. The intended respondents were not forthcoming with information that would form a huge basis on which this research could be accurately concluded.

⁴² Paton D, Siegel D and Williams L, ‘*A policy response to the e-commerce revolution*’, 296.

1.12. Outline of the dissertation and its flow of argument

Chapter one

This is the chapter that provides a background and context of the study, states the problem that is the focus of this study, provides the literature review on what has been written previously in the area of study, states the objectives of the study and questions that will be answered in the study, states the hypotheses that will be tested in the study, outlines the theoretical framework and the design methodology of the study. It is also in this chapter where the limitations likely to face the study are listed and a timeline for the period over which the study will be conducted is given.

Chapter two

This chapter will bear the theoretical framework through which the topic will be examined. It will contain the logical structure that guides the study. Here, key concepts are identified and the relationship between these concepts and the research topic are outlined.

Chapter three

This chapter will provide case studies of the use of taxation to achieve regulation in the betting sector in other jurisdictions. Two case studies will be discussed to show how taxes have been used to successfully or otherwise regulate betting in those jurisdictions.

Chapter four

This chapter first provides an analysis of the findings by answering the research questions and will briefly consider justifications for the imposition of betting tax in Kenya.

Chapter five

This will be the final chapter of the dissertation, it will provide a conclusion on the findings of the research and issue recommendations from the findings while identifying areas of future research.

2. CHAPTER 2. THEORETICAL FRAMEWORK

2.1. Introduction to theoretical framework

Taxes are generally considered to be the common burden for the maintenance of the state.⁴³ However, some taxes are imposed for other reasons beyond raising revenue for the government.⁴⁴ This research is mainly informed by legal theories that would justify imposition of a tax of any nature in society.

2.2. The social contract theory

The social contract theory was developed by many philosophers over time. According to Thomas Hobbes, the idea of self-protection and self-defense is inherent in man, and in order to do so, all his rights and freedoms were voluntarily surrendered to an authority (the state) in exchange for protection and preservation of life and property. This prompted the establishment of the ruler, who would be the total head of administration. According to Hobbes, the protection of the state is paid for by all the citizens in form of taxes.⁴⁵

According to John Locke, the state of nature was sensibly great and enjoyable. It was a condition of peace, goodwill, mutual assistance, and preservation.⁴⁶ However, the property was not secure. In that condition of nature, men had every one of the rights which nature could give them. Man, in the state of nature, felt the need to secure his property and with the end goal of assurance of their property, men entered into the social contract. Under the agreement, man did not surrender all his rights to one single individual. He surrendered just the right to maintain order and enforce the law of nature and retained the other rights, i.e., right to life, liberty and estate because these rights were considered common and basic privileges of men.⁴⁷

Having made a political society and government through their assent, men at that point increased three things which they needed in the state of nature: laws, judges to arbitrate laws,

⁴³ Richard M, Bird J and Scott Wilkie, "Designing Tax Policy: Constraints and Objectives in an Open Economy" *International Center for Public Policy Working Paper* 12-24 April 2012.

⁴⁴ Avi-Yonah, Reuven S, "The Three Goals of Taxation" 2005.

⁴⁵ Hobbes T, "Leviathan", *Cambridge University Press* Cambridge, 1651, 228-229.

⁴⁶ http://www.sophia-project.org/uploads/1/3/9/5/13955288/elahi_socialcontract on 26 March 2018.

⁴⁷ Barker E, Hopkins G, Locke J, Hume D and Rousseau J, "Social contract" *London, Oxford University Press* 1947.

and the official power important to enforce these laws.⁴⁸ This government needed funds to run and could only be raised through taxes.

Jean Jacques Rousseau was a French rationalist who gave another translation to the of social contract theory.⁴⁹ As indicated by him, social contract is not a verifiable truth but a speculative development of reason. Before the social contract, the life in the state of nature was happy and there was balance among men. As time passed, humankind confronted certain progressions. As the general population expanded, the methods by which individuals could fulfill their necessities needed to change. Individuals gradually started to live in families, and afterwards in larger groups made up of several families. Division of labour was introduced, both within and amongst families, and discoveries and innovations made life less demanding, giving rise to leisure time. Such leisure time unavoidably drove individuals to make comparisons between themselves and others, leading to shame and envy, pride and contempt.⁵⁰

In particular, the innovation of private property which constituted the pivotal moment in humanity's evolution out of a simple, pure state into one, characterized by greed, competition, vanity, inequality, and vice was the most important.⁵¹ As indicated by Rousseau, the original freedom, happiness, equality and liberty which existed preceding the social contract, were lost in the civilization. Through the social contract, another type of social association, the state, was shaped to guarantee rights, liberties freedom and equality.

To sum up all the different conceptualizations of the social contract theory, the first premise of social contract theory is that initially man lived in the condition of nature. There was no administration and there was no law to control him.⁵² Secondly, there were hardships and oppression within the society. To overcome these hardships, man went into two agreements.

⁴⁸ Barker E, Hopkins G, Locke J, Hume D and Rousseau J, "Social contract" *London, Oxford University Press* 1947.

⁴⁹ Barker E, Hopkins G, Locke J, Hume D and Rousseau J, "Social contract" *London, Oxford University Press* 1947.

⁵⁰ Barker E, Hopkins G, Locke J, Hume D and Rousseau J, "Social contract" *London, Oxford University Press* 1947.

⁵¹ Barker E, Hopkins G, Locke J, Hume D and Rousseau J, "Social contract" *London, Oxford University Press* 1947.

⁵² <http://www.e-ir.info/2012/10/09/the-social-contract-theory-in-a-global-context/> on 26 March 2018.

In the first agreement, *pact of unionis*, the people sought assurance of protection of their lives and individual property.⁵³ As a result of this pact a society was framed where individuals agreed to respect each other and live in peace and congruity.

In the second agreement, *pact of subjectionis*, the people joined and agreed to comply with an authority and surrendered their rights and freedom to an authority.⁵⁴ The authority guaranteed protection of life, property and to a certain extent liberty. To escape from the state of nature, they all agreed to live under basic laws and make an enforcement mechanism for the social contract and the laws that constituted it.

The state came into being on account of the two understandings. The government needed to fund performance of the duties it owed to the people. This led to the imposition of taxes to generate funds for the government.⁵⁵

2.3. Utilitarian theory

Utilitarianism focuses on the effects of an action.⁵⁶ The moral action is that which produces the greatest good for the greatest number. In other words, the happiness and general well-being of the majority should take priority over the individual. Utilitarianism is a theory which attempts to define the scope and freedom of individual liberty under state authority.⁵⁷ Because it draws a line between the rights of the individual and the rights of others, utilitarianism can be viewed as a form of justice.⁵⁸

Jeremy Bentham's basic assumption is that humans by nature avoid pain and seek pleasure.⁵⁹ He argues that individual happiness is the supreme good. A person should act in a manner that provides happiness for the greatest number.⁶⁰ In other words, happiness would be measure by a quantitative scale (measure happiness by amount or quantity). Those who commit social vices, then, should be punished by the quantity of unhappiness they create.

⁵³ http://www.sophia-project.org/uploads/1/3/9/5/13955288/elahi_socialcontract on 26 March 2018.

⁵⁴ http://www.sophia-project.org/uploads/1/3/9/5/13955288/elahi_socialcontract on 26 March 2018.

⁵⁵ Hobbes T, "Leviathan" *Cambridge University Press*, Cambridge, 1651, 228-229.

⁵⁶ Mill J, Bentham J and Ryan A, "Utilitarianism and other essays" *Harmondsworth, Middlesex, England*, Penguin Books 1987.

⁵⁷ <https://www.iep.utm.edu/util-a-r/> on 25 March 2018.

⁵⁸ <https://www.iep.utm.edu/util-a-r/> on 25 March 2018.

⁵⁹ Mill J, Bentham J and Ryan A, "Utilitarianism and other essays" *Harmondsworth, Middlesex, England*, Penguin Books 1987.

⁶⁰ Mill J, Bentham J and Ryan A, "Utilitarianism and other essays" *Harmondsworth, Middlesex, England*, Penguin Books 1987.

Bentham is an “act utilitarian.” Act utilitarians uphold two ideals: first, that the worth of an act should be judged according to its pleasant and unpleasant consequences; two, that a person should act in such a way that his act will promote the greatest good for the greatest number.⁶¹

John Stuart Mill believes that happiness is determined by the individual.⁶² In addition, he argues that no one individual can determine what will produce happiness for every individual. Thus, he believes that a democracy which provides for maximum individual participation and creates an environment for the pursuit of happiness is the best way to secure man’s quest for his own good and promote happiness. Thus, democracy is an avenue to provide individual happiness to the greatest number.

To define the extent that an individual should be allowed to exercise his liberty, Mill refers to the “harm principle” which says that the only good reason for restricting a person’s liberty is to prevent harm to others.⁶³ Mill argues that punishment should only be used if it would lead to better consequences than non-punishment.

Mill is a “rule utilitarian.” Rule utilitarians support three main ideas: one, that the moral worth of an act is judged according to the good or bad consequences that result from following a moral rule of conduct; two, that a person should follow a moral rule that brings more good consequences than another rule would; and three, that all moral rules which produce the greatest happiness for the greatest number should be obeyed.⁶⁴

2.4.Conclusion and Connection of the theories to taxation

Modern philosophers have focused on the legitimacy of taxes as a means of equality. Taxes are seen primarily as ‘the cost of the rights’. Here, any right guaranteed by the government is a positive right whose protection must be financed through taxes.⁶⁵ Thus, according to the social contract theory, the legitimacy of tax law is based on the liberal-democratic procedure by which

⁶¹ <https://www.iep.utm.edu/util-a-r/> on 25 March 2018

⁶² Mill J, Bentham J and Ryan A, “Utilitarianism and other essays” *Harmondsworth, Middlesex, England*, Penguin Books 1987.

⁶³ Mill J, Bentham J and Ryan A, “Utilitarianism and other essays” *Harmondsworth, Middlesex, England*, Penguin Books 1987.

⁶⁴ <https://www.iep.utm.edu/util-a-r/> on 25 March 2018

⁶⁵ Sugin L, ‘Theories of distributive justice and limitations on taxation: What Rawls demands from tax systems’ *72 Fordham Law Review*, 27.

positive law is produced and the obligation to pay taxes is included as a special case of the obligation in general to obey the law.⁶⁶

The utilitarian theory generally seeks to promote social welfare. Taxes can therefore be used to improve social conditions and bring happiness to the masses in that the state uses them to provide the most basic and common needs of its citizens. Also, an argument may be made that betting tax advances this quest for the greater good in society. When bookmakers are taxed at such high rates as capped by the Act, money gathered from the society through lost wagers is recovered through taxes and redistributed by the government. This holds true from the fact that often, most of the stakes placed in wagers end up in the hands of the bookmaker in the event of a loss. Taxation of the bookmakers at a high rate is greater a good than when the bookmakers keep all the proceeds of betting with minimal taxation. More on this will be discussed in chapter four.

⁶⁶ Menéndez A, “Justifying taxes: Some elements for a general theory of democratic tax law” *Kluwer Academic Publishers*, London, 2001, 1-27.

3. CHAPTER THREE: CASE STUDIES

3.1. Introduction to case studies

Other governments' decisions to use tax to regulate betting can be examined through case studies. To evaluate taxes on betting, this paper limits its area of study to comparison of the experience of other jurisdictions in regulating their betting markets. It is acknowledged, at this stage, that in drawing conclusions from such comparison other variables affecting the performance of betting markets may come into play. These variables shall be held constant for purposes of this research. By so doing, this chapter will outline the experience of two jurisdictions, the United Kingdom (UK) and France.

3.2. United Kingdom

3.2.1. Introduction

In the UK, the laws relating to gambling are less complicated. Most forms of gambling are legal in a well-regulated market.⁶⁷ As a result, betting and gaming has grown into big business with hundreds of retail betting shops and land-based casinos and poker rooms established throughout the jurisdiction. The UK led the journey to liberalisation of online gaming in Europe.⁶⁸ There are numerous UK based online gambling sites and many more foreign-based sites that legally provide their services to residents.⁶⁹

3.2.2. Regulation of gambling

The UK has perfected its regulation on the gambling market for more than five centuries.⁷⁰ Regulation has been shaped by moral, social and economic factors affecting the industry.⁷¹ The Gambling Commission regulates the industry as mandated under the Gambling Act of 2005.⁷² The Commission issues licenses to gambling operators and impose fines or revokes licenses, if necessary, when the terms of issuance are violated.⁷³ The objectives of the Gambling

⁶⁷ <https://thelawreviews.co.uk/edition/the-gambling-law-review-edition-2/1144073/united-kingdom> on 7 April 2018.

⁶⁸ www.theleader.info/2017/12/01/gambling-regulation-across-europe-increase/ on 7 April 2018.

⁶⁹ <http://www.bestcasinosites.net/blog/uk-gambling-law.php> on 7 April 2018.

⁷⁰ Crump J, "The perils of play: Eighteenth-century ideas about gambling".

⁷¹ Crump J, "The perils of play: Eighteenth-century ideas about gambling".

⁷² Section 20, *Gambling Act* (UK).

⁷³ Section 117, *Gambling Act* (UK).

Commission are: to prevent gambling from becoming a source of crime or disorder, being associated with crime or disorder, or being used to support crime; to ensure that gambling is conducted in a fair and open way and to protect children and other vulnerable persons from being harmed or exploited by gambling.⁷⁴ The commission also ensures that operators who offer gambling services, including those who do it online, meet the necessary standards.⁷⁵

When it comes to providing online gambling services to UK residents, only companies whose operations are based in the UK can be issued with licenses by the Gambling Commission.⁷⁶ However, the Gambling Commission has a whitelist of approved gambling jurisdictions.⁷⁷ Operators who obtain licenses from within those jurisdictions may also offer their services to UK punters.⁷⁸

3.2.3. Taxation of the gambling market

In the UK both amateur and professional gamblers do not pay tax on their winnings.⁷⁹ In 2001, betting levy, which was a 6.75% tax based on stakes was abolished.⁸⁰ This allowed punters to bet tax free whether they won or lost. To date, the winnings are still not taxable and punters do not need to declare the winnings as a source of income.⁸¹ However, it is necessary to declare winnings from gambling to Her Majesty's Revenue & Customs (HM Revenue & Customs) even though they are not taxed because declaring makes it easier to prove source of wealth in any future instances where one is tasked with proving their source of income or is audited for fraud and other financial crimes.

With the 2001 changes, all bookmakers were required to pay a 15% tax on gross gaming revenue at the point of supply.⁸² The point of supply taxation meant that only UK- based bookmakers, who offered their services to UK residents in UK, were required to pay the 15% tax. Bookmakers based outside the jurisdiction were not required to pay the tax because they

⁷⁴ Section 1, *Gambling Act* (UK).

⁷⁵ Section 89, *Gambling Act* (UK).

⁷⁶ Section 340, *Gambling Act* (UK).

⁷⁷ http://www.culture.gov.uk/Reference_library/Publications/archive_2007/whitelisting_criteria.htm on 7 April 2018.

⁷⁸ http://www.culture.gov.uk/Reference_library/Publications/archive_2007/whitelisting_criteria.htm on 7 April 2018.

⁷⁹ <https://www.casino.co.uk/guides/gambling-and-taxation/> on 1 April 2018.

⁸⁰ <http://www.dailymail.co.uk/sport/article-28835/Betting-tax-abolished.html> on 1 April 2018.

⁸¹ <http://www.dailymail.co.uk/sport/article-28835/Betting-tax-abolished.html> on 1 April 2018.

⁸² <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

did not supply their services from within the UK. In addition to this, the Remote Gaming Act of 2007 introduced regulation for online casino gaming setting the same tax base and rate as that for betting.⁸³

In 2014, there was introduced a 15% tax on gross gaming revenue at the point of consumption.⁸⁴ The point of consumption means that all bookmakers whose services are consumed in the UK were required to pay 15% tax on the gross gaming revenue from their services in UK. This was meant to bring offshore bookmakers under the regulation of the Gambling commission.⁸⁵

3.2.4. Impact of taxation

In 2001, when the betting levy was abolished and replaced by a 15% tax on bookmakers' gross gaming revenue at point of supply, more betting companies moved their online operations offshore.⁸⁶ This was because by so doing they needed not pay betting tax which was levied in the UK. Offshore bookmakers would only pay the UK corporate tax on profits while escaping the 15% betting tax paid by UK-based bookmakers.⁸⁷

As the online gambling market steadily grew over the subsequent decade this problem became more visible to the government.⁸⁸ In 2014 the Gambling Act 2005 was amended introducing a 15% tax on gross gaming revenue at the point of consumption.⁸⁹ This means that off-shore companies were obliged to pay tax on gross gaming revenue generated from UK-based punters to HM Revenue & Customs. Failure to do so would make a betting company lose its license or be ineligible to obtain or be re-issued with a UK gambling licence.⁹⁰

Since the UK was one of the largest and lucrative markets for the gambling industry, most off-shore bookmakers were interested in remaining within the UK market.⁹¹ Bookmakers with a significant market in the UK, who could afford to shoulder the point of consumption tax on gross gaming revenue, updated their licenses as opposed to taking their business elsewhere.⁹²

⁸³ <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

⁸⁴ *Gambling (Licensing and Advertising) Act 2014* (UK).

⁸⁵ *Gambling (Licensing and Advertising) Act 2014* (UK).

⁸⁶ 'The Gambling Act 2005: A bet worth taking?' The Department for Culture, Media and Sport 2011.

⁸⁷ 'The Gambling Act 2005: A bet worth taking?' The Department for Culture, Media and Sport 2011.

'The Gambling Act 2005: A bet worth taking?' The Department for Culture, Media and Sport 2011.

⁸⁹ *Gambling (Licensing and Advertising) Act 2014* (UK).

⁹⁰ *Gambling (Licensing and Advertising) Act 2014* (UK).

⁹¹ 'The Gambling Act 2005: A bet worth taking?' The Department for Culture, Media and Sport 2011.

⁹² 'The Gambling Act 2005: A bet worth taking?' The Department for Culture, Media and Sport 2011.

The point of consumption tax on gross gaming revenue has impacted the bookmakers' behaviour, therefore affected market growth and prevalence. On the one hand, this tax raises the budget of bookmakers and causes them to cut on costs such as advertising thus fewer adverts and promotional offers are seen.⁹³ Advertisement is directly linked to prevalence of betting activities.⁹⁴ Therefore, reduced advertisement leads to a reduced market size and prevalence.

On the other hand, both punters and bookmakers have strong incentives to participate in the regulated market.⁹⁵ These include the advantage of lower prices in the regulated market.⁹⁶ The prices are lower due to more competition as compared to the non-regulated market because more punters have moved to the regulated market.⁹⁷ This is an incentive for the punters to place bets in the regulated market. The bookmakers on the other hand have more marketing opportunities which are not available in the non-regulated market and the public trust associated with being regulated brings them more business.⁹⁸ The prevailing conditions are such that most bookmakers see it in their interests to become regulated in the UK.⁹⁹

A survey conducted in 2015 by the gambling commission found that the impact to the UK gambling market by the 2014 amendment to the Gambling Act was in no way as detrimental as many had feared it could be.¹⁰⁰

3.2.5. Findings from the UK

The case study of UK illustrates that taxation based on gross gaming revenue of the online gambling market leads to achievement of regulation. This is because taxation on gross gaming revenue produces the desired results of regulation. Regulation is meant to ensure that gambling takes place in an environment that is both conducive and legally governed. Taxation raises the budget for bookmakers and causes them to decrease advertisement and promotional offers. This in turn leads to lower punter participation thus achieving the effect of reduced prevalence

⁹³ *Gambling (Licensing and Advertising) Act 2014 (UK).*

⁹⁴ *Gambling (Licensing and Advertising) Act 2014 (UK).*

⁹⁵ <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

⁹⁶ <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

⁹⁷ Paton D, Siegel D and Vaughan W, "A Policy Response To The E-commerce Revolution: The Case Of Betting Taxation In The UK" *The Economic Journal* 2002.

⁹⁸ *Gambling (Licensing and Advertising) Act 2014 (UK).*

⁹⁹ <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

¹⁰⁰ <https://www.jackpotmobilecasino.co.uk/new-uk-gambling-act/> on 7 April 2018.

of gambling. The stronger the regulation of the gambling market, the more the incentives there are for operators to participate in a regulated market due to the conducive environment created for operation.

3.3. France

3.3.1. Introduction

France is a country with a longstanding Christian-Catholic tradition where gambling has been totally prohibited for a long time because it is considered immoral.¹⁰¹ A general ban on gambling relating to games of chance has been in place but over time, certain gambling activities authorised.¹⁰² There is very strict regulation on gambling in France due to moral underpinnings. Gambling services must be either offered in specific registered premises or provided by authorised operators.¹⁰³ The categories of online gambling that are legal in France are sports betting, horse racing, and poker. One gambling platform that is conspicuously absent is online casino games.¹⁰⁴

3.3.2. Regulation

French gambling laws are implemented by three main bodies. These are Pari-mutuel Urban (PMU), which is responsible for horseracing¹⁰⁵ while Française des Jeux (FDJ) is the entity that is responsible for lotteries and betting games.¹⁰⁶ The third is Autorite de regulation des jeux en ligne (ARJEL) which is an independent administrative authority that was specifically established to regulate online gambling in France.¹⁰⁷ ARJEL loosely translates to French for “the regulatory authority for online games”.

¹⁰¹ Valleur M, “Gambling and gambling-related problems in France” *National gambling Experiences*, Hôpital Marmottan, Paris, France.

¹⁰² Article L.324-1, *French Code of Homeland Security* (France).

¹⁰³ Article L.324-1, *French Code of Homeland Security* (France).

¹⁰⁴ *Gambling Act 2010* (France).

¹⁰⁵ <https://www.pmu.fr/> on 1 April 2018.

¹⁰⁶ <https://www.groupefdj.com/> on 1 April 2018.

¹⁰⁷ <http://www.arjel.fr/> on 1 April 2018.

Online betting was legalized in 2010 by the implementation of the French Gambling Act.¹⁰⁸ The French authorities deem online casino games too addictive and therefore do not permit online casinos.¹⁰⁹

3.3.3. Taxation

The gambling industry in France is faced with very high rates of taxes. The tax rate on online gambling is 46.30% levied on the bookmakers based on total stakes placed by the punters.¹¹⁰ In addition to that, online bookmakers are required to pay 33% corporation tax on profits.¹¹¹ Punters on the other hand must pay 2% of their winnings to the government as taxes.¹¹²

3.3.4. Impact of taxation

The development of the French online gaming market has two distinct stages. The first stage is the period pre-regulation (pre-2010) which was characterised by the declining dominance of PMU as unregulated competition provided a variety of gaming products at more attractive rates.¹¹³ This caused the online market which was largely unregulated to grow faster than PMU's online market that was heavily regulated during the same period.¹¹⁴ This meant that potential government tax revenue was not captured. The second stage is post-2010, where the market grew mostly as a result of new entrants into the locally regulated market following implementation of the new Act.¹¹⁵

The high tax rates coupled with significant market restrictions have become a barrier to entry for bookmakers.¹¹⁶ This is because it makes market entry less appealing. Similarly, it encourages bookmakers to remain unregulated and operate outside the jurisdiction of the regulators. The high tax rates on stakes also leads to lower investment in gaming due to the poor return on investment for punters. This in turn reduces levels of gaming activity within the regulated market.

¹⁰⁸ *Gambling Act 2010* (France).

¹⁰⁹ *Gambling Act 2010* (France).

¹¹⁰ <http://www.gamblingresearch.com/france-high-taxation-ruining-its-online-gambling-market/> on 2 April 2018.

¹¹¹ <http://www.gamblingresearch.com/france-high-taxation-ruining-its-online-gambling-market/> on 2 April 2018.

¹¹² <http://www.gamblingresearch.com/france-high-taxation-ruining-its-online-gambling-market/> on 2 April 2018.

¹¹³ PwC report on gambling in the EU 2011

¹¹⁴ PwC report on gambling in the EU 2011

¹¹⁵ PwC report on gambling in the EU 2011

¹¹⁶ PwC report on gambling in the EU 2011

In addition, a tax on stakes is not designed to adapt to additional gambling products that may be available online in future. For example, cash poker would not be regulated effectively under a stakes tax regime because the operators' profits are very low compared to the total value of all customer stakes. Similarly, offline games such as casino table games have an inflexible gross profit margin and are therefore not well suited to being taxed on a proportion on stakes.

3.3.5. Findings from France

The case study of France leads this research to important lessons in evaluation of regulation of online gambling through taxation. Firstly, for a newly liberalised gambling market such as the one in France, higher rates of tax coupled with significant market restrictions can become a barrier to entry for bookmakers seeking to establish themselves in the market. Gambling in France seems to be hindered by tough taxation. High rates of tax based on stakes does not appear to achieve regulatory control of the gambling market in France but acts as a deterrent. The rate of tax is a crucial factor in determining the expected level of regulation in a market. Higher tax rates encourage a lower rate of regulation which gives the government, regulating bodies and operators fewer opportunities to introduce socially responsible policies compared to highly regulated markets. A higher tax rate can also lead to lower investment in gaming due to the poor return on investment for punters. This may in turn reduce levels of gaming activity within the regulated market.

4. CHAPTER FOUR: DISCUSSION OF FINDINGS

4.1. Introduction to chapter four

This chapter will answer the research questions by discussing the findings of the case studies but first it shall establish whether there exists a connection between levying taxes and regulating conduct.

Secondly, since the purpose of this research is to provide an independent review of Kenya's approach to taxing betting with an intent of regulation, this chapter shall evaluate whether betting tax should be based on gross gaming revenue or on stakes. Particularly, this chapter considers the relative merits of a tax on gross gaming revenue against the benefits of a tax on stakes in terms of how these different tax regimes influence regulation of the betting market and the tax revenue generated by the industry.

Finally, this chapter will analyse the chosen model in Kenya which is a 35% tax on gross gaming revenue.

4.2. Can tax be used to regulate social conduct?

The question of whether taxation can be a means of achieving desired social conduct was the main subject of determination in the case *Virginia v. Sebelius* at a District court in the State of Virginia,¹¹⁹ The imposition by Congress of a financial penalty on people who declined to purchase medical cover, provided for in the Patient Protection and Affordable Health Care Act, was challenged in this case.

The State of Virginia contended that calling this levy a tax, as Congress did, added nothing to its legitimacy since the non-compliance punishment does not meet the criteria for a tax because the motivation behind it was to regulate conduct, not to generate revenue for the government. On the other hand, the Federal Government contended that taxation has frequently been used for regulatory purposes, and that a tax does not stop to be legitimate just on the grounds that it controls, disheartens, or even certainly discourages the exercises taxed.¹²⁰

While declining to uphold Virginia's challenge to the constitutionality of the Act, the Judge laid out two contending visions of tax collection. He observed that taxation has two well-understood objectives. Undoubtedly, as proposed by the state of Virginia, the first and most

¹¹⁹ *Virginia v. Sebelius*, Civil Action No. 3:10CV188-HEH (2010).

¹²⁰ *United States v. Sanchez*, 340 U.S. 42, 44 (1950).

generally acknowledged one is to raise revenue for fundamental government functions. The second objective of tax collection is redistribution of wealth. In addition, the judge stated that taxation has a third objective, which has not been seen in application broadly; a regulatory objective. In most developed countries, governments utilize the taxation framework to change the conduct of actors in the private sector, by incentivizing activities they wish to advance and by disincentivizing activities they wish to debilitate.¹²¹

Most analysts have faulted the utilization of taxation for regulatory purposes.¹²² Regulation, they contend, ought to either be straightforward or that it be done through subsidies or penalties.¹²³ They argue that tax collection bodies ought to be left to their appropriate role of collecting taxes, with a conceivable sense of accomplishing redistribution of wealth.¹²⁴

However, this regulatory capacity of the tax system is well-established. Indeed, it can be seen that a few types of taxes, for example, Pigouvian taxes intended to discourage certain exercises by compelling private actors to internalize their social expenses, are completely regulatory in nature. Pigouvian taxes are corrective taxes charged on the generator of a negative externality in order to mitigate the consequences of the externality.¹²⁵ Externalities include but are not limited to social costs. Social costs are the expenses to an entire society resulting from an activity.¹²⁶ When assessing the overall impact of its commercial actions in terms of social costs, a socially responsible business should not only consider its own production expenses but also, any indirect expenses or damages borne by others.¹²⁷

Taxation can therefore advance the goal of regulating human and social conduct by forcing private actors to internalize the social costs of their activities.¹²⁸

¹²¹ *Virginia v. Sebelius*, Civil Action No. 3:10CV188-HEH (2010).

¹²² Avi-Yonah, Reuven S., "Taxation as Regulation: Carbon Tax, Health Care Tax, Bank Tax and Other Regulatory Taxes" *Law & Economics Working Papers* Paper 21 2010.

¹²³ Avi-Yonah, Reuven S., "Taxation as Regulation: Carbon Tax, Health Care Tax, Bank Tax and Other Regulatory Taxes" *Law & Economics Working Papers* Paper 21 2010.

¹²⁴ Avi-Yonah, Reuven S., "Taxation as Regulation: Carbon Tax, Health Care Tax, Bank Tax and Other Regulatory Taxes" *Law & Economics Working Papers* Paper 21 2010.

¹²⁵ Arthur C. Pigou, "The Economics of Welfare", 1920.

¹²⁶ Goodwin N, "Internalizing externalities: making markets and societies work better" *Opinionsur virtual publication Free Monthly Publication* 52 2007.

¹²⁷ ¹²⁷ Goodwin N, "Internalizing externalities: making markets and societies work better."

¹²⁸ Porket J, "The pros and cons of government regulation", *Institute of Economic Affairs* 2 Lord North Street, London SW1P 3LB 23 January 2003.

4.3.Should betting tax be levied on the stakes or on gross gaming revenue?

Since it has been established above that taxation can achieve regulation goals, this research then focuses on the two types of taxes that may be levied on the betting industry and how effective each could be in achieving regulation. These are gross gaming revenue-based taxation and stakes-based taxation. A tax on stakes is levied on the total money gambled by the punters. While on the other hand a tax on gross gaming revenue for games in which the operator accepts risk is defined as total stakes less winnings. For games in which the operator accepts no risk gross gaming revenue is the revenue that accrues to the operator.

In chapter three, this paper makes key findings from the experiences of the two jurisdictions. First, a tax regime with a gross gaming revenue tax base such as the one in the UK seems to achieve higher levels of regulation of the online market. On the other hand, the stakes-based tax regime in France appears to limit regulation by making the locally regulated market less attractive to both the bookmakers and punters in comparison to non-regulated competition from outside the jurisdiction.

According to the findings in chapter three, a tax on gross gaming revenue delivers the highest regulation due to strong incentives both for bookmakers and punters. This outcome is consistent with the experiences seen in other European jurisdictions. The French betting sector has not performed as per the expectations due to a high tax rate based on stakes, while the UK market has grown strongly with high regulation in a lower tax rate environment based on gross gaming revenue.

Betting restrictions such as customer stakes limits or banning betting, previously applied in the UK and currently applied in France, significantly shift gaming from the regulated market to the non-regulated market given the share of the market. Such restrictions are designed to protect punters but they would drive activity away from the regulated market to an unregulated market where operators are not required to protect punters with measures such as under age controls.

A smaller unregulated market and larger regulated market in Kenya is expected to support greater punter protection and allow authorities to monitor and limit the extent of problems associated with gambling. Thus, a tax such as 35% on gross gaming revenue which incentivises bookmakers to be locally-regulated and customers to use locally regulated operators may be able to better support the control of problems associated with gambling and increase protection of punters than stakes-based taxes.

Looking forward, a tax on gross gaming revenue is also compatible with all types of gaming products unlike a tax on stakes which does not work with traditional forms of some casino games. This therefore avoids restricting the supply of gaming products which may be regulated online in the future. This also future-proofs the tax regime to future innovations in gaming.

The evaluation of the relative merits of a tax on gross gaming revenue and a tax on stakes for the regulation of online sports betting concludes that regulating the online sports betting market in Kenya with a tax on gross gaming revenue makes the most economic and social sense for the regulator, operators, and customers.

It is therefore true that a tax on gross gaming revenue delivers: the highest regulation by reducing the unregulated market, the highest growth of a regulated market in Kenya and the highest tax revenues. This is due to strong incentives both for bookmakers to become locally regulated and for punters to gamble with locally regulated bookmakers.

4.4. Betting tax model in Kenya

In order to evaluate the benefits of taxation in regulation of betting in Kenya, this chapter concludes by discussing the Kenyan case where betting is taxed at 35% on the gross gaming revenue. When we look at betting tax in Kenya, it ought to achieve the three goals of taxation; revenue collection, redistribution of wealth and regulation.

Betting tax undoubtedly raises revenue for the government. With huge turnovers and profit margins, the betting industry is worth billions of Kenyan shillings. It has been projected that the betting market could earn Kenya up to an estimated Ksh.500 million in taxes annually.¹²⁹

Most developed countries see taxation framework as an approach to redistribute national income.¹³⁰ Despite Kenya being a developing country, betting tax reintegrates to the national revenue and redistributes 35 percent of the money lost in stakes. This money is then used to fund sporting activities thus nurturing talent.¹³¹ In addition, this addresses the problem of profit repatriation without adequate taxation on profits made by foreign bookmakers and locally incorporated bookmakers with foreign shareholding.¹³² If there is inadequate taxation a lot of

¹²⁹ PwC, *Betting on Africa: Gambling Outlook: 2013-2017 (South Africa- Nigeria-Kenya)*, November 2013.

¹³⁰ *Virginia v. Sebelius*, Civil Action No. 3:10CV188-HEH (2010).

¹³¹ Section 29A, *Betting, Lotteries and Gaming Act* (Cap 131).

¹³² <https://www.economist.com/blogs/economist-explains/2017/10/economist-explains-5> on 24 March 2018.

wealth could be moved out of the country.¹³³ Betting tax is therefore a safeguard measure of the government aimed at protecting the citizens.¹³⁴

Betting tax may also be a means to equalize the benefits of money raised from betting. This is reached by ensuring that not only bookmakers but also the Kenyan people benefit from the proceeds of betting. Bookmakers are seen to reap huge benefits due to some factors such as low production and operating costs. The cost of production for bookmakers is quite low because they depend on wagers placed by the punters to run their businesses. The capital investment is relatively minimal because many of these companies work online and have few or no employees, minimal or physical presence thus no need for operation premises. In terms of benefits to society, besides the occasional winnings paid out to winners and scattered corporate social responsibility (CSR) projects such income is barely used to benefit society.

Based on these justifications for betting tax, it is evident that betting tax not only seeks to achieve regulatory objectives but also redistributive and safeguarding objectives

¹³³ <https://www.economist.com/blogs/economist-explains/2017/10/economist-explains-5> on 24 March 2018.

¹³⁴ Budget Statement for the Fiscal Year 2017/2018(1st July – 30th June) by Mr. Henry K. Rotich, EGH cabinet secretary for the national treasury March 30, 2017. Par 156.

5. CHAPTER FIVE: CONCLUSION AND RECOMMENDATIONS

5.1. Conclusion

This research has analysed case studies from the two European jurisdictions and concludes that a betting tax will result in a higher local regulation of the betting industry while generating higher tax revenues from betting.

These conclusions are based on key findings which are discussed in detail within chapter 4 of this paper. The experience of foreign jurisdictions that have already regulated online gaming supports the assertion that a tax on gross gaming revenue is the most effective way to regulate the betting industry.¹³⁵ This research finds that taxation of the sports betting market in Kenya has the potential to decrease significantly the proportion of the market which is currently unregulated by bringing the foreign bookmakers under the regulation of BLCB. The most effective means of doing so is with a tax on gross gaming revenue as captured in the betting tax currently in place. This research further finds that such taxation reduces the amount of money leaving the country in form of profit repatriations leading to better protection of the Kenyan economy and collection of more revenue from tax.

The findings are further supported by evidence that attempts to block citizens from accessing online betting sites have not proven to be wholly effective due to legal, practical and technical limitations. The online betting sector will always exist regardless of regulation; therefore, an effective tax and regulatory regime is the sure-fire way to reduce the size of the gaming market which is currently unregulated. Secondly, a tax on gross gaming revenue causes a higher section of the market come under regulation. This in turn reduces the size of the locally unregulated market and ensures a competitive market of locally regulated bookmakers. By so doing, a tax on gross gaming revenue supports the effective implementation of CSR policies, enabling greater control of social problems associated with gambling and protection of punters, as a higher proportion of Kenyan punters will be playing on sites that are licensed with appropriate regulatory oversight. Finally, a tax on gross gaming revenue works with all gaming products and therefore ensures the taxation regime remains relevant in regulation across other betting products which do not work with stakes.

¹³⁵ "Regarding taxes, we have now realised that the taxation model where a percentage of stakes is levied does not work" - Chairman, ARJEL (French gaming regulator), July 2011.

This research therefore concludes therefore that betting tax is the most effective tax regime with which to regulate the online sports betting market in Kenya and the most likely to achieve desired policy outcomes. In addition, a tax on gross gaming revenue is also compatible with all types of gaming products unlike a tax on stakes and therefore avoids restricting the supply of gaming products, future-proofing the tax regime to future innovations in gaming.

5.2.Recommendations

Based on the conclusion above, this research recommends that betting tax remains in place as is currently levied owing to the justifications provided for a tax on gross gaming revenue in favour of a tax on stakes.

Secondly, the state should improve integration in the management systems of financial flows through liaison between KRA and financial institutions as well as mobile money transfer systems to ensure that financial flows from betting are detected. This will improve compliance since KRA can easily monitor cashflows thus easing the calculation of gross gaming revenue with a more integrated system.

Finally, the Cabinet Secretary for the National Treasury should put in place guidelines on the implementation of betting tax to enable a seamless rollout of betting tax in the country with clarity which will aid in promoting compliance.

5.3.Future areas of research

Future research could investigate the effect of regulation of the betting industry in Kenya. There have been widespread concerns that overregulation of the betting sector could drive out direct foreign investment and end up killing the local betting industry.¹³⁶ Similarly, it has also been posited by AGOK that overregulation of the betting industry could lead to development of an underworld for unregulated betting.¹³⁷ These two concerns could be the basis of further research on overregulation of the betting sector.

¹³⁶ <https://www.standardmedia.co.ke/business/article/2001235594/betting-firms-say-tax-hike-will-kill-industry> on 25 March 2018.

¹³⁷ <http://www.businessdailyafrica.com/economy/Betting-firms-say-Uhuru-ill-advised-on-35pc-tax-rise/3946234-3983328-format-xhtml-um2y6az/index.html> on 30 August 2017.

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