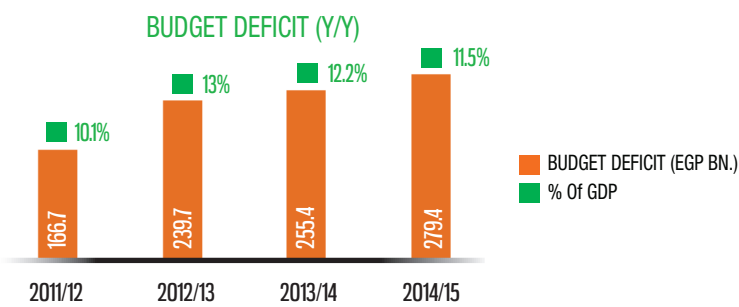


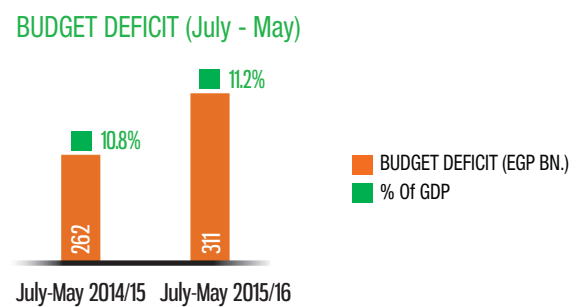
## FLASH NOTE:

# EGYPT ADOPTS THE VALUE ADDED TAX ...

THE EGYPTIAN GOVERNMENT HAS RECENTLY JOINED 150 COUNTRIES APPLYING THE VALUE ADDED TAX (VAT), COMPLETELY REPLACING THE GENERAL SALES TAX (GST) TO INCREASE TAX REVENUES AND CONTAIN THE RISING BUDGET DEFICIT CHALLENGE. THE VAT LAW, APPROVED BY THE PARLIAMENT IN AUGUST AND APPLIED IN SEPTEMBER 2016, IS PART OF THE GOVERNMENT'S FISCAL REFORM PROGRAM THAT INCLUDES REDUCING ITS EXPENDITURES THROUGH GRADUALLY CUTTING ENERGY SUBSIDIES AND INCREASING THE STATE'S REVENUES. TAX REVENUES REPRESENT ALMOST 75% OF TOTAL REVENUES, OF WHICH 45% COMES FROM TAXES LEVIED ON GOODS AND SERVICES. APPLYING THE VAT IS ALSO ONE OF THE ESSENTIAL STRUCTURAL REFORMS REQUESTED BY SEVERAL INTERNATIONAL BODIES SUCH AS THE IMF AND THE WORLD BANK FOR GRANTING EGYPT FINANCIAL SUPPORT.



Source: Central Bank of Egypt



## WHAT IS THE VAT?

VAT and GST are both indirect consumption tax imposed on sales of goods and services and paid by the consumer as a percentage of the final price according to different methods of collection. Indirect consumption tax is paid by the consumer and remitted to the government by the seller.

## VAT VS. GST

Despite belonging to the same tax category, applying VAT in Egypt will include some changes in terms of the way of calculation and tax rate in addition to goods and services exempted and subject to the tax.

### VAT

#### CALCULATION

Calculated as a percentage of the selling price at each production stage on the value added each time a good changes hands as it goes up the chain from a raw material to a consumer product. The buyer of a certain input is entitled to deduct all taxes already paid in previous production stages.

### GST

Calculated at the final sale as a percentage of the purchasing price.



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## TAX RATE

- ▶ The standard tax rate is 13% as stipulated in the law, to be increased to 14% starting from FY 2017/18.
- ▶ The law includes a table for goods and services known as Table Rates<sup>1</sup>, where each group included in it is subject to a different rate, ranging between 1% and 250%.
- ▶ The standard tax rate according to the GST law is 10%.
- ▶ Table Rates range between 1% and 200%.

## EXEMPTED GOODS & SERVICES

- ▶ The law exempted 56 goods and services that can be described as essentials<sup>2</sup>.
- ▶ The law exempted 23 goods from being subject to the tax.

## GOODS & SERVICES SUBJECT TO TAXATION

- ▶ All goods and services except for the exempted ones.
- ▶ All goods and only 17 services.

### AN EXAMPLE FOR CALCULATING VAT (Assuming that VAT is 13%)

- ▶ Firstly, if we assume that strawberry production costs 20 piasters then the VAT is 2.6 piasters. The farmer sells it for 22.6 piasters (cost of production + VAT), and sends 2.6 piasters to the government.
- ▶ Secondly, a factory makes strawberry jam that costs 60 piasters and sells it to the supermarket for 67.8 piasters. The VAT is 7.8 piasters (13% of the 60 piasters) however, the farmer had already remitted 2.6 piasters in the first stage so the factory remits the government 5.2 piasters and deduct the 2.6 previously paid by the farmer.
- ▶ Finally, the supermarket estimates cost of the jam for one pound and charge the consumer EGP1.13. The supermarket deducts the 7.8 piasters already paid in previous stages and pays the government 5.2 piasters.
- ▶ The government finally receives 13 piasters which is equal 2.6 piasters from the farmer, 5.2 piasters from the factory and 5.2 piasters from the supermarkets.

(This is just an explanatory example as agricultural products are exempted from the VAT)

## ADVANTAGES OF APPLYING THE VAT

- ▶ Overcoming tax evasion and enhancing tax compliance through taxing goods on multiple stages of production. If tax is evaded at any phase, the transaction gets noticed in the following production stages or at final sale as applying VAT urges producers to demand and keep invoices from sellers when buying their inputs to be able to deduct the tax paid in previous stages.
- ▶ Controlling the informal sector, as collecting the tax during different stages of production enables the government to collect taxes on goods or services provided by small scale suppliers.
- ▶ Expanding tax base through taxing more commodities and adding new services where advisory and electronic services will be subject to taxation for the first time, so the government can increase its tax revenues by EGP20 billion in FY 2016/17.
- ▶ Fixing public deficit imbalance that has kept increasing during the last few years, reaching EGP311 billion (11.2%) in July-May FY 2015/16 compared to EGP262 billion (10.8% of GDP) in the same period last year. This surge poses different risks, including hikes in government's debt which is majorly financed through banks operating in Egypt<sup>3</sup>, crowding out loans extended to the private sector.

<sup>1</sup> Goods and services taxed at different rates, either less than the standard tax rate, prescribed by the law, (coffee, soap, macaroni, pesticides, ...) or higher than the standard tax rate (certain types of home appliances, perfumes, soft drinks, certain types of vehicles, cigarettes, alcohols).

<sup>2</sup> Please refer to Page 4.

## IMPLICATIONS OF APPLYING THE VAT

- ▶ Despite having numerous advantages, applying VAT is expected to increase the inflationary pressures as new services, such as advisory services in different fields including construction and law in addition to electronic services like e-commerce, will be taxed for the first time and will witness a considerable rise in their prices. Moreover, applying a 13% tax instead of 10% will feed inflationary pressures and increase burdens on consumers.
- ▶ The government estimates the increase in the inflation rate to range between 0.5% for low-income Egyptians and up to 2.3% for the upper class. This estimation is based on the positive linkage between the consumption and tax paid as the VAT is mainly a consumption tax; the more you consume the more you pay.

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<sup>3</sup> Banks held about 78% of outstanding Treasury Bills in April 2016.

## LIST OF GOODS AND SERVICES EXEMPTED FROM VAT

▶ The Vat law included a list of exempted “necessities” commodities aimed at helping the poor to overcome the inflationary effect of the VAT:

### EXEMPTED GOODS

1. Dairy products
2. Baby formulas
3. Baby nutritional supplements
4. Eggs
5. Tea
6. Sugar
7. Mills products
8. All types of flour made bread and macaroni products
9. Livestock
10. Fish
11. Poultry
12. Food items, manufactured or sold to the final consumer directly through non touristic restaurants and shops that follow certain requirements determined by the minister of finance
13. Crude oil and natural gas
14. Liquefied petroleum gas
15. Natural materials, such as mining and quarrying products in its natural state
16. Production, sale, transfer and consumption of electricity
17. Production, purification and desalination of water
18. Newspapers, printing and writing
19. Postal and financial stamps

20. Books, university notes and magazines
21. Wheelchairs and their spare parts
22. Prosthetic parts
23. Hearing aids
24. Artificial kidney filters
25. Children incubators
26. Preserved or manufactured meat
27. Preserved or manufactured fish except caviar and smoked fish
28. Agricultural crops (except for tobacco)
29. Halva, molasses and honey
30. Legumes, grains, salt and manufactured spices
31. Gold and silver ore
32. Residues and waste from food and paper industry
33. Prepared food for animals, birds and fish except cats and dogs
34. Sales and lease of agricultural land, buildings, residential units and non-residential units
35. Pharmaceuticals
36. Special needs cars

### EXEMPTED SERVICES

1. Banking operations
2. Non-banking financial services, subject to the supervision of the Egyptian Financial Supervisory Authority
3. Post office saving book services

4. Leasing services
5. Education, training and scientific research
6. Services performed for the establishment and maintenance of worshiping places
7. Free services that are broadcast through radio, television or any other means
8. Asymmetric Digital Subscriber Line (ADSL) services to be exempted for one year
9. Library services provided by government or educational establishments for research or cultural centers of all kinds
10. Documenting and archiving services, publishing and museum services
11. Media Production Services and documentaries
12. News agencies and corresponding services
13. Farming services and breeding, harvesting and supply of agricultural labor
14. Non touristic water transportation for people, and air transport for people
15. Non-commercial services performed by non-profit organizations
16. Unions subscriptions
17. Burial services
18. Foreign currency exchange through exchange bureaus and banks
19. Land transportation services for individuals including transportation by taxi except for tourist transport
20. Health care services



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