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EGYPT

Rise and fall of fiscal justice after January's Revolution

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Introduction

Following the January 25 Revolution, fiscal policies were relatively unclear, reflecting the political momentum of 2011, and the conflict between the revolution's call for just policies and the business community's resistance to such policies.

As Finance Minister from 2004 to 2011, M. Youssef Boutros Ghali had implemented a set of fiscal policies, reducing custom fees, unifying income taxes at 20%, and passing the real estate tax law. He planned to turn the sales taxes' system into Value Added Tax (VAT).

Ghali built his fiscal philosophy around alleviating businessmen's fiscal burden to encourage them to pay their taxes. He believed that tax liability will stimulate the investments they make thus indirectly affecting gross tax revenue.

Ghali's fiscal philosophy was severely attacked by anti-Mubarak currents which gained political momentum after the fall of the former president in 2011. In this paper, I will go through fiscal policy changes in the years following the revolution and will determine how close or far they are from social justice goals advocated for by January's revolution.

The paper divides the fiscal policies' evolution into different phases according to the legislations implemented during each fiscal year after January's revolution and analyses these policies' effect on the country's financial situation through the available data on these years' final accounts.

2011 - 2012 a semblance of fiscal justice to calm down the revolution

In 2011, the state wanted to calm down angry popular crowds which became active during the January revolution, by implementing a set of economic policies: ending the unified income tax policy responsible for imposing the same fiscal burden on both middle-income households and big businessmen.

In the first budget adopted after the revolution for 2011 – 2012, it announced an additional 5% income tax on individuals and companies whose annual income exceeds 10 million Egyptian pounds (EGP).[1]

Also, for the first time, the state subjected speculations in the stock market to taxes, namely a 10% capital gains tax (CGT) on shares and listed companies' gain distribution.[2]

1 Law no. 51 of 2011 on the State's General Budget for the Fiscal Year 2012-2011 and on the amendment of some provisions of the income tax law

2 Egypt budget targets poor, introduces capital gains tax, Reuters, June 2011 goo.gl/aoqmZ1

Ghali's real estate tax law no. 196 of 2009 gained a bad reputation and was faced with strong opposition even under Moubarak, pushing the state to stop its enforcement in 2011 before making some amendments later.[3]

In parallel with raising low governmental salaries by adopting new rewards and incentives in the 2011 – 2012 budget, the state indirectly increased the citizens' revenues by alleviating the fiscal burden of middle-income households through raising the tax exemption ceiling from 9000 to 12 000 EGP.[4]

Fiscal modifications did not all benefit low-income households because during that year, the government also extended sales taxes, increasing cigarette taxes from 40 to 50%.[5]

The state's aim was to fix the budget deficit which it had decided to contain in 2011- 2012 after it increased spending on salaries during that same year.

Amid these changes, the state started negotiations with the International Monetary Fund (IMF) to get a loan, sparking controversy about a possible IMF interference in Egypt's fiscal policies.

However, the agreement didn't see the light because, at that time, the governing military council opposed this step.[6] Back then, Finance minister Samir Radwan denied that the loan was subject to conditions in contraction with the fiscal policies the state had adopted during the 2011-2012 period and which he considered as "expansionist" policies.[7]

However, fiscal policies with a social aspect adopted in the first budget after the revolution were faced with clear internal resistance. The best example is that the state wanted to postpone the adoption of the stock market tax for fear of arousing businessmen's anger.[8]

The new 12 000 EGP tax exemption ceiling was not implemented[9] because according to journalistic reports, the authorities were opposed to this measure when the final version of the 2011-2012 budget was adopted.[10]

3 Mohsen Abd El Razeq, Confusion in "real estate taxes" after the PM froze the enforcement of the new law, Al Masri Lyom, May 2011 goo.gl/5O7Wxd

4 Ahmad El Sayyed El Najjar: raising the tax exemption ceiling to 000 12 EGP: a decision taken by Samir Radwan and not by the current government, Al Bidaya, February 2013, goo.gl/dCUIUh

5 Law no. 49 of 2011 on the amendment of some provisions of the general sales tax law no. 11 of 1991

6 Egypt says will not need IMF, World Bank funds, Reuters, June 2011 goo.gl/t2mQI4

7 Samir Radwan in a comprehensive dialogue about Egypt's economy after the revolution, Wael Jamal and Mirit Majdi, El Chourouq, April 2012, goo.gl/cZ4Wnd

8 Same source

9 Ahmad El Sayyed Al Najjar: raising the tax exemption ceiling to 000 12 EGP: a decision taken by Samir Radwan and not by the current government, Al Bidaya, February 2013, goo.gl/dCUIUh

10 The high cost of living is devouring salaries and the government backs away from raising the tax exemption ceiling goo.gl/juYdAG

At the beginning of that year, when Kamal Al Janzouri became the Prime Minister of the transitional authority which remained until the 2012 presidential elections, the government submitted an official request to the IMF to get a $3.2 billion-dollar loan. But this time, the parliament was the one to oppose this measure. The first post-revolution council, mostly made up of the Islamist movement, strongly disagreed with the government appointed by the army on many issues other than the IMF's involvement, pushing the parliament to call for the dissolution of the government.[11]

Final accounts' highlights 2011- 2012

The State's tax revenues for 2011-2012 accounted for around 68.3% of state revenues, reflecting the decline in tax revenues' share of revenues when compared to the 72.4% registered in the previous year, according to the final accounts of both years.

This came at a time when the deficit of the total assets' uses, revenues, loan proceeds, and asset sales in 2011-2012 grew by some 22% compared to the previous year.

The final account estimated tax revenues at some 207 billion EGP, an increase of only 15 billion compared to 2010-2011 (around 7.8%), less than the average inflation rate for the same year, estimated at 8.6%, meaning that the real tax revenues decreased by at least 0.8% approximately.

The previous indicators reflect the increasing financial deficit and the urgent need for a tax policy of progressive nature that would be adopted for many years until it bears fruit and that would contribute to increasing state revenues and covering the state's increasing expenditure. Nevertheless, fiscal reforms which started in 2011- 2012 amid the revolution's momentum did not last long.

2012-2013 the new democracy between justice and its antonym

The controversy around the IMF's loan continued during 2012. Opposition currents prospered in the open democratic space that emerged after the revolution and warned against the dangers of finding agreements with infamous international institutions like the IMF known for its long history of unjust financial policies.

In April 2012, the IMF published a statement in which it called political forces in Egypt to agree on an economic reform program before getting the loan.[12]

As soon as he became president and took control of the legislative authority after the dissolution of parliament, Mohammad Morsi who belonged to the Islamist movement, made extensive amendments to the income tax law.

11 Egypt and the IMF in a few lines, Nivine Kamel, El Chourouq, July 2016, http://bit.ly/2hlo0Ln

12 The IMF asks political forces to agree on the 2013-2012 budget before receiving the loan, El Masri El Yawm, April 2012

Amendments included codifying progressive brackets adopted under the military council and reviving the idea of a possible imposition of taxes on stock markets activities.[13]

Amendments related to stock market activities came after a tax dispute between the tax authority under Morsi and businessman Nassef Sawiris.

This dispute was about Orascom Construction Industries (OCI S.A.E) - presided over by Sawiris - selling its cement section to Lafarge through the stock market in 2007. This deal that the business community usually calls an acquisition is supposedly subject to taxes, but Sawiris made the acquisition by selling his company's money market securities to the French company as if it was a regular sale of shares.

Orascom defended its legal position by considering that selling the shares through the stock market exempted it from the tax burden. The company and the tax authority then engaged in a highly- publicized public legal dispute.

Amid these circumstances, Morsi's tax amendments aimed at imposing a 10% lump-sum tax on revenues resulting from the sale of companies' shares or stocks, including different purchase and trade operations, in any acquisition exceeding 33% of the company's capital or voting rights.

By virtue of the law, acquisition through multiple operations were to be considered as one deal if it is made by the same buyer or people related to him within 12 months as of the first purchase date. Taxable profits are calculated based on the difference between the purchase price or nominal value as stated in the corporate charter and the acquisition price, without any exemption stipulated for in this law or any other law. [14]

In addition, amendments imposed the same taxes on profits made by natural or legal people at each Initial Public Offering (IPO) in the secondary market.[15]

In the amendments he made, Morsi did what the previous government couldn't do. He raised the personal annual income tax exemption ceiling for those whose income is below 12 000 EGP per year instead of 9000 EGP.[16] But this exemption was only implemented after Morsi's fall in July 2013.[17]

13 Law no. 101 of 2012 on the amendment of some provisions of the income tax law no. 91 of 2005 and adopting some tax concessions, contributing to social justice and reducing tax evasion cases

14 Same reference

15 Same reference

16 Same reference

17 The tax authority starts to implement additional income tax

Morsi's legislation on trading went through a second modification of the stamp duty according to which a proportional 1 per 1000 stamp duty was imposed to the buyer and to the seller for the sale or purchase of Egyptian or foreign securities.[18] The article on imposing this tax was repealed in a new legislative amendment in 2014 after Morsi's fall.[19]

While previous amendments paved the ground for social justice, the government was also preparing a sales taxes' extension, a tax burden known for obstructing social justice because it blindly imposes consumption taxes without considering the consumer's income or the tax they deserve to pay.

Finance minister under Morsi Momtaz Said announced that the government was considering replacing the sales tax with the VAT, a measure that will later be adopted to extend consumption taxes.

But what Morsi tried to do on the ground was extend to a wide range of products a sales tax announced by the state and retracted a couple of hours later.[20]

According to newspapers, the new sales tax was part of an understanding between the state and the IMF to obtain the loan for which negotiations were still ongoing at that time knowing that under Morsi, negotiations were about a larger $4.8 billion-dollar loan.[21]

Morsi's fourth tax law was related to real estate taxes which sparked an important controversy as soon as former finance minister Ghali suggested them. Perhaps what distinguishes Morsi's law the most is that it raised the tax exemption ceiling for housing real estate properties from 500 000 (market value per housing unit) to 2 million EGPs, minimizing opposition to the law.[22]

Final accounts' highlights 2012-2013

Taxes' share of total state revenues increased in 2012-2013 compared to the previous year and reached 71.6% but remained under its pre-revolution level.
This increase came at a time when the deficit in assets' uses, revenues, loan proceeds and assets' sales increased by some 53% compared to the previous year, reaching around 311 billion EGP.
That year, tax revenues reached 251 billion EGP, a 21.3% increase (44 billion EGP) compared to 2011-2012, and a 14.4% increase in real tax revenues compared to the same year's average inflation rate.

18 Law no. 9 of 2013 on the amendment of some provisions of the stamp duty law no. 111 of 1980 amended by law no. 104 of 2012

19 Law no. 53 of 2014 on the amendment of some provisions of the income tax law no. 91 of 2005 and the stamp duty law no. 111 of 1980.

20 The tax was imposed in law no. 102 of 2012 on the amendment of some provisions of the general sales tax law no. 11 of 1991 which was later repealed according to article 1 of law no. 58 of 2014.

21 Morsi adopts a tax increase on electricity, gas, cigarettes and sparkling water, Amir Haydar, Mohammad El Saadani, Lubna Salah El Dine, Abd Al Aziz El Saadani, El Masri El Yawm, December 2012, http://bit.ly/2i9XLI7

22 Law no. 103 of 2012 on the amendment of some provisions of the built-up area property tax law no. 196 of 2008

2013-2014 tax on rich people and a constitution for justice

After the developments of the 30th of June 2013, the IMF declared that any negotiations on the loan will be postponed until Egypt regains its political stability. Back then, the IMF's loan wasn't urgent as generous assistance flowed from the Gulf into Egypt after the army had ousted Mohammad Morsi.

The 2014 constitution adopted progressive taxes and article 38 stipulated the following: "individual income taxes shall be progressive, with multiple brackets and in accordance with the taxpayers' capacities." This showed that after the fall of Mohammad Morsi's regime, the new authorities preferred fair fiscal policies.

Before presidential elections, the interim president implemented a new income tax known as the "the rich people's tax" consisting of a three-year long 5% annual and temporary additional tax on all those whose income exceeds 1 million EGP, whether they are natural or legal people (i.e. entities like companies).[23]

Nevertheless, the transitional authority also extended sales taxes to close the budget deficit, exploited its legal right to cigarettes' price fixing and adopted ministerial decrees to increase tax collection.[24]

2014-2015 el-Sisi following in Morsi's steps

As soon as he became president and controlled the legislative authority while the parliament was still crippled, el-Sissi amended the income tax.

Among the new fiscal amendments adopted by el-Sisi was imposing taxes on the revenues of independent workers and professionals in the non-commercial sector abroad, knowing that Egypt was the heart of such professional activities.[25]

In an attempt to impose taxes on the stock market, El-Sisi's fiscal amendments imposed taxes on the distribution of companies' profits to shareholders, capital gains made from trading securities, and profits made by investing in foreign securities.[26]

23 Law no. 44 of 2014 on imposing an additional temporary income tax

24 The Ministry of Finance adopted decision no.30 of 2014 and 265 of 2014 on the increase of cigarette prices which are essential to calculate the sales' tax

25 Law no. 53 of 2014 on the amendment of some provisions of the income tax law no.91 of 2005 and the stamp duty law no. 111 of 1980

26 Same reference

In April 2015, the ministry of Finance unveiled the executive regulations of the law on the income tax amendments passed by Morsi. According to Reuters, the then minister of Finance said that imposing a 10% tax on stock trading and the distribution of companies' profits was "the lightest form of taxes."[27]

But in parallel with the lightest form of taxes on the stock market, trading dropped heavily, pushing the council of ministers to freeze the part related to taxing speculation for two years almost a month after it was passed and to prolong this measure for 3 additional years in November 2016.

Final accounts' highlight 2013-2014

In 2013-2014, taxes' share of revenues decreased to around 56.9% although tax revenues increased to around 260 billion compared to 251 billion EGP.

However, the decreasing taxes' share of revenues might reflect the important increase in the flow of grants from around 520 billion EGP in 2012-2013 to around 958 billion EGP in 2013- 2014 resulting from strong Gulf support to Egypt after the fall of Mohammad Morsi, knowing that this support was not linked to fiscal policy amendments as was the case with the IMF loan.

When comparing the 3.6% increase in the 2013-2014 tax revenues with the 10% average inflation rate registered in the same year, it appears that the real tax revenues decreased by more than 6.4%.

The deficit in the total assets' uses, revenues, loan proceeds, and asset sales grew less with 16.8% (363.3 billion EGP), reflecting the extraordinary revenues which came from the Gulf and postponed fiscal policy amendments.

Despite that, the situation didn't last long as Gulf assistance progressively started to decrease, pushing the state to change fiscal policies to please the business community and attract investments.

The revolution's policies fail in favor of businessmen

On the second day of the new fiscal year, el-Sisi nullified Morsi's decisions to extend sales taxes. In the same law (no.58 of 2014), he adopted new extensions of the same tax burdening citizens. The 2014-2015 budget showed that the state was headed towards a bigger extension of the sales tax by turning towards the VAT.
In August 2014, el-Sisi adopted new amendments of the real estate tax,[28] including tax exemptions for facilities of an economic nature affiliated to the armed forces, sparking a controversy about the nature of economic privileges given to the army.[29]

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27 Egypt's finance minister: the adoption of the executive regulations for the stock market profits law, Reuters, April 2015, http://bit.ly/2i5jDIu

28 Law no. 117 of 2014 on the amendment of some built-up area property tax law no. 196 of 2008

29 These are the economic sectors which the army entered in 12 months, Mohammad Hamama, Mada Masr, September 2016 http://bit.ly/2hVZlxX

Also, the implementation of the real estate tax faltered as analysis shows that this tax's revenues during the first two fiscal years in which it was implemented did not exceed 13% of the expected revenues.[30]

At the end of 2014, the government was promoting a global economic conference to attract foreign investments at a time when a crisis in foreign exchange reserves was looming on the horizon. This conference was held in March 2015 and after it, the government announced fiscal amendments which represented a new setback on the path to tax justice.

Legislative amendments made by el-Sisi in August 2015 nullified the temporary tax imposed by his predecessor on the rich people and imposed a 22.5% unified tax for all those whose annual income exceeds 200 000 EGP.[31]

The setback series continued in September 2016 with the adoption by the first parliament elected after the 30th of June 2013 of the VAT law which increased taxes from 10 to 13% with an expected increase to 14% in 2017-2018.

The adoption of the VAT wasn't immune to International Finance Institutions' (IFIs) pressure. In fact, the law was passed almost a month after the IMF agreed to give Egypt a $12 billion loan in an agreement based on the economic reform program prepared by the government and of which the main pillar was the extension of the consumption tax.[32]

Conclusion

The information included in this paper shows that the path to social justice in fiscal policies has been unstable since the 25th of January revolution. This is clear in all the suggested fiscal policies presented and retracted by the post-revolution governments under the military council, the Muslim Brotherhood, Adli Mansour or el-Sisi, which bent under popular pressure, the business community and IFIs.

Because of this blunder and of conspiracies to put the capitalist minority's interests above the people's, the government failed to undertake a radical change in the fiscal system. Consequently, it suffered from a continuous deficit in financial resources as expenditure unlimitedly increased and government spending doubled between 2011 and 2016. Most of these expenses were funded by all forms of borrowing, leading to a growing inflation and more debt for the people.

30 Real estate tax: a suspended law, Mona Diya', El Yawm El Sabeh, December 2015, http://bit.ly/2ibv0L7
31 Law no. 96 of 2015 on the amendment of some provisions of the income tax law no. 91 of 2005 and the decision about law no.44 of 2014 on imposing an additional temporary income tax
32 Statement: the IMF agrees to grant Egypt a 12$ billion loan, Aswat Masriya, November 2011, http://bit.ly/2gZIedV

This shows that the government didn't have a comprehensive economic vision to reduce inflation and debts with a clear fiscal structure and a separate strategy to increase the number of tax payers. Despite the deficit, it continued to spend and is now pushing the country towards the edge of sovereign default, making the new generations' future dependent on the mistakes of the past.