



Philosophy of Taxing Goods and Services in the Value Added Tax

"A Comparative Study"

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Introduction

In the modern commercial and fast-growing economic age, the value-added tax (VAT) is considered one of the most significant techniques the majority of world governments use to levy consumption taxes both on the consumption of goods and/or services provided within their territories. This paper aims to recognize the legislator's philosophy while taxing goods and services. It also traces back VAT over the years of its implementation in different countries so far; to recognize the evolution VAT has gone through during these years.

Since Egypt has been applying VAT for a long time, starting with the General Sales Tax Law No. 11 of 1991 till the Value Added Tax Law No. 67 of 2016 and its subsequent amendments, this paper aims to recognize the Egyptian legislator's philosophy in dealing with this

tax during these years. It, also, attempts to figure out the legislators view towards goods and services they chose to levy the consumption tax upon using VAT. In addition, this study tries to identify the compatibility between the Egyptian legislation and the other counterpart legislations in this same regard.

To achieve its goal, this study is divided into three chapters: The first chapter deals with the philosophy of restriction and exclusion Egyptian legislation followed during the initial stages VAT application. The second chapter explores the evolution of the Egyptian legislator's philosophy towards taxing all goods and services excluding those exempted. As for the third chapter, it discusses the extent to which the Egyptian legislation copes with its counterpart legislations in the same concern.

Chapter One

Restriction and Exclusion Policy and Its Effects

(1) Concept of the policy:

The value added subjected to this tax (the VAT) expresses the excess value acquired by the taxable good or service at each stage of its circulation. In other words, it is the value representing the difference between taxable goods or services prices at the end of one trading stage and their prices at the end immediately preceding one.

The value-added tax (the VAT) is similar to the successive turnover tax, as the latter is also levied on each stage of trading. However, there is a fundamental difference; (the VAT) allows the taxpayer to refund the input tax (paid in one of trading stages) from the output tax (payable in the next stage).

Generally speaking, when developing countries consider levying (the VAT) for the first time, they often restrict its application to certain goods and exclude the other goods from its scope. Moreover, they exclude all services from VAT initial application. This is occurred for two reasons: The first: the ease of application. The second: services do not represent a privileged place in different families' expenditures, in these countries. This approach differs in developed countries since the service sector is continually developing.

Such selective approach often results in many exemptions as well as many different tax rates. Commonly, this is due to certain economic, political and social conditions. However, this approach creates many practical difficulties.

Since Egypt is one of the developing countries adopting the approach most of these countries yield to, we have

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found Egypt follows this same approach, restriction and exclusion policy, throughout its history until 2016. Yet, it broadened the scope of this tax at a later stage, in 1991, to include certain services side by side to the manufactured goods.

As for the tax rates applied by successive tax consumption legislations in Egypt, they numerously varied in all these taxes application throughout Egypt history until the Consumption Tax Law No. 133 of 1981. This diversity of tax rates is still persistent in the Egyptians VAT legislation No. 67 of 2016. Also, it was existed in the Egyptians VAT legislation No. 11 of 1991

(2) Role of the policy and its effects:

(I) – The policy contributes to the diversity of tax rates:

Since Egypt followed the restriction and exclusion approach when applying the value-added tax under

Sales Tax Law No. 11 of 1991, the rates of this tax varied; as that law adopted proportional rates of taxable items values (such as: 5%, 10%, 25%, etc.), and qualitative rates (such as: Liter, Kilogram, etc).

According to Law No. 11 of 1991 the standard rate was 10%. This was applied – as a rule – to all taxable goods and services. However, Law No. 11 of 1991 has authorized the Republic President to amend the tax rate levied on certain goods and services. Accordingly, the President has rescripted several presidential decrees that amended tax rates for some goods and services, lowering this rate to 5% on some necessary goods, and raising it to 15%, 25%, 30% or 45% for some less necessary – but not luxury– goods, such as cars. These decrees also stated some special provisions, allowing to combine both qualitative and quantitative rates. As mentioned in table 1 related to goods and table 2 related to services, some

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goods subjected to the VAT at a quantitative proportional rate with a minimum tax value.

In addition, Article (2) and Article (7) of the General Sales Tax Law No. 11 of 1991 involved special provisions for goods and services exported abroad; since article 2 of this law levied tax on them at "zero" rate.

Consequently, the value-added tax rates levied in Egypt have been multiplied according to restriction and exclusion policy stipulated in Egyptian tax Law No. 11 of 1991.

In fact, this tax rates diversity applied in Egypt and parallel legislations adopting the same philosophy has resulted in many aspects of unfairness to taxpayers in many areas. It also revealed a decline in the neutrality of this tax within the scope in which it is levied.

(ii) Impacts of divers VAT rates on tax justice:

The approach of restriction and exclusion adopted by our General Sales Tax Law No. 11 of 1991 has had bad effects on tax justice. This is due to the diversity of tax rates applied whether low, medium or high. This approach either in Egypt or other countries may adopt more than a single standard rate. Such diversity negatively effects on tax justice. In the following lines, this study is handling these points:

(a) Effects of low VAT rates diversity on tax justice:

Tax legislation at any country may adopt diversity principle when imposing value-added tax in order to achieve some financial, economic, or social goals; such as increasing the tax revenue from consuming some goods, redistributing incomes among individuals in the society, or achieving social welfare, etc. That is exactly what happened in Italy at the end of the last century.

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During 1990s, Italy applied remarkable diversity of low VAT rates, as shown in the following table.

Table No. (1)

VAT rates in Italy (1987–1997)¹

<i>Period</i>	<i>First low rate</i>	<i>Second low rate</i>	<i>Average rate %</i>	<i>High rate %</i>	<i>Standard rate %</i>
1987	2	9	-	38	18
<i>From 7-3-1988</i>	2	9	-	38	19
<i>From 1-1-1989</i>	4	9	-	38	19
<i>From 13-5-1991</i>	4	9	12	38	19
<i>From 1-1-1993</i>	4	9	12	-	19
<i>From 1-1-1994</i>	4	9	13	-	19
<i>From February 24, 1995</i>	4	10	16	-	19
<i>From 1-1-1997</i>	4	-	-	-	20

¹ **The source:** Economia, Dipartimento di Economia Pubblica, Via del Castro.p. Laurenziano, 9 – 00161, Working Paper No. 40, Roma, (Italy).p. 26.

It is clear from this table that during the last decade of the last century (1987-1997) the legal structure of VAT rates in Italy changed eight times.

Despite this disparity and the diversity of VAT rates over that decade, it was proven that the use of multiple tax rates when applying the value-added tax in Italy was not an effective way to redistribute incomes, or to achieve social welfare there during that decade. Rather, this study proved that the overall effect of tax rates diversity was negative, and led to an increase in the degree of social hatred because of the inequality caused by this diversity.¹

(B) Effects of diverse standard VAT rates on tax justice:

It is common for multiple tax rates to come away from the standard rate applied in the concerned country. However, Mexico applied, in January 1, 1981, the value-

¹ Ibid.p.22.

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added tax at two different standard rates; the first rate was 15%, and it was applied to the entire territory of the country, and the other rate was preferential (10%) and was applied to the border area of Mexico with the United States of America, with a width of twenty kilometers.¹

In January of 2010, these two rates raised to 16% and 11%, respectively. This diversity led to the large number of Mexicans headed to this preferential area to shop from because of the goods cheap prices there emerging from this preferential treatment. Moreover, it led to dense waiting lists for those heading to and leaving these areas. In return, these negative effects raised many social and economic problems within Mexican taxpayers' community

¹ Vera Kononova and John Whalley, RECENT RUSSIAN DEBATE ON MOVING FROM VAT TO SALES TAXES AND ITS GLOBAL IMPLICATIONS, NBER WORKING PAPER SERIES, Working Paper 15615, Cambridge, MA 02138, December 2009, p.19.

and an increase of discontent in Mexican society about this preferential policy.¹

(C) Effects of multiple prices resulting from legislative defects on tax justice:

Drafting defects of VAT legislation may cause tax rates that do not comply with the philosophy of this legislation.

This is what exactly happened in Egypt under the Law No. 11 of 1991; Since that law was applied to some services exclusively at a standard rate of (10%), while it was applied to other services at a lower rate of (5%).

However, the flaws of the legislative drafting, which had accompanied some provisions of that law, led to a lack of justice in setting VAT rates for some services compared to other services.

¹ W. Davis, THE EFFECTS OF PREFERENTIAL VAT RATES NEAR INTERNATIONAL BORDERS: EVIDENCE FROM MEXICO, National Tax Journal, March 2011, 64 (1), 85-104, p. 85.

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This contributed to create an unjustified disparity in legal positions of various services beneficiaries as some luxury services subjected to VAT at the low rate (5%), such as tourist transportation. While at the same time other essential services subjected to VAT at the standard rate (10%), such as transportation of goods.

It is obvious that tax justice required the opposite. Moreover, this policy excluded some services of the VAT scope, such as engineering consultancies though other services of its types subjected to the VAT at the standard rate, such as the contracting service. This would not have happened if the tax legislation was free of drafting flaws.

(iii) Effects of diverse VAT rates on tax neutrality:

The state may levy the VAT according to the restriction and exclusion approach in order to give preference to some goods and/or services over others, by extending the scope of VAT to include some and exclude others.

The state may aim, for example, to discriminate against some items, by applying high tax rates upon. Such a situation – if occurred – negatively affects the principle of tax neutrality, but the state's tendency towards it may indicate its desire to achieve this non-neutrality.

However, poor regulation of VAT texts may negatively affect the purposes of the state or stand against its philosophy to achieve neutrality, when the VAT scope extends beyond the scope desired by the legislator, or when, on the contrary, this scope recedes from some goods and services intended– by the legislature – to subject to the VAT, or when the VAT application at different rates leads to cause some defects that affect the VAT neutrality within its narrow intended legal scope.

In such circumstances, the VAT neutrality is negatively affected and does not achieve the VAT goals intended by the legislator.

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Regarding to the VAT that Egypt applied in accordance with the restriction and exclusion approach over a quarter of a century (1991–2016), we find that it preferred to not neutralize this tax both in fields of goods and services together.

In the field of goods, the Egyptian VAT restricted its scope in manufactured goods only and excluded unmanufactured goods, except some unmanufactured goods that were included in table1 that accompanied that law, since they subjected to the VAT, though they were unmanufactured. As for services, the VAT was levied upon the services included in Table 2, which also accompanied that law, while other services were excluded from its scope.

Recognizing the right of the legislator to use this approach to distinguish some goods and services over others in order to achieve some social and economic

purposes along with the financial purpose of the tax, levying the VAT in Egypt in accordance with this approach led to narrow the scope of VAT by excluding some goods that the Egyptian legislator would not have put them out of the VAT scope if such approach was not adopted.

Also, the diversity of VAT rates led to discriminate some taxable goods, such as industrial detergents, compared to the exempted goods in a way that the legislator would not have accepted if they had recognized that before levying the VAT.

Chapter Two

Generality Policy in Taxing Goods and Services and Its Effects

(1) – Circumstances and Justifications of Generality Policy:

During times of economic crises, the state's income drops sharply because it is affected by decreasing of taxes revenue, whether direct or indirect taxes, resulting from decreasing of commodity and services prices in such circumstances. Moreover, Tax evasion is on the rise, and thus the public budget deficit increases. Consequently, it becomes impossible for the state to finance its budget in appropriate volume.

Though the state needs more social expenditures at such stage to stimulate the aggregate demand for goods and services consumption, it is difficult for the state to increase its revenue to achieve this by increasing the

prices of income taxes levied on labor and/or capital. This is because of its need, in such cases, to create more employment opportunities and encourage investment. Also, increasing the corporate tax in times of economic crises would generate a *Cobra Effect* deepening the crises. At such circumstances, the state finds that the best solution is to increase its public revenue or to maintain the volume of these revenue at the same level prevailing before the crisis though expanding the scope of the VAT and/or increasing its prices.

However, this procedure requires a reasonable estimation for the economic effects of these increases on both the macroeconomic and microeconomic levels; since the prices of goods and services will certainly rise – whether wholly or partially – due to the rise in tax rates,

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as "VAT rate increase is reflected in the whole or in part on the price of goods and services."¹

Were it licit to consider the shift towards the full implementation of the value-added tax a legislative reform, it is certain that such a reform may be futile. It may also leave behind negative effects on the distribution of income, or on the lower classes in some societies.²

When it comes to study the situation in Egypt, we discover it had gone in two parallel directions simultaneously. Firstly, it expanded the scope of the VAT levied on all goods, after it was limited to manufactured goods, Secondly; VAT was levied on all services, after it was exclusively limited to some services, as mentioned above.

¹ VALUE ADDED TAX IN THE ECONOMIC CRISIS CONTEXT

Mara Eugenia Ramona, Mara Cristian and Cuceu Ionut, Babes-Bolyai University Cluj-Napoca Faculty of Economics Science and Business. Cod JEL: H23, H3, H22, G18.2010.p.389.

² Jeffrey Owens and Edward Whitehouse, Tax reform for the 21st century 1996, MPRA Paper No. 21135, posted 7. March 2010, p.1.

In the same context, Egypt raised the standard VAT rate from 10% to 14%, excluding the fiscal year following this reform; since the standard VAT rate applied therein was 13% only.

However, Egypt annulled the high VAT rate of (25%), and compensated that by including many goods to which that rate was applied in the table enclosing that law, and levied the set tax at certain prices on these goods in addition to other VAT rates determined by the law in that table.

On the other hand, Egypt also annulled the other low rate applied on construction steel at (8%) and let the low rate that was applied to many goods and services at (5%) to be applied only on tools and machinery.

Looking at the comparative legislations that raised the VAT rates under the pressure of economic conditions as the case in Egypt, we find that many European Union

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countries have resorted to raising the standard VAT rate in 2009 following the global financial crisis that hit the world in 2008¹ with its negative economic effects prevailed all countries all over the world. The following table illustrates that:

Table No. (2)

Impact of the 2008 global financial crisis on the standard VAT rates in comparison with current rates in several countries²

<i>Country</i>	<i>Date of increasing the standard rate</i>	<i>Rate before</i>	<i>Rate after increase</i>	<i>Rate of increase</i>	<i>Current rate</i>
<i>NS. Czech</i>	January 1st 2010	19%	20%	1%	21%
<i>Estonia</i>	1st of July 2009	18%	20%	2%	20%
	March 15, 2010	19%	21%	2%	

¹ Ibid. Loc. Cit.

² – different references

– Caitlin Hartley and Molly Thompson, *Worldwide VAT, GST and Sales Tax Guide*, 2016, © 2016 EYGM Limited. London SE1 2DA United Kingdom. pp.1091 – 1094.

– Mara Eugenia Ramona, Mara Cristian and Cuceu Ionut, Babes-Bolyai University Cluj-Napoca, *VALUE ADDED TAX IN THE ECONOMIC CRISIS CONTEXT*. Faculty of Economics Science and Business. Cod JEL: H23, H3, H22, G18.2010.p.391.

<i>Country</i>	<i>Date of increasing the standard rate</i>	<i>Rate before</i>	<i>Rate after increase</i>	<i>Rate of increase</i>	<i>Current rate</i>
<i>Greece</i>	1st of July 2010	21%	23%	2%	23%
<i>Spain</i>	1st of July 2010	16%	18%	2%	
<i>Latvia</i>	January 1, 2009	18%	21%	3%	21%
	January 1st 2011	21%	22%	1%	
<i>Lithuania</i>	January 1, 2009	18%	19%	1%	21%
	September 1st	19%	21%	2%	
<i>Hungary</i>	1st July 2009	20%	25%	5%	
<i>Poland</i>	January 1st 2011	22%	23%	1%	21%
<i>Portugal</i>	1st of July 2010	20%	21%	1%	
	January 1st 2011	21%	23%	2%	27%
<i>Romania</i>	1st of July 2010	19%	24%	5%	23%
<i>Slovakia</i>	January 1st 2011	19%	20%	1%	
<i>Finland</i>	1st of July 2011	22%	23%	1%	23%
<i>United Kingdom</i>	January 1st 2010	15%	17.5%	2.5%	
	January 4, 2011	17.5%	20%	2.5%	20%

Thus, the financial policies in different European Union Countries have given us ten different levels of the VAT standard rates; The lowest of them is 15% (as it is forbidden for the countries of the Union to reduce the VAT standard rate to less than 15% according to the of the

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European Commission decision)¹ as in Cyprus and Luxembourg. The highest rate reached 25% as in Hungary, Sweden and Denmark, with an average rate of 20.7%. The standard rates of VAT in the European Union now range between 20% as in most EU countries and 27% as in Hungary, with an average tax rate of 23.5%.²

Going back again to the Egyptian VAT, we find that the current applied standard rate in conjunction with the transition to the generality of application is 14%. Though it is about 40% higher than the previous standard rate which was applied during the implementation of the policy of restriction and exclusion that was only 10%, but it is still one of the lowest standard rates all over the world.

¹ Ernst & Young, International VAT, A guide to practice and procedures in 21 Countries, Ernst & young international, London, 1991 p. 13

² Caitlin Hartley and Molly Thompson, Worldwide VAT, GST and Sales Tax Guide, 2016, © 2016 EYGM Limited. London SE1 2DA United Kingdom. Pp. 1091 – 1094.

Accordingly, it is clear to us that adopting generality philosophy in levying the VAT, or in raising the standard rate of this tax, is often surrounded by some difficult economic conditions, and Egypt did not turn to adopt these two philosophies except under the pressure of such circumstances

(2) Effects of raising the VAT standard rate in conjunction with the generality of application

(i) The role of a high standard rate in shifting the tax burden:

In fact, the effect of raising the VAT rates on taxable items' prices is not necessarily instantaneous, but depends on several factors such as: the nature of the market, economic conditions such as prosperity and

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depression, the elasticity of demand for the taxable item, etc.¹

Producers may prefer to absorb the high tax rate or a large part of it to maintain the demand for their products. This would negatively affect their profits, especially when they do not have a significant competitive position in the market, or when the competition is strong and the demand for their products is elastic, etc. Anyhow, the slight increase in the VAT rates may not have a tangible effect on the decrease of consumption, but it does bring considerable tax revenue to the state.

It is natural that the high VAT rates leads to high inflation rate.² Usually, any increase in the VAT rate leads to a parallel increase in prices, and consequently

¹ See the details of that: Dr. Abdel Hadi Moqbel, and Dr. Ahmed Youssef El-Shahat, Readings in Public Finance, Tanta University Library, 2010, pg. 192

² – Mara Eugenia Ramona, Mara Cristian and Cuceu Ionut, Babes-Bolyai University Cluj-Napoca, VALUE ADDED TAX IN THE ECONOMIC CRISIS CONTEXT. Faculty of Economics Science and Business. Cod JEL: H23, H3, H22, G18.2010.p.390.

to a high rate of inflation. Though the rise in the inflation rate at that time is just a temporary shock and may be declined at the long run, but this increase in prices will have a downward impact on contemporary income levels. Thus, one of the main effects of raising the VAT rate is the negative influence on contemporary income levels.

-Examples: In 2005, when the Dominican Republic moved towards VAT generality application on all goods and services – as happened in Egypt under Law No. 67 of 2016, the tax rate also raised on the same date – as happened in Egypt as well – but from the rate of 8% to a rate of 12%, i.e., about 50% rate increase of the previous one.

Though this nominal increase in the VAT rate has had its effect on increasing the actual VAT rate than earlier. While the nominal increase that ranged from 8% to 12%, the actual application of the VAT at the new rate (12%)

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proved that the increase in the – actual – VAT rate was at a higher ratio compared to its counterparts that were applied during the low nominal rate at 8%. The following table illustrates that:

Table No. (3)

Actual VAT rate in the Dominican Republic during adopting generality in levying the VAT and raising its standard rate to 12%, in 2005.

<i>Region</i>	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>Average</i>
<i>Rural areas</i>	2.13%	2.45%	3.13%	3.60%	4.42%	3.15%
<i>urban areas</i>	2.45%	2.88%	3.21%	4.07%	4.90%	3.50%
<i>Government Procurement</i>	2.61%	3.25%	3.73%	4.18%	4.68%	3.69%
<i>Average at the state level</i>	2.32%	2.80%	3.35%	4%	4.72%	3.44%

This table shows¹ that the – actual – tax rate in the lowest fifth of the families reached – in average– 2.32% after it was 1.48% when applying the previous– nominal– low rate (8%), i. e. in an increase of 64% from the previous actual rate. Besides, the actual VAT rate that affected the highest fifth of the families was 4.72% instead of 2.82% prevailed before raising the VAT rate; i. e. in an increase of 60% from the previous actual rate.

As for the other three fifths of the families, from the second to the fourth, the –actual – VAT rates were: 0.80%, 3.35% and 4% respectively after they were 1.81%, 2.13% and 2.57%, respectively, i.e., with an increase of 65%, 64% and 64% respectively from the previous actual rate.

¹ Glenn P. Jenkins, Hatice Jenkins and Chun-Yan Kuo, IS THE VALUE ADDED TAX NATURALLY PROGRESSIVE? Queen's Economics Department Working Paper No. 1059, Kingston, Ontario, Canada, K7L 3N6, 4-2006 pp. 12, 19.

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(ii) Effects of raising the standard VAT rate on tax revenue:

We could recognize the general indicators about the relationship between the high standard VAT rate and the percentage of its contribution to the total tax revenue in a country through the following table¹:

Table No. (4)

The relationship between the VAT rate increase and total tax revenue

<i>Country</i>	<i>VAT rate</i>	<i>Ratio of its revenue to tax revenue</i>
Denmark	25%	19.5%
Hungary	25%	26.1%
Sweden	25%	16.8%
Iceland	24.5%	29.7%
Norway	23%	19.2%

<i>Country</i>	<i>VAT rate</i>	<i>Ratio of its revenue to tax revenue</i>
United Kingdom	17.5%	18.2%
Portugal	17.5%	23.2%
Turkey	17%	24.2%
Germany	16%	18.4%
Spain	16%	17.5%

¹ – James R. Hines Jr., TAXING CONSUMPTION AND OTHER SINS NATIONAL BUREAU OF ECONOMIC RESEARCH, 1050 Massachusetts Avenue, Cambridge, MA 02138, Working Paper 12730, December 2006.p.34.

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Slovakia	23%	22.3%	Luxembourg	15%	15%
CZ	22%	18.3%	Mexico	15	18.7%
Finland	22%	17.4%	New Zealand	12.5%	24.7%
Poland	22%	22.00%	Australia	10%	12.1%
Belgium	21%	16.3%	South Korea	10%	17%
Ireland	21%	23.1%	Switzerland	7.5%	13.1%
France	20.6%	16.8%	Canada	7%	14.3%
Austria	20%	18.8%	Japan	5%	8.9%
Italy	20%	15.4%	Egypt	10%	26.6%
Greece	18%	21.8%	-	-	-

The table above shows clearly that the VAT revenue value to the total tax revenue in any country all over the world is directly proportional to its base rate; as its revenue increases when its base enlarged and its rates increases. Thus, the percentage of its contribution to the revenues of the state's budget increases compared to revenue of other taxes applied therein.

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In addition, the countries applied the VAT at a rate ranging between 20% and 25%, VAT contribution of its total revenues ranged between 18.3% of its tax revenue as in Czechoslovakia and 29.7% as in Iceland. Other countries that applied the VAT at a rate ranged between 15% and 20%, VAT contribution of its revenue to total tax revenue of those countries ranged from 15%, as in Luxembourg to 24.2% as in Turkey. As for those that applied the tax at a rate ranging between 10% and 12.5%, the contribution of the VAT revenue to their total tax revenues ranged between 12.1% as in Australia and 24.7% as in New Zealand.

(3) Effects of Generality Policy upon non–standard Rates

(i)– Effects on Positive Low Rates:

With the issuance of Law No. 67 of 2016 to generalize levying VAT upon all goods and services, it almost

annulled the low tax rate (5%). In fact, amendments of Investment Law No. 8 of 1997 by the law No. 7 of 2015 that issued to encourage investment in Egypt restricted the VAT Law No. 67 of 2016 by levying the VAT on capital goods and their spare parts in this low rate of (5%). Therefore, levying of the VAT in Egypt at the low rate (5%) was limited to these capital goods and their spare parts only.

As for the rest of goods and services that subjected to the Sales Tax at this low rate, according to Law No. 11 of 1991, some of them were enlisted in the table enclosing the new law, and remained subjected to the tax at this low rate, but the provisions of table tax – not the VAT– were applied to them. The most important of these provisions is the deprivation of input tax refund, thus such goods subjected to worse tax treatments than before, and

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the other goods were exempted from the VAT such as coffee and medicines even if they were imported.

As for the European Union countries, in February 2006, they agreed on the necessity of adopting a low rate, and applying it to some necessary goods and services, provided that they include intensive labor services. According to their views, reducing tax rates in such cases achieves both economic efficiency and social justice.¹ So, we believe that it is not acceptable to levy the Egyptian VAT at the low rate on capital goods only. Comparative legislation should be imitated in this regard, by levying the VAT at such a low rate on many essential goods and services, as happens in most countries of the world.^{2 3}

(ii)- Effects on the “zero” rate:

(a) Fields of applying the zero rate:

¹ Ibid. p. 4.

² Ibid. p. 1036 .

³ Ibid. p. 326 .

The zero rate is a special rate. It gives exporters the right to deduct or refund the input tax borne by taxable goods and services when they were exported to abroad, even though no output tax is due on them. Therefore, some comparative legislations describe it as an exemption with credit.

Mostly, the zero rate is applied in the case of export only; it is applied in France, for example, to goods exported to abroad and their related services, as well as to goods sold to any country of the European Union in addition to some financial transactions provided to consumers outside of the European Union.¹ However, there are many other countries applying the zero rate to many essential goods and services consumed within the state's borders, in addition to exports, in order to achieve some economic and social purposes; e.g. Mexico applies

¹ Caitlin Hartley and Molly Thompson, *Worldwide VAT, GST and Sales Tax Guide*, 2016, © 2016 EYGM Limited. London SE1 2DA, United Kingdom. P.37.

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a zero rate on exports and some medicines, dairy, and unprocessed foods.¹ Also, the United Kingdom applies the zero rate to many goods and services not exported to abroad, such as books, newspapers, periodicals, children's clothing, some foodstuffs, transport services, and medical drugs.²

As for Egypt, it applies the zero rate only to exports, but it also expands its scope to free cities, free zones, and free markets where goods and services entering these places are treated as if they were imported from the abroad even if they were coming from local markets. Also, goods and services may not exit from these places to the local market except after paying the VAT due, as if they were imported from abroad. As a rule, if such

¹ Ibid.p.656.

² David CASHIN and UNAYAMA Takashi, the Intertemporal Substitution and Income Effects of a VAT Rate Increase: Evidence from Japan. The University of Michigan, RIETI, April 2011, P.44.

goods and services remain in these places, no VAT is due.

(b) Tax treatment of inputs when the zero rate is applied:

The Egyptian legislator insists on the eligibility of taxpayers to recover – not deduct or refund – the input tax upon export, whether in the current VAT law, or in the previous law. Certainly, this view is incorrect because if the tax recovery system is proportional to the cases in which the tax is collected in error due to the inability of the refund system to address these issues as an inevitable result of the absence of input tax and output tax as in the case of supplying amounts to the tax administration as taxes but on exempt goods, or calculating a tax on goods subject to it, but at a tax rate

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that exceeds the tax rate stipulated by law, etc.¹ However, in case of exporting taxable goods and/or services, we find a big difference; since we find, in such a case, input tax and an output tax, even if the value of output tax were zero. As the output tax value became zero just because the items exported to abroad be subjected to the zero rate, not more.

This is because the refund system, according to its development in the VAT in comparative legislations is a system that allows the taxpayer to deduct all the input taxes incurred by all his taxable goods and services from the output taxes due on them when they are sold. It simply means deducting the input tax from the output tax due (Taxe sur Taxe)²

Look: Sayed Mohamed Abdelwahab, Discount Policy and Exemptions in Sales Taxes, Tax 5th Conference P. 16

² Andre Muller " L'assiette réelle de la taxe sur la valeur Ajoutée " thèse du doctorat, Dallaz, paris, 1965, p. 52.

Chapter Three

The Egyptian Table Tax and its Estimation

When the sales tax law No. 11 of 1991 was issued, it was accompanied, over the years of its application, by two tables: The first was: table No. (1) to some commodities that subjected to the consumption tax (by law No. 133 of 1981) before. While the second was: table No. (2) exclusively assigned to some taxable services.

If we look at the special provisions stipulated by Law No. 11 of 1991 for the goods of table No. 1 accompanying that law, we find that they were so numerous that it couldn't be said that the philosophy of VAT law applied to them. As for the rates to which these commodities subjected to, they were diverse at far extent.

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Some of these rates were proportional sometimes reached 100% of the taxable good value (such as: cigarettes and tobacco products). Other rates depended on quantity on either unit of weight (such as: tea and sugar), volume (such as: soft water), or number (such as: cigarettes). That table only adopted a low rate of 5% to some medicines.

As for table No. 2, accompanying Law No. 11 of 1991, it included several services exclusively, and subjected some of them to a tax at the standard rate of (10%), and the others at the low rate of (5%). All services were excluded from the right to refund.

When the VAT Law No. 67 of 2016 was issued, it included only a single table. This table included twenty-five groups of commodities and services; thirteen groups of them subjected to the table tax alone, and the other

twelve groups subjected to the table tax along with the VAT in the same time.

Though some goods subjected to the low rate of 5% under the annulled law (GST law), they continued to subject to the same rate under the new law (the VAT law). Actually, the legislature was unsuccessful when adopting the new tax treatment for these goods.

The old treatment, under the general provisions of the GST law, allowed taxpayers to deduct the input tax from the output tax. So, that treatment cleared these goods from any double taxation.

As for the new tax treatment, under the provisions of the table tax, double taxation with regard to these goods and services existed, and is even intended by the legislator. What a paradox!

At a time when the legislator was adopting restriction and exclusion philosophy with all its disadvantages; the

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lack of application generality of the refund system while levying the tax, such goods had enjoyed the right of refund therein. These goods do not have the right of refund; though the VAT law was primarily issued to get rid of such distortions existed in the repealed sales tax law. Among the most important of these distortions was: depriving taxpayers of the refund right!

When the legislator moved to reform the VAT, by Law No. 67 of 2016, it was natural, to adopt generality of submission to the VAT, along with generality of the refund right. Yet, what happened was the opposite. The legislator has adopted the policy of generality of submission to the VAT only, but has not adopted the policy of generality of the refund right. This is a big flaw. As a result of this flawed policy, some of the goods that had the refund right in the previous stage before the reform has lost it after the reform. This is completely

enough to decide that this reform was defective. It needs to be reconsidered

As for the double taxation intended by the legislator regarding the groups of the twelve commodities and services, which the legislator subjected them both to the table tax and the VAT at the same time, there is no doubt it represents a result of an unacceptable legislative regulation, and it is not worthy of the legislator, at the time it made great strides towards extending the scope of vat to include all goods and services, and raising the standard rate of the VAT at the same time by about 40% to become 14% instead of 10%

It is not suitable for the legislator, in such circumstances, to adopt this flawed treatment, which confirms will to raise the value of the tax revenue, even by sacrificing the simplest rules of justice, and perhaps even the local industry in some sectors.

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It is worthwhile for the legislator to review its position in this context in order for its tools to be straightened; especially it no longer needs to adopt such defective treatments.

Conclusion

This paper revealed the philosophy of Egyptian legislation when levying the value-added tax (VAT). It shows us that this philosophy passed through two major phases: the first phase began with Law No. 11 of 1991, and it may be called: the philosophy of restriction and exclusion; As that Egyptian tax legislation chose a specific type of goods (manufactured goods) whether they were local or imported, except those it might exempt from the tax and levied the VAT upon. Also, it chose only a certain number of services and levied the tax upon them.

In this regard, that was the same as the VAT approach. Therefore, we consider that the Egyptian sales tax introduced by Law No. 11 of 1991 was an incomplete application of the value added tax (VAT). In addition to the above goods and services, some other goods included in table No.1 that was stipulated in that law, and were subjecting to special provisions, away from the VAT provisions.

So, at a later stage, the philosophy of the Egyptian legislator underwent a major transformation; where it tended to levy the value-added tax (VAT) on all goods and services, except for those exempted. Thus, the philosophy of restriction and exclusion turned into the philosophy of generality in levying the VAT.

The Egyptian legislator found a justification for this transformation in the difficult economic conditions that Egypt went through; following the political turmoil took

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place in 2011. If we look at philosophies of comparative legislations in this regard, we find that the Egyptian legislator has followed them.

As this paper revealed, difficult economic conditions experienced by different countries often contribute to the transformation of the philosophies of their tax legislation, whether to the generality of levying the VAT, and/or to the direction of increasing the VAT rates as we saw in many comparative legislations, after the financial crisis that hit the world in 2008.

This paper revealed that the transformation of the Egyptian legislator's philosophy has good effects on the tax community, though the paper criticized the position of the Egyptian legislator because of the negative treatment of taxed goods and services according to provisions of the table accompanying this law.

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