

# Who is liable to pay VAT? A closer look at the Egyptian VAT Law

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Taxes are a source of revenue for the government which contribute to economic growth and infrastructure. Whilst there are several types of taxes, they can generally be classified as direct or indirect taxes. Direct taxes are levied on the income or profits of an individual or organisation and cannot be transferred to another person. Examples of direct taxes include income or corporate tax, property transfer tax, and capital gains tax. On the other hand, with respect to indirect taxes, businesses act as tax collectors and the burden of indirect taxes are ultimately borne by the final consumer or end user. Indirect taxes include sales tax, value-added tax ('VAT'), excise tax (also known as "sin tax" levied on specific goods which are harmful to human health or the environment). However, the question arises as to the transferability of indirect taxes; whether the burden of indirect tax be transferred to the supplier in a scenario where both the consumer or end user and supplier contractually agree to do so. In Egypt, by way of a judgment issued in 2010 for Petition No. 1315/75JY, the Court of Cassation established the principle in 'shifting' the indirect tax burden. In this article, we examine the facts and the implications arising from the judgment.

## Claim: who is liable to pay the general sales tax?

In this case, an employer filed a petition for the annulment of a judgment issued by the Court of Appeal ordering the employer to pay the sales taxes related to a construction contract notwithstanding its agreement with the contractor (i.e. the service provider) to shift the burden of tax and the contract price which included the tax due. According to the petitioner, the appealed judgment disregarded the agreement of the parties where the payment of all fees and taxes would be borne by the contractor, which inherently included sales tax.

## Court of Cassation judgment: upholding parties' agreement

The Court of Cassation deduced from the relevant sales tax legislation that the employer ('Petitioner'), being the consumer, is the party who is legally required to pay the sales tax to the contractor for the provision of services by the contractor, who will subsequently remit the tax to the tax authority. The Court of Cassation concluded that sales tax is a type of indirect tax which is ultimately the responsibility of the consumer while the service provider is the party legally required to collect and remit the tax to the tax

authority. However, the Court of Cassation went on to say that “*parties to a contract may agree to shift the payment burden to the service provider*”.

Therefore, given that the parties contractually agreed that the tax should be borne by the contractor, the Court of Cassation held that the appealed judgment contradicted the agreement of the parties, and accordingly ruled to annul the Court of Appeal’s judgment.

## Observations

While sales tax is no longer applicable in Egypt in accordance with the Value-Added Taxes Law (Law No. 67 of 2016) (‘VAT Law’), it is arguable that the principle established by

the Court of Cassation in connection with shifting the burden of tax under the sales tax regime should be applicable to the VAT regime. Both sales tax and VAT legislation<sup>1</sup> generally reflect international indirect tax principles and identify that: (i) the supplier or provider of goods and services is liable to collect and pay the tax to the tax authority; (ii) tax falls due when the goods are sold or service is provided; and (iii) the tax value shall be added to the price of the service. It is notable that these were the provisions in the Sales Tax Law upon which the Court of Cassation relied in reaching this conclusion the reasons for which are substantively identical to the VAT Law. Further, notwithstanding that the consumer or recipient generally bears the burden of tax under the sales tax regime, it is worth noting that the Court of Cassation respects the terms of commercial contracts where parties contractually agree to shift the payment burden to the service provider. Thus, to the extent parties contractually agree to pass the VAT burden to the service provider, this principle established by the Court of Cassation should be applicable and could, in the future, hypothetically be used to shift the VAT burden.

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*1Article 1 of the VAT Law provides that the taxpayer is the person required to collect and pay taxes to the tax authority, whether he is a producer, merchant or service provider. Article 2 provides that tax is due on commodities and services unless exempt explicitly by law. Article 5 provides that the tax falls due when the commodity is sold or a service is provided by the taxpayer. Article 11 provides that the value-added tax shall be added to the price of commodity or service sold by the taxpayer.*