SHARKAWY & SARHAN

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THE NEW INVESTMENT LAW INCENTIVES FOR SMES AND SOLAR POWER FACILITIES

SolarData Platform Egypt

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I- THE NEW INVESTMENT LAW

The New Investment Law (72/2017) (the "**New Law**") very recently issued on 31 May 2017, aims to create a better investment environment. Various reforms and incentives were introduced accordingly. The New Law highlighted several principles governing investments in general; these include, emphasizing on the government's role in supporting the micro, small and medium enterprises. The Executive Regulation of the New Law (ER) is yet to be issued, as it is expected to introduce further reforms and tools much needed to put in effect and clarify several issues pending under the New Law.

The New Law provides for general sets of guarantees and protections, it further furnished for three different sets of investment incentives; namely, General Incentives, Specific Incentives and Additional Incentives.

Specific and additional Incentives are to be granted to specific projects according to the <u>geographical distribution</u>, <u>type of activities</u> operated by the investment project. This shall be stated in details below.

Throughout the following, we outline in brief, guarantees and incentives stated under the New Law.

First, General Guarantees providing for a more secure and protected investment climate to all investment projects in Egypt for both national and foreign investors.

Second, incentives under the New Law include:

1- <u>General Incentives</u> are also provided for all investment projects subject to the New Law; these incentives include tax exemptions, land allocation and unified customs tax.
2- <u>Specific Incentives:</u> These are set out for specific projects, decided according to the type of activity and geographical area; Specific incentives in general include power and electricity projects as shall be explained below.
3- <u>Additional Incentives:</u> Even more distinctive, these projects will be defined by the prime minister and awarded on a case-by-case basis by the head of GAFI. These incentives include, private ports, subsidized utilities, subsidizing employees' tech. training, refund of land price as well as free land allocation to strategic projects.

In addition, the New Law introduces new bundle of procedural measures as well as setting out a clear identification of the investment schemes.

In light of the above, solar power projects subject to the New Law will benefit from the General Incentives and Guarantees, while only specific projects fulfilling the requirements stated below shall benefit from the specific and additional incentives.

Throughout the following, we will explain in details all General Incentives and Guarantees as well as specific and additional incentives applicable to solar power facilities.

1-Guarantees

All investment projects subject to the New Law (the "**Investment Project/s**") shall benefit from the same General Incentives and Guarantees as under the old investment law 8/1997.

A- General Guarantees

- Just and fair treatment, furthermore all investments shall not be subject to any arbitrary/ abusive procedures or discriminatory decisions[1];
- Expropriation of assets or nationalization of companies is not permitted;
- No administrative guardianship can be imposed on companies or establishments and no takeover is permitted on its assets or capital except by virtue of a final judicial verdict;
- The investor must be informed with all decisions related to his investment which must be reasoned, as shall be further regulated under the New Law executive regulation;
- Cancelation of the investment permission/license and/or withdraw of the project allocated land, the competent administrative entity must be with prior consultation with GAFI and only after giving the investor reasonable period to remedy its violations.

B- General Guarantees Designed To Encourage Foreign Investments

In addition, the General Guarantees stipulated under the New Law included specifically designed General Guarantees to attract foreign investments to Egypt, these include:

- Equal treatment for foreigners with nationals.
- Investors are guaranteed the right to repatriate their profit offshore. Prior to this guarantee, there were no legal restrictions on transferring FX funds abroad. The only obstacle was and still remains to be the availability of currency. However, as CBE's foreign currency reserves are recovering back to pre-2011 levels, the foreign currency crunch is gradually ceasing with more healthy economic indications on convertibility and repatriation;
- Either independently or collectively with others, all Investment Projects shall have the right to import, all required equipment or raw materials needed to establish, expand and operate the Project.

[1] Article 3(1, 3) of the New Law.

2- General Incentives

As stated above, all companies incorporated under the New Law -except those incorporated under the Free Zone Scheme- shall benefit from the following General Incentives:

- A 2% unified customs tax on imported equipment and machinery for the investment projects.
- Investors will enjoy stamp exemption from tax and notary registration fees on registration of articles of association, mortgages and loan agreements for 5 years from registration in the commercial registry.

3- Specific Incentives

A- Overview

The New Law provided for Specific Incentives for particular projects who would be eligible for such incentives.

These incentives are temporary, only available for three years. This entails that the investment project must be incorporated under the New Law within the three years following the issuance date of the Executive Regulation (yet to be issued).

These incentives are classified according to the geographical location of the project and type of activity as well as the type of activities operated in these Zones.

Specific incentives include tax deductions covering a portion of investment costs of the project depending on the zone in which the project is established and the activity. The deductions will be deduced from future profits. It is expected that the Executive Regulation will regulate this.

B- Geographical Location of the Project

The New Law divides the country into two zones (yet to be mapped under the ER):

1- Zone A: which likely will include Upper Egypt and Suez and other areas. Which will benefit from an income tax deduction to be deducted from the project profit of 50%, with a maximum of 80% of paid capital.

2- Zone B: which will be the rest of Egypt. Zone B projects will benefit from a deduction of 30% of the investment cost. The tax incentive is capped at a maximum of 80% of paid capital and over a period of a maximum of seven years.

However, not all activities within these zones will receive the Specific Incentives. Several decisions are to be issued by the Prime Minister in conjunction with other ministers will define which activity is required in which zone and sub-zone. Investors will get the incentive if they invest in the required activity within a specific sub-zone.

A- Type of Activity

According to the New Law, not all projects are situated in zone (A) are entitled to the income tax deduction to be deducted from the project profit of 50%, rather only projects practicing specific activities as shall be stipulated under the New Law's Executive Regulation will benefit from such incentive.

As to projects situated in Zone (B), the New Law included a list of the prioritized activities to benefit from this incentive, this list includes:

i. Electricity production and distribution projects identified by a virtue of a decree from the Prime Minister. (the "**Identified Power Projects**"). It must be noted that the Prime Minister did not issue yet any decrees stating the Identified Power Projects.
ii. The Small and Medium Enterprises (**SMEs**)as well as;

i- Electricity production and distribution projects

Upon the issuance of a decree from the Prime Minister with the Identified Power Projects. Those Identified Power Projects shall benefit from a deduction of 30% of the investment cost (shall be identified in details in the Executive Regulation)[2]. The tax incentive is capped at a maximum of 80% of paid capital and over a period of a maximum of seven years upon fulfilling all the following conditions:

- ✓ Established under the New Law within the three years following the issuance date of the executive regulation,
- ✓ Situated in Zone B and
- ✓ Included in the Identified power projects

However, investors must bear in mind that no shareholder or founder may include in funding or establishing the investment project the following:

i. The material assets of any company/entity that is established at the time of the issuance of the New Law, or;
ii. The material assets of any company/entity that is liquidated within the three years period following the issuance date of the ER[3].

This is to ensure that, only genuinely new investments benefit from the tax incentives and ban the restructuring or repackaging of already existing investments.

[2] Article 11(8) of the New Law.

[3] Article 12(4) of the New Law.

ii- <u>The Small and Medium Enterprises</u>

In regards to SMEs, the New Law did not set a clear definition of what shall be regarded as an SME and no further distinction was made in regards to the activities required for these entities in order to be eligible for the specific incentive in zone B. Taking into account that definition of SMEs may differ under different contexts.

However, according to the decision, 1081/2017 most recently issued from the Ministry of Trade and Industry, definition of medium and small enterprises subject to the newly issued Law Facilitating the Issuance of The Industrial Licenses no (15/2017) is as follows:

Size of Entity	Type of Entity	Requirements
Small Entity	Newly incorporated	Having a Minimum paid capital of 50,000 EGP(Fifty Thousand Egyptian Pounds) and a maximum of 5,000,000 (Five Million Egyptian Pounds)
	Established and operating	Having annual business operations with a minimum of 1,000,000 EGP (one million Egyptian Pound) and a maximum of 50,000,000 EGP (Fifty Million Egyptian Pounds)
Medium Entity	Newly incorporated	Having a Minimum paid capital of 5 million EGP(Five Million Egyptian Pounds) and a maximum of 15,000,000 EGP (Fifteen Million Egyptian Pounds)
	Established and operating	Having annual business operations with a minimum of 50,000,000 EGP (Fifty million Egyptian Pound) and a maximum of 200,000,000 EGP (Two Hundred Million Egyptian Pounds)

This could be interpreted that, any Solar Power Facility qualified as a Small or Medium Entity under the previous definition shall be entitled to the Specific incentive in zone B stated above (i.e. deduction of 30% of the investment cost), regardless of being listed under the Identified Power Projects or not.

Seeing that operations related to solar power & renewable energy is a targeted investment field for GAFI[4], We may also deduce that power generation facilities and SMEs may be included within projects to be prioritized in zone A, thus obtaining the 50% deduction of the investment costs. This however shall yet remain to be seen, pending a decision from the Prime Minister in conjunction with the competent minister.

In all cases specific incentives shall be granted by virtue of a certificate issued from GAFI's Chief Executive Officer.

4- Additional Incentives

The New Law further provides for Additional Incentives to be granted to projects entitled to the Specific Incentives as stated above (i.e. including SMEs and solar power facilities in the Identified Power Projects). These incentives shall be granted on a case-by-case basis, in accordance to a decision issued from the cabinet of ministers while taking into considerations the regulations and requirements identified in the New Law ER.

Additional incentives include:

1- In conjunction with the ministry of finance, a specialized custom ports for the investment project imports and exports may be established;

2- The government may pay/repay the investor in whole or in part the expenses incurred for providing access of basic utilities to the investment project building after operating the project;

3- The government may finance part of the technical training for the employees;

4- The government may Refund 50% of the total amount of the land price allocated for the industrial projects, in case the production commenced within two years from the date of obtaining the land;

5- Providing land for free for some strategic projects in accordance to the relevant laws and regulations.

It must be noted that other Extra Non-Tax Incentives may be granted by virtue of a decision issued from the cabinet of ministers upon a recommendation from the competent minister.

GAFI's Chief Executive Officer is competent with issuing the Additional Incentives certificate that is required to prove obtaining these incentives while no further approvals are required.

[4] https://www.gafi.gov.eg/Arabic/Sectors/TargetedSectors/Pages/default.aspx

II- Incorporation Requirements

1- General Incorporation Rules and Requirements

As general requirements, any Joint Stock Company (the "**JSC**") established under the New Law or the Companies Law must take into account the following rules and requirements:

- A Minimum number of three shareholders (while there is no maximum number of shareholders);
- Minimum Capital of Two Hundred and Fifty Thousand Egyptian Pounds (250,000EGP);
- Founding shareholders may be natural persons or juristic entities;
- No restrictions on the ownership of shares by foreigners. Generally, total foreign ownership is permitted. Some activities may not be carried out by foreigners or companies owned by foreign shareholders. These activities however doesn't include solar power activities (i.e. Generation or distribution);
- A JSC must have a board of directors comprising of a minimum of three directors. Whereas there are no restrictions on the nationality of directors;
- At the time of incorporation, shareholders must deposit no less than 10% of the total value of the issued capital. Within three months from incorporation, the founding shareholders must deposit no less than an additional 15% of the total value of the issued capital. Finally, the remaining unpaid issued capital must be paid within five years from incorporation.

2- Incorporation under the New Law

GAFI is responsible for providing incorporation and post incorporation services for companies to be established under the New Law.

The New Law states that, incorporation process should now be concluded online through the E-Incorporation Services System (the "**E-service System**") established and operated by GAFI. This E-service System was very recently launched on GAFI's official website[5]. However, incorporation through GAFIs' One Stop Shop is still operating and in effect.

Note

In case of applying through One Stop Shop, the company must take into consideration applying before the geographically competent One Stop Shop, taking into account the geographical location of the main headquarters of the project's operations. There are five One Stop Shop offices in Egypt, each covering specific governorates, namely; Cairo, Alexandria, Ismailia, Asuit and 10th of Ramadan[6].

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[5] https://www.gafi.gov.eg/English/eServices/Pages/default.aspx

[6] https://www.gafi.gov.eg/english/Howcanwehelp/OneStopShop/Pages/default.aspx

Whether the investor/shareholder decides to incorporate the company through GAFI's E-services or One Stop Shop, the previously stated General Rules and Requirements would be applied.

Furthermore, it must be noted that the New Law's ER expected to be issued soon shall yet to clarify several issues related to incorporation, however throughout the following we shall highlight the main reforms in light of the New Law.

1- The authorities are under a duty to respond to the application for incorporation of an investment project within a maximum of <u>one business day</u> from fulfilling al required documents. This however is not yet the practice; we may expect further reforms in the future leading to such facilitated and swift process and timeline.
2- An investor will have a consolidated number for his entity. During the licensing process and throughout operations, all the different authorities will deal with the investor using this consolidated number. We expect the ER to further regulate the issue; this however is not yet in effect.

Post incorporation procedures will be governed only by GAFI. Post incorporation procedures will also benefit from the electronic system such as general assemblies' ratification, capital increase and decrease, and use of electronic ledgers.

3- Incorporation Requirements under the FIT Scheme

For power project facilities with capacities more than 500 KW, in order to establish an SPV and take part in the FIT scheme, the investor must first be qualified for the FIT scheme. Qualification letter is obtained from the "Central Unit for Feed in-Tariff Projects". After being qualified, the consortium will begin establishing the SPV in Egypt. During and after incorporation the SPV must comply with several legal requirements stipulated in EGYPTERA (EERA) decision as shall be stated below[7]. This decision included some <u>General Rules</u> to be regarded by the consortium as well, these include:

- The maximum capacity permissible for one SPV is 50MW.
- The total share of a member who joins several consortia shall not exceed the value of capital required to establish a plant with a capacity of 100MW per site of the same technology (i.e. solar, wind). To ensure compliance with these rules, each member will be required to disclose, upon applying for the interim license, its ownership in other qualified companies under the feed-in tariffs program. The site is defined as the geographical area where all power plants are connected with the same Egyptian Electricity Transmission Company (the"**EETC**") substation. It must be noted that this restriction is temporary; it shall

[7] http://egyptera.org/Downloads/Licenses/request/%D9%82%D9%88%D8%A7%D8%B9%D8%AF.pdf

remain in effect during the two years following the company's commercial operational date.

i- Establishment and pre operational requirements

- The qualified consortium Establishing a Special Purpose Joint Stock company(SPV) under the Investment Law;
- The SPV's object must be "Designing, constructing, managing, operating and maintaining electricity power plants from renewable sources (solar/wind energy) under the feed-in-tariff program, in accordance with the applicable law, regulations and decrees";
- All the consortium members must participate in the SPV's capital;
- The collective percentage of participation of the consortium members must be less than 51% of the SPV's capital;
- The consortium leader must hold at least 25% of the SPV's capital;
- The minimum issued capital must be Fifteen Million Egyptian Pounds (15,000,000 EGP) at the time of incorporation, or its equivalent in other currencies;

ii- Post Operational requirements

- The consortium leader must maintain a percentage of shares not less than 25% of the SPV's capital during the first two years from the project's commercial operational date;
- The EERA must be notified with any changes occurring to the SPV's shareholders structure;
- The SPV must assign a manager responsible for all relations/dealings with the EETC, Egyptian Electricity Holding Company (EEHC) and New & Renewable Energy Authority (NREA).

It must be noted that these Post Operational requirements are only specific requirements related to the FIT Scheme SPVs while other technical and operational requirements and compliance conditions related to solar power facilities in general under the New Electricity Law shall be applied.

Annex (1) Incorporation Documents

The documents required to establish a JSC include the following:

	Document	Comments
1	Power of Attorney ("**POA**")	Issuance from each foreign/national shareholder in favor of the person/lawyer responsible for incorporating the company.
2	Name Certificate	The purpose of the name certificate first is to ensure that no other company is registered under the same name, and to protect the name of the company until it is incorporated. The certificate is obtained from the commercial registry at GAFI. The validity of the certificate is 15 days. If 15 days lapse before submitting the incorporation application, the certificate will be renewed at the same commercial registry.
3	Bank Certificate	A bank account must be opened in the name of the company under incorporation on behalf of the shareholders where the capital of the new company will be deposited. As part of the incorporation procedures, the company will need to deposit <u>10% of the issued capital</u> in order to obtain the bank certificate. A bank certificate is then obtained and presented to GAFI as part of the incorporation process.
4	Identification Documents	The founders must provide copies of the Shareholder's natural person's Identification Cards for Egyptians and passports for foreigners. In case of a shareholder Juristic Person, a copy of the Commercial Registry should be presented.
5	Security Clearance For Foreign Shareholders	Security clearances are required for any foreign shareholder, whether the shareholder is a natural or juristic person.

6	Copy of the Auditors' and Accountants Register extract	In application to the obligation upon the JSC to hire a registered auditor. Therefore, while establishing the JSC, the founders/representative must present this document.
7	Auditor appointment certificate	In application to the obligation upon the JSC to hire a registered auditor. Therefore, while establishing the JSC, the founders/representative must present this document.
8	Copy of the Bar association ID for the legal counsel	The company under establishment must appoint a legal counsel in the Articles of Association ("AOA"). This is a formal requirement relating as part of the procedures of incorporation. It is not a substitute to contracting for legal services outside the AOA. The legal counsel must be admitted before the Bar association as an attorney at law before the court of appeal.
9	Lease contract	Although a lease is not required for incorporation, a company under incorporation must provide an address for the headquarters of the company at the time of incorporation and preferably, it should be the one the company will end up using. Furthermore, providing a lease agreement is a requirement for obtaining the tax card, which is essential for the company to operate. Therefore, it is best that the company proceed with finding a reasonable headquarter and enter into a lease agreement in the name of the new company (under incorporation).
10	Company's' Bylaws (Articles Of Association):	As a rule, the model articles issued by the General Authority for Investment and Free Zones ("GAFI") should be used, the company under establishment shall only be required to fill in the information in this template. The company may however introduce some modifications to the model pending approval and revision from GAFI.
11	Approval of the free zone Board of directors	According to GAFI's instructions, In case the company is established under the Free Zone investment Scheme, the approval of the free zone's board of directors must be presented.