Delivering mobile connectivity in MENA: A review of mobile sector taxation and licence extension

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Executive Summary

The report provides an overview of the tax and fee regime applied to mobile services in seven MENA[1] countries: Algeria, Egypt, Morocco, Tunisia, Jordan, Turkey and Saudi Arabia, covering key general taxes, such as VAT and corporation tax, as well as sector-specific taxes and regulatory fees. The tax and fee regimes in these countries are compared to international benchmarks through metrics such as tax and fee payments as a share of revenue and the potential impacts of tax reform are discussed. Finally, the benefits of licence extension, renewal and longer duration are discussed.

Overview of taxes and fees

In the selected MENA countries, a range of sector-specific taxes and regulatory fees are levied both on operators and consumers, in addition to general taxation.

General taxes

Some countries apply differential general tax rates on mobile services.

- In Egypt, mobile services are subject to a rate of VAT that is 8 percentage points higher than the general rate.
- In Tunisia and Jordan, higher rates of corporation tax apply to mobile operators, at 35% and 24% respectively.

Some Middle Eastern countries, such as Saudi Arabia, do not levy VAT or sales tax and rely instead on sector-specific royalty fees.

Excise Taxes

Sector-specific taxes on mobile services are applied in various forms in Tunisia, Turkey, Egypt and Jordan. In Jordan and Turkey, excise taxes are levied at relatively high rates of 26% and 25% (5% for data) and excise taxes made up 57% and 49% of total tax payments in 2015 and 2014 respectively. Other forms of excise taxes include connection activation fees in Turkey and a telecom stamp duty on invoices in Tunisia.

[1] MENA is defined as: Algeria, Comoros, Djibouti, Egypt, Libya, Mauritania, Morocco, Somalia, Sudan, Tunisia, Bahrain, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Oman, Palestine, Qatar Saudi Arabia, Syria, Turkey, UAE and Yemen. This is consistent with the approach used in GSMA (2016), 'The Mobile Economy: Middle East and North Africa'.

Regulatory fees

All seven countries in the sample levy multiple regulatory fees. In countries such as Algeria and Egypt, there are as many as eight different regulatory fees, which may add to tax and fee complexity as well as increase overall payments.

Regulatory fees on revenue, such as licence fees and Universal Service Fund (USF) contributions, exist in the majority of countries. Some Middle Eastern countries are subject to regulatory fees on revenue of 10% or more:

Table 1: Regulatory fees on revenue, as a share of total revenue

Country	Regulatory fees on revenue, % total Revenue
Saudi Arabia	17% for voice/SMS revenue, 10% for data revenue
Turkey	16.85%
Jordan	10%

Source: Deloitte analysis of operator data 2013-2015, desktop research

These operators are also subject to other regulatory fees including annual spectrum fees, numbering fees and base station fees. For instance in Egypt operators pay a fee of EGP 1-1.5 per number and fees of EGP 300 per base station.

In Saudi Arabia 49% of tax and fee payments in 2013 were regulatory fees and in Turkey regulatory fees accounted for 17% of sector revenue.

Recent changes in taxes and fees

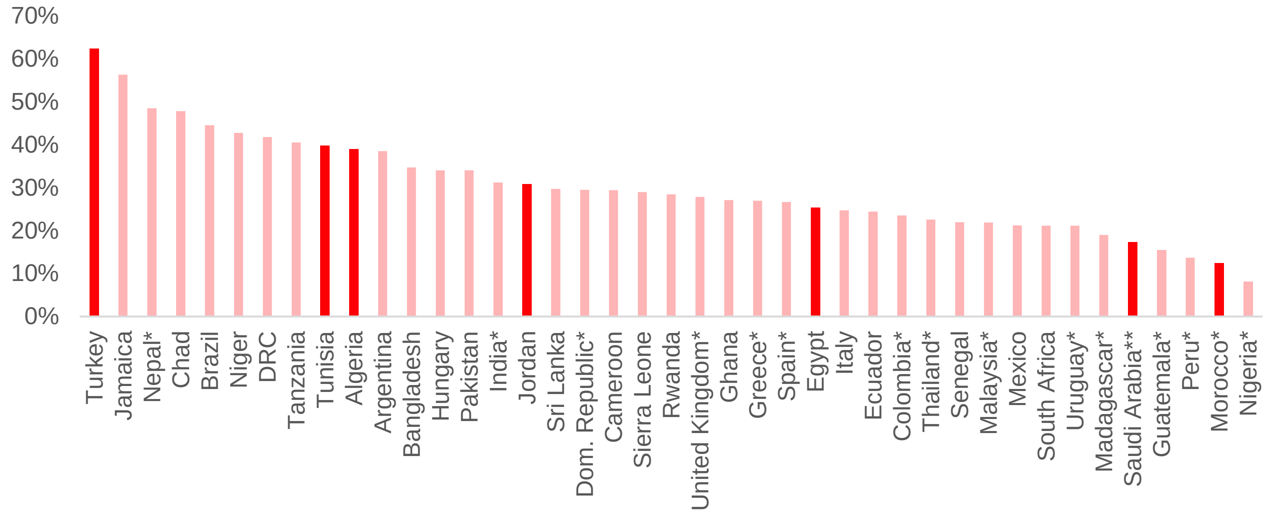
Several countries have increased the level of taxes and fees in recent years:

- Egypt introduced a VAT and increased the mobile-specific rate from 15% to 21%.
- Saudi Arabia is introducing a fee of 5% of net operating income on the new unified licences during the extension period.

Contribution of the mobile sector

There is considerable variation across the seven MENA countries in the size of tax and fee payments relative to sector revenues. Tax and fees payments account for a particularly large share of revenue in Turkey, while the share in Tunisia and Algeria is also higher than the majority of countries for which data is available.

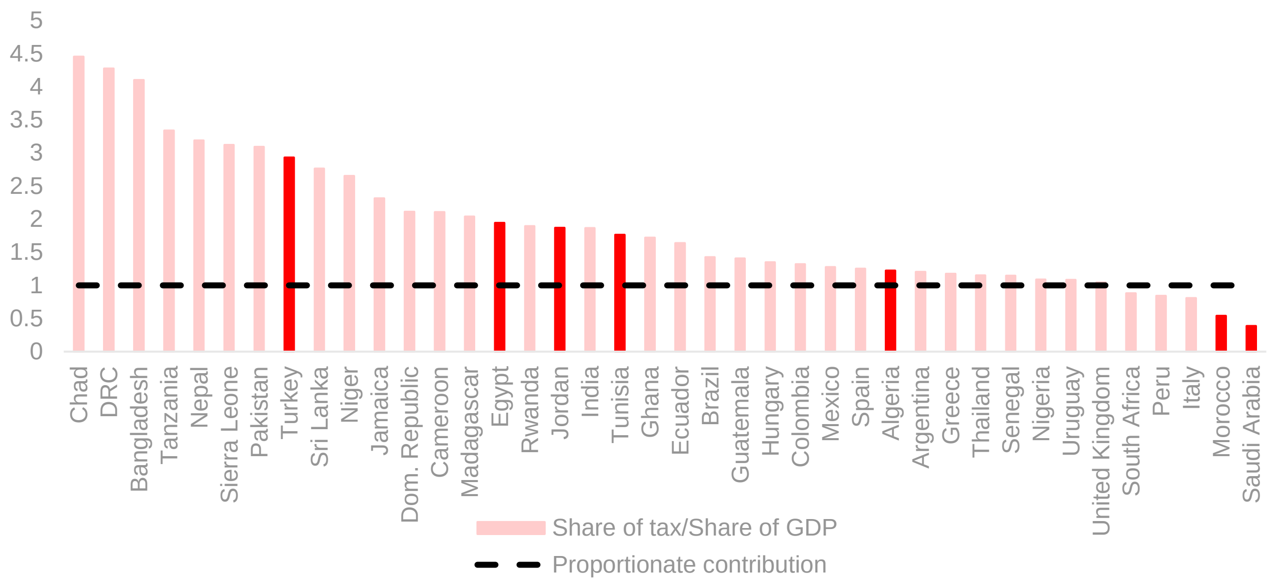
Figure 2: Tax and fee payments as a share of sector revenues



Source: Deloitte analysis of operator data, 2013-2015, * 2014, ** 2013

In many countries, particularly developing countries with large informal sectors, the mobile sector is over-taxed, relative to its economic footprint. Operators in Turkey, Egypt, Jordan, Tunisia and Algeria all over-contribute to tax revenue when taking into account the size of the mobile sector.

Figure 3: Economic and fiscal contribution of the mobile sector[2]



Source: Deloitte analysis of operator data 2013-2015, GSMA Intelligence, World Bank and IMF

[2] Share of tax = mobile sector tax and fee payments divided by total tax revenues. Share of GDP = mobile sector revenue divided by GDP.

Impacts of sector-specific taxes and fees

Affordability

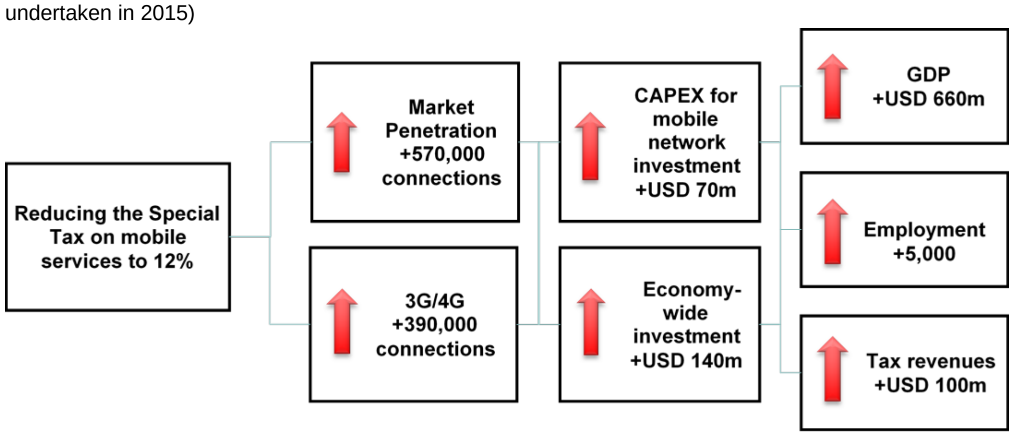
Taxes and regulatory fees on mobile services may add to the affordability barrier and lower the consumption of such services by potentially affecting prices.

Excise taxes account for around half of operators' tax and fee payments in Jordan and Turkey, and over a third in Tunisia. These taxes, which are levied over and above general taxation, are not supported by international organisations such as the IMF, World Bank and OECD, which support revenue raising through broad-based general taxation.[3] The excise taxes may be distortionary and lead to higher prices that constrain growth in connectivity. In Turkey, taxes and fees account for nearly 6% of the income for the poorest 20% of the population.

The cost of a handset often represents the biggest cost barrier for the poorest sectors of the population, which often prevents people from consuming mobile services all together. Therefore, taxes and fees on handsets, such as the import duty on handsets in Tunisia and the special consumption tax of 25% in Turkey, may limit growth in mobile penetration and reduce the large benefits of mobile services.[4]

Reducing taxes and fees may lead to a reduction in the price of mobile devices and services, improving affordability and connectivity. For example, in Jordan it was estimated that reducing the Special Tax to 12% on mobile services would have the potential to generate 570,000 new connections. These have the potential to drive higher economic growth.

Figure 4: Impacts in 2020 of reducing the special tax on mobile services to 12% in Jordan, relative to no tax change (analysis undertaken in 2015)



[3] Bird and Zolt (2003) "Introduction to Tax Policy Design and Development" for a course on Practical Issues of Tax Policy in Developing Countries, World Bank, April 28-May 1, 2003
[4] Taxes and fees on the mobile sector, Principles, best practice and options for reform, Deloitte/GSMA, Forthcoming

Source: Deloitte/GSMA (2015); Digital inclusion and mobile sector taxation in Jordan

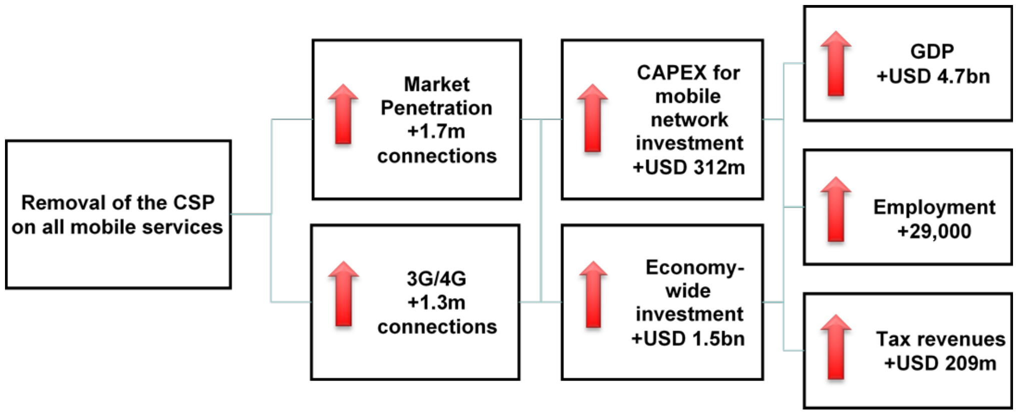
Investment

Taxes and fees, particularly regulatory and revenue fees such as the revenue fees in Turkey and Jordan which account for nearly 17% and 11% of revenue, may lead to a reduction in investment. Taxes and fees applied on gross revenues directly reduce the profitability of all operators, independent of their level of investment. These fees are inefficient for the government as they may lead to lower market volumes and higher prices than a revenue equivalent tax on profits.[5] The seven MENA countries levy several regulatory fees on revenue as well as other regulatory fees.

A large number of fees may increase tax complexity, potentially increase operator's costs and raise uncertainty, which could have large impacts on investment due to the long payback period. Reducing taxes and fees can lead to increases in investment, improving network quality and coverage.

For example, in Saudi Arabia it was estimated that removing the Communications Services Provision (CSP) tax would have the potential to increase CAPEX by US$ 312 million.[6] Based on evidence on the costs of new sites and site upgrades, this may represent about 2,000 new base stations or upgrading 10,000 sites to mobile broadband.[7]

Figure 5: Impacts in 2020 of removing the CSP on all mobile services relative to no tax change (analysis undertaken in 2014)



Source: Deloitte/GSMA (2014); Economic Analysis of mobile sector taxation in the Kingdom of Saudi Arabia. Note that this report was not published.

Licence extension

Longer licence terms and transparent renewal processes for spectrum licences may have benefits for operators, by providing greater certainty about future operations. This in turn can create benefits for consumers, as the business environment may be more conducive to network investment. In Europe, there appears to be a trend towards longer licence durations, with the

[5] Taxes and fees on the mobile sector, Principles, best practice and options for reform, Deloitte/GSMA, Forthcoming
[6] Deloitte/GSMA (2014); Economic Analysis of mobile sector taxation in the Kingdom of Saudi Arabia. Note that this report was not published.
[7] Site cost and upgrade assumptions are based on a review of evidence, as presented in: Analysys Mason (2011), Demand and supply options available for mobile backhaul; Analysys Mason (2011), The momentum behind LTE

European Commission recently recommending minimum licence terms of 25 years. Regulators in MENA may be able to drive benefits by adopting a similar approach.

For existing spectrum licences, regulators may be able to generate benefits by extending licence terms ahead of the licence expiry dates. Doing so would reduce operators' annual amortisation costs and lead to higher EBIT margins, with potential benefits for the government and for consumers:

- Increased corporation tax payments as a result of higher EBIT margins.
- Improved incentives for network investment and investment in new spectrum licences, leading to improved network coverage and quality.
- Increased scope for price reductions, improving affordability.

Illustrative example: Impact of licence extension

An operator holds a 20-year licence, originally valued at US$ 1 billion. When there are 15 years of the licence term remaining, the licence is extended by 10 years, so it then expires in 25 years' time.
The longer remaining licence term reduces annual amortisation costs:

	Original licence			After extension	
Value	Duration (years)	Annual amortisation	Amortisation balance after 5 years	Years left after extension	New annual amortisation
USD 1 billion	20	USD 50 million	USD 750 million	25 years	USD 30 million

As amortisation costs are US$ 20 million lower, EBIT increases by this amount, which contributes to higher corporation tax collection.* Therefore, the extension may have direct benefits for governments, as well as potential benefits for operators and consumers.

Change in EBIT	USD 20million
Corporation tax rate	20%
Change in annual tax revenue	**USD 6 million**

*The analysis assumes the licence is extended at no cost and the operator makes a positive taxable profit.

In Saudi Arabia licences were unified (i.e. operators can provide fixed, mobile and internet services) and extended by 15 Hiriji years[8] to 2047. The extension has reduced one operator's annual amortisation costs by around US$ 115 million.[9] Licence extensions of five years, at no cost to operators, have been observed in Palestine and Algeria, while there is limited visibility of licence extension processes and fees in some other MENA countries.

[8] Hiriji years are based on the Islamic lunar calendar and only contain 360 days
[9] Zain (2016); Zain Saudi Arabia mobile operating licence extended for additional 15 years by Kingdom's CITC

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