



EGYPT TOMORROW SEMINARS SERIES

Regulatory Frameworks for New Business Models

CAIRO - MAY 15, 2018



Center for International
Private Enterprise

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ABOUT THE SEMINAR AND EGYPT TOMORROW ECONOMIC FORUM (ETEF)

The seminar, titled “Regulatory Frameworks for New Businesses Models” was held under CIPE’s Egypt Tomorrow Economic Forum (ETEF). Formed in late 2012, ETEF is a forum that consists of a diversified group of Egyptian entrepreneurs (predominately youth), with interest in working towards promoting economic growth and development in Egypt. In early 2013, members of the forum developed an economic vision for Egypt and identified priority areas for improvement in order to realize this vision. Since then, CIPE has been working with ETEF members to further explore and discuss strategic issues related to each of their identified priority areas.

To support the forum, CIPE follows a two-track, complementary approach. The first track involves holding seminars for a limited number of forum participants to discuss specific issues/topics relevant to the ETEF economic vision and priorities identified. These seminars serve as capacity building and knowledge sharing venues to a great extent. The second track entails hosting issue-specific seminars that bring together a wider group of stakeholders – legislators, senior government officials, opinion leaders, business associations’ leadership, media, and academics – to share their expertise and knowledge and engage in a more elaborated and detailed discussion of issues. The latter track contributes to enriching the debate on many important issues and challenges and developing a clearer and more in-depth view and appreciation of these issues to support stakeholders in developing sound economic strategies and policies.

BRIEFING ON THE SEMINAR



On May 15, 2018, the Center for International Private Enterprise (CIPE) hosted a seminar to discuss the new business models that are emerging in the Egyptian market, and explore the requisite legal and regulatory framework that should be put in place to accommodate these new models. The seminar, which was titled “Regulatory Frameworks for New Businesses Models”, was held under CIPE-sponsored Economic Forum “Masr Bokra”. It came on the heels of the passage of a new law that regulated the sharing economy platforms for ground transportation (ride-sharing platforms, commonly referred to as Uber and Careem). The seminar was also held in response to a call by many new ventures, particularly those relying on alternative finance platforms associated with the sharing economy, to educate legislators and raise their awareness about the different nature of these new business models with regards to their financing, and their business valuation methods, which should entail looking beyond their capital or generated profits.

SEMINAR PROCEEDINGS

Lobna Afify, CIPE Program Officer, welcomed the participants and provided background information on the Economic Forum “*Masr Bokra*”. Afify emphasized that equally important “*Masr Bokra*” forum provides a unique opportunity for business leaders, entrepreneurs and other interested individuals to meet, network and share experiences. Afify pointed out that CIPE is partnering with the Egyptian Center for Economic Studies to set up an “*Academy*” for developing a cohort of high-caliber individuals with a good understanding of economic issues in general and the business environment in particular; and the capacity to meaningfully engage in making public policy. The Academy will offer tailored curriculum, including case studies. She concluded by sharing information on the recently held seminar on the role of local administration in promoting investment and enhancing economic development at the local level; and invited the participants to review the seminar’s paper and share their views and suggestions with CIPE.



Dr. Mohamed Abdel-Mottaleb, former Associate Professor of Nano Materials at the Nile University, founder of X-PayTech-Cashless Communities Solutions, and member of “*Masr Bokra*” forum, moderated the discussion. In his opening remarks, Dr. Abdel-Mottaleb pointed out the successes of the “*Masr Bokra*” forum, including informing a number of laws that were recently issued (e.g., the Industrial License Law, Investment Law); and initiating and furthering the discussion on transitioning Egypt to a cashless economy and the establishment of the National Council for Payments. He stressed that the discussions and deliberations held so far by the forum and the retreats did indeed benefit the making of the new laws. Dr. Abdel-Mottaleb argued that the new businesses (e.g., Uber and Careem), are not merely new forms of companies but rather new business models, which have gained traction globally. He noted that Egypt is still grappling with these new models and trying to understand their implications and requirements. He stressed that the difficulty in understanding these new business models stems from the fact that they represent a marked departure from the traditional business thinking that many in Egypt still adhere to. He stated that it is

common to find many individuals who are not able to grasp the idea that while many of these ventures do not necessarily generate profits early on, yet that are successful in raising capital (even while losing millions of dollars). He underscored that need for a paradigm shift—a new thinking regarding new business ventures, particularly start-ups—to better understand these new models. He explained that, in Egypt, the prevailing thinking for the past 30-40 years, was that a business venture that did not generate enough revenues or profits should be shut down. He stressed that such a thinking is not shared in other parts of the world, where a company is not expected to cover its expenses in the first three years of operations or make profit in the first five years; but rather it is expected to raise more capital and expand. He concluded by saying that in discussing new business models, it is important to explore the different financing methods; examine the financial risks associated with these business models, which he views as more significant than the legal ones, as investors stand to lose their money; and look into issues related to regulating these ventures, and trading their shares in the stock market.



Dr. Mohsen Adel, the Vice Chairman of the Egyptian Stock Exchange, was the first speaker. He reiterated that the question whether existing legal and regulatory frameworks and organizational structures can accommodate the new business model—the sharing economy—is not only relevant in Egypt, but also across the world. He stressed that the sharing economy is creating a new reality, which is still evolving—a new reality in the making. As far as Egypt is concerned, he asserted that the short answer to the question is no. He added that the reality on the ground confirms that the sharing economy is developing at a very fast pace, and at the same time, it is being shaped, to a great extent, by all the existing anomalies and deformities in the Egyptian economy. On a more of a general note, Dr. Adel provided some context for the emergence of the sharing economy worldwide, highlighting that, in part, practices of centralized decision-making called for a move towards economic liberalization and reinventing or restructuring the economic growth model world-wide. This in his view led to the emergence of new business models (e.g., Uber, Careem, Airbnb) and alternative finance platforms and cryptocurrencies (e.g., Bitcoin). He added that



the new reality of sharing economy, and its fast-paced evolution have raised critical issues related to its funding sources and regulation. He stressed that the legal status of these new platforms varies substantially from country to country, with some countries working on developing regulatory frameworks to ensure appropriate oversight of these platforms. With regards to funding sources, Dr. Adel noted that there are mixed on alternative finance platforms, the main source of finance for the sharing economy. While many in the capital market welcome these platforms, yet they also view them with some trepidation. He went on to elaborate on how the alternative finance platforms operate; explaining that these platforms serve as intermediaries between entrepreneurs, who present their ideas on the platform, and anonymous funders. He added that on some platforms, it is most likely that investors do not become shareholders, but rather the platform itself holds the shares. However, on other platforms, potential investors are known, and the presented ideas are more developed and supported by a feasibility study, in this instance, investors become direct, individual shareholders in the ventures. He noted that generally speaking these ventures are not listed on the stock exchange and are not subject to disclosure requirements. He explained that this raises a variety of significant issues that need to be well considered when developing a regulatory framework to accommodate the new sharing economy, especially that the organizational structures in Egypt are not adequately developed, and did not keep pace with the fast-evolving sharing economy. Dr. Adel shared with the participants a first-hand account of the problems arising from the very nature of these ventures, which, in his view, pose regulation challenges. He stated that during the discussions of the draft law on the ride-sharing services, housing the servers in Egypt became one of the most critical problems facing the regulators, which, in his view, should not have been the case; the focus should have been on how can one make best use of the data. Given the Egyptian context, he alerted that creating a new regulatory framework to govern these new businesses will likely lead to two problematic outcomes: increasing the burden on an already struggling administrative structures that will find it difficult to deal with



challenges associated with these new ventures; and 2) some ventures will start to operate completely outside this regulatory system. These outcomes are highly relevant given the existing anomalies in the Egyptian economy, particularly the expansive informal sector; and the tendency to overregulate and not provide enough incentives to businesses (the draft law on food carts and street vendors is a case in point). He added that one of the major challenges facing regulators is the ability to think strategically, identify the purpose and goal of the regulation, and come up with new and creative responses to the challenges at hand. In other words, regulators need to be clear whether they want to correct or adjust an existing situation, or to realize a long-term vision for the economy, the latter, in his view, should be at the heart of the regulatory approach. To elaborate on his point, he gave an example of the Bitcoin phenomena, noting that while some view the Bitcoin as revolutionary, breaking away from the control of the central banks over monetary policy, others view it as a bubble mirroring the dot-com bubble of 2001. In this regard, the issue becomes do we need to regulate the Bitcoin or develop a long-term vision regarding it. On creating funding sources for these ventures, Dr. Adel stated that legitimate funding sources did not keep up with the evolution of the sharing economy; and bureaucracy and cumbersome requirements continue to rule (e.g., the requirements of the LE 2 billion SME Initiative). In his opinion, the question then becomes: How can we develop funding sources for these business models that align with their non-traditional and innovative nature, and also take into consideration the fact that they are not part of the formal economy. Thus, in asking “what is the most appropriate regulatory framework to accommodate the growing sharing economy?” regulators must take into consideration the following elements: 1) changes in global economic thinking; 2) the need to revitalize the economy (noting that informal sector represents a fundamental component of the economic structure in Egypt, and that it significantly contributes to economic output and employment); and 3) what funding sources will be made available for these ventures. Dr. Adel raised another key concern related to making new laws and regulations: building awareness of these new laws, and ensuring that they are

widely disseminated. In this regard, he noted that while the recent Companies Law and Bankruptcy Law addressed many of the key areas of concern, and brought positive changes, yet many stakeholders are not aware of these changes. Finally, he pointed out to the recent amendment of the Capital Markets Law, which aimed at invigorating the Egyptian Exchange by addressing existing deficiencies in the law, and introducing futures trading and a commodities exchange (among other changes). He noted that while the set of economic laws that were recently issued are well coordinated, complement one another, and are to some extent flexible, yet, they remain more or less a conventional response to existing traditional problems; regulating the sharing economy goes beyond this, it requires an innovative approach to the many issues associated with these non-traditional and unregulated activities (e.g., cryptocurrency mining, other forms of Uber-like, ride-sharing services, etc.). Dr. Adel wrapped up his remarks by reiterating the two crucial elements that need to be central to any discussion of regulating the sharing economy: providing alternative financing mechanisms, and ensuring adequate oversight and monitoring of these mechanisms; and reorganizing the structures of the Egyptian economy.



In his remarks, **Mr. Sherif Hefni**, Co-Founder and Partner of Levari LLP, a Cairo-based international law firm, focused on underscoring the difference between legal theory and practice: best laws when applied in practice might not work. In his view, the recently passed economic laws while great in theory, are not so great in practice. To elaborate on his argument, he noted that while the introduction of the shareholder agreements in the recently amended Companies Law is good in theory (these agreements are the core documents that protect investors, entrepreneurs, start-ups, medium-sized businesses looking for finance), yet, in practice they are not. The ministerial regulations which introduced the concept of shareholder agreements only stipulated that these agreements are now accepted under the law (they are to be ratified by shareholder resolutions), however, the regulations fell short of specifically addressing key issues related to how these agreements should work in practice. The regulations did not cover critical issues such as

the protection for minority shareholders, the extent to which rights of investors will apply, and the resolution of legal disputes. Contrasting the “regulatory approach” in Egypt with that in other countries, Mr. Hefni stated that for example, in the United Kingdom the simple rule underlying the regulatory approach is that everything is allowed unless it causes a problem. Describing it as an evolutionary approach to law, he explained that the idea is that parties can agree to whatever they want to agree to, if a problem arises, it is sorted out, if the problem becomes a bigger problem (e.g., involving national security or public policy), at this point the law can be changed to address the problem. He noted that he had witnessed massive changes in Egypt since 2011, the most interesting, in his view, is the development of the private sector, which he said has the ability to do whatever it wants to do regardless of the law. In this regard, he lamented the practice of massive offshoring, which he described as a standard market practice. He explained that, frustrated with the local laws and restrictions, Egyptian investors began establishing offshore companies (in Cayman Islands, Mauritius and BVI), whereby the holding companies and all related agreements are located abroad, while all activities and operations take place in Egypt.



Mr. Hefni described this practice as “shameful”, particularly when it comes to business valuation, as it is the offshore holding company that is valued, while in reality, everything about the company is Egyptian—the entrepreneurs, the leadership, the operations. He added that this offshoring practice stems from the fact that the laws in Egypt do not go far enough to protect the investors, which attests to the distinction between legal theory and legal practice. While Mr. Hefni acknowledged that the government’s response to the issue of ride-sharing services was good, in the sense that it actively listened and developed a law to regulate it, yet he pointed out to an area in the law that is particularly problematic, namely, requiring up to LE 30 million for issuing a license. In his view this requirement is going too far with the regulation; and is detrimental to the ride-sharing start-ups, practically destroying the ride-sharing market and pushing people away from the formal sector to the informal sector. In the same vein, he views the government’s approach



to handling the data control concerns related to ride-sharing services as inadequate. While he acknowledges that the government's concerns over data security were legitimate, yet, the regulators fell short in providing investors with the regulation or support needed to facilitate their meeting these concerns. Thus, Hefni placed understanding the private sector in general, and the commercial aspects of the industry to be regulated in particular as an important matter governments should attend to when creating laws. Addressing the issue of financial risks, Hefni stressed that valuation of companies, especially SMEs, is very difficult in Egypt, noting that valuation of technology-based companies is still immature in the Egyptian context due to the lack of a fully developed grasp of the issues, and also because the existing laws do not facilitate it. He echoed Dr. Adel's concern regarding the cumbersome requirements faced by SMEs in seeking financing from banks. In his view, providing investors (domestic and foreign) with more protection should help in addressing the SME finance problem. Mr. Hefni pointed to an issue which he finds frequently overlooked in many business valuation discussions, namely the rights that comes with the shares (ordinary and not preference shares). This is particularly relevant in Egypt now that the Companies Law recognizes shareholders' agreements. For example, under some scenario an investor with 10 percent of the company could have the right to three board seats, while an investor with 90 percent of the company could have the right to one board seat; this right (of the 10 percent shareholder), he noted, translates into more value, and in turn increases the value of these shares. This issue, he said, is not very well appreciated or understood in the Egyptian market. He added that the issue of offshoring becomes more pronounced when it comes time for these companies to expand and go public, which in his experience takes from one to two years to get a company ready for its initial public offerings (IPOs). Mr. Hefni explained that this offshoring practice represents a missed opportunity for the Egyptian stock market and the Egyptian economy as a whole, as these companies list in the stock exchanges in Amsterdam, London or New York, where they gain valuation and an increase in the market

outside Egypt, while their operations are fully located in Egypt. In an effort to correct this situation he called for taking steps to change this situation by developing professional business valuers who are qualified and experienced, and at the same time, working on changing the current practice of offshoring by providing better conditions and protection for investors. Finally, Mr. Hefni underscored the importance of taking advantage of a recently introduced investment incentive that allows investors to leverage their investments against personal income tax. This incentive of providing tax benefits for business investment can provide tremendous benefits to the economy by incentivizing wealthy Egyptians to invest rather than hold their wealth in banks.

Before opening the floor for questions, the moderator, Dr. Abdel Mottelb highlighted two observations which he views as critical to the discussion. First, he noted that generally speaking, the overarching approach or underlying philosophy governing the making of laws in Egypt is restrictive rather than being permissive. Second, while acknowledging that the recently issued economic laws do indeed reflect a degree of harmonization, yet he alerted to an article in the Companies Law which denies any individual who was declared bankrupt by a court order to hold a board seat. This, in his view, is inconsistent with the efforts reflected in the Bankruptcy Law that attempt to destigmatize and decriminalize bankruptcy. On a different note, he shared with the audience an interesting concept he was exposed to while attending the recently held Vested Summit, held in Al Gouna on May 11-12, 2018. He explained that the idea, which is advanced by the Peace Innovation Lab of Stanford University, could be summed up as “The easiest way to achieve peace worldwide is through doing business”. Creating value for people to work together translates into creating lasting peace, which will last beyond the lifetime of laws and regulations.

According to this concept, entrepreneurs become peace emissaries, who through promoting investments and entrepreneurship establish lasting peace. Finally, Dr. Abdel Mottelb attempted to unpack the sharing economy term, and drew attention to the difference between the term sharing economy, which entails sharing one’s assets, and the term the “Share Economy” which entails giving access to one’s assets, in other words, giving others a share in these assets, rather than lending it to them. He added that the term Share Economy however, has gained popularity as it is more attractive as it embodies positive values.

KEY POINTS AND THEMES FROM THE FLOOR DISCUSSION

Following the presentations, the floor was opened for discussion, participant raised some questions and issues arising out of the presentations. Following are the most salient issues raised by the participants and the responses from the panel:

- Issues highlighted by participants during the floor discussion included the need for undertaking regulatory impact analyses (RIA) to critically assess the positive and negative effects of proposed regulations; the importance of meaningfully conferring, and directly engaging with the informal sector when attempting to support it, and integrate it in the formal economy; the lack of harmony between the recently issued economic laws; the lack of integration between ministries working in the economic sphere; and the poor enforcement of laws and regulations (such as that interest rates on loans offered to SMEs would not exceed 5 percent), and court rulings.



- One participants noted that small entrepreneurs providing their services on line (such as graphic designers) face much difficulty in opening bank accounts, and thus are unable to receive transfers from abroad for the services delivered. In general banks do not welcome dealing with small entrepreneurs. At the same time, the Central Bank also places restrictions on transferring monies through the mobile for on legal persons.
- Dr. Adel responded to an inquiry about what it takes to realize the change in mindset that he referred to in his remarks. He stated that Egypt has more than 18,000 laws, regulations and directives regulating the economy, and many of these laws are antiquated dating back to the 1800's. The change in mindset, he explained, can happen through: realizing and acknowledging existing problems;

coordination; developing a good grasp of the changes that are taking place around the world; and being future-oriented and looking at regulations through the lens of realizing a longer-term vision rather than through the lens of control and centralization. In this regard, he cited the Indian government's audacious experiment with shaking up the economy by adopting a decision of removing two of its largest bills from circulation (a controversial decision), and undertaking a massive initiative to provide bank accounts for the poor, reaching 240 million citizens in one year. Dr. Adel also cautioned against the current practice of setting up parallel systems through issuing laws and regulations, as an alternative to holistically resolving deep-seated structural problems. That said, he acknowledged that this practice is still ongoing, and expected to continue for a while, which creates more problems that will need addressing. On thinking outside the box, he suggested that serious consideration should be given to the idea of taking advantage of nation-wide presence of the Egyptian postal system facilities and engaging them in providing loans to the poor.



- Mr. Hefni addressed a question regarding the likelihood of Egypt adopting the principle of “everything is allowed unless it causes a problem”, which he referred to in his remarks, and whether the current political and security context in Egypt can permit this. He explained that while political and economic conditions should be taken into consideration, it is important to differentiate between progress and fear. He noted that all countries face political, economic and security challenges, but a regulatory approach that is driven by fear and the desire to control is not the answer. He noted that freedom to contract, the essence of contract law, is being undermined in Egypt by over regulation, driven by the desire to control. He agreed with Dr. Adel that a change in mindset is what is much needed; and went on to explain that this change can be achieved, over the long term, by stepping away from fear and the



desire to control; and focusing on finding ways to resolve long-term problems and assuming the role of an enabler and supporter. He concluded by saying that while the recently issued ride-sharing law responds to short term issues, yet, it will not be adequate for the long term, as the industry is still evolving. He contrasted this approach to regulation with the approach taken by the UK government in response to the Uber's employment rights issue "gig economy". In the latter case, the government acted as an enabler; and worked with the different parties to develop some regulations, with an eye on meeting future needs, in other words an agile framework, which does not over-regulate the service. On a different note, he acknowledged that are challenges to the rule of law, noting that two key elements, the predictability and enforcement of law, are significantly undermined in Egypt. Using an example of an intellectual property dispute, he explained that in some instances, the injured party would seek a parallel mean of resolution (e.g., through tailored regulations devised by the Cairo Regional Centre for International Commercial Arbitration), as it is sometimes difficult to reach a timely, and fair resolution through the court system. Finally, on the want to change, Dr. Hefni stressed that having a critical mass in power with the desire to change, and having young people in decision-making positions should stimulate the change process.

Lobna Afify concluded the session by acknowledging the contributions of the panelists and participants. She acknowledged the importance of engaging the informal sector in such a discussion, as noted, adding that CIPE will share the proceedings of this seminar with the participants, and invited everyone to share any ideas or suggestions that should be included in future discussions.



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