Global Private M&A Guide - Limited External Content - Egypt

Quick reference guide

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# Due diligence, pricing and closing

**Typical due diligence issues**

Finalizing due diligence before execution of the acquisition agreement is market practice in Egypt. A due diligence exercise would usually cover corporate structure, licenses and permits, property titles, regulatory, tax, labor and social security compliance, material contracts, change of control provisions, material IP and IT, litigation and environmental matters.

Typically, issues highlighted during the diligence process are dealt with as matters to be rectified by the seller as a condition precedent to closing, by a purchase price reduction, by indemnities given by the seller or by putting in place escrow arrangements or deferred payment mechanisms.

**Pricing and payment**

The Financial Regulatory Authority (FRA) requires that the purchase price of shares, for both listed and unlisted shares of a joint stock company (the most commonly used business vehicle in Egypt), is deposited in an Egyptian bank if the transaction: (i) exceeds EGP 100,000; or (ii) the seller and/or the buyer is a non-Egyptian entity, or a foreigner.

Payment must be effected through the Egyptian Exchange (EGX), using a broker licensed by the FRA. The EGX accept either of the following two mechanisms for settlement of the purchase price:

The purchase price is deposited in the broker's Egyptian bank account. The broker then transfers the purchase price to the seller's bank account once the share transfer has taken place through the EGX.

The purchase price is deposited in the seller's Egyptian bank account directly. The FRA regulations allow for this mechanism if the purchase price is deposited within one month, at most, before submitting a request for the share transfer, provided that the respective bank issues a certificate addressed to the EGX and the FRA confirming receipt of the purchase price, and its use being solely to fund the acquisition of the underlying shares.

An escrow bank mechanism will also be acceptable, provided that the purchase price is deposited in an Egyptian bank account. There are some exemptions to the cash deposit requirement, for example, this requirement does not apply to a transfer of shares between ancestors and descendants, or between a company and its subsidiaries for restructuring purposes. In any event, such exemptions from paying the purchase price must be approved by the FRA.

**Signing/closing**

**Share sale**

Any transfer of unlisted shares in an Egyptian joint stock company (the most commonly used business vehicle in Egypt) must take place before the EGX through a licensed broker, and the transfer of title to the shares is evidenced by the EGX transfer certificates when such shares are not deposited/registered with Misr for Central Clearing, Depository and Registry (MCDR). However, if the shares being transferred are registered with the MCDR, the legal document evidencing completion of transfer of title is the custodian statement. Now, it is required by law that all shares of joint stock companies be registered with the MCDR. Usually, the seller and the buyer appoint the same broker to execute the transaction before the EGX. It is possible for each party to appoint its own broker, but this will require extra cost.

The process of transferring title to unlisted shares of a joint stock company involves several procedures, including:

A codification process (i.e., creating a unified EGX code for the trading parties (seller(s) and buyer(s)), to the extent such codification is not already created at any point prior to the sale.

A share trading process, which includes preparing and submitting a set of documents by the seller, the buyer as well as the target company. The EGX usually takes three business days to review the transaction file and request any further documents. The pricing committee within the EGX would need to review the transaction's file and approve it in specific cases, including if a transaction's or a group of related transactions' purchase price is equal to or exceeds EGP 20 million.

The EGX usually issues the share transfer certificates proving the transfer of the sold shares to the buyer on the same day of execution. However, if the shares being transferred are registered with the MCDR, the transaction goes through the MCDR following its execution at EGX.

Certain aspects of the process described above could in practice change from time to time based on internal circulars or policies of the relevant regulators (e.g., the FRA or the EGX) that are not necessarily publicly available.

**Asset sale**

There is no specific legal framework regulating asset sale deals in Egypt. The transfer of title of the relevant business assets is done though separate instruments, depending on the relevant asset class, to cover the transferred business components (such as the sale of real property, assignment or contract amendment, licenses and permits amendments or transfers, etc.). It is common, though, for the parties to enter into a master asset sale agreement, or a business transfer agreement, in order to regulate the overall sale process and set out the commercial terms and protection package negotiated by the parties. The approach to the due diligence exercise would naturally differ when the underlying structure of the transaction is intended to be implemented through an asset sale, to identify the legal means through which each selected asset will be transferred (e.g., the selected assets need to be capable of being assignable or transferred pursuant to their underlying agreements or ownership documents).

Asset sale deals are commonly seen where there is a restructuring, business carve-outs or carve-ins or splitting of business units. Completion of an asset transfer is often a time consuming process, depending on the relevant classes of assets being transferred, but this is particularly the case with regard to the transfer of employees and the sale of real property (due to the property registration process through the notary public).

# Approvals/registrations

**Foreign investment restrictions**

Generally, there are no foreign investment restrictions in Egypt. In 2017, substantial reforms were introduced to create a new Investment Law, aimed at attracting new investments to Egypt by providing additional incentives and guarantees, removing the existing impediments for foreign and domestic investment, protecting investors from bureaucracy and corruption, and streamlining the procedure for establishing projects and obtaining licenses. However, some industries or sectors may require minimum percentages of Egyptian shareholding or participation, such as carrying out commercial agency activities and security activities. As a general rule, a foreign investor must apply for a security clearance as part of the procedure for investing in Egypt or setting up a company. This clearance includes the submission of a specific form covering the required personal and business-related information. Submission of the form in itself does not hinder the investment in Egypt, except for certain nationalities where the security authorities do not allow for investment before clearance has been obtained. In addition, investment, conducting business, ownership of real estate properties in Sinai by foreigners has some security-related restrictions whereby the prior approval of the Sinai Development Authority is required.

Otherwise, there are generally no issues with foreign investment in Egypt. The Investment Law grants foreign investors the same treatment as Egyptian investors in a manner incentivizing investment. Examples of incentives granted by the Investment Law include: (i) granting investors the right to set up and operate their businesses in foreign currencies transferred from abroad without restrictions; (ii) permitting foreign investors to freely dispose of their assets, liquidate their projects and convert proceeds in local currency into foreign currency through registered banks without restrictions; and (iii) investment projects also have the right to export their products without a license or being registered in the Register of Exporters.

**Antitrust/merger control**

Egypt has, technically, introduced a mandatory suspensory pre-merger control regime. However, while the legal requirement is there, according to the Egyptian Competition Authority (ECA), there is currently no need to notify transactions because the Executive Regulation was not issued, which, according to the ECA, will enable the ECA to implement the merger control regime.

However, given that the Executive Regulation could come into force with little warning, we recommend obtaining legal advice on any transaction which may meet the prescribed notification thresholds.

For further information, see the more detailed section on "Antitrust/merger control".

**Other regulatory or government approvals**

Generally, there are no other specific approvals required. However, depending on the sector of business, certain approvals may be required from certain governmental bodies. For example, certain approvals of the Ministry of Health are required for transactions in the health sector, and certain approvals may be required from the Central Bank of Egypt, or the FRA for transactions in the banking sector and the FRA for the non-banking financial sector. For the pharmaceuticals and med-tech manufacturing sectors, the pre-approval of the Egyptian Drug Authority is also required.

# Employment

Egyptian labor law is largely employee-biased and designed to protect employees. The most common employment issues relevant to M&A transactions in Egypt are layoffs or employee transfers following an acquisition.

For employees who are laid off, the acquiring entity, as a market practice, compensates them with severance packages equivalent to that of unjustified termination of employees, which may amount to two months per year of service (for unlimited-term employment contracts), and a salary equivalent to the remaining period for limited-term contracts in addition to the termination notice period.

Further, the Egyptian Labor Law regulates redundancy of employees for economic reasons. This can be relevant to entities prior to or post M&A transactions. However, in practice, redundancy is a lengthy process and, historically, the respective authority has not granted any approvals for redundancy. Therefore, market practice is to agree amicably with the employees on exits.

# Tax

Tax in Egypt strongly depends on practice. The following tax regulations have been introduced, which may affect M&A transactions.

**Value-added tax (VAT)**

VAT applies to the supply of goods and services, at a standard rate of 14%. There are other rates for some certain goods and services, in addition to some exemptions. All companies are required to prepare and file a monthly VAT return with the relevant Egyptian tax authorities.

**Capital Gain Tax**

Capital gains realized by a resident/non-resident person due to the disposal of or the sale of unlisted shares will be subject to a capital gains tax at the rate of 22.5%. The capital gain is the difference between the sale price and the ownership cost of the share. The ownership cost may be determined based on different references, including the book, nominal and fair market value depending on the tax analysis/assessment given by the tax advisor.

Capital gains realized by a resident/non-resident person due to the disposal of, or the sale of, listed shares will be subject to a capital gains tax at the rate of 10%.

**Stamp duty tax**

A "Stamp Tax/Duty" regime applies to the total value of trading in securities (i.e., Egyptian or foreign securities, listed or unlisted), excluding public treasury bills and bonds, without any deductions regarding expenses.

Stamp duty taxes are as follows:

0.05% on the resident buyer, and another 0.05% on the resident seller

0.125% on the non-resident buyer and another 0.125% on the non-resident seller.

Stamp tax increases to 0.3% when the transaction is a sale or acquisition of 33% or more of the: (i) shares; (ii) voting rights; or (iii) assets & liabilities of a resident company, in return for shares in another resident company.

If multiple transactions conducted by one legal person related to a company exceed this 33% limit during the two years following the first transaction, the seller and buyer are subject to a 0.3% rate on the total amount of the transactions, with the right to offset any stamp duty already paid on the transactions (0.125% or 0.05%, as referred to above).

**OECD's Two Pillar Solution**

The OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting has put forward a so-called Two-Pillar Solution to address the tax challenges arising from the digitalization of the economy. Pillar Two is intended to introduce a global minimum effective rate of tax of 15% for large businesses in each jurisdiction where they operate and will lead to fundamental changes in the international tax system. It is currently being implemented in a large number of jurisdictions.

Groups will need to consider how the Pillar Two rules could impact on the life cycle of M&A transactions from the pre-acquisition phase (including transaction planning (such as the choice of acquisition structure and financing) and due diligence of the target group), the acquisition phase (such as contractual risk allocation around Pillar Two) to the post-acquisition phase and the impact of Pillar Two on any post-acquisition integration.

# Post-acquisition integration

For information on post-acquisition integration matters, please see our [Post-acquisition Integration Handbook](https://www.bakermckenzie.com/en/insight/publications/resources/post-acquisition-integration-2023).

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