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Afghan Taxes: Amnesty Program Deadline Creates Urgency for Contractors to Address Longstanding Legal Questions

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The Afghan Ministry of Finance (MoF) has for years sought to impose income taxes, customs duties, or similar charges on all U.S. Government (USG) contractors operating in Afghanistan. Many contractors have avoided paying their tax bills (or even dealing with the MoF) due to ambiguity about their legality and reimbursability under USG contracts, resulting in a build-up of assessed back taxes and penalties. Recently, the Afghan MoF has offered an amnesty program that substantially lessens penalties for contractors willing to pay their outstanding tax bills. Many contractors are now facing an immediate decision as to whether it is time to finally address these legal questions.

For years, the USG and the Afghan government disagreed over the taxation of USG contractors. The Afghan government initially sought to impose taxes on all USG contractors, whether acting as primes or subs. Over time, USG agencies succeeded in entering into bilateral agreements with the Afghan government to provide tax exempt status for certain classes of contractors. This ad hoc approach added to



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the confusion over the applicability of MoF taxes.

The Department of Defense (DoD) early on entered into a Military Technical Agreement (MTA) between the International Security Assistance Force and the Interim Administration of Afghanistan and the NATO-Afghanistan Status of Forces Agreement (SOFA). DoD took the position that the MTA granted tax exempt status for all contractors and subcontractors, but the Afghan government took a narrower reading. Then, in 2014, DoD and the Afghan government entered into a Bilateral Security Agreement (BSA) providing clear income tax exemptions for USG DoD contractors, subcontractors, and their employees that are not resident in Afghanistan.¹ The Afghan government initially took—but then somewhat retreated from—the position that the BSA does not cover tax liability for years prior to 2015 or most subcontractors.

The U.S. Agency for International Development (USAID) obtained a tax exemption from the MoF for its Strategic Objective Grants Agreements (SOAGs). The Department of State's Bureau of International Narcotics and Law Enforcement (INL) had yet another agreement with limited effect. Other agencies lacked any agreement to exempt contractors from taxation at all.

In July 2018, the USG and Afghan governments executed a new agreement to address tax exemptions for USG awards related to economic, technical, and humanitarian assistance.² In effect, this new agreement fills certain gaps in the tax exemption apparatus. The scope of the agreement applies to activities from June 1, 2018 onward no matter when the assistance was initially furnished by the USG.

This disjointed approach has permitted the Afghan government to apply taxes inconsistently to USG contractors and subcontractors based on which agency awarded the contract, the scope and terms of the contract, and the time period for performance. Not knowing how to deal with the tax bills they receive, many contractors have simply avoided the issue for years—putting them at risk for revoked business licenses, restrictions on importation of goods and suppliers, frozen local bank accounts, personnel movements, and even the arrest of contractor personnel.

For some time, the Afghan MoF has offered a tax penalty amnesty program for USG contractors to pay back taxes and minimize penalties. The program permits qualifying contractors who have not yet filed income tax forms between 2002-2017 to file and pay in full overdue tax liability and only remit 5% of assessed tax penalties, relieving them of the other 95% of tax penalties. The deadline for taking advantage of the program is **December 20, 2018**. There is little possibility that this deadline will be further extended.

In deciding whether to take advantage of the amnesty program, contractors are also considering whether their USG customers will reimburse them for the tax payments. This question requires contractors to study their particular circumstances.

In December 2015, DoD issued a [final rule](#) stating that the BSA exempts contractors and subcontractors from Afghan taxes, so any such payments are not reimbursable.³ However, it is not so clear that taxes and penalties periods prior to the BSA will not be reimbursed. Contracting officers from DoD and other Federal agencies have of-

ten looked to the particular circumstances—which agency is involved, the period involved, the type of contract at issue, and the terms and conditions of that contract—to determine whether to reimburse payments for Afghan taxes and penalties.

As an example, most contracts and sub-contracts—including DoD contracts prior to the December 2015 final rule—were silent on the issue of Afghan taxes. Yet standard Federal Acquisition Regulation (FAR) clauses can come into play. Under FAR 52.229-8, contractors operating under cost-reimbursement contracts in foreign countries may be able to recover taxes as allowable operating costs. Contractors op-

erating under fixed-price contracts may be able to claim reimbursement for both taxes and penalties under FAR 52.229-6 if the contracting officer agrees to treat the Afghan taxes and penalties as “after-imposed” and not incurred through contractor’s fault, negligence, or failure to follow instructions of the contracting officer.

Nichols Liu is a U.S. law firm specialized in serving government contractors. Our team includes experienced claims attorneys and a former Defense Contract Audit Agency (DCAA) auditor and has an exclusive arrangement with a leading accounting firm that specializes in Afghan taxes.

¹ MOF Memorandum, “Tax exemption ruling of the attached companies proposed by the Ministry of Finance, Resolute Support (RS), and the Embassy of United States of America,” <https://www.ahg.af/wp-content/uploads/2015/04/Redacted-MOF-Group-Tax-Exemption-Ruling-English.pdf>.

² Agreement Between the Government of the United States of American and the Government of the Islamic Republic of Afghanistan Regarding the Provision of Tax Exemptions for Assistance, <https://www.ahg.af/wp-content/uploads/2018/09/USA-AFG-Tax-Agreement-27-July-2018.pdf>.

³ DoD Final Rule, <https://www.gpo.gov/fdsys/pkg/FR-2015-12-30/pdf/2015-32870.pdf>.

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