

GRAPPLING WITH TAX EXEMPTIONS UNDER FOREIGN ASSISTANCE CONTRACTS, GRANTS, AND COOPERATIVE AGREEMENTS

*Andrew Victor & Samuel Jack**

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I. INTRODUCTION

When the U.S. Government provides foreign assistance to developing countries, it is typically with the condition that the assistance be exempt from local taxes.¹ In turn, the U.S. Government expects organizations that perform foreign assistance contracts, grants, and cooperative agreements to invoke these exemptions.² As discussed in this article, this policy is designed to maximize the effectiveness of U.S. foreign aid, but it can pose implementation challenges for the U.S. Government and firms performing foreign assistance awards.

1. See U.S. AGENCY FOR INT’L DEV., AUTOMATED DIRECTIVES SYSTEM (ADS) § 349.3.1.1 (2003) [hereinafter USAID ADS].

2. See FAR 52.229-6(i).

** Andrew Victor is an associate with Nichols Liu LLP. Samuel Jack is an attorney with the U.S. Agency for International Development (USAID), Office of the General Counsel. This article was co-authored by Mr. Jack in his personal capacity. The opinions expressed in this article are his own and do not necessarily reflect the views of USAID or the U.S. Government. The authors wish to thank Raphael Metzger, Robert Nichols, Jennifer Norling, and Scott Sheffler for their review of this article and insights.*

Government contractors and grant- or cooperative-agreement recipients that operate abroad enter a web of legal obligations. They must comply not only with U.S. law, such as the Federal Acquisition Regulation (FAR) or the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance), but also with local law.³ U.S. and foreign compliance requirements can intersect when it comes to taxes—specifically, the foreign legal obligation to pay a local tax and the allowability of such payments for reimbursement under the FAR or Uniform Guidance.⁴

Jurisdictions, whether foreign or domestic, can impose a variety of taxes upon contractors and recipients, such as income or sales taxes. Entities working overseas may be assessed customs duties to import supplies into a country and excise taxes, which are paid when a contractor or recipient purchases a specific good, such as gasoline, or engages in a specific activity, such as driving a truck on a highway.⁵ In many countries, firms are required to pay value added tax (VAT) at various points in the supply chain.⁶ Because of the way taxes are levied, a contractor or recipient may find it difficult to recognize that a tax is being paid.

While exemptions may be available, invoking the exception can be challenging. Depending on the country, contractors and recipients may be unable to invoke effectively the tax exemption because of local tax bureaucracies, inconsistent treatment by local vendors, or a general lack of understanding of the scope of the exemption. In these situations, U.S. Government personnel must assess whether the tax exemption was truly “available” and if the tax payment is otherwise allowable.⁷ This decision requires an understanding of federal regulations and the applicable bilateral agreement with the host nation, as well as the functioning of the local tax system.

For contractors and recipients, navigating tax exemptions can be a frustrating, time-consuming process that might not be worth the effort. Some organizations certainly shrug and view paying (and not being reimbursed for) a potentially exempt tax as a cost of doing business.⁸ For others, particularly smaller recipients, the stakes can be higher; payment of taxes for which

3. In addition to contracts, grants, and cooperative agreements, the U.S. Government delivers foreign assistance through a variety of financing mechanisms, direct government assistance, and “other” transactions, all of which are outside the scope of this article.

4. See 2 C.F.R. § 200.470(b)(1) (2019); FAR 31.205-41(a)(1).

5. See Encorp, ASBCA No. 51293, 01-1 BCA ¶ 31,165, at 153,934, 153,936 (noting that Encorp was assessed import duties on construction materials and equipment, and excise taxes on steel bars).

6. See 2 C.F.R. § 200.470(c). See generally Anna Zhang, *Value Added Tax Rates (VAT) by Country*, U.S. COUNCIL FOR INT’L BUS., <https://www.uscib.org/value-added-tax-rates-vat-by-country/> [<https://perma.cc/X6QR-42DY>] (last visited Oct. 31, 2019) (providing examples of VAT rates in many countries).

7. See FAR 29.101(b).

8. Cf. Robert Nichols et al., *Afghan Taxes: Amnesty Program Deadline Creates Urgency for Contractors to Address Longstanding Legal Questions*, 1 PUBKLAW (Dec. 3, 2018), <https://pubkgroup.com/law/afghan-taxes-amnesty-program-deadline-creates-urgency-contractors-address-long-standing-legal-questions> [<https://perma.cc/5662-VXY8>].

there is an exemption may result in a disruptive cost disallowance.⁹ Organizations operating abroad must take the time to understand the tax regimes in the countries in which they are working and make clear-eyed decisions on whether and how to segregate taxes among their expenses.

This article begins with a general discussion of the allowability of tax payments under federal contracts, grants, and cooperative agreements and the relevant case law. It proceeds to describe the kinds of exemptions that exist when performing overseas, how such exemptions are invoked, and practical considerations for determining the allowability of foreign tax payments, notwithstanding the availability of an exemption. It concludes by discussing the contract disputes process and the significantly more complex process for appeals of disallowances under grants and cooperative agreements. While this article focuses on allowability under foreign assistance awards issued by the U.S. Agency for International Development (USAID), it will discuss the government-wide legal requirements and draw upon the practices of other agencies, most notably the Department of Defense (DoD).

II. THE APPLICABLE REGULATIONS

U.S. foreign assistance is primarily delivered through “acquisition” and “assistance” agreements.¹⁰ The government may engage in (1) an “acquisition,” whereby it issues a contract for purposes of obtaining a good or service for its direct benefit, which is governed by the FAR; or (2) “assistance,” whereby the government issues a grant or cooperative agreement (an “assistance agreement”) to effectuate a public benefit, which is governed by the Uniform Guidance.¹¹

Whether operating under “acquisition” or “assistance,” firms can face significant tax burdens in the foreign jurisdiction in which the agreement is performed.¹² Since these costs are incurred in order to perform the award, both the FAR and the Uniform Guidance generally treat foreign tax payments as allowable costs under cost-reimbursement contracts, grants, and cooperative agreements, subject to certain exceptions and nuances, as discussed next.

9. See U.S. AGENCY FOR INT’L DEV., STANDARD PROVISIONS FOR NON-U.S. NONGOVERNMENTAL ORGANIZATIONS: A MANDATORY REFERENCE FOR ADS CHAPTER 303 (ADS 303mab) § RAA10(c) (2019) [hereinafter USAID ADS 303mab] (noting that cost will not be allowable when the recipient fails to obtain an exemption).

10. See U.S. AGENCY FOR INT’L DEV., 2018 PROGRESS REPORT 2 (2018), https://www.usaid.gov/sites/default/files/documents/1868/MOAA_2018ProgressReport_05-28-19-ForPosting.pdf.

11. See Federal Grant and Cooperative Agreement Act of 1977, Pub. L. No. 95-224, §§ 4-6, 92 Stat. 3, 4-5 (1978); 2 C.F.R. § 200.100(b) (2019); FAR 1.101.

12. See, e.g., SPECIAL INSPECTOR GEN. FOR AFG. RECONSTRUCTION, SIGAR AUDIT 13-8, TAXES: AFGHAN GOVERNMENT HAS LEVIED NEARLY A BILLION DOLLARS IN BUSINESS TAXES ON CONTRACTORS SUPPORTING U.S. GOVERNMENT EFFORTS IN AFGHANISTAN 1-3, 6 (2013) [hereinafter SIGAR AUDIT] (explaining the taxes that firms are subject to in Afghanistan, which resulted in the Afghan Government collecting \$921 million from 2008 to 2012).

A. The FAR

There is a deep body of decisional law and interpretive guidance addressing the cost principles in FAR part 31. Principally, these rules allow the government to determine reimbursable costs under cost-reimbursement contracts and cost-reimbursement subcontracts.¹³ The cost principles' tax allowability provision, FAR 31.205-41, provides that federal, state, and local taxes "that are required to be and are paid or accrued in accordance with generally accepted accounting principles ['GAAP']" are allowable costs.¹⁴ Fines and penalties that may be incurred with unpaid taxes, however, are not considered taxes themselves.¹⁵ Jurisdictions levy fines and penalties, such as charging interest on outstanding tax liabilities, for the late or underpayment of taxes, and are considered a different obligation.¹⁶ While FAR 31.205-41 does not specifically discuss the allowability of foreign taxes, foreign taxes are generally treated as analogous to state and local taxes for purposes of allowability under this cost principle.¹⁷

Despite the straightforward premise that taxes are allowable costs—taxes are, arguably, the epitome of "costs of doing business"—the allowability of tax payments is subject to a slew of caveats.¹⁸ Chiefly for purposes of this article, a tax for which the government provides an "exemption" is not an allowable cost under either the FAR or Uniform Guidance because the government expects contractors and recipients to take advantage of any potential reduction in cost.¹⁹ The FAR defines "exemption" for these purposes as "freedom from taxation in whole or in part and includes a tax abatement or reduction resulting from mode of assessment, method of calculation, or otherwise."²⁰ As discussed below, the scope and application of such exemptions can be the source of considerable confusion, particularly overseas.

13. See FAR 31.103(b)(1)(i).

14. FAR 31.205-41(a)(1).

15. See *id.*; see also KAREN MANOS, GOVERNMENT CONTRACTS COSTS & PRICING 607 (3d ed. 2009); Westech Int'l, Inc., ASBCA No. 57296, 11-2 BCA ¶ 34,822, at 171,347 (segregating state taxes from penalties and interest, but holding that all three expenses were allowable because the contracting officer disapproved payment but did not direct the contractor to litigate the legality of the state taxes).

16. See *Lockheed Corp. v. Widnall*, 113 F.3d 1225, 1228 (Fed. Cir. 1997) (discussing allowability of taxes, interest, and penalties, and how the intentional underpayment of taxes can be construed as a form of borrowing or indirect financing by the contractor).

17. See, e.g., DEF. CONTRACT AUDIT AGENCY, FAR 31.205 COST PRINCIPLES, CHAPTER 68 – TAXES 68-17 (2019). Note that the FAR cost principle addresses foreign tax credits that reduce the contractor's U.S. federal income tax. See FAR 31.20541(d).

18. Notably, federal income taxes are not allowable. See 2 C.F.R. § 200.470(b)(1)(iii) (2019); FAR 31.205-41(b)(1). Likewise, "fines and penalties"—such as for failure to pay or late payment of taxes—are not considered "taxes" subject to this cost principle. FAR 31.205-41(a)(1).

19. See 2 C.F.R. § 200.470(b)(1)(i); FAR 31.205-41(b)(3); FAR 52.229-6(i).

20. FAR 31.205-41(b)(3). The purpose of this rule is apparent: the government will not reimburse contractors for taxes that would not be paid in the normal course of business. See generally FAR 31.205-41.

While not the focus of this article, these rules can also be invoked under fixed-price contracts.²¹ With respect to taxes, contractors are required to include all federal, state, and local taxes in the contract price.²² For contracts to be performed overseas, the USAID Acquisition Regulation (AIDAR) allows modification of this clause to specify that the taxes referred to therein are U.S. taxes.²³ Similarly, the standard FAR clause for fixed-price contracts to be performed abroad requires inclusion of all taxes in the contract price.²⁴ Notably, there is no comparable language in the Uniform Guidance, as the vast majority of assistance is delivered on a cost-reimbursement basis.²⁵

B. The Uniform Guidance

For many years, the U.S. Government's rules for grants and cooperative agreements were set forth in a series of Office of Management and Budget (OMB) "Circulars" that addressed particular topics related to financial administration of assistance awards.²⁶ In late 2013, the OMB promulgated the Uniform Guidance to provide a government-wide framework for award management, synthesizing and superseding guidance from the OMB Circulars.²⁷

21. See FAR 31.102 (requiring the use of the FAR part 31 cost principles whenever a fixed-price contract clause requires the determination or negotiation of costs).

22. See FAR 29.401-3(a); FAR 52.229-3(b)(1).

23. AIDAR 752.229-70. The purpose of this rule is to distinguish U.S. taxes, which are considered permissible contract costs, from foreign taxes, which are typically unallowable. See, e.g., Encorp, ASBCA No. 51293, 01-1 BCA ¶ 31,165, at 153,939 (finding the clause expressly precluded Pakistani taxes and thus the contractor was bound).

24. See FAR 52.229-6(c)(1). As with the cost-reimbursement contract clause, it imposes on the contractor the duty to invoke all available tax exemptions, stating:

Unless otherwise provided in this contract, the contract price includes all applicable taxes and duties, except taxes and duties that the Government of the United States and the government of the country concerned have agreed shall not be applicable to expenditures in such country by or on behalf of the United States.

Id.; see FAR 52.229-6(i).

25. See generally 2 C.F.R. §§ 200.0–200.521 (2019).

26. See Scott S. Sheffler, *A Reasoned Case for a "Grant Disputes Act,"* 47 PUB. CONT. L.J. 209, 221–22 (2018).

27. See Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, 79 Fed. Reg. 75,871, 75,872 (Dec. 19, 2014) (to be codified at, *inter alia*, 2 C.F.R. pts. 1, 25, 170, 180 & 200); Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, 78 Fed. Reg. 78,590, 78,590 (Dec. 26, 2013) (to be codified at 2 C.F.R. pts. 200, 215, 220, 225 & 230). The Uniform Guidance is not a regulation *per se* and, technically, not binding on recipients. See 2 C.F.R. §§ 1.105(b), 180.15, 182.15. Instead, agencies were given until December 2014 to implement an OMB-approved version of the guidance that would carry the force of law. See Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, 79 Fed. Reg. at 75,872. The USAID provisions adopted the Uniform Guidance, stating:

Under the authority listed above the Agency for International Development adopts the Office of Management and Budget (OMB) guidance Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards to Non-Federal Entities (subparts A through F of 2 CFR part 200), as supplemented by this part, as the Agency for International Development (USAID) policies and procedures for financial assistance administration.

The Uniform Guidance provides a model for federal agencies for all aspects of award management, including a set of cost allowability principles.²⁸ Upon adopting the Uniform Guidance, most agencies promulgated supplemental regulations that also govern their assistance awards.²⁹

Although the Uniform Guidance has allowed for more consistency in the administration of federal assistance programs, there remains little decisional law interpreting its requirements. While a particular procurement regulation may have several cases explaining its operation, there is unlikely to be comparable case law addressing its counterpart in the Uniform Guidance.³⁰ In such circumstances, recipients may reference the FAR and associated authorities to inform their approach, although there are distinctions between the regulations and, perhaps more importantly, agencies' management approaches under each set of rules can vary.

In addressing cost allowability, the Uniform Guidance defines "disallowed costs" as "charges to a [f]ederal award that the [f]ederal awarding agency or pass-through entity determines to be unallowable, in accordance with the applicable [f]ederal statutes, regulations, or the terms and conditions of the [f]ederal award."³¹ Awardees have the primary "responsibility for administering [f]ederal funds in a manner consistent with . . . program objectives, and the terms and conditions of the [f]ederal award," though agencies must provide oversight to ensure that recipients are applying the cost principles consistently.³² As fewer contractual remedies are available to either the government or recipient under assistance, cost disallowances are one of the primary ways in which the government enforces award terms and regulatory requirements, and disallowances are a key source of disputes.³³

Subpart E of the Uniform Guidance provides cost principles applicable to most non-profit entities—including a clause addressing the allowability of taxes.³⁴ Since a recipient can face significant tax burdens in the foreign

2 C.F.R. § 700.2.

28. *See id.* §§ 200.400(a), 200.401(a).

29. *See, e.g., id.* § 700.2.

30. *Cf.* Kenneth J. Allen, *Federal Grants: A Comprehensive Overview and Comparison to Federal Contracting*, BRIEFING PAPERS, May 2016, at 4 (positing that grants live in a different legal world than procurement contracts).

31. 2 C.F.R. § 200.31.

32. *Id.* § 200.400(b), (e). Agencies must negotiate, approve, and review awardees' cost allocation plans and indirect cost proposals. *Id.* § 200.400(e). Note that, depending on the agency, a government employee who is empowered to make, amend, or terminate assistance awards is referred to as the "grants" or "agreements" officer and is equivalent to a contracting officer for purposes of assistance awards. *See id.* § 780.20(d).

33. *See* 2 C.F.R. § 200.338(b); Teaching & Mentoring Communities, Inc., No. A-14-75, at 2 (U.S. Dep't of Health & Human Servs., Departmental Appeals Bd. May 12, 2015), <https://www.hhs.gov/sites/default/files/static/dab/decisions/board-decisions/2015/dab2636.pdf> (recognizing that cost disallowance is the appropriate remedy for costs charged to a grant in violation of federal cost principles). *See generally* KENNETH J. ALLEN, *FEDERAL GRANT PRACTICE: A GUIDE FOR THE GOVERNMENT AND GRANTEEES* 1212 (2019) (explaining the remedy of disallowance).

34. *See* 2 C.F.R. §§ 200.100(c), 200.470(a)(1) (2019); FAR 31.702. Note that a cooperative agreement to a for-profit would be governed by FAR part 31 and a contract to non-profit would be governed by subpart E. *See* OFFICE OF MGMT. & BUDGET & U.S. GEN. SERVS. ADMIN., CATALOG

jurisdiction in which the assistance agreement is performed, and these costs are incurred in order to perform the award, the Uniform Guidance generally treats foreign tax payments as allowable costs under cost-reimbursement grants and cooperative agreements.³⁵ Under section 200.470 of the Uniform Guidance, “taxes which the non-[f]ederal entity is required to pay and which are paid or accrued in accordance with GAAP . . . are allowable” costs.³⁶ However, as relevant to this article, the Uniform Guidance also provides that “[t]axes from which exemptions are available to the non-[f]ederal entity directly or which are available to the non-[f]ederal entity based on an exemption afforded the [f]ederal [g]overnment and, in the latter case, when the [f]ederal awarding agency makes available the necessary exemption certificates” are not allowable.³⁷ Additionally, this provision expressly allows “Value Added Tax (VAT) Foreign taxes” that are “charged for the purchase of goods or services that a non-[f]ederal entity is legally required to pay in country [as] an allowable expense under [f]ederal awards.”³⁸

III. TREATMENT OF EXEMPTIONS DOMESTICALLY

Unlike other cost principles, a relative dearth of case law interprets FAR 31.205-41, and essentially none provides any insight into the Uniform Guidance tax provision. While some decisions from the courts, boards of contract appeals, and the Government Accountability Office interpret the FAR provision, most of these cases focus on the methods of allocating taxes to contracts.³⁹ However, a few decisions in the domestic context provide guideposts for navigating the allowability of foreign tax payments.

For example, in *Information Systems & Networks Corp. v. United States (Information Systems)*, the U.S. Court of Appeals for the Federal Circuit held that the term “exemption” in FAR 31.205-41 is to be read broadly to include state

OF FEDERAL DOMESTIC ASSISTANCE 1196 (2013). This analysis becomes more convoluted at the subcontract/subaward level (e.g., a contract to a non-profit that, in turn, issues a subcontract to a for-profit concern).

35. See 2 C.F.R. § 200.470(c). As relevant to this discussion, the vast majority of USAID awards are issued on a cost-reimbursement basis. Given the often complex and unpredictable environments in which USAID operates, cost-reimbursement contracts and assistance agreements provide flexibility for contractors and recipients to invoice based on costs incurred. See generally FAR 16.301-2(a)(2) (authorizing the use of cost-reimbursement contracts when “[u]ncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract”). That said, as of this writing, USAID is pursuing a procurement reform initiative that looks to increasingly use “pay-for-results” acquisition and assistance mechanisms, such as using firm-fixed-price and fixed-amount awards. See U.S. AGENCY FOR INT’L DEV., ACQUISITION AND ASSISTANCE STRATEGY 6 (2018); see also 2 C.F.R. § 200.45 (defining “[f]ixed amount awards”).

36. 2 C.F.R. § 200.470(b)(1).

37. *Id.* § 200.470(b)(1)(i).

38. *Id.* § 200.470(c).

39. These disputes largely arise in situations in which a contractor makes payments from a home office or over-applies tax refunds and credits. See generally *MANOS*, *supra* note 15, at 607–16 (“Many of the disputes about costs of taxes have involved issues of allocability and, more particularly, the method of allocating taxes to contracts . . .”).

tax abatements, tax reductions, and other kinds of exemptions.⁴⁰ The case involved a contractor that held cost-reimbursement contracts with the federal government.⁴¹ As a Maryland S-corporation, the contractor did not pay income tax; instead, its single shareholder paid federal and Maryland income tax on dividends generated by the corporation.⁴² The company subsequently submitted a request to the Defense Contract Audit Agency (DCAA) for reimbursement of the shareholder's state income tax payments.⁴³ The DCAA rejected the request, and the contractor filed suit and litigated the issue up to the Federal Circuit.⁴⁴

The Federal Circuit ruled on two key aspects of the dispute, setting important precedent in this area. First, it held that an entity seeking to claim a tax payment as an allowable cost under FAR 31.205-41 must be the *contractor* in privity with the government, not an *owner*.⁴⁵ Second, the court explained that the term "exemption" in FAR 31.205-41 "means freedom from taxation in whole or in part," including but not limited to tax abatements or tax reductions.⁴⁶ Therefore, FAR 31.205-41 is to be read broadly so that it applies to tax abatements, tax reductions, and other kinds of exemptions.⁴⁷ The ability to obtain similar tax reductions or refunds in the foreign context likely would make the tax unallowable as well.

The nature of the governmental assessment imposed on a contractor or recipient is also critical to understanding whether the tax should be reimbursed. In *Westech International, Inc. (Westech)*, the Armed Services Board of Contract Appeals (ASBCA) addressed whether a contractor could be reimbursed for the payment of Arizona transaction privilege taxes (TPT) under a cost-plus-award-fee contract with the Army.⁴⁸ The contract included FAR 52.216-7 (DEC 2002), the Allowable Cost and Payment clause, which provides "for reimbursement of the allowable costs of supplies and services purchased directly for the contract and of allocable and allowable indirect costs."⁴⁹ After the contractor paid the TPT, which it incurred from sales of tangible personal property used in research and development, it submitted a claim to the Army for the payments.⁵⁰ The Army rejected the claim, taking the position that the contractor should not have paid the TPT because an exemption existed under Arizona law for property used in research and development.⁵¹

On appeal to the ASBCA, the contractor argued that its TPT payments were allowable because it was required to pay the TPT and no exemption

40. See *Info. Sys. & Networks Corp. v. United States*, 437 F.3d 1173, 1177–78 (Fed. Cir. 2006).

41. See *id.* at 1174.

42. See *id.* at 1174–75.

43. See *id.* at 1175.

44. See *id.* at 1175–76.

45. See *id.* at 1177.

46. *Info. Sys. & Networks Corp.*, 437 F.3d at 1176 (quoting FAR 31.205-41(b) (2004)).

47. See *id.* at 1177–78.

48. See *Westech Int'l, Inc.*, ASBCA No. 57296, 11-2 BCA ¶ 34,822, at 171,345.

49. *Id.*; see also FAR 52.216-7(b).

50. See *Westech Int'l, Inc.*, 11-2 BCA ¶ 34,822, at 171,345–46.

51. See *id.* at 171,346.

applied.⁵² The Army maintained that a provision of Arizona law provided an exemption to the TPT for tangible personal property used in research and development.⁵³ The ASBCA held that the contractor's payments were allowable costs.⁵⁴ The ASBCA also rejected the Army's entreaty for the board to rule in the first instance that the TPT exemption was operative without a definitive statement from an Arizona court.⁵⁵ The board refused to do so, stating that Arizona courts should address that issue first and that, if the Army really believed that an exemption applied, the Army should have instructed the contractor to litigate that issue in Arizona.⁵⁶ Extending the principle of *Westech* to contractors or recipients operating overseas, a required payment to which no exemption applied would most likely be allowable.

As demonstrated by these domestic cases, the allowability of tax payments is fact-specific, and entities incurring costs imposed by a government may need to conduct a detailed analysis of applicable corporate and tax laws to determine whether an exemption is available. With this in mind, in the next section we discuss a specific form of exemption—those available to the U.S. Government in the context of foreign assistance awards.

IV. TAX EXEMPTIONS INTERNATIONALLY

U.S. law requires that any new agreement between the United States and a foreign government for the delivery of U.S. assistance include a provision exempting the assistance from taxation or allowing for reimbursement of the tax.⁵⁷ In the case of USAID foreign assistance programs, prior to providing assistance, the United States enters into an agreement with the host government to, among other things, “establish the USAID Mission as a special [m]ission; identify the privileges and immunities to be provided to USAID personnel . . . and list other general terms and conditions” for the provision of assistance.⁵⁸ Importantly, these bilateral agreements implement the “long-standing policy that [foreign] assistance should be exempt from host

52. *See id.*

53. *See id.* at 171,347.

54. *See id.*

55. *See id.*

56. *See Westech Int'l, Inc.*, 11-2 BCA ¶ 34,822, at 171,347; FAR 31.205-41(a)(2)(ii).

57. *See Consolidated Appropriations Act, 2014*, Pub. L. No. 113-76, § 7013(a), 128 Stat. 5, 496-97 (2014); *see also USAID ADS, supra* note 1, § 155.3.2(a) (2004). This policy is intended to maximize the effectiveness of U.S. foreign assistance. It has been criticized in recent years as the international development community has pushed for aid recipients to improve “domestic resource mobilization,” namely the improvement of host country tax-collection systems. Critics argue that a policy that exempts a large slice of foreign investment from local tax hinders a country's efforts to develop a sustainable tax system. *See, e.g.,* Émilie Caldeira et al., *La Fiscalisation de l'aide Publique au Développement: Enjeux pour l'efficacité Économique des Pays Receveurs et la Crédibilité Politique des Donneurs* [*The Paradox of Tax Exemptions of Official Development Assistance in Developing Countries*], FONDATION POUR LES ÉTUDES ET RECHERCHES SUR LE DÉVELOPPEMENT INTERNATIONAL [FOUND. FOR STUDY & RES. INT'L DEV.] 1, 3, 7 (2018) (Fr.).

58. USAID ADS, *supra* note 1, § 349.3.1.1.

government taxes by setting forth the privileges and exemptions from taxes and duties for USAID-financed supplies and services.”⁵⁹

These bilateral agreements typically exempt a variety of taxes and fees, including (1) “[c]ustoms duties, tariffs, import taxes, or other levies on the importation, use, and re-exportation of goods or personal belongings;” (2) “[t]axes on the income, profits, or property of non-[local] organizations . . . and non-[local] individual contractors” and recipients; and (3) “[t]axes levied on the last transaction for the purchase of goods or services . . . including sales taxes, [VAT], or taxes on purchases or rentals of real or personal property.”⁶⁰

Even if a contractor or recipient is not individually exempted from the tax, it is considered to be exempt if an exemption is “afforded” to the government.⁶¹ Since foreign assistance may not be subject to local (i.e., host country) taxation, firms implementing foreign assistance awards covered by a bilateral agreement that includes a tax exemption will generally be unable to recover local taxes incurred under the award as an allowable cost.⁶²

For contracts, this restriction is typically implemented through the clause at FAR 52.229-8, Taxes-Foreign Cost-Reimbursement Contracts, which must be included “in solicitations and contracts when . . . the contract is to be performed wholly or partly in a foreign country.”⁶³ It states in relevant part:

Any tax or duty from which the United States Government is exempt by agreement with the Government of [name of the foreign government], or from which the [c]ontractor or any subcontractor under this contract is exempt under the laws of [country], shall not constitute an allowable cost under this contract.⁶⁴

The Uniform Guidance does not include standard terms and conditions.⁶⁵ As a result, USAID, like other federal agencies, has developed agency-specific standard provisions that it includes in grants and cooperative agreements.⁶⁶ With respect to tax payments, USAID’s standard assistance provision provides:

Host government taxes are not allowable where the [a]greement [o]fficer provides the necessary means to the recipient to obtain an exemption or refund of such taxes, and the recipient fails to take reasonable steps to obtain such exemption or refund. Otherwise, taxes are allowable in accordance with the Standard Provision, “Allowable Costs,” and must be reported as required in this provision.⁶⁷

59. *Id.*

60. *Id.* § 155.3.2(e) (2004).

61. FAR 31.205-41(b)(3); *see* 2 C.F.R. § 200.470(b)(1)(i) (2019).

62. *See* U.S. AGENCY FOR INT’L DEV., STANDARD PROVISIONS FOR U.S. NONGOVERNMENTAL ORGANIZATIONS: A MANDATORY REFERENCE FOR ADS CHAPTER 303 (ADS 303maa) § RAA12(c) (2019) [hereinafter USAID ADS 303maa].

63. *See* FAR 29.402-2(a).

64. FAR 52.229-8(a).

65. *See generally* 2 C.F.R. § 200.0–200.521.

66. Agencies’ standard grant terms and conditions will typically incorporate the Uniform Guidance, including applicable cost principles. *See, e.g.,* NAT’L SCI. FOUND., GRANT GENERAL CONDITIONS (GC-1) § 1(b) (2019) (“The applicable [f]ederal administrative standards are incorporated by reference and are contained in 2 CFR § 200, [Uniform Guidance].”).

67. USAID ADS 303maa, *supra* note 62, § RAA12(c); USAID ADS 303mab, *supra* note 9, § RAA10(c).

While this provision establishes the same underlying rule as the FAR clause⁶⁸ (i.e., that taxes for which an exemption is available are unallowable), it offers the possibility that such costs may be allowable if the government makes available to the recipient the necessary means by which to enforce the exemption and the recipient makes a good faith effort to obtain the exemption. As discussed below, the issue of whether a tax exemption can be effectively “unavailable,” notwithstanding its existence in law, has been the subject of considerable confusion and controversy within the international development community.

V. IDENTIFYING FOREIGN TAX EXEMPTIONS

Notwithstanding the apparent simplicity of the tax allowability rule, it is not self-executing.⁶⁹ Rather, the scope and application of the tax exemption is governed by the procedures established in the particular country and the terms of the overarching agreement between the U.S. Government and the host country concerning the delivery of foreign assistance.⁷⁰ While these bilateral agreements are intended to exempt all forms of taxation, in practice, the agreements differ and certain taxes may not be covered.⁷¹ For example, a bilateral agreement may not exempt certain provincial taxes or newly instituted taxes.⁷² In other cases, the contract is not provided under the bilateral agreement or the tax is imposed by a third country (e.g., a country through which goods are transported for delivery in the country receiving U.S. assistance). In most cases, taxes paid by citizens of the host country are not covered by an exemption.⁷³ A tax falling into one of these categories would not be “exempt” and is potentially allowable.

The experience of contractors operating in Afghanistan over the past two decades underscores the complexity of identifying applicable tax exemptions in some contexts. The U.S. Government has not adopted a comprehensive intergovernmental agreement with the Afghan government; instead, individual agencies (e.g., USAID, the DoD, and the State Department) have executed agency-specific agreements exempting contractors and recipients from taxation.⁷⁴ This patchwork approach has led to inconsistent tax results across agencies and required contractors and recipients to navigate a shifting landscape of local tax requirements and bilateral agreements. Note that this is

68. See FAR 52.229-8(a).

69. See USAID ADS, *supra* note 1, § 155.3.2(c) (2004).

70. See *id.*

71. Only taxes on “foreign assistance” delivered under the annual Department of State, Foreign Operations, and Related Programs Appropriations Act are subject to the § 7013 prohibition on host country taxation. See Consolidated Appropriations Act, 2014, § 7013(a), 128 Stat. at 496–97. For instance, USAID programs that deliver Title II food aid, namely Food for Peace, may not be exempt. See USAID ADS, *supra* note 1, § 155.3.2(b) (2004); 22 C.F.R. § 211.3(b) (2019).

72. See U.S. AGENCY FOR INT’L DEV., PROCUREMENT EXECUTIVE’S BULLETIN (PEB) No. 2017-02, EXEMPTIONS AND ALLOWABILITY OF HOST-COUNTRY TAXES 3 (2017) [hereinafter PEB 2017-02].

73. See *id.*

74. See SIGAR AUDIT, *supra* note 12, at 3–4.

separate from the requirement for the contractor or recipient to file an annual report on taxes paid to foreign governments. The report is intended to help the U.S. Government assess the effectiveness of a host country's tax exemption system, but reporting does not obviate the requirement to seek tax relief.⁷⁵

For example, on the one hand, USAID's Strategic Objective Grant Agreements with the Afghan Government, dated September 19, 2005,⁷⁶ include a provision exempting USAID's grant and cooperative agreement recipients and their subcontractors from Afghan taxes imposed on USAID-financed activities.⁷⁷ DoD contractors, on the other hand, were covered by the May 2003, Status of Forces Agreement (SOFA) for a large portion of the U.S. engagement in Afghanistan.⁷⁸ The DoD interpreted the SOFA to provide tax-exempt status for all contractors and subcontractors, but the Afghan Government posited that it applied only to prime contractors.⁷⁹ In 2014, the United States and the Afghan Government executed a bilateral security agreement that provided tax exemptions for contractors and subcontractors supporting U.S. forces.⁸⁰ Then, in July 2018, the countries entered into a new agreement to address tax exemptions for federal awards providing economic, technical, and humanitarian assistance to Afghanistan.⁸¹ The scope of this agreement applies to certain assistance activities from June 1, 2018, onward, no matter when the assistance was provided.⁸²

This agency-by-agency approach over the past eighteen years and the shifting scope of the DoD agreements, in particular, have presented legal and logistical challenges to contractors and recipients operating in Afghanistan.⁸³ The availability of tax exemptions depend on which agency awards the contract or assistance agreement, the scope and terms of the award, and the period of performance. Given this complexity, in some cases, contractors have struggled to identify the applicable exemption and paid taxes that were exempt, effectively absorbing such levies as a cost-of-doing-business.⁸⁴

75. See USAID ADS 303maa, *supra* note 62, § RAA12(c); USAID ADS 303mab, *supra* note 9, § RAA10(c). See generally DFARS 252.229-7011; AIDAR 752.229-71.

76. Four such agreements for various developmental goals provide that U.S. foreign assistance used for development and civil society projects was to be "free from any taxes imposed under laws in effect in [Afghanistan]." SIGAR AUDIT, *supra* note 12, at 4.

77. See Strategic Objective Grant Agreements for the Strategic Objective of a Thriving Economy Led by the Private Sector, Afg.-U.S., Annex 2, § B.4(b), Sept. 19, 2005, Temp. State Dep't No. 05-253.

78. See SIGAR AUDIT, *supra* note 12, at 4. Contractors supporting the North Atlantic Treaty Organization's (NATO) International Security Assistance Force fell under a separate agreement, the Military Technical Agreement (MTA). See *id.* at 5.

79. See *id.* at 7-8.

80. See Security and Defense Cooperation Agreement, Afg.-U.S., art. 17, ¶ 3, Sept. 30, 2014, 54 I.L.M. 290.

81. See Agreement Regarding the Provision of Tax Exemptions for Assistance, Afg.-U.S., July 27-28, 2018, T.I.A.S. No. 18,728. Note that the agreement excludes assistance provided under the Strategic Objective Grant Agreements (SOAGs). See *id.* art. I, ¶ 2.

82. See *id.* art. V.

83. See SIGAR AUDIT, *supra* note 12, at 13.

84. In other cases, contractors refused to pay the tax, on the basis that they were covered by the exemption, and suffered various consequences, such as restrictions on importation of goods

VI. INVOKING AN EXEMPTION

Assuming a particular tax is exempt, the contractor or recipient will be required to take steps to avail itself to the exemption, either directly at the point of sale, or by paying the tax and seeking reimbursement from the foreign government.⁸⁵ In the case of foreign assistance awards, this process can present challenges to contractors and recipients, who are often left navigating foreign tax bureaucracies in order to invoke an exception or obtain reimbursement.

In many countries, contractors and recipients will be required to follow detailed guidance from the U.S. Government to claim an exemption or seek reimbursement of a local tax. This guidance and applicable exemptions may differ based on the federal agency awarding the contract or assistance agreement.⁸⁶ In the case of USAID programs, this guidance will often be referenced in the special contract requirements set forth in section H of the solicitation and resulting contract.⁸⁷ A typical USAID contract clause reads:

VAT and customs duties are excluded from the ceiling price of the Contract. USAID will provide the Contractor documentation to assist the Contractor in obtaining VAT and customs duties exemption from the Government of [Country]. The Contractor shall not submit invoices to USAID for reimbursement that include VAT or customs duties without obtaining prior Contracting Officer (CO) approval that the taxes are allowable.⁸⁸

However, these provisions can look very different based on the country of performance. In Uganda, for example, the applicable bilateral agreements exempt taxes, but the Government of Uganda does not allow for tax exemption at the point of sale, nor is the contractor/recipient instructed to seek reimbursement from the host government, meaning that contractors and recipients may bill USAID for expenses inclusive of VAT.⁸⁹ Accordingly, the

and supplies, revoked business licenses, frozen local bank accounts, and the detention or arrest of their personnel. *See id.* at 9.

85. *See* PEB 2017-02, *supra* note 72, at 1. Direct exemption at the point of sale is generally preferable because it typically minimizes the need to navigate local tax authorities to obtain reimbursement. Countries with direct exemption procedures may establish a “tax exempt” list and provide necessary certificates to U.S. Government-funded contractors and recipients to be able to invoke the exemption when purchasing from local vendors. *Cf.* Anthony Bizien, Note, *Taxation Roulette: Examining the Unpredictability of the Afghan Business Tax for U.S. Government Contractors*, 45 PUB. CONT. L.J. 533, 536 (2016).

86. *See* Nichols et al., *supra* note 8, at 2.

87. *See, e.g.*, U.S. AGENCY FOR INT’L DEV., REQUEST FOR PROPOSAL NO. SOL-497-15-000010, MONITORING AND EVALUATION SUPPORT 45 (Feb. 25, 2015), https://www.usaid.gov/sites/default/files/documents/1861/SOL-497-15-000010_M&E_Support.pdf.

88. *See, e.g., id.* (“VAT and customs duties are excluded from the price of the contract. USAID will provide the contractor correspondence to assist the contractor in obtaining this exemption from the Government of Indonesia. The contractor shall submit 0% VAT invoices for any payments.”). Note that many USAID Missions have staff that are dedicated to facilitating the processing of VAT and customs exemption requests for contractors and recipients. *See generally* PEB 2017-02, *supra* note 72, at 2 (discussing development of Mission-specific policies/procedures as a “best practice”).

89. *See* U.S. AGENCY FOR INT’L DEV., REQUEST FOR PROPOSAL NO. 72061718R00009, UGANDA HEALTH SYSTEMS STRENGTHENING ACTIVITY 17 (Apr. 5, 2018), <https://www.fbo.gov/utlils/view?id=5bbc332eb55997a88fb77f0f8311c1d7>.

solicitation provision instructs the contractor to “submit original VAT tax invoices/receipts, [an] original certified summary (using a format provided by USAID) and one copy of all documents to USAID by the 25th of the month after the calendar year quarter end.”⁹⁰ USAID—not the contractor—will then “seek a VAT refund from the Government of Uganda.”⁹¹ The refund is not returned to the contractor (as the contractor already received reimbursement directly from USAID).⁹²

The USAID supplemental tax guidance referenced in these clauses, as well as any supplemental documentation necessary to invoke the exemption (e.g., exemption certificates) or obtain reimbursement, will often be provided separately to the contractor or recipient.⁹³ Since the guidance is tailored to the terms of the bilateral agreement and the host country’s tax and legal systems, it provides the most relevant instructions for determining allowability. Suffice it to say that exemptions and reimbursement practices vary significantly across the globe, so it is critical that organizations closely follow these instructions and work with USAID mission staff as necessary to navigate the applicable procedures.

VII. DETERMINING ALLOWABILITY

Notwithstanding the availability of such guidance, contractors and recipients often encounter difficulty invoking exemptions or being reimbursed by local government tax authorities. In such a scenario, the taxes will be unallowable unless the contractor is able to demonstrate strict conformance with applicable policies.⁹⁴ USAID has allowed taxes on this basis and has provided clarifying guidance to its acquisition and assistance workforce on allowing taxes when, “[d]espite efforts undertaken by the contractor or recipient to pursue the host-country tax exemption or refund, the host-country government [does]

90. *Id.*

91. *Id.*

92. *Id.* “The [c]ontractor is responsible for ensuring that [s]ubcontractors and grantees comply with this requirement. All VAT claims, for the [c]ontractor, [s]ubcontractors and grantees, must be submitted to USAID through the prime [c]ontractor.” *Id.*

93. Some USAID Missions have made this guidance publicly available. *See, e.g.*, U.S. AGENCY FOR INT’L DEV., WORKING TOGETHER: USAID/SENEGAL IMPLEMENTING PARTNERS HANDBOOK 15 (Mar. 2017), https://www.usaid.gov/sites/default/files/documents/1860/USAID_Senegal_Implementing_Partners_Handbook_April2017.pdf. For example, the USAID/Senegal Handbook provides:

It is the contractor’s responsibility to initiate and conduct tax exemption procedures. At the start of each program, USAID introduces the contractor to the relevant departments of the Customs and Tax Services. The contractor then files the specimen signature of a member of their staff, usually the chief of party, which makes it possible to initiate tax exemption operations backed with a copy of the funding DOAG or assistance agreement USAID has signed with the Government of Senegal.

Id.

94. *See* PEB 2017-02, *supra* note 72, at 1–2.

not grant the exemption or refund.”⁹⁵ The notice affirms that a contracting or grant officer may determine that, in such cases, “an exemption cannot be reasonably obtained and is not available for purposes of allowability.”⁹⁶

Whether a contractor or recipient has met its burden in establishing that an exemption is effectively “not available” under the cost principles depends on a variety of factors specific to the country. It is typically insufficient for an organization to merely assert that it has submitted a reimbursement request and has not been paid. Instead, the notice provides that the contractor or recipient may need to demonstrate that it has: (1) followed “the tax exemption or reimbursement procedures that the host government agreed upon with USAID” (and were subsequently provided to the contractor or recipient); (2) complied with “host-country law in attempting to invoke the exemption or right to reimbursement;” or (3) “otherwise challenge[d] the tax assessment.”⁹⁷ It is the responsibility of the contractor or recipient to demonstrate that it used “best efforts” to invoke an exemption and USAID may request relevant documentation to verify that the contractor did so.⁹⁸

If all else fails, the FAR provides express authority to allow tax payments, despite a contractor’s failure to adequately invoke an exemption, if “the contracting officer determines that the administrative burden incident to obtaining the exemption outweighs the corresponding benefits accruing to the [g]overnment.”⁹⁹ This rule has been interpreted in some contexts to constitute a *de minimis* exception, whereby tax payments falling under a certain dollar figure (e.g., \$500) will be allowable if recovery of the payments would be particularly cumbersome.¹⁰⁰ This is a case-by-case determination based on a cost-benefit analysis that weighs the burden to the contractor or recipient, agency resources needed to facilitate such payments, and the U.S. Government’s strong policy interests in ensuring that foreign assistance payments are not subject to local taxation.¹⁰¹

VIII. PRACTICAL CONSIDERATIONS FOR CONTRACTORS AND RECIPIENTS

In practice, invoking an exemption does not always go smoothly, and some contractors or recipients may forego available exemptions because of practical

95. *Id.* at 1. The PEB provides several scenarios in which a tax payment could be allowed, “despite the potential availability of an exemption or reimbursement.” *See id.* at 4–5.

96. *Id.* at 1.

97. *Id.* at 4.

98. *See id.* at 1, 4.

99. FAR 31.205-41(b)(3). Note that there is no comparable exception under the Uniform Guidance, although the cost principles have generally been interpreted to provide the discretion to allow such *de minimis* payments, notwithstanding the existence of an exemption. *See generally* 2 C.F.R. § 200.470(b)(1)(i) (2019).

100. *See generally* Consolidated Appropriations Act, 2017, Pub. L. No. 115-31, § 7013(c), 131 Stat. 135, 624 (2017) (providing that foreign taxes of a “*de minimis* nature” need not be reported to Congress).

101. *See* PEB 2017-02, *supra* note 72, at 1, 4–5.

challenges in having them recognized. In some countries, for example, contractors and recipients may face resistance from the foreign government to recognizing a tax exemption, which can result in extensive documentation requirements, fees, and, ultimately, long delays in obtaining reimbursement.¹⁰²

Disputes with the U.S. Government related to tax allowability often materialize after a contractor or recipient has attempted to invoke an exemption and been told that they are required to pay the local tax. Contractors may be obligated under local law to pay the tax and may fear repercussions.¹⁰³ In some countries, these concerns are well founded.¹⁰⁴ The contractor or recipient may be told that their operating licenses will be revoked and property will be seized if they do not pay the tax, or threats may be made against personnel, which can raise legitimate security risks.¹⁰⁵ This can be a compelling basis for allowing a tax payment.

In other cases, the contractor or recipient may be simply misinterpreting the requirements or confusing the legal basis for the tax exemption. For example, non-governmental organizations (NGOs) may be entitled to tax-exempt treatment in a foreign jurisdiction based on their non-profit status, regardless of the availability of a tax exemption afforded to U.S. Government contractors or recipients.¹⁰⁶ In that case, the contractor or recipient will need to actively maintain its non-profit status *or* follow the exemption process, as the local taxes will not be allowable costs under either FAR 31.205-41 or 2 C.F.R. § 200.470.¹⁰⁷

Additional issues may arise in exercising exemptions at lower tiers. In some cases, a foreign government may recognize that a prime contractor or recipient may avail itself of an exemption, but fail to apply the full scope of an exemption to subcontractors or subrecipients.¹⁰⁸ Or, while a prime may be aware of an exemption, its local partners might lack awareness of the exemption's scope.¹⁰⁹ This can lead to situations where, for example, a subcontractor pays a vendor, but, in doing so, pays prices that include excludable taxes.¹¹⁰

102. *Cf., e.g.*, SIGAR AUDIT, *supra* note 12, at 10–11 (discussing additional requirements and fees imposed by the Afghan Government).

103. *See Bizien, supra* note 85, at 543–44.

104. *See, e.g.*, SIGAR AUDIT, *supra* note 12, at 13 (noting that “lack of clarity on these tax issues resulted in some personnel working on U.S. contracts being arrested, increased costs to U.S. government contracts, and may have interrupted contractor support to U.S. military operations”).

105. *See id.* at 9.

106. *See* PEB 2017-02, *supra* note 72, at 4.

107. *See* 2 C.F.R. § 200.470(b)(1) (2019); FAR 31.205-41(b). *See generally* Potentia Namibia Recruitment Consultancy, No. A-14-79, at 4 (U.S. Dept. of Health & Human Servs., Departmental Appeals Bd. Dec. 17, 2014), <https://www.hhs.gov/sites/default/files/static/dab/decisions/board-decisions/2014/dab2607.pdf> (holding that Namibian VAT taxes paid by a for-profit recipient of Centers for Disease Control and Prevention (CDC) cooperative agreement were not allowable costs under the terms of the agreement).

108. *See, e.g.*, SIGAR AUDIT, *supra* note 12, at 7.

109. *See, e.g., id.* at 12.

110. *See, e.g.*, PEB 2017-02, *supra* note 72, at 4 (discussing that a vendor may insist on payment of the tax despite attempt to invoke an exception); Encorp, ASBCA No. 51293, 01-1 BCA ¶ 31,165, at 153,934 (explaining a second-tier trucking subcontractor paid import duties fearing for delays in contract performance although ostensibly aware of an exemption).

The subcontractor may learn of an exemption only after it has paid the vendor and then seek to recover such tax payments at a later point.¹¹¹ Often, the subcontractor cannot get a refund from the vendor and seeks a refund from their prime, which may be difficult.¹¹²

The upshot is that contractors and recipients can often actively communicate with their U.S. Government point of contact, such as an agreement or contracting officer or their respective technical representatives. Even though tax exemptions arise from a bilateral agreement between two sovereign governments, best practice usually involves confirming the availability of the tax exemption with the cognizant federal agency and the foreign government agency, such as a local or regional tax authority, as appropriate. If a contractor or recipient can engage the U.S. Government, foreign government, and its subcontractors in a substantive discussion of the available exemption—preferably before incurring tax costs—there may be greater success in achieving the benefits of tax exemptions.¹¹³ By memorializing the parties' understanding early in the process, contractors and recipients may be able to overcome challenges in being reimbursed.

IX. APPEALING A TAX ALLOWABILITY DETERMINATION

While many tax allowability issues can be avoided by diligently pursuing exemptions and working closely with U.S. government personnel, disputes inevitably arise. Many such disagreements can be resolved through informal mediation with the contracting or grant officer and resolution outside of the formal disputes process. U.S. government staff in the country is often very familiar with the local tax exemption or reimbursement process and can quickly assess the validity of a contractor's or recipient's claim.¹¹⁴ However, as with many cost issues, contractors and recipients facing the disallowance of incurred costs totaling many thousands of dollars may be incentivized to formally appeal this determination.

Under the FAR, this process is relatively straightforward and follows the Contract Disputes Act (CDA).¹¹⁵ For example, the contractor may—after

111. See e.g., *Encorp*, 01-1 BCA ¶ 31,165, at 153,939 (denying appeal where prime contractor sought to recover payments made by its second-tier subcontractor for import duties that were subject to an exemption where prime contractor failed to take all steps necessary to obtain exemption).

112. See SIGAR AUDIT, *supra* note 12, at 11–12.

113. This advice would also apply in the fixed-price context. For example, drawing on experiences in Afghanistan, DoD contracts and subcontracts may be silent on the issue of Afghan taxes, but they will include standard FAR clauses that may be relevant. See SIGAR AUDIT, *supra* note 12, at 33. Contractors facing certain local tax charges may rely on FAR 52.229-6, for example, to seek reimbursement for taxes and penalties under fixed-price contracts if the contracting officer finds such expenses to be “after-imposed” and not incurred through contractor's fault, negligence, or failure to follow instructions of the contracting officer. This could potentially provide the contractor with relief, notwithstanding the existence of an exemption.

114. Cf. FAR 52.229-6–52.229-9.

115. See FAR 52.233-1 (citing 41 U.S.C. § 7101–7109 (2012)).

being unable to obtain tax reimbursement from the local government—seek to pass on to the U.S. Government the tax costs on the basis that the exemption is, in effect, unavailable. Alternatively, in conducting a financial audit, an auditor may question tax payments to foreign governments, which may lead to a disallowance of costs and issuance of a bill of collection to the contractor.¹¹⁶ In either case, the contractor could contest the disallowance by initiating the CDA claims process: the filing of a (certified) claim to the contracting officer for a written, final decision, and, if denied, an appeal to either the cognizant board of contract appeals or the U.S. Court of Federal Claims.¹¹⁷

The appeal process for assistance agreements is less straightforward. While the claim-generation process is similar, recipients must typically exhaust an agency-specific administrative appeals process and, thereafter, have limited options for judicial review.¹¹⁸ As with contracts, tax allowability disputes typically arise from a grant officer's finding that a tax cost is unallowable, which may be based on a specific cost determination or the findings of a financial audit.¹¹⁹ While some disagreements concerning tax allowability may be resolved by engaging the grant officer concerning the basis for the disallowance, others will lead to an impasse and issuance of a final decision.¹²⁰

It is at this stage that the recipient must invoke the agency administrative appeals process. The Uniform Guidance does not provide standard requirements in this area, meaning that agencies have developed their own, agency-specific, procedures (and which remain “far from uniform” between agencies).¹²¹ While most agencies provide that appeals will be decided by an agency official at a level above the grant officer who issued the final decision, the standard of review, burden of proof, hearing rights, and other rights and procedures are governed by agency-specific practices, if they exist at all.¹²²

116. See USAID ADS, *supra* note 1, § 625.3.4.1–2 (2011). See, e.g., SIGAR AUDIT, *supra* note 12, at 1. See generally USAID ADS, *supra* note 1, § 591 (2019) (“The chapter provides the policy directives and required procedures for planning and conducting financial audits of USAID-funded contractors, recipients, and host government entities.”).

117. See 41 U.S.C. §§ 7103(a)(1), 7103(d), 7104(a), 7104(b)(1), 7105(b)(1); see also FAR 32.605(a); FAR 33.203(c).

118. See Sheffler, *supra* note 26, at 217; see also ALLEN, *supra* note 33, at 1222.

119. See 2 C.F.R. § 200.338(b) (2019) (allowing the federal awarding agency to deny use of funds for “all or part of the cost of the activity or action not in compliance [with the terms of the award]”).

120. See, e.g., Potentia Namibia Recruitment Consultancy, *supra* note 107, at 1 (discussing the CDC's Grants Management Officer's disallowance of costs based on an audit finding by the HHS Office of Inspector General that the recipient used funds to pay a value-added tax (VAT) to the Government of Namibia). The recipient “appealed this determination to the CDC Agency Review Committee (ARC) pursuant to 42 C.F.R. Part 50, subpart D, and the ARC upheld the determination.” *Id.* The disallowance was subsequently appealed to the Departmental Appeals Board. See generally *id.*

121. See Sheffler, *supra* note 26, at 230; see also ALLEN, *supra* note 33, at 1222 (“[T]he regulations of many federal agencies have what resembles the pre-litigation ‘claim’ in federal procurement contracting under the Contract Disputes Act.”).

122. See, e.g., 2 C.F.R. § 700.15(b)–(c) (2019) (providing for appeal of decisions by the USAID agreement officer). But see *id.* § 200.341 (requiring agencies, “[u]pon taking any remedy for non-compliance . . . [to] provide the [recipient] an opportunity to object and provide information

Several major grant-issuing agencies have published detailed regulations that outline this process, including requirements for a grant officer's final decision, deadlines for appealing the decision, submission instructions, and evidentiary/documentation requirements.¹²³ In this regard, USAID's supplement to the Uniform Guidance provides:

Any dispute under or relating to a grant or agreement will be decided by the USAID [a]greement [o]fficer. The [a]greement [o]fficer must furnish the recipient a written copy of the decision. . . . Decisions of the USAID [a]greement [o]fficer will be final unless, within 30 calendar days of receipt of the decision, the recipient appeals the decision to USAID's Assistant Administrator, Bureau for Management, or designee as delegated in Agency policy.¹²⁴

Though less detailed than some comparable regulations, USAID's regulatory appeal process provides USAID recipients facing the disallowance of tax costs a means to seek relief at a level above the agreement officer.¹²⁵ With their appeal, a recipient is required to "include all relevant and material evidence to support its position."¹²⁶ The agency analyst responsible for the appeal will typically review the appeal file and consult with staff from the relevant USAID Mission, Office of Acquisition and Assistance, and the Office of the General Counsel and may seek additional information as necessary to resolve the appeal.¹²⁷ As with most agencies, the appeal decision is considered final and not subject to further administrative appeal.¹²⁸

The recipient is not precluded from seeking judicial review if dissatisfied with the resolution of the administrative appeal, though its options are more limited in this regard than under procurement contracts. The Administrative Procedure Act provides jurisdiction in U.S. district courts for cases contesting "final" agency actions (e.g., an assistance appeal decision) and allows for the setting aside of agency actions found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."¹²⁹ This standard is generally considered to be "narrow" and deferential to government decision-making.¹³⁰ In the alternative, some precedent holds that a recipient may invoke U.S. Court of Federal Claims' Tucker Act jurisdiction on the basis that an assistance agreement constitutes a "contract" under the black-letter principles of contract formation.¹³¹ However, other decisions of the Court of

and documentation challenging the suspension or termination action, in accordance with written processes and procedures published by the [f]ederal awarding agency").

123. See, e.g., 2 C.F.R. § 2900.22(b)(1)(i)–(ii) (2019); 32 C.F.R. § 22.815(b)–(e) (2018); 45 C.F.R. §§ 16.1–16.23 (2018).

124. 2 C.F.R. § 700.15(a)–(b) (2019); see also USAID ADS, *supra* note 1, § 303.3.23.2 (2019); USAID ADS 303mab, *supra* note 9, § M113(a)–(b).

125. See USAID ADS, *supra* note 1, § 303.3.23.2 (2019).

126. *Id.*

127. See *id.*

128. See 2 C.F.R. § 700.15(d).

129. See 5 U.S.C. §§ 704, 706(2)(A) (2018).

130. See ALLEN, *supra* note 33, at 1250, 1252; Sheffler, *supra* note 26, at 257–58.

131. See *Thermalon Indus., Ltd. v. United States*, 34 Fed. Cl. 411, 419 (1995); see also 28 U.S.C. § 1491(a)(1) (2012) (granting jurisdiction for claims based upon any "express or implied contract with the United States"); Sheffler, *supra* note 26, at 241.

Federal Claims suggest a more limited interpretation of the Tucker Act's jurisdictional grant, and this area remains largely unsettled.¹³²

It seems particularly unlikely that a court of competent jurisdiction will seek to overturn agency decisions involving the interpretation of bilateral agreements, foreign tax law, and cost allowability. Suffice it to say, recipients face significant hurdles in obtaining judicial relief from agency cost disallowances. As a result, recipients facing tax allowability appeals generally look to the agency administrative appeals processes for effective relief. Given this landscape, contractors and recipients are best served to try to avoid disallowances and, if unsuccessful, to work closely with the agency to mitigate potential harm.

X. CONCLUSION

Foreign tax compliance is among the many risks that organizations performing foreign assistance awards face. The complexity of this cost item—including the need to navigate the scope and interpretation of international agreements, comply with country-specific guidance, and diligently pursue exemptions—makes it rife with misunderstandings, disallowances, and, ultimately, disputes. By strictly following applicable guidelines, diligently pursuing exemptions or reimbursement, and working collaboratively with government officials, contractors and recipients can prevent disallowances and help ensure that U.S. foreign assistance is maximized for its intended purpose.

132. See, e.g., *Rick's Mushroom Serv., Inc. v. United States*, 76 Fed. Cl. 250, 261 (2007), *aff'd*, 521 F.3d 1338 (Fed. Cir. 2008).