

PD-AAW-806

MAN-53252

AUDIT OF  
CUSTOMS PROBLEMS ENCOUNTERED UNDER  
THE BILATERAL AGREEMENT IN EGYPT  
Audit Report No. 6-263-88-1  
November 30, 1987

## memorandum

DATE: November 30, 1987

REPLY TO  
ATTN OF: Joseph R. Ferri, RIG/A/CairoSUBJECT: Audit Of Customs Problems Encountered  
Under The Bilateral Agreement In Egypt

TO: Mr. Marshall D. Brown, Director USAID/Egypt

This report presents the results of a limited-scope, program results audit of Customs Problems Encountered Under the Bilateral Agreement between the United States Government and the Government of Egypt. The audit showed that USAID/Egypt's program has made excellent progress in addressing customs problems. Two significant issues, however, still need to be resolved. Customs duties continue to be paid by U.S. contractors. Also, the parties to the Bilateral Agreement disagree on whether the Agreement permits the duty-free importation of AID-financed project passenger vehicles. This report makes two recommendations to mitigate the bad effects of these conditions. The Mission's comments on a draft of this report are contained as Appendix 1. One recommendation was closed on the basis of these comments.

Please provide us within 30 days your written comments on further actions planned or taken to close the other recommendation contained in this report.

Background

In 1978, the Government of Egypt (GOE) and the United States Government signed the Bilateral Agreement which governs the AID program in Egypt. Under the Agreement, AID personnel and contractors and AID-financed commodities were exempted from paying Egyptian customs duties. Individual project agreements between the GOE and USAID/Egypt restated these customs exemptions. Nevertheless, the duty-free privileges accorded the AID program in Egypt were not always realized.

The American Contractors in Egypt (ACE), an organization representing American contractors working in Egypt, documented their working problems in a letter to the Director, USAID/Egypt dated March 26, 1986. Customs problems

were a major complaint. The contractors wrote that "...In practice, local customs officials do not always observe this agreement (Bilateral Agreement), assessing duties on contractor imported consumable items such as parts, tools and other supplies. The contractor incurs extensive delays in retrieving these imports and, in many cases, is forced to pay the assessed duties since the costs associated with any delay become extensive."

Information obtained from the Mission during the audit stated that "...These problems (customs) have seriously delayed project implementation and have increased project costs. In addition, customs problems and their associated costs have increased the value of claims by USAID contractors against the Egyptian government. The net result of customs problems has been a decrease in the amount of development benefits received by the people of Egypt from AID programs."

The dollar magnitude of customs problems was not known because there were no readily available records. One U.S. contractor, however, estimated the cost at several million dollars. This estimate included unnecessary payments of duty and storage fees, waste of human resources, and costs of project delays.

As a result of the increasing volume of customs problems, the Mission formed a group in 1985 in its Project Support Office to assist in resolving customs problems. Since that time, basically one person has handled contractor complaints by working as an intermediary with GOE Customs officials.

#### Audit Objectives And Scope

The Office of the Regional Inspector General for Audit/Cairo made a limited-scope, program results audit of Customs Problems Encountered Under The Bilateral Agreement In Egypt. The objectives were to determine the magnitude of the customs problems and to evaluate the extent to which the Mission program had addressed the problems.

The audit fieldwork was done between March and May 1987. Interviews were held with the General Director of the Egyptian Customs Administration, officials from USAID/Egypt, U.S. contractors in Egypt, and shipping and clearing agents in Cairo and Alexandria. Pertinent documents were reviewed at USAID/Egypt and contractors' offices. The audit was made in accordance with generally accepted government auditing standards.

## Results Of Audit

The audit showed that precise figures were not readily available concerning the magnitude of the customs problems in Egypt. It is probably safe to say, however, that most projects experienced some sort of customs-related problems resulting in overall costs of millions of dollars to the AID program in Egypt.

The audit also showed that USAID/Egypt had effectively addressed and solved some problems and was actively working to solve others. Nevertheless, two major issues required further Mission attention. These issues involved the continuing problems of: (a) U.S. contractors paying customs duties in order to facilitate releases of project commodities; and (b) the different interpretations of the Bilateral Agreement as to whether project-financed vehicles can be imported duty free.

1. USAID/Egypt Actions Have Been Effective - Considering the magnitude and complexity of the customs problems, USAID/Egypt has dealt effectively with some problems and was progressing satisfactorily to resolve others.

In background notes prepared in 1986 for the new U.S. Ambassador on USAID/Egypt customs problems, the Mission stated that virtually all USAID-financed projects in Egypt had suffered from problems with the Customs Administration in Egypt. In 1986, there were 119 active AID projects obligated at about \$5 billion. Some generic problems stemmed from interpretations of the Bilateral Agreement by the Customs Administration. Other more specific problems were due to the excessive documentation required and the unfamiliarity of U.S. contractors and project officials with complicated and bureaucratic customs regulations. In either case, customs problems seriously delayed project implementation and increased project costs.

Discussion - The general conditions at the time the Mission briefed the Ambassador were that USAID/Egypt projects were encountering problems with getting the duty-free importation privileges accorded the AID program under the Bilateral Agreement. A report to the Ambassador described the problems as follows:

(a) The Customs Administration never fully accepted the exemptions stipulated in the Bilateral Agreement. Thus, customs duties were levied on project- and

contractor-owned commodities and, in particular, on spare parts and consumable items. The Customs Administration also placed restrictions on the quantities imported of spare parts, consumable items, and personal effects.

- (b) The Customs Administration insisted on temporary release rather than exemption of project- and contractor-owned commodities. (A temporary release merely defers the customs liability and is not considered a true exemption.)
- (c) The Customs Administration applied new laws and decrees to USAID/Egypt-financed commodities even when the exemptions in the Bilateral Agreement provided relief from the provisions of these laws and decrees. Commodities were held in Customs until the case for exemption from these laws or decrees was accepted by high-level customs officials.

USAID/Egypt started to address these problems seriously in 1985 when it established a position for an American to act as a Special Assistant within the Office of Project Support. The major focus of this position was on resolving customs and import/export issues facing the AID program in Egypt. Since that time, USAID/Egypt's strategy has been to deal with customs problems on two levels. The first level has been to deal with the Minister of Finance or the Minister of Economy, and in some cases with the Prime Minister, to resolve generic problems affecting all USAID/Egypt-financed contractors. The second level has been to work with the Customs Director and his staff to follow up on agreements reached with the higher GOE levels and to resolve contractors' individual problems.

USAID/Egypt made excellent progress in resolving certain customs problems given the short timeframe and the difficulty and complexity of dealing with Customs and its laws and regulations. The results of these efforts have been more efficient use of commodity resources. For example, a Project Support Office official said that one general problem affecting all contractors was completely solved. This problem concerned Law No. 186 of 1986 which imposed a 20-percent customs duty annually on equipment that was temporarily released for the purpose of use or hire inside Egypt. The Customs Director, at the request of the Mission, issued a memorandum clarifying that the customs duty specified in this law was not to be applied to AID-financed contractors.

Another general problem on which progress was made related to vehicles, and in particular passenger vehicles, imported for AID-financed projects. These vehicles were released from Customs on temporary release rather than being exempted from duties. This meant that the vehicles had to be reexported at the end of the project or customs duty had to be paid. The Customs Director claimed that the Bilateral Agreement did not provide for exemption of passenger vehicles.

The Minister of Finance, responding to USAID/Egypt's initiatives in April 1987, instructed the Customs Administration to issue exemption decrees for the approximately 200 vehicles that were no longer in use, if the vehicles were turned over to the appropriate GOE agencies or to the Customs Administration. With regard to the other vehicles, numbering about 1,100 and which continue to be used on specific projects financed by AID, customs exemption decrees would be issued if the vehicles were turned over to a government agency or donated to the Customs Administration.

It was recognized later that such exemption decrees could only be issued by the Prime Minister. USAID/Egypt management officials who met with the Prime Minister stated that he would support issuing such decrees in order to clean up the backlog, and would support any necessary changes in the law to allow their exemption in the future without the need for a Prime Minister's decree. These actions could take care of the immediate problem of vehicles already in country, but do not solve the basic problem of exempting further USAID/Egypt-financed vehicles, as discussed on page 8.

Despite these and other positive cases that can be cited, two significant issues discussed below required further concern by USAID/Egypt.

2. Customs Duties Continue to be Paid by USAID/Egypt-Financed Contractors - The audit disclosed many cases in which USAID/Egypt-financed contractors paid customs duties in order to have commodities released from Customs. Project commodities were supposed to be imported duty free under the terms of the Bilateral Agreement. Contractors considered it expedient to pay the duties rather than wait a long time to get the commodities released duty free. Available records did not readily identify the frequency of these situations, but one contractor indicated it was not unusual to pay the duties in order to free up the

commodities in question. Contractors and/or USAID/Egypt, therefore, incurred unnecessary costs in carrying out the authorized development projects.

Discussion - One contractor, for example, reported paying \$5,531 in customs duty for eight shipments in order to get the goods released. A clearing agent for U.S. contractors confirmed that in many other cases it paid customs duties after approval of the consignees to do so. This agent gave three recent examples of duties paid in order to get shipments released for two different AID-financed projects. The amounts paid were \$588; \$382; and \$390. According to USAID/Egypt records, another USAID-financed contractor was asked recently to pay \$4,346 in customs duties for four shipments of project commodities that were released on a temporary rather than exempted basis about a year ago.

With respect to project commodities, the Bilateral Agreement says:

"Any supplies, material or equipment introduced into or acquired in the Arab Republic of Egypt by the Government of the United States of America, or any American contractor financed by that Government for purposes of any program or project conducted hereunder, shall, while such supplies, material or equipment are used in connection with such a program or project, be exempt from any taxes on ownership or use of property and any other taxes in the Arab Republic of Egypt, and the import, export, purchase, use, or disposition of any such supplies, material or equipment in connection with such a program or project shall be exempt from any tariffs, customs duties, import and export taxes, taxes on purchase or disposition of property, and other taxes or similar charges in the Arab Republic of Egypt."

Contractors with whom the auditors discussed these matters claimed that they absorbed the costs, and that customs duties were never billed to USAID/Egypt. This claim was not validated because of the great deal of audit work that would be involved. Whether the contractors absorbed the cost or passed it on to USAID/Egypt, the payment of customs duties violated the terms of the Bilateral Agreement and was unfair to the affected party.

In some cases, it was probably beneficial for contractors to pay duty rather than to wait and get the commodities duty free. The accumulation of storage charges at ports and the

penalties for delays can greatly outweigh the payment of customs duties if commodities are critical for the completion of the project. For example, an AID-financed contractor reportedly paid \$15,918 to the Alexandria Port Authority in storage charges due to the delay in releasing six shipments. 1/

The auditors discussed the payment of customs duties by U.S. contractors with the General Director of the Customs Administration. The Director said that any AID-financed contractor entitled to the exemption under the Bilateral Agreement could recover amounts paid as customs duties upon request, if the contractor proved that the exemption was deserved. The Director added that recoveries could be made on a case-by-case basis through USAID/Egypt. Recovery of duties paid does not deal effectively with the fact that duties should not have been assessed in the first place.

The audit disclosed no practicable way of totally avoiding customs problems because of the large number and diversity of transactions and the difficult and bureaucratic processes involved in importing goods for the USAID/Egypt program. Thus, the report makes no specific recommendations to avoid the payment of duties. The auditors believed, however, that continued efforts by the Mission were needed to protect the interests of the program and those of AID-financed contractors.

The existing Mission structure for handling customs problems has been effective recently and appears to be a way of interfacing with the GOE on customs issues. Project funds, however, should not be used to pay customs duties or other charges exempted by the Bilateral Agreement. USAID/Egypt-financed contractors should be reminded of this. Nor should AID-financed contractors bear such unnecessary costs. In cases where such costs have been paid, contractors should be encouraged to pursue refund claims through the Office of Project Support.

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1/ USAID/Egypt found that Decree No. 37 of the General Authority for the port of Alexandria, issued July 15, 1986, exempted goods arriving as gifts or assistance to Egyptian Government agencies from storage charges. USAID/Egypt-financed contractors were notified of this exemption and provided copies of the decree.

### Recommendation No. 1

We recommend that USAID/Egypt issue a notice to remind all USAID/Egypt-financed contractors that customs duties cannot be passed on to USAID/Egypt. This notice should encourage AID-financed contractors to request the Customs Administration, through USAID/Egypt, to reexamine such cases where duties were paid.

Management Comments - The Mission said that Contractor Notice 18-87, issued September 25, 1987, notified all current AID contractors, as well as Associate Directors, Office Directors and Project Officers, that AID funds may not be used to pay - or to reimburse payment of - customs duties. Contractors were also informed of this, and that recovery of duties paid could be sought from the Customs Administration with the assistance of USAID/Egypt. The Mission, therefore, requested that this audit recommendation be closed.

Office Of Inspector General Comments - In view of the action taken by USAID/Egypt, Recommendation No. 1 was closed upon issuance of this report.

3. Disagreements Exist With The GOE Customs Administration On Vehicle Customs Clearances - The Customs Administration has insisted on temporary release rather than exemption of AID-financed vehicles from customs duties on the basis that the Bilateral Agreement exemption did not cover vehicles. USAID/Egypt, however, interprets the words "supplies, material and equipment" in the Bilateral Agreement to provide exemption from duties and other taxes for all vehicles, including passenger vehicles. USAID/Egypt has not resolved this difference in interpretation or dealt with it effectively through administrative procedures. As a result, project vehicles have not been exempted from customs duties and contractors have encountered difficulties and incurred additional costs when attempting to turn over vehicles to the GOE at the completion of a project.

Discussion - Customs officials did not see any problems with releasing AID-financed vehicles on a temporary basis because these vehicles could be used during the life of the project. At project completion, the vehicles could either be retained by the GOE implementing agency, reexported, or turned over to the Customs Administration. GOE implementing agencies, however, have consistently refused to accept vehicles at project completion without a customs exemption because

duties imposed by the Customs Administration were higher than the vehicle's market value. As a result, contractors were required by Customs to pay the assessed duties. According to USAID/Egypt views, such payments would violate the Bilateral Agreement. Reexport of the AID-financed vehicles would be contrary to AID regulations.

As stated earlier, the problems with project vehicles stem from GOE Customs officials' interpretation of whether these vehicles are afforded duty-free status under the terms of the Bilateral Agreement. In our opinion, vehicles, whether they are passenger vehicles, vans, or station wagons, are equipment items necessary for project implementation and, therefore, should be exempted from customs duties as are other items of "...supplies, material and equipment." The key to this problem is clarification of the Bilateral Agreement; however, USAID/Egypt is reluctant to open discussions on the agreement for other reasons.

Project Support Office officials responsible for handling customs problems considered a viable alternative to seeking revision of the Bilateral Agreement was to establish the duty-free status of project vehicles in future project agreements. The auditors were persuaded that it was worth pursuing this course of action because the agreements are project specific and are ratified by the Peoples Assembly and implemented by issuance of specific Presidential decrees. Accordingly, these project agreements should carry more weight with Customs Administration officials.

Passenger vehicles have been the focal point of the customs problem for the GOE since 1983 when the GOE issued a regulation prohibiting importation of passenger vehicles over four cylinders by government agencies unless approved by the Prime Minister. Customs officials indicated that they would consider exempting other types of vehicles such as pick-ups, trucks, or 4-wheel drive vehicles, if necessary for the project. GOE officials have been concerned about the importation of AID-financed vehicles because some Customs officials believe that sedans are subject to misuse by GOE and contractor project officials.

In order to control the number of passenger vehicles being bought for projects, USAID/Egypt, in February 1982, issued Staff Notice No 82-11 which required approval of the Mission Director prior to importing passenger vehicles. Nevertheless, USAID/Egypt stated in an internal memorandum dated January 1987 that, "Since that time (February 1982),

AID financed the importation of several hundred of passenger vehicles but we are not aware of the Mission Director's approval of any of them nor of any project agreements mentioning the topic."

USAID/Egypt needs to ensure compliance with this notice and enforce the exemption which it believes is provided for under the Bilateral Agreement. These actions would ensure that only passenger vehicles approved by the Mission Director are imported, and probably reduce the number imported by USAID/Egypt. Enforcement of the Bilateral Agreement would mean that all vehicles imported would be free of duty, thereby making more effective and economical use of project resources and facilitating the transfer of vehicles at project completion.

#### Recommendation No. 2

We recommend that USAID/Egypt:

- a. include in all future project agreements appropriate language to provide specific exemption for vehicles from customs duties and other local taxes, and state specifically the number of vehicles needed for each project; and
- b. take appropriate management action to ensure compliance with Staff Notice No. 82-11 and other pertinent instructions issued with regard to vehicles.

Management Comments - Concerning the first part of Recommendation No. 2(a), the Legal Office was requested by the Project Support Office to provide a legal opinion concerning possible amendment of the Standard Provisions of project agreements to include language exempting vehicles, specifically passenger vehicles, from customs duties and other taxes.

The Legal Office responded it had two significant reservations about modifying future project agreements with the GOE so as to make explicit the inclusion of vehicles within the broad category of "supplies, material or equipment" entitled to duty-free importation.

These two reservations were stated as:

"(1) The current phrase - "supplies, materials or equipment" - is certainly intended by AID, worldwide, to apply to all imports of whatever type, if AID is doing the

financing. By adding explicit reference to one category of such imports - "vehicles" - we would be strengthening the possible argument from Customs that other categories not specifically listed, e.g., spare parts or consumable supplies, are not entitled to duty-free treatment."

"(2) Also, by seeking such explicit language in upcoming grant agreements, we imply weakness in our current position which I believe, is legally strong. That is, once we seek such new language, but before we obtain it as to each and every project, Customs could argue that projects with the "old" language clearly do not include duty-free treatment of vehicles; otherwise, why is AID seeking new language?"

The Legal Office suggested that this recommendation be closed and that the Mission proceed with an alternative approach of working with the Minister of Finance, apparently on a case-by-case basis, which could be evaluated after about a year.

Office Of Inspector General Comments - The alternative approach suggested by the Legal Office has been the way in which the Mission has operated for years. It is unreasonable to think that each time a vehicle is imported for an AID project that the Mission might have to seek the duty-free treatment already accorded to it under the Bilateral Agreement. Moreover, the Mission evidently misunderstood the report point. The report did not recommend changing the Worldwide Project Agreement Standard Provision Language. It simply recommended including in future project agreements with the GOE, appropriate language to provide exemption for vehicles from customs duties and other local taxes.

The real solution lies in clarifying the language of the Bilateral Agreement. The draft report submitted to the Mission for the exit conference included such a recommendation: "Amend the language of the Bilateral Agreement, if necessary, to incorporate specific exemption from customs duties and other taxes for vehicles."

In the exit conference, Mission officials explained that this was not a practical recommendation because the Mission and the Embassy were unwilling to renegotiate the Bilateral Agreement. One of the reasons mentioned was that the GOE would ask to change other provisions presently favoring the U.S. In view of the Mission's reluctance to amend the Agreement, we revised the report to include the suggestions presented by the Project Support Office in the exit

conference. This suggestion is the revised Recommendation No. 2(a) presented in this report, which we believe will strengthen the Mission's efforts in enforcing the exemption contained in the Bilateral Agreement.

The Mission also did not agree with the second part of Recommendation No. 2(a) which said that the number of vehicles needed for each project should be specifically stated in the Project Agreement. The Mission did not believe it was feasible nor would it would serve any useful purpose to do so. The Mission said it did not intend to implement this part of the recommendation.

The Mission's position again is surprising. In 1983, the Mission agreed that the number of vehicles would be stated specifically in future project agreements. The Mission Legal Advisor in his letter dated November 22, 1983, to the GOE Minister of Finance stated:

"I agreed that we would provide a list of those projects which are in the process of importing more than 10 such vehicles. For future projects, the Project Agreement will specifically state the number of such vehicles."

It is unclear why the Mission's position has changed. Projecting the number of vehicles needed for any project is not that difficult and is required for project procurement plans. Stating the number of vehicles in the project agreement will facilitate dealing with the Customs Administration because the agreement is project specific as opposed to the generally applicable Bilateral Agreement.

In view of the Mission's reluctance to take the recommended steps to alleviate the situation with respect to the importation of vehicles, Recommendation No. 2(a) will remain open until appropriate action has been taken.

Management Comments - The Mission agreed with Recommendation No. 2(b) and promised to rewrite Mission Order 5-8 within the next three months to provide more specific guidance to project officers on vehicle procurement, customs regulation and registration and monitoring of project vehicles. This Mission Order also will require the Mission Director's approval on sedan procurements. The Mission said it will issue a Contractor Notice simultaneously with the revised Mission Order. Over the next few months, USAID/Egypt said it also will be considering additional approaches to further

alleviate the problems associated with project vehicles in Egypt. The Mission requested closure of this part of the recommendation.

Office Of Inspector General Comments - We appreciate the Mission's planned actions which when implemented could satisfy the audit recommendation. Recommendation 2(b) will remain open until the promised Mission actions have been taken and reviewed by our office.

The full text of USAID/Egypt's response is contained as Appendix 1 to this report.

# memorandum

DATE: 10 November 1987

REPLY TO  
ATTN OF:

Marshall D. Brown, DIR

APPENDIX 1

Page 1 of 9

SUBJECT:

Draft Audit Report: Audit of Customs Problems Encountered  
under the Bilateral Agreement in Egypt (RIG/A/C-88-50)

TO:

Joseph Ferri, RIG/A/Cairo

USAID has reviewed the final draft of the subject report. Below please find our official response.

## Recommendation No. 1

We recommend that USAID/Egypt issue a notice to remind all USAID/Egypt-financed contractors that customs duties cannot be passed on to USAID/Egypt. This notice should encourage AID-financed contractors to request the Customs Administration, through USAID/Egypt, to reexamine such cases where duty was paid.

Contractor Notice 18-87, issued 25 September 1987, notified all current AID contractors, as well as Associate Directors, Office Directors and project officers, that AID funds may not be used to pay - or to reimburse payment of - customs duties. Contractors were also informed that recovery of duties paid could be sought from the Customs Administration with the assistance of USAID. A copy of Contractor Notice 18-87 is attached. We therefore request that this audit recommendation be closed.

## Recommendation No. 2

We recommend that USAID/Egypt:

- a. Include in all future project agreements appropriate language to provide specific exemption for vehicles from customs duties and other local taxes, and state specifically the number of vehicles needed for each project; and
- b. Take appropriate management action to ensure compliance with Staff Notice No. 82-11 and other pertinent instructions with regard to vehicles.

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With regard to Recommendation No. 2(a), USAID's Office of Project Support has requested advice of the Legal Office concerning possible amendment of the Standard Provisions of project agreements (ProAgs) to include language exempting vehicles, and specifically passenger vehicles, from customs duties and other taxes. A copy of this memo is attached. We will advise you of the answer received from the Legal Office.

USAID does not believe, however, that it is feasible nor that it would serve any useful purpose to state the number of vehicles needed for a project in the relevant project agreement. As you know, at the time a ProAg is signed, USAID has a reasonable estimate of the number of vehicles that will be needed for a project. However, if a specific number is stated in the ProAg, Customs may not allow the import of additional vehicles at a later date if project conditions change, as frequently occurs, and more vehicles are needed. Customs might then require a ProAg amendment prior to allowing the duty-free entry of vehicles beyond the stated amount. We would not want to become involved in amending a Pro Ag for such minor changes. Further, disaggregation of our project contributions to this level is normally and better contained in Project Implementation Letters or other implementing documents, thus providing flexibility to treat changes in detail as they occur. Therefore, USAID does not intend to implement this part of the recommendation.

With regard to Recommendation No. 2(b), USAID intends to do the following:

1. Mission Order No. 5-8, titled "Procurement and Accounting for Project-Funded Vehicles," will be re-written and re-issued within the next three months to provide more specific guidance to project officers and other USAID staff on vehicle procurement, customs regulations, vehicle registration and monitoring of project vehicles. Included in this Mission Order will be a ban on the import of sedans for use as project vehicles, unless separately justified and approved by the Mission Director, as set forth in Staff Notice No. 82-11.

2. A Contractor Notice will be issued simultaneously with revised Mission Order 5-8 to remind contractors of AID and mission procurement policies and regulations and their responsibilities with regard to procurement, registration and monitoring of project vehicles.

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Over the next few months, USAID will be considering additional approaches to further alleviate the problems associated with project vehicles in Egypt, including the following:.

1. Discussions with the Customs Administration will focus on granting exemption to AID-financed vans, pickups and trucks at the time of entry into Egypt which is not currently the practice. This would relieve AID contractors of the annual time-consuming process of renewing the temporary release and would eliminate the need for USAID and the GOE agencies to seek customs exemption at a later date.
2. Before approving the procurement of vehicles for ongoing projects, USAID may consider requiring the counterpart GOE agency to certify in writing that it will be responsible for obtaining, if required, a decree from the Prime Minister exempting the vehicles from customs duties and other taxes and for obtaining, if required, the Prime Minister's approval of the import of vehicles over four cylinders. This will place the responsibility of complying with GOE regulations on the counterpart agencies and reduce the administrative burden currently borne by USAID and AID-financed contractors.
3. Under new contracts for consulting and construction services, consideration will be given to requiring consultants and contractors to provide their own vehicles, either through purchase or lease of American manufactured vehicles, instead of providing them with project vehicles. This would reduce the number of vehicles requiring exemption from customs duties, as contractor-owned or leased vehicles, including sedans if desired, would enter Egypt under the system of temporary release and be re-exported at the close of the contract. This would also eliminate the frustration contractors currently face while trying to dispose of project vehicles at contract termination and the GOE agencies, on the other hand, would not be required to take possession of worn out vehicles.

We hope that the actions outlined above will meet the audit recommendations. In particular, we believe that Recommendation No. 2(b) can be closed on the current record, given our firm and detailed forward planning. Recommendation No. 1 is also appropriate for closure at

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this time. As to Recommendation No. 2(a), we expect, once Legal Office advice is in hand, to adopt a firm position on the basis of which that recommendation, also, can be closed. USAID staff will be happy to meet with you and to discuss any issues or questions you may have.

attachment: a/s

# USAID, Cairo

17-87

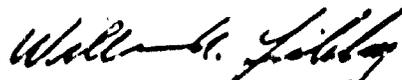
Payment of GOE Customs Duties

28 September 1987

AID contractors are reminded that since the Bilateral Agreement and subsequent project agreements exempt the AID program in Egypt from customs duties and other taxes, AID funds may not be used to pay - or to reimburse payment of - customs duties. Depending on the nature of the violation of this rule by an AID contractor, penalties range from a requirement to reimburse AID for costs improperly billed, to debarment or suspension, to criminal liability.

Contractors who have paid customs duties on commodities exempted under provisions of the Bilateral Agreement may seek recovery of those duties from the Customs Administration, according to the Customs Director. The Customs Administration has asked that all requests for recovery of customs duties be channelled through AID's Office of Project Support. Contractors interested in pursuing recovery of customs duties should contact Donella Russell or Ashraf Soos in the Office of Project Support at ext. 3348 or 3315.

William A. Libby



Office of Project Support

## memorandum

APPENDIX 1

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DATE: 8 November 1987

REPLY TO  
ATTN OF:Donella J. Russell, DR/PS *DR*

SUBJECT: Proposed Changes in Project Grant Standard Provisions

TO: Kevin O'Donnell, SLA

Thru: Frank Miller, OD/PS *FM*

A recent draft audit report - Audit of Customs Problems Encountered under the Bilateral Agreement in Egypt (RIG/A/C-88-50) - recommended, among other actions, the following:

Recommendation No. 2

We recommend that USAID/Egypt:

- a. Include in all future project agreements appropriate language to provide specific exemption for vehicles from customs duties and other local taxes, and state specifically the number of vehicles needed for each project...

Therefore, we would like to request that your office review for adoption the following addition (underlined in text) to Project Grant Standard Provisions Annex II. This addition reiterates the Bilateral Agreement exemption clause 5(a). [N.B. USAID does not intend to adopt the second part of this recommendation, i.e., to state the number of vehicles needed for a project in the ProAg.]

Section B.4 taxation

- (a) This Agreement and Grant will be free from any taxation or fees imposed under laws in effect in the territory of the Grantee.
- (b) In accordance with the Economic, Technical and Related Assistance Agreement (Presidential Decree No. 458/1978), between the Parties, any supplies, material or equipment, including all types of motor vehicles, introduced into or acquired in the territory of the Grantee by the Government of the United States, or any American contractor financed by that Government for

OPTIONAL FORM NO. 10  
REV. 1-81  
5010-104-01 (GPO) 1980  
5010-110

purposes of this Project, shall, while such supplies, material or equipment are used in connection with this Project, be exempt from any taxes on ownership or use of property and any other taxes in the territory of the Grantee, and the import, export, purchase, use, or disposition of any such supplies, material or equipment, including all types of motor vehicles, in connection with such a program or project shall be exempt from any tariffs, customs duties, import and export taxes, taxes on purchase or disposition of property, and other taxes or similar charges in the territory of the Grantee. No tax (whether in the nature of an income, profit, business, or other tax), duty, or fee of whatsoever nature shall be imposed upon any American contractor financed by the Government of the United States hereunder. For the purposes of this Agreement the term "American contractor" shall include individuals who are citizens or legal residents of the United States, corporations or partnerships organized under the laws of the United States, foreign corporations a majority of whose total stock is owned by United States shareholders, and joint ventures or unincorporated associations consisting entirely of individuals, corporations or partnerships which fit any of the foregoing categories.

- (c) To the extent that: (1) any contractor, including any consulting firm, any personnel of such contractor financed under the Grant, and any property or transaction relating to such contracts; and (2) any commodity procurement transaction financed under the Grant, are not exempt from identifiable taxes, tariffs, duties or other levies imposed under laws in effect in the territory of the Grantee, the Grantee will, as and to the extent provided in and pursuant to Project Implementation Letters, pay or reimburse the same with funds other than those provided under the Grant.

This office has previously suggested an alternative clause to (c) above which you may wish to consider, as well:

- (c) To the extent services related to the Project and funded by the Grant are performed by American contractors or consultants, the contractor, its subcontractors and those of their employees and families, who are not citizens of and ordinarily resident in the territory of the Grantee, shall, during the performance of such services in the territory of the Grantee, be exempt from any tariffs, customs duties, import and export taxes, taxes on the purchase, use or disposition of property, including motor vehicles, income and social insurance taxes and other taxes or similar fees or impositions

imposed by the Grantee within its territory. Should any such tariffs, duties, taxes, fees or similar impositions be paid, inadvertently or otherwise, by the aforementioned American contractors or consultants, their subcontractors or their non-Egyptian employees, the full amount so paid shall be promptly refunded by the Grantee. Any such refunds shall be made from funds other than those provided by the Grant.

For your information, I am attaching a copy of the subject audit report.

attachments: a/s

## memorandum

DATE November 15, 1987

REPLY TO  
ATTN OFSLA, Kevin O'Donnell *KFM*

APPENDIX 1

Page 9 of 9

SUBJECT:

Proposed Changes in Project Grant Standard Provisions

TO:

DR/PS, Donella Russell

NOV 18 REC'D

Ref. Your memo of November 8, 1987

You have asked for Legal Office views on responding to an audit recommendation that our future bilateral project agreements with the GOE be modified so as to make explicit the inclusion of vehicles within the broad category of "supplies, material or equipment" entitled to duty-free importation.

I appreciate that, in one sense, this approach would seem a solution to the problem addressed in the audit report, namely, that Customs officials do not always recognize that vehicles are intended to qualify under the current broad wording for duty-free treatment. However, I would have two significant reservations about such a new approach:

(1) The current phrase - "supplies, materials or equipment" - is certainly intended by AID, worldwide, to apply to all imports of whatever type, if AID is doing the financing. By adding explicit reference to one category of such imports - "vehicles" - we would be strengthening the possible argument from Customs that other categories not specifically listed, e.g., spare parts or consumable supplies, are not entitled to duty-free treatment. Nor does it seem workable to address this concern by listing, specifically, every conceivable category of imports.

(2) Also, by seeking such explicit language in upcoming grant agreements, we imply weakness in our current position which I believe, is legally strong. That is, once we seek such new language, but before we obtain it as to each and every project, Customs could argue that projects with the "old" language clearly do not include duty-free treatment of vehicles; otherwise, why is AID seeking new language?

As to whether we really do have a problem with vehicles, and if so how best to address it, I thought we were on the right track some months ago with our approach of seeking intervention of the Minister of Finance wherever we believe Customs is being unreasonable. In this regard, the Minister in effect, earlier this year, overturned the restrictive position of Customs and the Tax Office, respectively, on (a) duty-free treatment of spares and (b) Egyptian taxes as applicable to third-country expatriates. Thus, if we have a serious problem with Customs concerning duty-free treatment of vehicles, I believe we should work with the Minister. Only if that approach does not succeed should we (in my view) consider change in what, after all, is standard worldwide grant agreement language.

Assuming the Mission wishes to adopt the above-proposed strategy, I would suggest that the auditors be asked to close their recommendation on the current record. Progress with our alternative approach could be evaluated after, say, a year.

cc: DR/PS, F. Miller

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MAY 1962 EDITION  
GSA FPMR (41 CFR) 101-11.6  
5010-108

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