
**Committee of Experts on International
Cooperation in Tax Matters**

Nineteenth session

Geneva, 15-18 October 2019

Item 3 (j) of the provisional agenda

Taxation of official development assistance projects

Update on the work on the Tax Treatment of ODA Projects

Note by the Secretariat

Summary

This note is presented FOR DISCUSSION (and not for approval) at the nineteenth session of the Committee to be held in Geneva on 15-18 October 2019.

The note includes the draft revised version of the Guidelines on the Tax Treatment of ODA Projects that was attached to note [E/C.18/2019/CRP.6](#), which was presented for a first discussion at the Committee's eighteenth session (New York, 23-26 April 2019). It also includes in the Annex the written comments that were subsequently received on that previous note.

At its nineteenth session, the Committee is invited to continue its discussion of the attached revised Guidelines, focussing in particular on the written comments included in the Annex.

1. At the seventeenth session of the Committee (Geneva, 16-20 October 2018), the Committee decided that further work on the issue of the tax treatment of ODA projects should be carried out by a new Subcommittee on the Tax Treatment of Official Development Assistance (ODA) Projects, which was given the following mandate:

The Subcommittee is mandated to address the issues arising from the tax treatment of ODA projects and, in particular, to update and finalize the 2007 Draft Guidelines on the Tax Treatment of ODA projects that were attached to note E/C.18/2018/CRP.5, taking into account, among other things, the annotations included in that document and the written comments sent by Committee members. In carrying on that work, the Subcommittee shall

- Pay special attention to the experience of developing countries and of governmental and inter-governmental donor agencies.
- Ensure that its work draws upon and feeds into, as appropriate, the relevant work on the issue done in other fora, especially the Platform for Collaboration on Tax.

The aim of the Subcommittee shall be to present to the Committee a revised version of the 2007 Draft Guidelines for consideration with a view to their adoption at the first meeting of the Committee in 2020. Updates on the progress of the work shall be provided to the Committee at each preceding session. The Subcommittee may request the Secretariat to develop necessary inputs and provide necessary support within its resources.

2. At its eighteenth session (New York, 23-26 April 2019), the Committee had a first discussion of the draft revised guidelines included in note [E/C.18/2019/CRP.6](#), which took account of the decisions taken at the Subcommittee's first meeting held in London on 10-11-12 March 2019.

3. The discussion during that session focussed primarily on the introduction and on the section of the draft that included the guidelines. The following reflects the main substantive issues raised during the discussion:

- In response to concerns expressed by a Committee member regarding the exception to the principle of not requesting tax exemptions in cases where there are serious concerns about the payment of tax to a recipient country, it was agreed that further work was needed on the wording of the exception.
- Referring to guideline 2, another member of the Committee asked for a more balanced approach that would avoid what appeared to be a commitment by developing countries.
- A representative from ATAF suggested that guideline 13 be redrafted so as to avoid using the 183-day period as a proxy for the concept of permanent establishment. He indicated that ATAF would provide a draft of different wording for that purpose.

4. In response to the invitation included in paragraph 6 of note [E/C.18/2019/CRP.6](#), a number of written comments were subsequently sent on the note. These comments are included in the Annex.

5. At its nineteenth session on 15-18 October 2019, the Committee is invited to continue its discussion of the attached revised Guidelines, focussing in particular on the written comments included in the Annex. The Committee is also invited to ask Committee members and country observers wishing to send additional written comments on the attached note to do so by email to the Secretariat at taxcommittee@un.org before **31 January 2020**.

6. The Subcommittee intends to meet again before the April 2020 meeting of the Committee. Based on the discussion of this note at the Committee's April and October 2019 meetings and on the written comments already received and those that will be sent after the nineteenth session, the Subcommittee will then revise and complete the Guidelines for final discussion and approval at the Committee's twentieth session in April 2020.

GUIDELINES ON THE TAX TREATMENT OF ODA PROJECTS

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Executive Summary

The practice of granting tax exemptions with respect to official development assistance (ODA) projects is widespread among developing countries. A recent survey shows that such exemptions are most often provided with respect to value-added taxes, customs duties as well as corporate taxes, personal income taxes and payroll taxes, including taxes withheld at source. There are no reliable estimates of the overall tax revenues foregone through such exemptions.

The Addis Ababa Action Agenda, which includes a comprehensive set of measures aimed at addressing the challenges of financing the 2030 Sustainable Development Goals, includes a commitment to “consider not requesting tax exemptions on goods and services delivered as government-to-government aid, beginning with renouncing repayments of value-added taxes and import levies.”

This note includes a set of Guidelines that were developed by the United Nations Committee of Experts on International Cooperation in Tax Matters in light of this commitment. The Guidelines seek to facilitate the consideration of whether or not tax exemptions should be requested with respect to ODA projects.

These Guidelines recognize that while each donor is free to establish the conditions under which it is willing to provide ODA, it should recognize that tax exemptions create significant difficulties for developing countries and run counter to the objective of strengthening domestic resource mobilization.

The Guidelines suggest that where there is sufficient confidence in governance structures and in the tax system of a developing country, donors should be encouraged to refrain from requesting exemptions from tax for transactions relating to ODA projects in that country, unless the rules in the recipient country for taxing ODA-related transactions fail to comply with internationally recognized tax principles.

The Guidelines deal exclusively with the tax treatment of projects involving development assistance provided by governments and their aid agencies, including assistance provided through international governmental organizations. They incorporate a number of existing international tax principles that are reflected in multilateral instruments as well as in the network of bilateral tax treaties; they recommend that the tax treatment of transactions related to ODA projects comply with these principles.

The Guidelines are not binding in any way and are drafted in general terms to facilitate their understanding by people who have limited tax expertise. They have been prepared for purposes of assisting donors and developing countries in determining the appropriate tax treatment of ODA projects. The Guidelines should facilitate the discussion of tax issues between donors

and recipients of ODA. They should also avoid a proliferation of different rules, which would reduce transparency and increase the administrative and compliance burden of both donors and recipients. Since many donors already follow the policy of not requesting tax exemptions for the ODA that they provide, the Guidelines should promote a greater consistency in this area.

The Guidelines first deal with general considerations relevant to the issue of whether tax exemptions should be granted with respect to ODA projects. They recommend that donors should not require exemptions except to the extent that the tax rules of a recipient country are not consistent with the internationally recognized tax principles reflected in the Guidelines or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration of that country. As a quid pro quo for the donors not requesting exemptions, the Guidelines recommend that recipient countries ensure that their tax treatment of transactions relating to ODA projects be consistent with these internationally recognized tax principles. Guidelines 11 to 18 describe these principles in relation to the following:

- Income taxation – employment remuneration
- Income taxation – profits and payments to foreign enterprises
- Indirect taxation – humanitarian crises
- Indirect taxation – personal property and household goods of workers
- Indirect taxation – temporary admission

The Guidelines also address the situations where specific exemptions are requested for ODA projects. In that case, the Guidelines recommend that officials from the Ministry of Finance or the tax administration of the recipient country should be involved in the negotiation and drafting of these exemptions and that the recipient country should ensure that all legal requirements necessary to give force of law to these exemptions are satisfied. The Guidelines also provide that the relevant parts of any document providing for such exemptions be made publicly available. They also stress the importance of forecasting, and doing an analysis of, the foregone tax revenues resulting from these tax exemptions as well as using mechanisms that minimise administrative burdens and reduce fraud in relation to the application of these exemptions. Regardless of whether or not tax exemptions for transactions related to ODA projects are granted, the Guidelines also recommend that donors comply with the information and withholding tax requirements of recipient countries with respect to payments to taxable entities.

Detailed explanations on the Guidelines include a summary of the pros and cons of tax exemptions for ODA projects as well as a discussion of each of the Guidelines included in this note.

INTRODUCTION

1. The *Addis Ababa Action Agenda*,¹ which was endorsed by the UN General Assembly in its 2015,² includes a comprehensive set of concrete actions in order to address the challenges of financing and creating an enabling environment for the achievement of the 2030 Sustainable Development Goals. One of these actions deals with tax exemptions related to government-to-government assistance:

We will also consider not requesting tax exemptions on goods and services delivered as government-to-government aid, beginning with renouncing repayments of value-added taxes and import levies.³

2. The Guidelines included in this note were developed by the United Nations Committee of Experts on International Cooperation in Tax Matters in order to facilitate the consideration of whether or not tax exemptions should be requested with respect to international assistance projects.

3. International assistance may be provided to a country by foreign governments, government-controlled agencies, international organizations, non-governmental organizations (NGOs), companies or individuals. Such assistance may be designed to facilitate development or reform, may respond to natural disasters or other humanitarian crises, may take the form of peacekeeping operations, or may advance other development or welfare purposes. It may take different forms, such as grants, concessional loans and goods or services provided in kind. It may result from bilateral or multilateral assistance projects. These Guidelines, however, apply exclusively to international assistance that is provided to a country or jurisdiction by the government of a foreign country (or its subdivisions or agencies) either directly or through a multilateral development institution. This corresponds to the concept of official development assistance (ODA),⁴ which is the term generally used in these Guidelines.

1 United Nations, *Addis Ababa Action Agenda of the Third International Conference on Financing for Development (Addis Ababa Action Agenda)*, final text of the outcome document adopted at the Third International Conference on Financing for Development (Addis Ababa, Ethiopia, 13–16 July 2015).

2 Resolution 69/313 of 27 July 2015.

3 *Addis Ababa Action Agenda*, section C (International Development Cooperation), paragraph 58.

4 The concept of Official Development Assistance (ODA) was developed by the OECD Development Assistance Committee (DAC) for the purposes of measuring government-to-government assistance flows. The OECD provides the following general definition of ODA:

“ODA is the resource flows to countries and territories on the DAC List of ODA Recipients (<http://oe.cd/dac-list>) and to multilateral development institutions that are:

- i. Provided by official agencies, including state and local governments, or by their executive agencies; and
- ii. Concessional (i.e. grants and soft loans) and administered with the promotion of the economic development and welfare of developing countries as the main objective.”

The OECD also clarifies that ODA does not include “military aid and promotion of donor’s security interests” as well as assistance provided for “primarily commercial objectives e.g. export credits” (see OECD, *What is ODA?*, at <http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/What-is-ODA.pdf>).

4. Tax⁵ exemptions for various transactions under ODA projects are granted by many developing countries, typically at the insistence of donors. These exemptions apply in situations such as the following:

- Goods are imported by a non-resident on a temporary basis (possible exemption from customs duties, VAT and other indirect taxes);
- Goods are imported by a non-resident, but will not be re-exported (possible exemption from customs duties and VAT);
- Goods are imported by a resident, to be paid for using project funds (possible exemption from customs duties and VAT);
- Goods or services are purchased from a local supplier, using project funds (possible exemption from VAT);
- A non-resident individual comes to the country to provide services as an employee to be paid for using project funds (possible exemption from individual income tax and social contributions);
- A non-resident contractor provides services under a contract financed with project funds (possible exemption from income or corporate tax);
- A resident company (or a non-resident having a permanent establishment in the country) is hired to provide services to be financed using project funds (possible exemption from income or corporate tax);
- Resident individuals are hired to work for a resident or non-resident contractor with project funds (possible exemption from individual income tax and social contributions).

5. A recent publication of the African Tax Administration Forum, *The Taxation of Foreign Aid – Don't ask, Don't tell, Don't know*⁶ includes a list of common ODA exemptions⁷ and shows the extent to which the practice of granting tax exemptions with respect to ODA projects is widespread among developing countries. That publication, which reports the results of a survey of 20 developing countries (including 15 from sub-Saharan Africa), indicates that nearly all these countries (95%) provide tax exemptions for ODA with respect to value-added taxes while 85% provide tax exemptions with respect to customs duties and around 60% with respect to corporate taxes, personal income taxes and payroll taxes, including taxes withheld at source.⁸

5 In these Guidelines, references to “tax exemptions” cover exemptions from domestic taxation as well as exemptions from customs duties. These exemptions refer to any form of relief, whether total or partial. Also, references to indirect taxes generally refer to value-added taxes (VAT), goods and service taxes (GST) as well as broadly-based or specific sales and consumption taxes, including excise taxes

6 African Tax Administration Forum, *The Taxation of Foreign Aid – Don't ask, Don't tell, Don't know*, May 2018.

7 Id. Table 1, p. 10.

8 Id. p. 5.

The survey also indicates that in most countries, there are no published estimates of the tax revenues foregone through these exemptions.⁹

6. The tax rules applicable in developing countries will often provide for an exemption without the need for a specific exemption for ODA projects. For example, a non-resident importing goods which will be taken out of the country after being used for a project might qualify under the terms of a general customs regime for temporary imports. Also, a non-resident which provides services paid by a foreign donor without having a permanent establishment in the developing country where the work is carried on might not be subject to income or corporate taxes under the income tax legislation of that country or under the terms of a generally applicable tax treaty, again without specific reference to the ODA project.

7. Each donor is of course free to establish the conditions under which it is willing to provide ODA. Some donors may be concerned that the imposition of taxes would decrease resources available for development activities and that it would be difficult to rally domestic support for payment of taxes.

8. Donors should recognize, however, that tax exemptions create significant difficulties for developing countries and run counter to the objective of strengthening domestic resource mobilisation. One of the four principles for strengthening the effectiveness of development cooperation that were endorsed in 2011 by 161 countries through the Busan Partnership for Effective Development Co-operation is that co-operation “investments and efforts must have a lasting impact on eradicating poverty and reducing inequality, on sustainable development, *and on enhancing developing countries’ capacities, aligned with the priorities and policies set out by developing countries themselves*” [emphasis added].¹⁰

9. Donor countries, their aid agencies and the international organizations through which ODA is provided to a country should therefore refrain from requesting exemptions from tax for transactions relating to ODA projects in that country except to the extent that, and only as long as, the rules in the recipient country for taxing ODA-related transactions fail to comply with internationally recognized tax principles or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration that country.

SCOPE AND PURPOSES OF THE GUIDELINES

10. The Guidelines deal exclusively with the tax treatment of ODA provided by governments (including governments of political subdivisions and local governments) or their agencies, whether the ODA is provided directly or through international organizations (these governments, agencies and international organizations being collectively referred to as “donors”). While many of the recommendations formulated in the Guidelines could possibly

9 Id, p. 15.

10 Communiqué of the *Busan Partnership for Effective Development Co-Operation – Fourth High Level Forum on Aid Effectiveness*, Busan, Republic of Korea, 29 November-1 December 201, paragraph 11, available at <https://www.oecd.org/dac/effectiveness/49650173.pdf>.

apply to international assistance provided directly by NGOs, private assistance raises a distinctive set of issues and is therefore not addressed in these Guidelines. Also, to the extent that a project involves public and private funding, the Guidelines only apply to the extent that the public funding constitutes ODA.

11. The Guidelines incorporate a number of existing international tax principles that are reflected in multilateral instruments as well as in the network of bilateral tax treaties based on the OECD and UN Model Tax Conventions. The Guidelines recommend that the tax treatment of transactions related to ODA projects comply with these principles.

12. The Guidelines have been prepared for purposes of assisting donors and recipient countries in determining the appropriate tax treatment of ODA projects. The Guidelines should facilitate the discussion of tax issues between donors and recipients of ODA. They should also avoid a proliferation of different rules, which would reduce transparency and increase the administrative and compliance burden of both donors and recipients. Since some donors already follow the policy of not requesting tax exemptions for their ODA projects, the Guidelines will also promote a greater consistency in this area, thereby reducing situations where the tax administration of a developing country must administer different tax rules with respect to two or more donors, sometimes for their participation in the same development project.

13. Although these Guidelines are intended to be prospective, donors and recipient countries are encouraged to review existing agreements in the light of the Guidelines.

14. The Guidelines are not binding in any way and are drafted in general terms to facilitate their understanding by people who have limited tax expertise. Care should therefore be taken when incorporating their principles in binding instruments. To the extent that the Guidelines reflect what is already found in the domestic laws of recipient countries or in relevant treaties (including tax treaties) concluded by these countries, there is no need to adopt them through legally binding instruments. It is recognized, however, that the existing network of tax treaties is far from comprehensive, especially as regards developing countries, and that a large number of countries are not yet parties to the multilateral instruments in the field of indirect taxes that are referred to in these Guidelines. One possibility would be for a recipient country to unilaterally ensure (e.g. through legislative changes) that ODA projects are taxed in accordance with these Guidelines. Alternatively, a recipient country could implement the principles reflected in these Guidelines through bilateral instruments that would be given force of law in that country.

GUIDELINES

A. *General considerations*

1. Donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should not require exemptions from the taxes levied in recipient countries with respect to transactions relating to ODA projects, except to the extent that the tax rules in the recipient country that would apply to these transactions are

not consistent with these Guidelines or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration of that country.

2. Recipient countries should ensure that their tax treatment of transactions relating to ODA projects is consistent with these Guidelines.
3. Recipient countries as well as donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should make every effort to ensure that officials from the Ministry of Finance or the tax administration of the recipient country are involved in the negotiation and drafting of any provisions dealing with the tax treatment of transactions related to ODA projects, including where another ministry or government agency is taking the lead in the negotiation of any agreement, letter, memorandum of understanding or other document that will include such provisions. Unless expressly agreed otherwise, these provisions should deal exclusively with the tax treatment of the donor countries, their aid agencies as well as international governmental organizations through which ODA is provided and should not extend to other parties such as subcontractors.
4. The recipient country should ensure that all legal requirements necessary to give force of law to any agreement, letter, memorandum of understanding, or other document dealing with the tax treatment of transactions related to ODA projects are satisfied. Recipient countries as well as donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should ensure that the parts of any such agreement, letter, memorandum of understanding or other document that relates to the tax treatment of transactions related to ODA projects are publicly available.
5. Where tax exemptions for transactions related to ODA projects are granted, recipient countries should make every effort to forecast the revenue impact of these exemptions and to do a tax expenditure review of them.
6. Where tax exemptions for transactions related to ODA projects are granted, countries are encouraged to use mechanisms that minimise administrative burdens and reduce fraud.
7. For instance, where it is considered that tax relief from indirect taxes, including customs duties, must be granted with respect to goods or services used or supplied in relation to an ODA project of a country, aid agency or international governmental organization in cases other than those described in the above Guidelines, the taxes covered by the relief should be clearly identified, using where possible the tax terminology of the recipient country, and the relief should be
 - a) restricted to clearly identified goods and services that are strictly necessary for the purposes of the project, and
 - b) in the case of goods and services to be acquired specifically for that project, restricted to goods and services that are not available in the recipient country.
8. Also, where such relief from indirect taxes, including custom duties, is granted with respect to goods and services used in relation to an ODA project, that relief should be granted through a refund or voucher method and, in the case of imported goods, through an automated customs management system rather than through a direct exemption processed manually. The tax administration of the recipient country should also adopt

procedures to ensure that goods and services on which indirect tax will be relieved are used for the purpose of the relevant project.

9. Any agreement concerning such relief from indirect taxes, including custom duties, with respect to goods used in relation to an ODA project should stipulate that when the relevant goods are disposed of in the recipient country or otherwise diverted from their intended purpose, the general domestic rules on disposal or diversion apply equally to these goods, in particular with respect to procedural aspects and the imposition of duties, taxes, interest and penalties in case of disposal or diversion.
10. Regardless of whether or not tax exemptions for transactions related to ODA projects are granted, donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should comply with the information and withholding tax requirements of recipient countries with respect to payments to taxable entities made in relation to these projects.

B. *Internationally-recognized tax principles applicable to ODA projects*

Part B of the Guidelines describes internationally-recognized tax principles that donor countries, their aid agencies as well as international governmental organizations through which ODA is provided may expect recipient countries to follow. As indicated in Guideline 1, tax exemptions for ODA projects are justified to the extent that the tax rules in the recipient country are not consistent with these principles.

a) *Income taxation – employment remuneration*

11. The remuneration, including employment-related benefits, for employment services related to an ODA project that an individual derives from that individual's employment by the government of the country or agency thereof that finances that project should not be taxable in the recipient country if the individual
 - a) is not a national of that jurisdiction, and
 - b) is not a resident of that jurisdiction or became a resident solely for the purposes of rendering these services.
12. The remuneration, including employment-related benefits, that an individual to whom Guideline 11 does not apply derives from employment services related to an ODA project of a country, aid agency or international governmental organization, should not be taxable in the recipient country if all the following conditions are met:
 - a) the individual is not a resident of the recipient country,
 - b) during the project, the individual is not present in the recipient country for a period or periods exceeding in the aggregate 183 days in any twelve-month period beginning or ending in the relevant tax year;
 - c) the remuneration is paid by, or on behalf of, an employer who is not a resident of the recipient country, and
 - d) that remuneration is not borne by a permanent establishment which the employer has in that country.

b) *Income taxation – profits and payments to foreign enterprises*

13. Payments that a country, aid agency or international governmental organization makes in connection with an ODA project to an enterprise that is not an enterprise of the recipient country, as well as profits derived by that enterprise from activities exercised in connection with that project, should not be subject to any income or corporate tax in the recipient country unless such payments or profits are attributable to activities carried on in the recipient country during a period or periods exceeding in the aggregate 183 days in any twelve month period beginning or ending in the relevant tax year or are attributable to the activities carried on in the recipient country by the enterprise of a self-employed person who is present person in that country during a period or periods exceeding in the aggregate 183 days in any twelve month period beginning or ending in the relevant tax year.

Note by the Secretariat

Guideline 12 will need to be reviewed once the work on taxation and the digitalization of the economy has been completed in order to ensure that it properly reflects situations where source taxation rights are typically recognized.

14. Any specific exemption from income or corporate tax granted with respect to activities of enterprises that carry on activities in connection with an ODA project:
- a) should not be available to enterprises of the recipient country, and
 - b) should be designed in a way that does not result in an unintended exemption of a foreign enterprise in its state of residence.

c) *Indirect taxation - humanitarian crises*

15. No indirect taxes, including custom duties, should be imposed on the import of goods to be used to respond to humanitarian crises such as natural disasters, famine, or health emergencies. For that purpose, countries should implement the rules of, or become parties to,
- a) Chapter 5 (Relief Consignments) of the Specific Annex J to the *International Convention on the simplification and harmonization of Customs procedures*, as amended (commonly referred to as “the Revised Kyoto Convention”), and
 - b) Annex B.9 (Concerning goods imported for humanitarian purposes) to the *Convention on temporary admission* (commonly referred to as “the Istanbul Convention”).
16. Goods that are provided domestically to, or imported by, a foreign country, aid agency or international governmental organization for direct use in response to a humanitarian crisis, and services closely connected with such supplies, that would – if imported - qualify as “relief consignments” or “goods for humanitarian purposes” for import duty and tax exemption on temporary admission, should be relieved from domestic indirect taxes.

d) *Indirect taxation – personal property and household goods of workers*

17. Personal property and household goods of workers coming to a recipient country for the purpose of an ODA project should be exempt from indirect taxes, including customs duties, as long as these workers' stay is merely temporary and is related to that project.

e) *Indirect taxation – temporary admission*

18. No indirect taxes, including customs duties, should be imposed on the temporary admission of goods to be used for the purposes of an ODA project. For that purpose, countries should implement the rules of, or become parties to,
- a) Chapter 1 (Temporary Admission) of the Specific Annex G to the Revised Kyoto Convention”), and
 - b) the parts of the *Convention on temporary admission* (commonly referred to as “the Istanbul Convention”) that relate to temporary admission of certain goods.

EXPLANATIONS ON THE GUIDELINES

A. *General considerations*

1. *Donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should not require exemptions from the taxes levied in recipient countries with respect to transactions relating to official development assistance (ODA) projects, except to the extent that the tax rules in the recipient country that would apply to these transactions are not consistent with these Guidelines or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration of that country.*

15. Until recently, donors were traditionally reluctant to agree to the recipient country's imposition of taxes in connection with their ODA projects. This might be because they consider that the effectiveness of the funds that they allocate to ODA will be greater if no part of these funds is diverted towards general budgetary support of the recipient country. It might also be, in some cases, that donors may actively oppose providing any financial assistance to the government that can be used directly for general budgetary purposes as they do not support certain expenditures financed by the regular budget. For example, the donor may be responding to a humanitarian crisis and providing support directly to refugees, but may wish to provide no support to the government. Such an unwillingness to provide general budgetary support to the recipient may arise from any number of foreign policy reasons, or might relate, for example, to a judgment by the donor that the recipient's public expenditure management framework is so flawed (e.g., involving substantial corruption) that direct budgetary support runs the risk of being largely wasted or diverted. Another possible reason for a reluctance to finance taxes in the recipient country is a concern that the recipient's tax policy is unreasonable in some way, e.g. as regards rates of taxation, which may be unusually high; as regards the determination of the tax base, which could be different from usual standards applicable to such taxes; or as regards some discriminatory feature of the tax.

16. These reasons, however, must be reviewed in light of global efforts to strengthen domestic resource mobilization and, in particular, of the commitment, included in the Addis Ababa Action Agenda, to “consider not requesting tax exemptions on goods and services delivered as government-to-government aid”.¹¹.

17. Concerns that a donor may have about public expenditure management in the recipient country may be warranted in some countries. However, a number of recipient countries have made substantial progress in this area. This suggests that, to the extent that the main concern of a donor is weak public expenditure management (e.g. a donor may feel that any direct budgetary support through the payment of taxes would be vulnerable to corruption and mismanagement), this concern can be addressed on a case-by-case basis by reviewing the situation in the particular countries to which the donor is providing ODA. A review of the public expenditure management framework and an assessment of the performance of a tax administration of a recipient country could convince donors that this concern has been satisfied. Such a review could take advantage of the initiatives currently under way in a number of countries with the participation of the IMF, World Bank and other agencies.

18. Support for domestic resource mobilization efforts has become an increasingly important part of overall ODA over recent years. This increased willingness to provide support for increasing tax revenues points to a potential incoherence in simultaneously insisting on tax exemptions. It is hard to find a convincing rationale for a donor who would provide financial support for domestic resource mobilization while simultaneously insisting on tax exemptions, since the same mix of support can be provided without any exemptions by reducing the level of financial support.

19. The substantial changes that have been made to the tax systems of developing countries in recent years must also be taken into account. As a general matter, the level of tax rates has come down. Income tax rates in virtually all developing countries are much lower than they were, say, 30 years ago. Likewise, tariffs have been reduced or eliminated. As far as the assertion of tax jurisdiction is concerned, many developing countries have unilaterally retrenched their taxing jurisdiction to what would be typically be permitted under bilateral tax treaties. To the extent that a concern may remain about the tax system of a recipient country, the remedy might lie not in total exemption from tax of activities financed by ODA but a more limited exemption as would be called for under generally-recognized international tax principles.

20. Moreover, the problems that the administration of tax exemptions for ODA projects create for recipient countries should be taken into account.

21. First, given the weakness of tax and customs administrations in many countries that are recipients of ODA, fraud is always a concern where tax exemptions are made available. Where tax or customs exemptions are granted, there is a substantial possibility of abuse of such exemptions. The abuse is likely to be more serious for indirect taxes. In the case of direct taxes,

11 See paragraph 1.

a typical issue is whether a particular contractor pays tax on its income from a project. The amount of tax at stake is relatively contained. However, in the case of indirect taxes, goods that have entered the country on an exempt basis can find their way into domestic commerce. If there is fraud in customs, all kinds of goods might be allowed to enter without paying VAT or customs duty, even though these goods should not actually qualify for exemption. The volume of goods involved might be several times the amount of the actual assistance. Depending on how the exemption is administered, fraud may well also arise from exempting local purchases from VAT. If the contractor is allowed to make purchases VAT-free upon presentation of an exemption card, the exemption is likely to be abused. Given the significant size of ODA, this potential for tax fraud can have a significant adverse effect on the domestic tax system.

22. Second, tax exemptions impose administrative costs on the tax administrations of recipient countries which need to keep track of the various exemptions provided and implement them. This difficulty is amplified by the diversity of the practices and expectations of the multiple donors that recipient countries may need to deal with. The administrative burden and the risk of fraud can vary depending on the way that exemptions are structured. Reducing this burden and risk of fraud for recipient countries is one of the factors that have motivated some donors to review their policy concerning tax exemptions.

23. Third, the granting of tax exemptions can raise legal issues. In some countries, there is no proper legal basis for exemptions, i.e. they might be based on agreements that do not have the force of law. Even where a duly ratified treaty or law establishes exemptions, there are often difficulties of interpretation arising from vague drafting, particularly where the exemptions are provided in laws separate from, and not properly integrated with, the tax laws. These difficulties are compounded where the Ministry of Finance and the tax authorities are not consulted prior to the granting of the tax exemptions and have not been involved in the drafting of the relevant legal provisions. Also, where issues of interpretation arise, it is often not clear how disputes should be resolved, i.e. whether courts of the recipient country should be the final arbiters of such disputes. Many developing countries would be wary of allowing foreign courts or arbitrators decide disputes concerning their own taxes.

24. Fourth, tax exemptions can cause economic distortions detrimental to domestic production in recipient countries. If, for example, imported goods to be used for an ODA project are exempt, but no exemption is available for domestic purchases, then there will be a distortion in favor of imports.

25. Fifth, depending on how they are structured, tax exemptions can result in substantial transaction costs. Because policies on seeking tax exemptions may differ from donor to donor, officials in recipient countries need to familiarise themselves with various requirements, which can be confusing and complex particularly if the tax administration is weak. Since these policies are superimposed on an existing legal framework, new legal issues may be presented (for example, whether a particular charge constitutes a “tax” which is eligible for exemption, or is instead a fee or user charge which is not eligible for exemption). In the case of VAT, exemptions tend not to work well, since they require the complex allocation of input credits (this would not be required if the exemption took the form of zero rating, but then the problem

would be the creation of VAT refund claims on the part of suppliers, which places a strain on weak tax administrations). There will also be substantial costs in terms of administrative overhead (legal, monitoring and budgetary) on the part of the donor (the donor's budget rules may prohibit financing of taxes, which will require checking reimbursable expenses to see whether they include taxes; agreements need to be drafted and contracts reviewed). Where problems arise, human resources have to be devoted to deal with them. In other words, the requirement to operate a special regime, as compared with the generally applicable tax regime, makes the contracts in question more expensive to administer.

26. Finally, granting tax exemptions to any market participants always runs the risk of creating pressures for further exemptions, whether directly as a means of alleviating competitive distortions that the initial exemption created or indirectly by creating a precedent that others can call on. Many recipient countries already find it hard to resist the pressure to grant specific tax exemptions when prospective private sector investors ask for such exemptions as an encouragement to invest on their territory. In addition, some recipient countries have complained that even where a donor agrees to finance the payment of tax with respect to a specific ODA project, consultants who are bidding to execute the project are requesting tax exemptions simply because they have obtained exemptions for similar projects and wrongly assume that being exempt from tax with respect to income derived from ODA projects is the norm. Many donors have actually urged developing countries to cut back on exemptions in their wider tax systems in order to strengthen domestic resource mobilization. This does not sit comfortably with continuing to press for exemptions for ODA projects.

27. These difficulties that tax exemptions pose for recipient countries often undermine the development objectives that the aid itself is intended to serve. The increase in ODA that is contemplated by the Addis Ababa Action Agenda will amplify these difficulties.

28. These difficulties combined with the improvement of tax systems in developing countries and a greater recognition of the need for strengthening domestic resource mobilisation have led to a growing acceptance of the principle that the general rules of taxation should apply to ODA projects. For instance, in 2004, the World Bank changed its policy to allow financing of reasonable, non-discriminatory tax costs. Recipient countries do not have to provide exemptions for Bank-financed projects, where their taxation system has been determined to be a reasonable one for purposes of this policy. The determination by the World Bank as to which taxes are treated as costs that can be financed by loans is made on a country-by-country basis as part of the Bank's overall country assistance strategy. Thus far, experience with applying the policy shows that in only very limited cases are taxes found to be unreasonable and therefore ineligible for Bank financing. The net result is that virtually all taxes have been considered as eligible for financing (of course, if a country were to introduce an unreasonably high tax, the Bank could consider it ineligible). The Inter-American Development Bank (IDB) and Asian Development Bank (ADB) subsequently adopted similar policies. Similarly, the French Development Agency (*Agence Française de Développement* or AFD) has for a number of years included in certain aid agreements the financing of taxes. Development agencies in

other countries, such as the United Kingdom, Norway, the Netherlands and Belgium, have adopted a similar policy.

29. Guidelines 1 and 2 endorse that approach. They recognize, however, that in some cases, there may be valid reasons for insisting on tax exemptions despite the various developments and considerations described above. This would be the case to the extent that the tax rules of the recipient country are not consistent with the internationally recognized tax principles reflected in the Guidelines. Also, in exceptional cases, exemptions might be justified to address serious concerns with the payment of tax to a country resulting from a review of the governance structure, tax system or tax administration of that country. One example would be where the governance structure of the recipient country is such that there is a serious risk that taxes paid with respect to the ODA project would be diverted to uses that the donor would clearly disapprove. Another example would be where the tax system of the recipient country seeks to levy taxes that are discriminatory or are clearly excessive (as regards their rate or structure) compared to what similar countries would levy in similar circumstances. A third example would be where corruption in the tax administration of the recipient country would be so endemic that it would likely result in a large part of the taxes paid not being available to finance the budgetary expenditures of that country.

30. Where such considerations justify a request for tax exemptions, donors should adopt a targeted approach and, where possible, restrict the exemptions to situations where these considerations are relevant. There is no reason why a tax exemption needs to be extended on a blanket basis. It can be tailored to minimize the difficulties for the recipient country.

31. It is recognized that circumstances may change to the point where a donor country's assessment of the governance structure, tax system or tax administration of a recipient country may no longer justify paying taxes to that country. Also, serious deficiencies in the governance structure, tax system or tax administration of a recipient country may only appear during the implementation of a project. In these cases, the donor country will of course be entitled to require tax exemptions as a condition for continuing its assistance project. It may also suspend disbursements, or even the implementation of the project, until these deficiencies are addressed.

32. In the case of donors that operate in many countries, it would be cumbersome to look at the details of the governance structure and the tax regime in each country. It would, however, be a duplication of effort for each donor to carry out such a review on its own. Also, where different donors are involved in the same assistance project, applying a different tax treatment to their respective contributions raises equity and administrative issues. This raises the question as to whether internationally agreed standards could be applied to the tax treatment of all ODA. Unfortunately, it would be quite difficult to agree internationally on such standards and cumbersome to establish procedures for their application to each recipient country. Necessarily, judgment is involved and accordingly the best approach may simply be to leave this determination to each donor concerned. Duplication of effort can, however, be minimized if both donors and recipients share information. If the decisions reached are shared among donors, together with any responses that the authorities wished to make in the case of taxes

considered unreasonable, then all could benefit from the analysis carried out. The intention would not be to pass a judgement on the wider quality of a country's tax system but simply to make it easier for donors to conclude that taxes in a particular country are (or are not) broadly in line with normal international practice, and hence create some presumption that they should be allowed to apply to ODA projects. In practice, therefore — and as is to some degree already the case in relation to public expenditure management systems — donors could rely on reviews carried out by others, to the extent that those reviews are supported by credible documentation and analysis. The public disclosure of the tax-related provisions of agreements concluded between donors and recipient countries, as suggested in Guideline 4, will contribute to this sharing of information.

33. If, despite the above considerations, the donor simply is unwilling to provide general budgetary support through the payment of taxes, the recipient country may have little choice than to accept the granting of tax exemptions. In such a case, however, it will still be important to take account of the procedural and administrative concerns reflected in these Guidelines.

2. *Recipient countries should ensure that their tax treatment of transactions relating to ODA projects is consistent with these Guidelines.*

34. As a quid pro quo for donors not insisting in specific tax exemptions for ODA projects, recipient countries need to ensure that their tax treatment of transactions related to these projects is consistent with principles that are typically incorporated in widely-agreed international instruments. These Guidelines include a list of such principles.

3. *Recipient countries as well as donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should make every effort to ensure that officials from the Ministry of Finance or the tax administration of the recipient country are involved in the negotiation and drafting of any provisions dealing with the tax treatment of transactions related to ODA projects, including where another ministry or government agency is taking the lead in the negotiation of any agreement, letter, memorandum of understanding or other document that will include such provisions. Unless expressly agreed otherwise, these provisions should deal exclusively with the tax treatment of the donor countries, their aid agencies as well as international governmental organizations through which ODA is provided and should not extend to other parties such as subcontractors.*

35. Guidelines 3 to 9 deal with procedural aspects related to the drafting and implementation of specific tax provisions related to ODA projects in case it is decided to agree bilaterally on such provisions.

36. Agreements covering ODA projects are often negotiated between representatives of the country, aid agency or international governmental organizations providing ODA and officials of the recipient country. Depending on the nature of the project, these officials might represent different ministries of the government of that country. There is no guarantee, however, that officials representing the tax authorities of that country will be consulted.

37. Given the technicality of tax legislation, the special procedural rules that might apply to the adoption of such legislation and the need to take account of administrative tax concerns, it is important that officials representing the tax authorities of a recipient country be involved in the negotiation and drafting of any specific tax provision dealing with ODA projects even if another ministry or government agency is taking the lead in the negotiations. Both the recipient countries and the donors should therefore insist that officials representing the tax authorities of the recipient country be involved in the negotiation and drafting of these provisions.

38. Whether these officials should come from the Ministry of Finance or the tax administration of the recipient country or from both is a matter that should be decided by that country taking into account the various responsibilities that have been granted to its tax administration. The officials that should be involved are those that would normally be responsible for designing tax rules applicable to foreign taxpayers. In many cases, these would be officials of the Ministry of Finance. In some jurisdictions, however, the tax administration has the responsibility of designing and implementing tax legislation; in such a case, it would seem appropriate to have representatives from the tax administration involved in the negotiation and drafting of provisions dealing with the tax treatment of ODA projects. Regardless of which tax officials are involved, it will be important for officials from the Ministry of Finance and the tax administration of the recipient country to liaise and cooperate as regards both the negotiation and the implementation of these provisions. Also, since the tax exemptions might cover different types of taxes that may be administered by separate parts of the tax administration, it would be necessary for the recipient country to ensure that all relevant parts of its tax administration are consulted.

39. Guideline 3 also provides that the provisions granting tax exemptions to donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should not be interpreted as extending to other parties, such as subcontractors, unless such extension is clearly provided for. Donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should make sure that the private parties involved in the implementation of ODA projects do not wrongly assume that they are entitled to the same exemptions and that these private parties do not try to obtain such exemptions from the recipient countries.

4. *The recipient country should ensure that all legal requirements necessary to give force of law to any agreement, letter, memorandum of understanding, or other document dealing with the tax treatment of transactions related to ODA projects are satisfied. Recipient countries as well as donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should ensure that the parts of any such agreement, letter, memorandum of understanding or other document that relates to the tax treatment of transactions related to ODA projects are publicly available.*

40. Tax exemptions for ODA projects may be provided through a variety of legal instruments and may require different administrative practices being applied to a substantial number of different transactions in the context of each country's general tax rules. Exemptions might be

granted, for example, through specific exemptions in domestic law directed to international assistance, through bilateral agreements, letters or memoranda of understanding.

41. In many countries, however, the constitution or the law impose restrictions as to how tax provisions may be adopted. Frequently, there will be rules according to which any tax charge or tax exemption must be authorized by law in order to be enforceable. Such rules will often apply regardless of the instrument in which the tax exemption is granted (e.g. a bilateral treaty, memorandum of understanding or any form of bilateral agreement).

42. There have been cases where tax exemptions included in a bilateral agreement concluded between a donor and the government of a recipient country have been found not to be enforceable because such rules had not been complied with. It is therefore necessary to ensure that any agreements providing for tax exemptions with respect to an ODA project will be implemented in accordance with these rules. In cases where tax exemptions for transactions related to ODA projects are contemplated, the parties are encouraged to use legal instruments that support the rule of law in recipient countries by:

- Making sure that the exemption is provided by law or, if provided under agreements, that the agreements are authorized by law;
- Identifying with specificity the transactions benefiting from exemption, the applicable taxes, and the conditions for benefiting from exemption.

43. Participation of the appropriate officials from the Ministry of Finance or tax administration in the negotiation of these exemptions will often be the best way of ensuring that this is done.

44. Giving force of law to exemptions with respect to subnational taxes may require the involvement of subnational governments. It should not be assumed that generally-worded exemptions apply to subnational taxes.

45. The transparency of the legal provisions granting tax exemptions is crucial. The parts of any agreement, letter, memorandum of understanding or other document that relate to the tax treatment of transactions related to ODA projects should be made publicly available. This should be agreed to by the recipient countries as well as the donors.¹² For example, the United States has long followed the practice of publishing the treaties and agreements through which it secures tax exemptions for the ODA that it provides, which facilitates the identification of potential risks of tax avoidance.¹³

12 ATAF suggests that the publication of the entire ODA project agreement, and not only the parts thereof dealing with taxation, could be done directly by donors or through a central repository such as the one through which the International Aid Transparency Initiative (IATI) already provides information on ODA projects. See *The Taxation of Foreign Aid – Don't ask, Don't tell, Don't know*, supra note 6, at page 2.

13 Id. at page 18, which includes an example of non-taxation resulting from a personal tax exemption granted with respect to ODA which was identified because of the publication of such an agreement by the United States.

46. Publication of a recipient country's laws on its web site may contribute to making legal provisions granting tax exemptions to ODA projects publicly available. Similarly, the registration of a country's treaties envisaged by Article 102 of the United Nations Charter will contribute to the public disclosure of the tax exemptions that are included in treaties.

5. *Where tax exemptions for transactions related to ODA projects are granted, recipient countries should make every effort to forecast the revenue impact of these exemptions and to do a tax expenditure review of them.*

47. Also, to provide the transparency and information needed for policy making and public discussion, recipient countries should seek to forecast the amount of tax revenues that will be lost as a result of these exemptions. They should also consider preparing and publishing tax expenditure analyses indicating the tax actually foregone as a consequence of exemptions granted with respect to foreign assistance. The application of exemptions through a system of vouchers or refunds (see below) would facilitate the preparation of such tax expenditure analyses.

48. Clearly, however, the extent to which a country will be able to correctly forecast and report on the foregone tax revenues resulting from tax exemption for ODA projects will depend on its administrative capacity.

6. *Where tax exemptions for transactions related to ODA projects are granted, countries are encouraged to use mechanisms that minimise administrative burdens and reduce fraud.*

49. Where it has been agreed to exempt from tax transactions related to ODA projects, it is important to do so in a way that minimize the burden, for the recipient country, of administering that exemption while, at the same time, minimizing the scope for tax fraud.

50. Guidelines 7 to 9 provide guidance as to how this may be done in the area of indirect taxes and customs duties. As regards reliefs related to direct taxes, requiring taxpayers to declare the income received that is subject to an exemption and to identify the provisions under which the exemption is claimed facilitates risk-management of tax audits as well as the calculation of the amount of foregone tax revenues attributable to this type of tax exemption.

7. *For instance, where it is considered that tax relief from indirect taxes, including customs duties, must be granted with respect to goods or services used or supplied in relation to an ODA project of a country, aid agency or international governmental organization in cases other than those described in the above Guidelines, the taxes covered by the relief should be clearly identified, using where possible the tax terminology of the recipient country, and the relief should be*
 - a) *restricted to clearly identified goods and services that are strictly necessary for the purposes of the project, and*
 - b) *in the case of goods and services to be acquired specifically for that project, restricted to goods and services that are not available in the recipient country.*

51. Guidelines 7 to 9 deal with the drafting and implementation of specific provisions for the relief from indirect taxes, including import duties, with respect to goods and services related to ODA projects. These Guidelines should apply when it is decided that the recipient country should grant relief beyond the situations dealt with through subsequent Guidelines dealing with indirect taxes.

52. Tax exemptions from indirect taxes and import duties that are currently found in bilateral agreements are often worded too broadly. Many of these agreements fail to clearly identify the type of goods that qualify for the exemption otherwise than by reference to general terms such as “equipment”, “instruments”, “machinery”, or even broader terms such as “supplies”, “assets” or “resources”, albeit limited to what is “necessary” to carry out the project, or is “financed by” the donor. In some agreements, the latter reference is in fact the only limitation to the scope of the exemption.

53. If it is considered that a tax exemption from indirect taxes, including custom duties, must be granted with respect to goods used or supplied in the context of ODA projects, it is paramount that from the outset there be as little doubt as possible as to which goods qualify for exemption. Indeed, whereas initially both parties may have a clear idea of what qualifies for exemption, that understanding may often change over time. A clearly and unambiguously defined scope of application is also a prerequisite for efficient administration by the recipient country’s authorities. The goods for which an exemption is made available should therefore be clearly identified by the agreement; preferably the agreement, or an annex thereto, should list the goods or categories of goods concerned, ideally by reference to their HS classification code.

54. Especially for materials that can easily be diverted to the local market, such as raw materials (e.g., construction materials) and other commodities (e.g., fuel), the agreement, or an annex thereto, should determine maximum quantities; at the very least, the agreement should provide for a mechanism to determine such maximum levels in common accord and prior to the introduction of the goods into the recipient country.

55. Also, from a tax policy perspective, donors should not insist on, and recipient countries should not grant, tax exemptions for goods that are identical or essentially similar to those available on the local market of the recipient country.

56. Moreover, the terminology used to identify the taxes for which exemption is granted is often unclear and sometimes inconsistent. The terms range from just “customs duties” over “all customs duties and taxes” and “import duties, customs duties and other taxes” to “all taxes or charges”, and sometimes specifically refer to “value added taxes”. Some agreements even provide exemption from import restrictions or prohibitions, whether or not limited to what would be “otherwise required for reasons of public health or safety”. Certain agreements include a reference to export taxes, restrictions or prohibitions. Agreements rarely define the terms used or contain a list of the taxes covered by the exemption. This wide variation also appears between agreements concluded by the same donor country and there may even be inconsistency within the same agreement.

57. This lack of precision may raise questions of interpretation. When the exemption is for “customs duties” only, it may be argued that other taxes due on importation (e.g., GST/VAT, excise tax/other consumption taxes) are not exempt, whereas under a clause referring to “import duties, customs duties and other taxes” they clearly are. In the latter case, however, the question may arise whether service charges such as harbor dues, warehouse or handling charges or fees and the like are also waived, whereas there may be less doubt under a clause referring to “all taxes and charges”.

58. Such issues of interpretation are compounded by the inconsistencies between the various agreements a country may have entered into, whether as a donor country or as a recipient country. Minor variations between the various agreements require constant and careful attention, in particular by the competent authorities of the recipient country, who often lack sufficient administrative capacity to do so effectively and efficiently.

59. It is therefore important that taxes covered by the exemption be clearly identified, using the tax terminology of the recipient country. Ideally, a list of the recipient country’s taxes and levies for which exemption is granted will be included in the agreement itself,¹⁴ or in an annex, with a general provision allowing the agreement to continue to apply if these taxes are modified or replaced by broadly similar taxes.

8. *Also, where such relief from indirect taxes, including custom duties, is granted with respect to goods and services used in relation to an ODA project, that relief should be granted through a refund or voucher method and, in the case of imported goods, through an automated customs management system rather than through a direct exemption processed manually. The tax administration of the recipient country should also adopt procedures to ensure that goods and services on which indirect tax will be relieved are used for the purpose of the relevant project.*

60. Countries use different procedures for granting import duty and indirect tax exemptions. Some countries grant immediate exemption while other countries require some or all exempt importers to pay import duties and taxes and file for reimbursement at a later date. Also, a number of francophone African countries have introduced a treasury voucher system to monitor exemptions, in particular for ODA projects. Existing instruments generally do not advocate a particular method for granting or controlling exemptions in general or in relation to ODA projects in particular.

61. From an administrative perspective, a system where the exemption is processed manually at the time it is requested should be discouraged. A reimbursement or voucher method and the use of an automated customs management system are generally to be preferred and Guideline 8 recommends the use of these methods.

62. A reimbursement system offers a number of advantages, including relieving the strain on the verification stage, which has the double advantage of speeding up the clearance process and making more customs personnel available for post-clearance controls (audits, physical

14 See e.g., paragraph 3 of Article 2 (Taxes Covered) of the OECD and UN Model Tax Conventions.

checks) that are both more efficient and more trade-friendly. Experience shows that reimbursement systems can be successfully implemented, leading in some cases to an increase of government revenue.¹⁵

63. When implemented and administered properly, the voucher system used by some francophone African countries¹⁶ can also be an effective method for eliminating or greatly reducing abuse and revenue loss from this type of exemption. Under this system, import duties and taxes in connection with qualifying projects are payable by way of treasury credit vouchers issued by the government. ODA public procurement bids must be submitted on a tax-inclusive basis, which thus requires the bidders to carefully plan and calculate their projects. When the contract is assigned, treasury vouchers are issued to the contractor up to the contractor's forecasted amount of duties and taxes.¹⁷ Any excess tax burden falls on the contractor. The system thus has a built-in control mechanism: bidders will be careful not to overstate their tax forecast to obtain the contract, while an understatement leaves the contractor to bear the excess tax burden when the contractor wins the bid. In addition, it allows the government of the recipient country to keep track of foregone amounts of duties and taxes.

64. While this system is straightforward for import duties and taxes and for single-stage domestic sales taxes, it is more complicated for "domestic VAT" (i.e. VAT on domestic supplies, other than import VAT). Indeed, the amount of domestic VAT for which exemption and thus treasury vouchers may be claimed is not necessarily equal to the amount of output VAT (i.e. the total consideration for the supply multiplied by the VAT rate) but is the net amount of VAT due (i.e. the output VAT minus the input VAT on domestically sourced supplies or taxed imports), the forecasting of which may prove to be more difficult.

65. Contractors under ODA projects for which duty and tax exemptions are available thus have an incentive to insist on outright VAT exemption for their domestically sourced supplies, which "break" the VAT chain and thus undermine the VAT system of input tax credits. Indeed, domestic suppliers further down the supply chain will also claim exemption, thus leading to "exemption creep" in the VAT system.¹⁸ Another potential weakness of the voucher system may be the risk of forgery of vouchers, although with proper controls in place this risk should not be too difficult to manage.

15 E.g., Mali, cited in *Customs Modernization Handbook*, World Bank 2005, p. 238, box 10.9

16 See e.g. for Guinea: Instruction No 196/414/PM/MBRSP of 13 December 1996 on the tax treatment of government procurement: <http://www.droit-afrique.com/images/textes/Guinee/Guinee%20-%20Regime%20fiscal%20marches%20publics.pdf>

17 The system identifies which duties and taxes may be financed by the government through treasury vouchers, and which taxes must always be borne by the contractor. For instance, under the Guinea rules (see previous footnote) only (1) import duties and taxes on goods the ownership of which is transferred to the recipient country in the course of the project or which are incorporated into the constructions that are transferred to the recipient country, and (2) VAT on the domestic supplies under the contract are payable with "chèques sur le Trésor Série Spéciale" or "CTSS". For contracts which are only partly donor-financed, vouchers are issued only in proportion to the foreign aid provided.

18 See L. Ebril, M. Keen, J.-P. Bodin and V. Summers, *The Modern VAT*, IMF 2001, p. 89.

66. Guideline 8 also recognizes that whatever system is used, the tax administration of the recipient country should ensure that proper administrative procedures are applied to ensure that goods and services on which indirect tax will be relieved are used for the purpose of the relevant project. Even if a list of exempted goods and their quantity is provided to the tax administration, the tax administration may find it problematic to monitor the quantity of such goods that are eligible for exemption. Fuel taxes (e.g. VAT and excise taxes on fuel) are particularly prone to abuse; while exemptions from such taxes are frequently requested, recipient countries should be particularly wary of granting such exemptions.

67. In the case of imported goods, such procedures would typically include

- Establishing a clear and strict authorization procedure to identify the importer, the type and quantity of the goods and the exempt use for which they will be imported;¹⁹
- Verification upon importation, to reconcile the goods, the import declaration and supporting documents presented to customs with the prior authorization; and
- Post-clearance controls to verify whether the imported goods are put to, and are not diverted from, their exempt use.

68. In the case of imported goods, the use of an automated customs management system, such as the ASYCUDA²⁰ developed by UNCTAD, will help administer any available exemptions while facilitating trade by reducing transaction time and costs.

9. *Any agreement concerning such relief from indirect taxes, including custom duties, with respect to goods used in relation to an ODA project should stipulate that when the relevant goods are disposed of in the recipient country or otherwise diverted from their intended purpose, the general domestic rules on disposal or diversion apply equally to these goods, in particular with respect to procedural aspects and the imposition of duties, taxes, interest and penalties in case of disposal or diversion.*

69. Most agreements providing for relief from indirect taxes with respect to goods used or provided in the context of ODA projects do not stipulate what happens when these goods are subsequently disposed of or diverted from their intended purpose. In most cases, duties and taxes should become payable under general domestic rules related to disposal or diversion of goods on which tax was not previously paid. Guideline 9 addresses that issue and provides that the application of domestic rules applicable to such disposals and diversions should be clarified in order to avoid any uncertainty, in particular with respect to procedural aspects and the imposition of duties, taxes, interest and penalties.

10. *Regardless of whether tax exemptions for transactions related to ODA projects are granted, donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should comply with the information and withholding tax*

19 For example, one country has had recourse to a team of engineers in order to determine the quantity of materials required for specific projects, which allowed it to limit the quantity for which an exemption could be claimed.

20 Automated System for Customs Data (ASYCUDA) (see <https://asycuda.org/en/>).

requirements of recipient countries with respect to payments to taxable entities made in relation to these projects.

70. Under most tax systems, persons that make certain payments to resident or non-resident taxpayers are required to inform tax authorities about these payments and, in some cases, to withhold tax on these payments. This is typically the case for the payment of remuneration to employees and subcontractors. Regardless of whether tax exemptions for transactions related to ODA projects are granted or whether they are themselves exempt from tax for other reasons, donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should assist the tax authorities of recipient countries by complying with the applicable information and withholding tax requirements with respect to payments that they make to taxable entities in relation to these ODA projects.

B. *Internationally-recognized tax principles applicable to ODA projects*

a) *Income taxation – employment remuneration*

11. *The remuneration, including employment-related benefits, for employment services related to an ODA project that an individual derives from that individual's employment by the government of the country or agency thereof that finances that project should not be taxable in the recipient country if the individual*

a) is not a national of that jurisdiction, and

b) is not a resident of that jurisdiction or became a resident solely for the purposes of rendering these services.

71. Guideline 11 is based on the provisions of paragraph 1 of Article 19 of the *United Nations Model Double Taxation Convention between Developed and Developing Countries* (the UN Model)²¹ and the *OECD Model Tax Convention on Income and on Capital*²² (OECD Model). These provisions are found in almost all bilateral tax treaties currently in force. As noted in the Commentary on these models “[s]imilar provisions in old bilateral conventions were framed in order to conform with the rules of international courtesy and mutual respect between sovereign States”.²³ The principle that a state should not levy income tax on the remuneration of employees of another state who perform governmental services on the territory of the former state is now universally accepted and has therefore been included in these Guidelines. It must be stressed, however, that this principle applies only to employees of a state and does not extend to other parties, such as subcontractors, who provide services to a state.

21 United Nations, Department of Economic and Social Affairs, *United Nations Model Double Taxation Convention between Developed and Developing Countries 2017*, (New York: United Nations, 2018), available at http://www.un.org/esa/ffd/wp-content/uploads/2018/05/MDT_2017.pdf.

22 OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, https://doi.org/10.1787/mtc_cond-2017-en, available at https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#page1.

23 Paragraph 2 of the Commentary on the UN Model Tax Convention, quoting paragraph 1 of the Commentary on the OECD Model Tax Convention.

72. Nothing in these Guidelines affect the exemptions to which various members of diplomatic missions or consular posts are entitled under the general rules of international law or under multilateral instruments such as the *Vienna Convention on Diplomatic Relations* and the *Vienna Convention on Consular Relations*. These exemptions are applicable regardless of whether or not specific exemptions are granted with respect to government employees providing services in the context of a particular ODA project.

73. Like paragraph 1 of Article 19 of the UN Model and OECD Model and like the two Vienna Conventions mentioned in the previous paragraph, Guideline 11 provides an exception that allows a recipient country to tax the remuneration paid to local personnel who are permanent residents or nationals of that country. That exception is intended to ensure that locally-recruited personnel (e.g. security guards hired for the duration of an ODA project) are not entitled to the same treatment as employees of a state sent to a foreign country.

74. The Guideline does not address the treatment of employees of international organizations as there is less international consensus on this issue. On the one hand, it could be argued that such employees, when providing services in relation to an ODA project, should be treated like any employee of the states that are members of that international organization and that provide the funding of that organization. On the other hand, tax treaties typically do not provide a special treatment for employees of international organizations. In any event, the tax treatment of employees of international organizations in the states that are members of that organization is often regulated by the agreements under which these organizations are established.

12. *The remuneration, including employment-related benefits, that an individual to whom Guideline 11 does not apply derives from employment services related to an ODA project of a country, aid agency or international governmental organization, should not be taxable in the recipient country if all the following conditions are met:*
 - a) *the individual is not a resident of the recipient country,*
 - b) *during the project, the individual is not present in the recipient country for a period or periods exceeding in the aggregate 183 days in any twelve-month period beginning or ending in the relevant tax year;*
 - c) *the remuneration is paid by, or on behalf of, an employer who is not a resident of the recipient country, and*
 - d) *that remuneration is not borne by a permanent establishment which the employer has in that country.*

75. Guideline 12 provides for an exemption from income taxation in a recipient country in a case where a person employed by a foreign enterprise exercises his/her employment in the recipient country for a short period of time in connection with an ODA project. That exemption is based on a rule found in almost all bilateral tax treaties and incorporated in paragraph 2 of Article 15 of the UN Model and the OECD Model.

76. This exemption would typically apply to employees of foreign commercial enterprises that are performing work in the recipient country pursuant to contracts concluded with the donor. Since these individuals would not be employed directly by that donor, they would not

be entitled to the exemption referred to in Guideline 11 and should be subject to the normal taxation rules of the recipient country, subject to this exemption for short-term employment activities.

77. Since the wording of this exemption is derived from that used in tax treaties, it should be interpreted in the same way. The reference to “resident” should therefore be given the meaning that it generally has for the purposes of tax treaties and the interpretation of the 183-day rule should be in accordance with the guidance found in the Commentary on the UN Model and OECD Model.

b) Income taxation – profits and payments to foreign enterprises

13. *Payments that a country, aid agency or international governmental organization makes in connection with an ODA project to an enterprise that is not an enterprise of the recipient country, as well as profits derived by that enterprise from activities exercised in connection with that project should not be subject to any income or corporate tax in the recipient country unless such payments or profits are attributable to activities carried on in the recipient country during a period or periods exceeding in the aggregate 183 days in any twelve month period beginning or ending in the relevant tax year or are attributable to the activities carried on in the recipient country by the enterprise of a self-employed person who is present person in that country during a period or periods exceeding in the aggregate 183 days in any twelve month period beginning or ending in the relevant tax year.*

78. The negative form in which Guideline 13 is drafted is intended to reflect the circumstances in which, under the existing international principles incorporated in bilateral tax treaties, a country is typically prevented from taxing the profits of foreign enterprises.

79. Indeed, most bilateral tax treaties, and the UN and OECD models on which they are based, provide that, as a general rule subject to certain exceptions, foreign enterprises that are paid from abroad to carry on activities in a country should only be taxable in that country on profits attributable to these activities when these are carried on in that country through a permanent establishment, fixed base or, in some cases, a presence of a sufficient duration (typically 6 months).

80. Guideline 13 is based on that principle but, given the differences of formulation and interpretation of the concepts of “permanent establishment” and “fixed base”, as well as the need to formulate a simple test that can be easily applied by the tax administrations of recipient countries, it includes a single criterion, i.e. whether the profits are attributable to activities carried on in the recipient country during a period or periods exceeding in the aggregate 183 days in any twelve month period.

81. This Guideline applies to enterprises that are not residents of the recipient country. The term “enterprise” applies to all forms of business organizations and would therefore apply to a large company as well as to an individual consultant providing services as a sole proprietorship. The Guideline is intended to cover, among other things, situations where an individual who is

not a resident of the recipient country performs work in that country in a non-employment relationship as part of an ODA project.

82. As is the case for other Guidelines, the reference to “resident” should be given the meaning that it generally has for the purposes of tax treaties.

Note by the Secretariat

The explanations on Guideline 13 will be supplemented by a series of examples illustrating the application of the Guideline to different enterprises, including enterprises of self-employed persons.

14. *Any specific exemption from income or corporate tax granted with respect to activities of enterprises that carry on activities in connection with an ODA project:*
- a) should not be available to enterprises of the recipient country, and*
 - b) should be designed in a way that does not result in an unintended exemption of a foreign enterprise in its state of residence.*

83. If a country, aid agency or international governmental organization insists on a tax exemption for enterprises that will carry on activities in connection with an ODA project, Guideline 14 first recommends that such exemption, at a minimum, should not apply to local enterprises and sub-contractors so that only foreign enterprises that are paid directly by the donor country, organization or agency are entitled to claim that exemption. This recognizes that the recipient country should have the final say in deciding whether or not local enterprises should be taxed; it also avoids the difficult issues involved in trying to determine which enterprises should be entitled to a general exemption granted with respect to an ODA project.

84. Guideline 14 also recommends that the exemption should be designed in a way that avoids unintended exemption in the country of residence of a foreign enterprise. The tax legislation of many countries, and a number of tax treaties, exempt from tax profits of local enterprises that are attributable to permanent establishments located in other countries on the assumption that such profits will be taxable in these other countries. The combination of these provisions with a tax exemption granted in a bilateral agreement with respect to activities related to ODA projects could result in non-taxation without the tax authorities of both countries being aware of that situation. The involvement of tax authorities in the negotiation of tax provisions applicable to ODA projects (as is recommended in Guideline 3) should reduce the risk of this happening. At the time of the negotiation of such provisions, the tax officials from the recipient country should look at the tax law of the donor country and any applicable tax treaty in order to identify such cases of non-taxation.

c) Indirect taxation - humanitarian crises

15. *No indirect taxes, including custom duties, should be imposed on the import of goods to be used to respond to humanitarian crises such as natural disasters, famine, or*

health emergencies. For that purpose, countries should implement the rules of, or become parties to,

- a) *Chapter 5 (Relief Consignments) of the Specific Annex J to the International Convention on the simplification and harmonization of Customs procedures, as amended (commonly referred to as “the Revised Kyoto Convention”), and*
- b) *Annex B.9 (Concerning goods imported for humanitarian purposes) to the Convention on temporary admission (commonly referred to as “the Istanbul Convention”).*

85. Supplies by donor countries, international governmental organizations and agencies thereof to respond to acute humanitarian crises constitute a subcategory of ODA projects that has the following characteristics:

- to be effective, such consignments must be delivered rapidly to their ultimate recipients, i.e. those affected by the crises, and
- the case for relieving such supplies from taxes and duties is particularly strong, as there is little economic sense in taxing such supplies (the recipients do not have ability-to-pay), and the revenue risks involved in exempting such supplies are equally small.

86. The existence of transparent and harmonized rules regarding the tax treatment of emergency aid that would already be in place before a crisis occurred is paramount for swift and efficient donor intervention.

87. Many countries have adopted domestic tax provisions regarding “relief consignments”, but there is substantial variation in their scope of application, both with respect to the type of taxes and with respect to the type of supplies. Few countries appear to have specific provisions on temporary admission for relief consignments, although there is usually a general regime for temporary admission in the customs laws.

88. In addition to these domestic law provisions, a number of countries have entered into bilateral assistance agreements with other countries, international organizations, their agencies or other donors. While these agreements may cover many of the issues discussed below, they may not systematically address all of them. Moreover, these agreements often show differences, minor or major, between them both regarding the duties and taxes as well as the nature of activities covered. Furthermore, by their nature, such agreements only cover activities by the contracting donor country, organization or agency, and their facilities are thus not available to others. Finally, such agreements are usually not published or publicly disseminated, or at least not systematically or in the same way as ordinary tax laws and regulations, thus lacking transparency and adding to the complexity of applying them. In many countries, tax and customs officials may not have ready access to them or be familiar with their terms.

89. A number of international instruments currently exist in this area. These mainly concern clearance procedures and relief from import and export duties and taxes, but do not cover taxes on domestic transactions. Also, these instruments have not been universally adopted. The main

international instruments in this area are managed by the World Customs Organization (WCO).²⁴ They are:

- Chapter 5 on Relief Consignments of the Specific Annex J to the Revised Kyoto Convention.²⁵ The Guidelines to which also comprise the Recommendation of the Customs Co-operation Council to expedite the forwarding of relief consignments in the event of disasters, and the UN Model Agreement on Customs Facilitation in International Emergency Humanitarian Assistance; and
- Annex 9.B. (Goods imported for humanitarian purposes) to the Istanbul Convention.²⁶

90. Guideline 15 recommends that countries implement the principles of these existing international instruments either by becoming a party to the relevant multilateral conventions or by unilaterally incorporating their principles in their domestic law. This would overcome the need for countries to enter into bilateral agreements to deal with humanitarian crises.

91. The following principles should be followed when designing rules and administrative practices to implement this Guideline for exempting relief consignments from import duties and taxes:²⁷

- A definition of “relief consignments” should be included along the following lines:

goods, including vehicles and other means of transport, foodstuffs, medicaments, clothing, blankets, tents, prefabricated houses, water purifying and water storage items, or other goods of prime necessity, forwarded as aid to those affected by disaster; and

*all equipment, vehicles and other means of transport, specially trained animals, provisions, supplies, personal effects and other goods for disaster relief personnel in order to perform their duties and to support them in living and working in the territory of the disaster throughout the duration of their mission.*²⁸

24 The WCO is the working name adopted by the Customs Co-operation Council, an intergovernmental organization established in 1952 to enhance the effectiveness and efficiency of customs administrations; see <http://www.wcoomd.org/>.

25 *International Convention on the simplification and harmonization of Customs procedures* (as amended), done at Kyoto on 18 May 1973, commonly referred to as “the Revised Kyoto Convention”. The Revised Kyoto Convention is comprised of the Body of the Convention, of a General Annex, and of ten Specific Annexes, most of which are further divided into two or more Chapters. Countries may accede to the Convention without accepting any or all of the Specific Annexes and/or Chapters (Article 8(3) of the Convention). See http://www.wcoomd.org/Topics/Facilitation/Instrument%20and%20Tools/Conventions/pf_revised_kyoto_conv/Instruments for the list of signatories

26 *Convention on Temporary Admission*, done at Istanbul on 26 June 1990, commonly referred to as “the Istanbul Convention”. Similar to the Revised Kyoto Convention, the Istanbul Convention comprises a body and different Annexes. Countries may accede to the Convention without accepting all Annexes, although they have to accept at least Annex A on Temporary Admission Papers and one other Annex (Article 24(4) of the Convention). See http://www.wcoomd.org/Topics/Facilitation/Instrument%20and%20Tools/Conventions/pf_revised_kyoto_conv/Instruments for the list of signatories.

27 See Chapter 5 on Relief Consignments of the Specific Annex J to the Revised Kyoto Convention.

28 Ibid.

- Countries may find it useful to refer to the following definition of “disaster” in Article 1 of the *UN Model Agreement on Customs Facilitation in International Emergency Humanitarian Assistance*:

A serious disruption of the functioning of the society, causing widespread human, material, or environmental losses which exceed the ability of affected society to cope using only its own resources.

The term covers all disasters irrespective of their cause (i.e. both natural and manmade).

- Accelerated and simplified clearance procedures for relief consignments should be provided²⁹ so that customs clearance of relief consignments is carried out as a matter of priority and simplified and expedited clearance procedures can be used, such as the lodging of a simplified, provisional or incomplete declaration, pre-arrival declarations, clearance outside normal hours and without normal charges as well as examination/sampling in exceptional circumstances only. Such clearance procedures should be provided for in the customs legislation and the necessary procedures should be planned for in advance and documented so that they can be implemented in short order.
- The exemption from duties, taxes and restrictions applicable provided for relief consignments should include³⁰ a waiver from economic export prohibitions or restrictions, and export duties and taxes otherwise payable; as well as a waiver from import prohibitions and restrictions, and import duties and taxes, for relief consignments received as gifts by approved organizations for use by or under the control of such organizations, or for distribution free of charge by them or under their control.
- Goods imported for humanitarian purposes, i.e. medical, surgical and laboratory equipment and other relief consignments that do not qualify for the exemption for relief consignments, should be granted temporary admission with total relief from import duties and taxes, and without the application of economic import restrictions or prohibitions;
- Temporary admission of such goods should not be subject to stricter conditions than the following:
 - In order to qualify for that exemption, the goods should be owned by a person established outside the territory of temporary admission and should be made available free of charge.
 - Medical, surgical and laboratory equipment should be intended for use by hospitals and other medical institutions which, finding themselves in exceptional circumstances, have urgent need of it, and must not be readily available in sufficient quantity in the territory of temporary admission; and

29 See Standards 2 and 3 of Chapter 5 of the Specific Annex J to the Revised Kyoto Convention.

30 Recommended Practices 5 and 6 of Chapter 5, Specific Annex J to the Revised Kyoto Convention.

- Relief consignments should be dispatched to persons approved by the competent authorities in the territory of temporary admission.
92. In addition to the general recommendations regarding accelerated and simplified clearance, whenever possible, an inventory of the goods together with a written undertaking to re-export should be accepted for medical, surgical and laboratory equipment in lieu of a customs document and security.
93. Temporary admission of relief consignments should be granted without a Customs document or security being required. However, the Customs authorities may require an inventory of the goods, together with a written undertaking to re-export.
94. The time period for temporary admission should be determined in accordance with the needs for medical, surgical and laboratory equipment; and should be at least twelve months for relief consignments.
16. *Goods that are provided domestically to, or imported by, a foreign country, aid agency or international governmental organization for direct use in response to a humanitarian crisis, and services closely connected with such supplies, that would – if imported – qualify as “relief consignments” or “goods for humanitarian purposes” for import duty and tax exemption on temporary admission, should be relieved from domestic indirect taxes.*
95. There are currently no international standards with respect to the exemption of relief consignments from domestic indirect taxes. To avoid distortion, it would be appropriate to grant the same favorable tax treatment to relief consignments that are sourced or supplied to a foreign country, aid agency or international governmental organization for use in response to a humanitarian crisis under the same conditions and circumstances as imported relief consignments would enjoy pursuant to the instruments discussed above.
96. Guideline 16 therefore recommends that a similar exemption be granted with respect to domestically supplied goods, and services closely connected with such supplies, that would – if imported – qualify as “relief consignments” or “goods for humanitarian purposes” for import duty and tax exemption on temporary admission. Such exemption from domestic transfer taxes could be achieved either on the side of the supplier (by zero-rating qualifying domestic supplies) or on the side of the purchaser (by granting refund of domestic taxes paid). From an administrative point of view, the latter method is preferred as it allows for tighter controls. Also, the foreign a country, aid agency or international governmental organization that would benefit from such an exemption from domestic transfer taxes should be identified beforehand in the same manner as beneficiaries of import duty and tax exemption for such relief consignments.

97. The VAT legislation of some countries of some countries already provide that type of exemptions.³¹

d) Indirect taxation – personal property and household goods of workers

17. *Personal property and household goods of workers coming to a recipient country for the purpose of an ODA project should be exempt from indirect taxes, including customs duties, as long as these workers' stay is merely temporary and is related to that project.*

98. It is an internationally recognized³² practice not to impose import duties and taxes on personal effects of non-resident travellers subject to specified limits as to type and quantity of the goods, and the time-limit during which such goods may stay in the country concerned. This is a particular form of temporary admission. In addition, persons who move their place of residence to a country are often allowed to import their household goods into that country free of import and export duties and taxes, again subject to limitations as to type and quantity of the goods concerned;³³ that exemption is specifically recognized in various international instruments for diplomats, consular personnel and staff of international organizations.

99. The situation of non-resident workers³⁴ dispatched to a recipient country in the context of an ODA project does not necessarily fall into any of these broad categories of exemptions: they are not the typical tourist travellers that are primarily targeted by the former category of exemptions, they typically do not enjoy diplomatic status, and they typically do not transfer their residence to the recipient country.

100. Bilateral assistance agreements typically provide relief from import duties and taxes for personal property of workers dispatched to the recipient country in the context of projects funded under that agreement. The following is a typical example:

The personal property of experts charged with the execution of projects and programs in the context of this agreement and who are not citizens of [the recipient country] and do not permanently reside there, is exempt from duties, taxes and other charges when imported into [the recipient country]. When such goods are transferred in [the recipient country], the excises due must be paid in accordance with the provisions in force in [the recipient country].

101. Exempting the personal property of such workers from indirect taxes, including import duties, is justified as long as their stay is merely temporary and is related to the ODA project.

31 See, for instance, [*examples to be added, which could include reference to Jamaica GCT and IMF sample VAT legislation*]

32 Chapter 1 on Travellers of Specific Annex J to the Revised Kyoto Convention; specific Annex B.6 of the Istanbul Convention also concerns travellers' personal effects, and Chapter 3 on Relief from Import Duties and Taxes of Specific Annex B to the Revised Kyoto Convention. With respect to household goods, the Guidelines to Chapter 3 of Specific Annex J state that there "is presently no standard set of conditions among WCO Members for granting relief", this being an area for further harmonization.

33 While virtually all countries provide for import duty and tax exemption for personal effects of non-resident travellers, only some countries grant relief in general for household goods of persons who move their residence to their territory. Often this type of exemption is limited to "returning residents", i.e. residents of the country that return to their former residence after having spent a prolonged period of time abroad.

34 For this purpose, "workers" refers to employees as well as self-employed persons.

Since there is currently no established international practice that specifically deals with import duty and tax exemption for personal effects and household goods of persons who are not travellers but at the same time do not necessarily intend to relocate their place of residence, this Guideline therefore recommended that such exemption be generally provided. This should be done subject to the following conditions:

- the scope of the exemption be defined by recourse to the internationally established notions of “personal effects” and “removable articles” that exist for travellers and persons relocating their place of residence;
- the type of taxes covered by the exemption be clearly defined by using the terminology of the country which grants the exemption, and, ideally, by individually listing the country’s duties and taxes for which exemption is granted;³⁵
- the beneficiaries of the exemption be clearly defined, and residents of the recipient country be denied the exemption;
- the exemption should be limited to property that will be present in the country for a predetermined time period;
- the application of temporary admission rules (notably the obligation to re-export within a predetermined time-period) be limited to specified high-value or high-risk goods (e.g., vehicles);
- in the case of vehicles, the exemption should be restricted to previously-used vehicles and should be conditional on the vehicle not being disposed of;
- the other procedures and conditions be those of similar exemptions that are well-established in the domestic legislation of the recipient country.

102. Recipient countries may opt to incorporate this exemption along the lines of these recommendations into their domestic legislation, either indiscriminately for all personnel working under an assistance agreement or only for those who work under an assistance agreement that provides for this benefit “in accordance with the recipient country’s domestic law provisions in force”. Alternatively, such an exemption may be agreed to bilaterally.

e) *Indirect taxation – temporary admission*

18. *No indirect taxes, including customs duties, should be imposed on the temporary admission of goods to be used for the purposes of an ODA project. For that purpose, countries should implement the rules of, or become parties to,*
 - a) *Chapter 1 (Temporary Admission) of the Specific Annex G to the Revised Kyoto Convention”), and*
 - b) *the parts of the Convention on temporary admission (commonly referred to as “the Istanbul Convention”) that relate to temporary admission of certain goods.*

35 See e.g., paragraph 3 of Article 2(Taxes Covered) of the UN Model and the OECD Model.

103. The benefits of not imposing import duties and taxes on goods which are intended to stay only temporarily and for a particular purpose in a given country are widely recognized both by traders and by customs authorities. There are strong economic, social and cultural reasons for not imposing the import duties and taxes that would otherwise be due, for instance to allow traders to test foreign goods before they decide to import them, or to stimulate exchanges in the cultural, educational and scientific area. The customs procedure that provides for relief from import duties and taxes on goods imported for a specific purpose and on the condition that they be re-exported in the same state is commonly known as temporary admission.

104. Temporary admission plays a central role in the tax treatment of ODA projects, as many of the goods that are imported for the purpose of carrying out such projects are not intended to stay in the recipient country beyond the completion of the project (e.g., construction tools and equipment imported for the purpose of carrying out a construction project).

105. Most countries have provisions on temporary admission in their domestic legislation. In addition to these domestic law provisions, a number of countries have entered into bilateral assistance agreements with donor countries, international aid organizations or other donor or aid agencies which contain provisions on temporary importation. These agreements often show differences, minor or major, between them and compared to the corresponding domestic law provisions. Furthermore, by their nature, such agreements only cover activities by the contracting donor country, organization or agency, and their facilities are thus not available to other donors. Finally, such agreements are usually not published or publicly disseminated, or at least not systematically or in the same way as ordinary tax laws and regulations, thus lacking transparency and adding complexity.

106. There are also a number of multilateral agreements and conventions regarding temporary admission. The main instruments in this respect are the previously-mentioned Istanbul Convention³⁶ and Chapter 1 on Temporary Admission, Specific Annex G to the Revised Kyoto Convention. The Revised Kyoto Conventions contains the basic provisions for all customs procedures, including the fundamental principles concerning temporary admission. The Istanbul Convention, on the other hand, contains more details regarding specific categories of goods, and regarding customs documents and guaranteeing associations. It is also more liberal than the Revised Kyoto Convention in that it also provides for relief from economic prohibitions and restrictions for temporary admission goods;³⁷ specific Annexes B.1 to E of the Istanbul Convention include the list of goods that should be granted temporary admission with total relief from duties and taxes.

36 The Istanbul Convention combines into a single instrument all the existing provisions on temporary admission in a multitude of earlier conventions and agreements on the ATA (“ATA” is a combination of the French “*admission temporaire*” and the English “temporary admission”) carnet with respect to specific types of goods. The ATA carnet system is one of the most important internationally accepted systems for the movement of goods under temporary admission through multiple Customs territories. It relies on an international chain of guaranteeing associations that provide the security for any duties and taxes which may become liable on the temporarily admitted goods.

37 The Kyoto Convention only encourages parties to adopt “a less restrictive practice” regarding economic prohibitions or restrictions with respect to temporary admission goods.

107. To ensure maximum transparency, predictability and harmonization, it is recommended that countries implement the principles of the Istanbul Convention and the Revised Kyoto Convention as a minimum standard either by becoming a party to these conventions or by unilaterally applying their principles. This would alleviate the need for countries to enter into bilateral agreements which, as noted above, hamper transparency and harmonization in this area.

108. Only if and to the extent a need still exists with respect to ODA projects to deviate from the general domestic rules on temporary admission, special rules may be agreed upon bilaterally to deal with specific issues relating to the carrying out of the project (e.g., usage or special categories of goods not normally allowed for temporary importation, longer time-limits during which goods are allowed to stay in the country, etc.). Alternatively, domestic law may grant customs a margin of discretion, circumscribed by the existence of an assistance agreement, to deviate on certain points from the general rules on temporary admission and subject to prior application to that effect by a qualifying importer.

ANNEX

WRITTEN COMMENTS RECEIVED ON NOTE E/C.18/2019/CRP.6

A. Comments from the African Tax Administration Forum

1. Paragraph 1(28) of the Commentaries to the OECD Model Tax Convention, indicates that a permanent establishment can be deemed to exist only if the place of business has a certain degree of permanency. The alluded level of permanency is where activities are performed in a country for a period of more than 6 months (183 days). The paragraph, however, acknowledges that a place of business may constitute a permanent establishment even though it exists for a shorter period of time because the nature of the business is such that it will only be carried on for that shorter period of time. The paragraph continues to provide examples of such exceptional cases as:-

- where the activities were of recurrent nature; in such cases, each period of time during which the place is used needs to be considered in combination with the number of times during which that place is used (which may extend over a number of years).
- where activities constituted a business that was carried on exclusively in that country; in this situation, the business may have short duration because of its nature but since it is wholly carried on in that country; its connection with that country is stronger.

2. These commentaries are also contained in paragraph 6 of the 2017 UN Model Tax Convention of 2017 since the Tax Committee of Experts accepts the incorporation of the commentaries in the UN MTC.

3. Several examples are discussed in the OECD Commentary in respect of the above exceptions. For instance, in the case of a five (5) years drilling contract; a foreign enterprise, of State A, could only conduct the drilling activities for 3 months in a year in State B due to poor weather conditions. Under this circumstance, it is considered that the time required for a permanent establishment is met due to the recurring nature of the activities regardless of the fact that any continuous presence lasts less than 6 months.

4. The question, therefore, is whether the above circumstances or business activities may arise in respect of Official Development Assistance (ODA) projects. In our view, the answer to that question is affirmative since developing countries, who are typically the recipient countries, continue to receive ODA in a wide range of activities including but limited to:-

- i. Humanitarian relief activities;
- ii. Education assistance;
- iii. Technical support – Advisory services on various issues; and
- iv. Construction activities in respect of infrastructure projects.

5. The issues covered in **iii** and **iv** above have over the years increased as developing countries accelerate infrastructure development activities. Therefore, it is not uncommon to observe such services being rendered by a non-resident enterprise through an ODA project. Thus, there is an imminent risk the proposed guideline may be abused if the trigger for

permanent establishment status is explicitly left as 183 days without any further considerations as alluded to in the UN and OECD MTC and commentaries to Article 5.

6. In addition, during the Base Erosion and Profit Shifting (BEPS) discussion, Action 7 considered the risk associated with fragmentation of contracts in order to avoid P/E status. This led to further revision of the OECD MTC as well as the UN MTC by the introduction of anti-fragmentation provisions in their Article 5.

7. Given the complexity and the associated BEPS risk of permanent establishments, we are concerned that application of a single criterion as indicated in Paragraph 13 and Paragraph 80 of the Guidelines on the Tax Treatment of the ODA Project will make the situation worse by creating opportunities for BEPS through ODA projects.

8. To address this imminent risk, we suggest that Paragraph 13 be revised to the effect that the non-resident enterprise would be taxable in the ODA recipient country where a permanent establishment is created under the provisions of Article 5 of the UN Model Tax Convention. Further recipient countries may consider aligning the ODA Agreement on this issue to the provisions of the Bilateral Tax Treaty between the recipient country and donor country or the service provider country, as the case may be.

9. We, therefore, suggest Paragraph 13 should read as follows:

Payments that a country, aid agency or international governmental organization makes in connection with an ODA project to an enterprise that is not an enterprise of the recipient country, as well as profits derived by that enterprise from activities exercised in connection with that project, should not be subject to any income or corporate tax in the recipient country unless such payments or profits are attributable to a permanent establishment in the recipient country in the relevant tax year as provided in Article 5 of the UN Model Tax Convention or are attributable to a fixed base of an independent personal services in the relevant tax year as provided in the Article 14 of the UN Model Tax Convention.

10. In addition, Paragraphs 79 and 80 needs to be revised to reflect the position that Paragraph 13 would be interpreted in light of the UN Model Tax Convention and the commentaries thereto. Thus, we suggest the following redrafting: -

Indeed, most bilateral tax treaties, and the UN and OECD models on which they are based, provide that, as a general rule subject to certain exceptions, foreign enterprises that are paid from abroad to carry on activities in a country should only be taxable in that country on profits attributable to these activities when these are carried on in that country through a permanent establishment, fixed base or, in some cases, a presence of a sufficient duration (~~typically 6 months~~)

Guideline 13 is based on that principle but, given the differences of formulation and interpretation of the concepts of “permanent establishment” and “fixed base”, *these concepts should be interpreted based on the UN Model Tax Convention and the Commentaries thereto*. ~~as well as the need to formulate a simple test that can be easily applied by the tax administrations of recipient countries, it includes a single criterion, i.e. whether the profits are attributable to activities carried on in the recipient country during a period or periods exceeding in the aggregate 183 days in any twelve month period.~~

B. Comments from Titia Stolte-Detring

Executive Summary, paragraph 5 (p. 2) and Part B of the Guidelines, introduction (p. 9)

11. It is suggested that donor countries should refrain from claiming tax exemptions if they have sufficient confidence in the governance structures of a **particular** developing countries. To my knowledge development aid is realized on the basis of framework agreements which are applicable for a long period of time and which have the legal quality of government agreements. Those agreements often follow a model a donor country has developed, that leaves no room for an individual analysis of circumstances in the recipient country. Since they are applicable for an undefined period of time (similar to DTAs) they would need renegotiation in order to give up tax exemption rules.

12. It is suggested, that donor countries may (only) ask for tax exemption, if and to the extent that tax rules in the recipient country are not consistent with internationally recognized tax principles (see also Executive Summary, no. 9). The problem I see with this methodical approach is that it is stipulated that internationally recognized tax principles should be part of the national law of the recipient country, whereas national tax law sometimes/often does not follow that approach. The guidelines in nos. 11 and 12 reflect Articles 19 and 15 of the MTCs. Although internationally recognized they might not be reflected in the national law, that follows other principles (e.g. principle of residence). For example, German income tax law does not provide for the rules reflected in Art. 19 and 15 of the MTC; they are only transported into German law by way of a DTA, so if Germany was the recipient country the donor agency from a country, with which no bilateral tax treaty existed, could request tax exemptions.

13. My suggestion is to redraft the recommendation stating that – where no tax treaty between the donor and the recipient state is applicable – the recipient country may in general tax remuneration received from...with the exception of remuneration...(guideline 11) or remuneration...(guideline 12).

14. The caveat for existing DTA is important, because otherwise situations of double non-taxation might be created.

15. Unintended double non-taxation could also be the consequence of guideline 13. Although the need for simplicity (see Explanations, no. 80) is a valid argument, the guideline might interfere with an existing DTA: if the DTA provides for a p.e. after 3 months (paragraph 3 of Art. 5) the recipient country would lose its taxing right, that the DTA conveys, by means of guideline 13, so that in the end neither the recipient nor the donor country may tax the income attributable to that p.e. (at least in cases where the donor country applies the exemption method in its DTA).

16. Vice versa, where an existing DTA provides for a p.e. after 12 months, the recipient country would not – irrespective of guideline no. 13 – have a taxing right.

Executive Summary, paragraph 7 at the end (page 3)

17. Is the statement, that “many” donors already follow the policy of not requesting tax exemptions in line with the enumeration on page 14, no. 28 (only five states are named) or is “some” more appropriate (see Executive Summary, no. 12, 4th sentence)?

Guidelines, General Considerations

18. In paragraph 7 of the Executive Summary it is stated that the Guidelines are not binding in any way, whereas the General Considerations no 1 (page 7) say: "...except to the extent that the tax rules in the recipient country that would apply to these transactions are not consistent with these Guidelines".

19. The interpretation that could follow from this wording is that the Guidelines are in fact binding.

Comments on the Explanations on the Guidelines

20. The background given in no. 15 might need some redrafting. From what I know donor countries have to decide whether they want to provide:

a. general = direct budget support, where the donor country transfers money to the recipient country for its free disposal

or

b. technical support (ODA projects). If the technical support project is taxed by the recipient country, the tax goes to the budget of the recipient state and is at its free disposal. Because the donor country does not provide a direct contribution to the budget of the other states this is called indirect budget support.

21. Based on this definition the sentences "...if no part of these funds is diverted towards general budget support.." or "Such unwillingness to provide general budgetary support..." would be inaccurate (see also no. 33: "if the donor simply is unwilling to provide general budgetary support through the payment of taxes").

22. Given the often indefinite applicability of ODA-framework agreements I wonder whether donor countries really pay attention to circumstances and criteria that might change during the duration of such a framework agreement (e.g. the recipient's public expenditure management, the recipient's expenditure policy, e.g. towards military purposes) (see also no. 29 of the Explanations).

C. Comments from Elfrieda Stewart Tamba

[First comments]

Another condition consistent with general International Tax Principles should be added

23. [Amend Guideline 11 as follows:]

a) Income taxation – employment remuneration

11. The remuneration, including employment-related benefits, for employment services related to an ODA project that an individual derives from that individual's employment by the government of the country or agency thereof that finances that project should not be taxable in the recipient country if the individual

a) is not a national of that jurisdiction, ~~and~~

- b) is not a resident of that jurisdiction or became a resident solely for the purposes of rendering these services, *and*
- c) *is taxed on said employment remuneration without the recipient jurisdiction.*

See page 9 of the Guidelines (*Internationally-recognized tax principles applicable to ODA projects*).

24. Note: ATAF Model Agreement expresses this principle as follows: “Intending to conclude an Agreement for the elimination of double taxation with respect to taxes on income without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance....”

Tightened to Generate more Taxes for Source/Recipient Jurisdiction

25. [Amend Guideline 12 as follows:]

12. The remuneration, including employment-related benefits, that an individual to whom Guideline 11 does not apply, derives from employment services related to an ODA project of a country, aid agency or international governmental organization, should not be taxable in the recipient country if all the following conditions are met:

- a) the individual is not a resident of the recipient country,
- b) during the project, the individual is not present in the recipient country for a period or periods exceeding in the aggregate *half the number of days during which the project is carried out in any twelve-month period beginning or ending in the relevant tax year* ~~183 days in any twelve-month period beginning or ending in the relevant tax year;~~
- c) the remuneration is paid by, or on behalf of, an employer who is not a resident of the recipient country, and
- d) that remuneration is not borne by a permanent establishment (*as defined by the laws of the recipient country*) which the employer has in that country.

See page 9 of the Guidelines (*Internationally-recognized tax principles applicable to ODA projects*).

Tightened to Generate more Taxes for Source/Recipient Jurisdiction

26. [Amend Guideline 13 as follows:]

b) Income taxation – profits and payments to foreign enterprises

13. Payments that a country, aid agency or international governmental organization makes in connection with an ODA project to an enterprise that is not an enterprise of the recipient country, as well as profits derived by that enterprise from activities exercised in connection with that project, should not be subject to any income or corporate tax in the recipient country unless such payments or profits are attributable to activities carried on in the recipient country (*including through a permanent establishment as defined in its laws*) during a period or periods exceeding in the aggregate *half the number of days during which the project is carried out in any twelve-month period beginning or ending in the relevant tax year* ~~183 days in any twelve-month period beginning or ending in the relevant tax year~~ or are attributable to the activities carried on in the recipient country

(including through a fixed base as defined in its laws) by the enterprise of a self-employed person who is present person in that country during a period or periods exceeding in the aggregate ***half the number of days during which the project is carried out in any twelve-month period beginning or ending in the relevant tax year*** ~~183 days in any twelve-month period beginning or ending in the relevant tax year.~~

See page 10 of the Guidelines (Internationally-recognized tax principles applicable to ODA projects).

This should be subjected to a reasonability test

27. [Amend Guideline 17 as follows:]

d) Indirect taxation – personal property and household goods of workers

17. ***Reasonable pPersonal*** property and household goods of workers (***considering, inter alia, their position, socioeconomic class, status, and family size***) coming to a recipient country for the purpose of an ODA project should be exempt from indirect taxes, including customs duties, as long as these workers' stay is merely temporary and is related to that project.

See page 11 of the Guidelines (Internationally-recognized tax principles applicable to ODA projects).

[Additional comments]

28. Please see [below] my further inputs. As tabled at the last Committee meeting, I have serious concerns regarding certain provisions of the drafting. I have tried to flag said serious concerns and have proposed certain rewording in an attempt to bring more fairness and balance in the drafting in favor of and courtesy to developing countries. ...

29. [As regards the third paragraph of the Executive Summary:]

This note includes a set of Guidelines that were developed by the United Nations Committee of Experts on International Cooperation in Tax Matters in light of this commitment. The Guidelines seek (to facilitate the consideration of whether or not tax exemptions should be requested with respect to ODA projects)

Suggest that the last sentence be restructured to read exactly as the Addis Ababa Action Agenda. Hence it should not be “whether or not” but should instead read – to facilitate the consideration of not requesting tax exemptions on goods and services delivered.

30. [As regards the fifth paragraph of the Executive Summary:]

The Guidelines suggest that where there is sufficient confidence in governance structures and in the tax system of a developing country, donors should be encouraged to refrain from requesting exemptions from tax for transactions relating to ODA projects in that country, unless the rules in the recipient country for taxing ODA-related transactions fail to comply with internationally recognized tax principles.

Suggest a rewording to read: “the guidelines suggest that in accordance with the objectives of the Addis Ababa Agenda and domestic resource mobilization donors should not request exemptions on transactions relating to ODA projects in a developing country.

Argument- the AAAA already states donors should consider not requesting exemptions. If a donor is investing in a water project there isn't any reason to link not asking for exemption to full adherence if the donor is already willing. Some donors are currently not insisting on exemptions without this requirement. There isn't a need to link with this requirement of adherence. My concern is really in the structuring of the provision.

31. [As regards the sixth paragraph of the Executive Summary:]

*The Guidelines deal exclusively with the tax treatment of projects involving development assistance provided by governments and their aid agencies, including assistance provided through international governmental organizations. They incorporate a number of existing international tax principles that are reflected in multilateral instruments as well as in the network of bilateral tax treaties; they recommend that the tax treatment of transactions related to ODA projects **generally** comply with these principles.*

At the meeting in London it was suggested inclusion of the word “generally”.

32. [As regards the seventh paragraph of the Executive Summary:]

*The Guidelines are not binding in any way. ~~They are~~—are drafted in general terms to facilitate their understanding by people who have limited tax expertise. They have been prepared for purposes of assisting donors and developing countries in determining the appropriate tax treatment of ODA projects. The Guidelines should facilitate the discussion of tax issues between donors and recipients of ODA. They should also avoid a proliferation of different rules, which would reduce transparency and increase the administrative and compliance burden of both donors and recipients. Since ~~many~~**some** donors already follow the policy of not requesting tax exemptions for the ODA that they provide, the Guidelines should promote a greater consistency in this area.*

The guidelines as written are binding on the developing countries because they state that if a developing country does not comply fully with the international tax rules then the donor should request and insist on exemptions. Hence we continue to request a rewrite of the relevant paragraphs above.

At the London meeting it was agreed that the word “many” will be changed to “some”. The use of the word “some” is a better representation of the situation at present.

33. [As regards the eighth paragraph of the Executive Summary:]

The Guidelines first deal with general considerations relevant to the issue of whether tax exemptions should be granted with respect to ODA projects. They recommend that donors should not require exemptions. (except to the extent that the tax rules of a recipient country are not consistent with the internationally recognized tax principles reflected in the Guidelines or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration of that country. As a quid pro quo for the donors not requesting exemptions,)

Suggest that the sentence stops at “exemptions”. That the sentences in bracket be eliminated.

Suggest that the [rest of the] paragraph [below] be reworded to read thus: “the guidelines recommend/encourage recipient countries apply internationally recognized tax principles in the tax treatment of ODA projects.”

((the Guidelines recommend that recipient countries ensure that their tax treatment of transactions relating to ODA projects be consistent with these internationally recognized tax principles.)) Guidelines 11 to 18 describe these principles in relation to the following:

Income taxation – employment remuneration

Income taxation – profits and payments to foreign enterprises

Indirect taxation – humanitarian crises

Indirect taxation – personal property and household goods of workers

Indirect taxation – temporary admission

34. [As regards the ninth paragraph of the Executive Summary:]

*The Guidelines also address the situations where specific exemptions are requested for ODA projects. In that case, the Guidelines recommend that officials from the Ministry of Finance **and** or the tax administration of the recipient country should be involved in the negotiation and drafting of these exemptions and that the recipient country should ensure that all legal requirements necessary to give force of law to these exemptions are satisfied. The Guidelines also provide that the relevant parts of any document providing for such exemptions be made publicly available. They also stress the importance of forecasting, and doing an analysis of, the foregone tax revenues resulting from these tax exemptions as well as using mechanisms that minimise administrative burdens and reduce fraud in relation to the application of these exemptions. Regardless of whether or not tax exemptions for transactions related to ODA projects are granted, the Guidelines also recommend that donors comply with the information and withholding tax requirements of recipient countries with respect to payments to taxable entities.*

[Suggest that the phrase “from the Ministry of Finance or the tax administration of the recipient country” be replaced by ““from the Ministry of Finance and the tax administration of the recipient country”]

35. [As regards paragraph 6:]

*6. The tax rules applicable in **some** developing countries will often provide for an exemption **from** ----- without the need for a specific exemption for ODA projects. For example, a non-resident importing goods which will be taken out of the country after being used for a project might qualify under the terms of a general customs regime for temporary imports. Also, a non-resident which provides services paid by a foreign donor without having a permanent establishment in the developing country where the work is carried *_on* might not **in some countries** be subject to income or corporate taxes under the income tax legislation of that country or under the terms of a generally applicable tax treaty, again without specific reference to the ODA project.*

Suggest inclusion of the words “in some countries” or the use of “might or might not” as this is not the practice in all developing countries. In some countries such companies and or individuals are subject to income tax.

36. [As regards paragraph 7:]

*7. Each donor is of course free to establish the conditions under which it is willing to provide ODA. Some donors may be concerned that the imposition of taxes would decrease resources available for **its** development activities and that it would be difficult to rally domestic support for payment of taxes.*

[Suggest to add “its” before activities.]

37. [As regards paragraph 9:]

9. Donor countries, their aid agencies and the international organizations through which ODA is provided to a country should therefore refrain from requesting exemptions from tax for transactions relating to ODA projects in that country ((except to the extent that, and only as long as, the rules in the recipient country for taxing ODA-related transactions fail to comply with internationally recognized tax principles or in exceptional cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration that country.))

Suggest elimination of the sentences in brackets and same be replaced with references to domestic resource mobilization, the Addis Ababa Agenda and the SDGs.

38. [As regards paragraph 10:]

10. The Guidelines deal exclusively with the tax treatment of ODA provided by governments (including governments of political subdivisions and local governments) or their agencies, whether the ODA is provided directly or through international organizations (these governments, agencies and international organizations being collectively referred to as “donors”). (While many of the recommendations formulated in the Guidelines could possibly apply to international assistance provided directly by NGOs, private assistance raises a distinctive set of issues and is therefore not addressed in these Guidelines.) Also, to the extent that a project involves public and private funding, the Guidelines only apply to the extent that the public funding constitutes ODA.

Suggest elimination of the sentences referencing NGOs, there isn’t any need to include since as is indicated in the sentence that the mention of NGOs raises different issues. It could also be mis-interpreted and could be used by NGOs. The paper is centered on ODA provided by governments and their agencies.

39. [As regards paragraph 11:]

11. The Guidelines incorporate a number of existing international tax principles that are reflected in multilateral instruments as well as in the network of bilateral tax treaties based on the OECD and UN Model Tax Conventions. The Guidelines recommend that the tax treatment of transactions related to ODA projects comply with these principles.

Suggest rephrasing as follows: “the guidelines recommend that the tax treatment of transactions related to ODA projects use/adopt these principles”. In this suggestion the word “comply” is changed to the word “use/adopt”. The use of the word comply appears like giving the developing country an ultimatum. You comply with the international tax principles in these guidelines or the donor will insist on exemptions. The priorities of a certain donor maybe different like more on governance instead and may be disposed to deferring to the tax law of a recipient country.

40. [As regards Guideline 1:]

1. Donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should not require exemptions from the taxes levied in recipient countries with respect to transactions relating to ODA projects, (except to the extent that the tax rules in the recipient country that would apply to these transactions are not consistent with these Guidelines or in exceptional

cases where serious concerns with the payment of tax to that country result from a review of the governance structure, tax system or tax administration of that country.)

Same concern as stated in many of my comments above.

41. [As regards Guideline 2:]

2. *Recipient countries should ensure that their tax treatment of transactions relating to ODA projects is consistent with these Guidelines.*

Suggest rewording as follows: “Recipient countries are encouraged to apply/adopt the tax treatments relating to ODA projects as contained in these guidelines”.

42. [As regards Guideline 5:]

5. *Where tax exemptions for transactions related to ODA projects are granted, recipient countries should make every effort to forecast the revenue impact of these exemptions and to do a tax expenditure review of them. **TO ALSO MONITOR THEIR IMPLEMENTATION AND THAT THE INFORMATION REQUIREMENTS ARE MET.***

43. [As regards Guideline 8:]

8. *Also, where such relief from indirect taxes, including custom duties, is granted with respect to goods and services used in relation to an ODA project, that relief should be granted through a refund or voucher method [**PREFERABLY USING THE TAX ADMINISTRATION AUTOMATED SYSTEMS**] and, in the case of imported goods, through an automated customs management system rather than through a direct exemption processed manually. The tax administration of the recipient country should also adopt procedures to ensure that goods and services on which indirect tax will be relieved are used for the purpose of the relevant project. [**THIS COULD BE DONE THROUGH RISKED BASED AUDITS AND REPORTING**]*

44. [As regards the Introductory paragraph of Part B:]

Part B of the Guidelines describes internationally-recognized tax principles that donor countries, their aid agencies as well as international governmental organizations through which ODA is provided may expect recipient countries to follow. ((As indicated in Guideline 1, tax exemptions for ODA projects are justified to the extent that the tax rules in the recipient country are not consistent with these principles.))

Suggest elimination of the last sentence. The UN Committee should not make such an emphatic statement that exemptions are justified because a recipient country is requiring taxation for example on non-resident although such provision is in their organic law. Also some richer countries may be requiring taxes like in the case example narrated by the IMF at the London meeting.

45. [Suggests the following changes as regards paragraph 21:]

*21. First, given the weakness of tax and customs administrations in many countries that are recipients of ODA, fraud is always a concern where tax exemptions are made available. Where tax or customs exemptions are granted, there is a substantial possibility of abuse of such exemptions. The abuse is likely to be more serious for indirect taxes. In the case of direct taxes, a typical issue is whether a particular contractor **or sub***

*contractor pays tax on its income from a project. The amount of tax at stake is relatively contained. However, in the case of indirect taxes, goods that have entered the country on an exempt basis can find their way into domestic commerce. If there is fraud in customs, all kinds of goods might be allowed to enter without paying VAT or customs duty, even though these goods should not actually qualify for exemption. The volume of goods involved might be several times the amount of the actual assistance. Depending on how the exemption is administered, fraud may well also arise from exempting local purchases from VAT. If the contractor is allowed to make purchases VAT-free upon presentation of an exemption card, the exemption is likely to be abused. Given the significant size of ODA, this potential for tax fraud **and its multiplier effects** can have a significant adverse effect on the domestic tax system.*

46. [Suggests the following change as regards paragraph 22:]

*22. Second, tax exemptions impose administrative costs on the tax administrations of recipient countries which need to keep track of the various exemptions provided and implement them. This difficulty is amplified by the diversity of the practices and expectations of the multiple donors that recipient countries may need to deal with. The administrative burden and the risk of fraud can vary depending on the way that exemptions are structured. Reducing this burden and **the associated** risk of fraud for recipient countries is one of the factors that have motivated some donors to review their policy concerning tax exemptions.*

47. [Suggests the following changes as regards paragraph 24:]

*24. Fourth, tax exemptions can cause economic distortions detrimental to domestic production in recipient countries. If, for example, imported goods to be used for an ODA project are exempt, but no exemption is available for domestic ~~purchases~~ **importers of the same type goods**, then there will be a distortion in favor of importations.*

48. [Suggests the following changes as regards paragraph 26:]

*26. Finally, granting tax exemptions to any market participants always runs the risk of creating pressures for further exemptions, whether directly as a means of alleviating competitive distortions that the initial exemption created or indirectly by creating a precedent that others can call on. Many recipient countries already find it hard to resist the pressure to grant specific tax exemptions when prospective private sector investors ask for such exemptions as an encouragement to invest on their territory. In addition, some recipient countries have complained that even where a donor agrees to finance the payment of tax with respect to a specific ODA project, consultants, **contractors and or sub contractors** who are bidding to execute the project are requesting tax exemptions simply because they have obtained exemptions for similar projects and wrongly assume that being exempt from tax with respect to income derived from ODA projects is the norm. Many donors have actually urged developing countries to cut back on exemptions in their wider tax systems in order to strengthen domestic resource mobilization. This does not sit comfortably with continuing to press for exemptions for ODA projects.*

49. [As regards paragraph 28:]

These difficulties combined with the improvement of tax systems in developing countries and a greater recognition of the need for strengthening domestic resource mobilisation have led to a growing acceptance of the principle that the general rules of taxation should apply to ODA projects. ((For instance, in 2004, the World Bank changed its policy to

allow financing of reasonable, non-discriminatory tax costs. Recipient countries do not have to provide exemptions for Bank-financed projects, where their taxation system has been determined to be a reasonable one for purposes of this policy. The determination by the World Bank as to which taxes are treated as costs that can be financed by loans is made on a country-by-country basis as part of the Bank's overall country assistance strategy.)) Thus far, experience with applying the policy shows that in only very limited cases are taxes found to be unreasonable and therefore ineligible for Bank financing. The net result is that virtually all taxes have been considered as eligible for financing ((of course, if a country were to introduce an unreasonably high tax, the Bank could consider it ineligible))). The Inter-American Development Bank (IDB) and Asian Development Bank (ADB) subsequently adopted similar policies. Similarly, the French Development Agency (Agence Française de Développement or AFD) has for a number of years included in certain aid agreements the financing of taxes. Development agencies in other countries, such as the United Kingdom, Norway, the Netherlands and Belgium, have adopted a similar policy.

The statement on the WB is incorrect. As I have stated in several discussions, the WB, its contractors and sub contractors request exemptions. The sentences in the bracket should be eliminated. It maybe their professed policy not to but that is not obtaining on the ground. Said statement is grossly incorrect. WB is saying one thing in public and doing the exact opposite on the ground.

The sentence in the second bracket should be eliminated. We do not need to speak for the WB on their ineligibility issue.

50. [Suggests the following change as regards paragraph 29:]

*29. Guidelines 1 and 2 endorse that approach. They recognize, however, that in some cases, there may be valid reasons for insisting on tax exemptions despite the various developments and considerations described above. This would **COULD** be the case to the extent that the tax rules of the recipient country are not consistent with the internationally recognized tax principles reflected in the Guidelines. Also, in exceptional cases, exemptions might be justified to address serious concerns with the payment of tax to a country resulting from a review of the governance structure, tax system or tax administration of that country. One example would be where the governance structure of the recipient country is such that there is a serious risk that taxes paid with respect to the ODA project would be diverted to uses that the donor would clearly disapprove. Another example would be where the tax system of the recipient country seeks to levy taxes that are discriminatory or are clearly excessive (as regards their rate or structure) compared to what similar countries would levy in similar circumstances. A third example would be where corruption in the tax administration of the recipient country would be so endemic that it would likely result in a large part of the taxes paid not being available to finance the budgetary expenditures of that country.*

51. [As regards paragraph 31:]

31. It is recognized that circumstances may change to the point where a donor country's assessment of the governance structure, tax system or tax administration of a recipient country may no longer justify paying taxes to that country. Also, serious deficiencies in the governance structure, tax system or tax administration of a recipient country may only appear during the implementation of a project. In these cases, the donor country ((will of course be entitled to require tax exemptions as a condition for continuing its

assistance project.)) It may also suspend disbursements, or even the implementation of the project, until these deficiencies are addressed.

Suggest the words in brackets be changed to “may”.

52. [As regards paragraph 32:]

32. *In the case of donors that operate in many countries, it would be cumbersome to look at the details of the governance structure and the tax regime in each country. It would, however, be a duplication of effort for each donor to carry out such a review on its own. Also, where different donors are involved in the same assistance project, applying a different tax treatment to their respective contributions raises equity and administrative issues. This raises the question as to whether internationally agreed standards could be applied to the tax treatment of all ODA. Unfortunately, it would be quite difficult to agree internationally on such standards and cumbersome to establish procedures for their application to each recipient country. Necessarily, judgment is involved and accordingly the best approach may simply be to leave this determination to each donor concerned. Duplication of effort can, however, be minimized if both donors and recipients share information. If the decisions reached are shared among donors, together with any responses that the authorities wished to make ((in the case of taxes considered unreasonable,)) then all could benefit from the analysis carried out. The intention would not be to pass a judgement on the wider quality of a country’s tax system but simply to make it easier for donors to conclude that taxes in a particular country are (or are not) broadly in line with normal international practice, and hence create some presumption that they should be allowed to apply to ODA projects. In practice, therefore — and as is to some degree already the case in relation to public expenditure management systems — donors could rely on reviews carried out by others, to the extent that those reviews are supported by credible documentation and analysis. The public disclosure of the tax-related provisions of agreements concluded between donors and recipient countries, as suggested in Guideline 4, will contribute to this sharing of information.*

Suggest that the sentence in bracket be eliminated. How would unreasonable be determined? This would be the tax law of a country. How would this vary from one donor to another donor. Do not think the guidelines should make such commentary especially when there isn’t a measurement for determining what is unreasonable and what is reasonable.

53. [As regards paragraph 33:]

33. *If, despite the above considerations, the donor simply is **INSISTING ON EXEMPTIONS FOR ITS PROJECT** (unwilling to provide general budgetary support through the payment of taxes,) the recipient country may have little choice than to accept the granting of tax exemptions. In such a case, however, it will still be important to take account of the procedural and administrative concerns reflected in these Guidelines.*

Suggest that the inserts replace the sentence in brackets.

54. [As regards paragraph 34:]

34. *As a quid pro quo for donors not insisting in specific tax exemptions for ODA projects, recipient countries need to ensure that their tax treatment of transactions related to these projects is consistent with principles that are typically incorporated in widely-agreed international instruments. These Guidelines include a list of such principles.*

Suggest the rewording here. Suppose a recipient country follows all these rules but is the #1 corrupt country or vice versa. Flagging this as a must with the use of the word ensure is not balanced especially when the donors may or may not. So if a country withholds on the salary of a GIZ consultant then the donor country should insist on exemptions although the withholding requirement is in their tax law while richer countries maybe withholding on similar type salary as is the case with Australia and the IMF.

55. [Suggests the following change as regards paragraph 38:]

*38. Whether these officials should come from the Ministry of Finance or the tax administration of the recipient country or from both is a matter that should be decided by that country taking into account the various responsibilities that have been granted to its tax administration. The officials that should be involved are those that would normally be responsible for designing tax rules applicable to foreign taxpayers. In many cases, these would be officials of the Ministry of Finance. In some jurisdictions, however, the tax administration has the responsibility of **ADVISING**, designing and implementing tax legislation; in such a case, it would seem appropriate to have representatives from the tax administration involved in the negotiation and drafting of provisions dealing with the tax treatment of ODA projects. Regardless of which tax officials are involved, it will be important for officials from the Ministry of Finance and the tax administration of the recipient country to liaise and cooperate as regards both the negotiation, **DESIGN** and the implementation of these provisions. Also, since the tax exemptions might cover different types of taxes that may be administered by separate parts of the tax administration, it would be necessary for the recipient country to ensure that all relevant parts of its tax administration are consulted.*

56. [Suggests the following change as regards paragraph 39:]

*39. Guideline 3 also provides that the provisions granting tax exemptions to donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should not be interpreted as extending to other parties, such as **CONTRACTORS AND** subcontractors, unless such extension is clearly provided for. Donor countries, their aid agencies as well as international governmental organizations through which ODA is provided should make sure that the private parties involved in the implementation of ODA projects do not wrongly assume that they are entitled to the same exemptions and that these private parties do not try to obtain such exemptions from the recipient countries.*

57. [Suggests the following change as regards paragraph 50:]

*50. Guidelines 7 to 9 provide guidance as to how this may be done in the area of indirect taxes and customs duties. As regards reliefs related to direct taxes, requiring taxpayers to declare the income received that is subject to an exemption and to identify the provisions under which the exemption is claimed facilitates risk-management of tax audits as well as the calculation of the amount of foregone tax revenues attributable to this type of tax exemption. **ALSO TO ASSIST IN THE DIRECT TAXES SO AS TO MINIMIZE TAX AVOIDANCE BY CONSULTANTS.***

58. [Suggests the following change as regards paragraph 54:]

54. Especially for materials that can easily be diverted to the local market, such as raw materials (e.g., construction materials) and other commodities (e.g., fuel), the agreement, or an annex thereto, should determine maximum quantities; at the very least,

*the agreement should provide for a mechanism to determine such maximum levels in common accord and prior to the introduction of the goods into the recipient country. **IT IS ADVISABLE THAT SPECIFICALLY FUEL AND OTHER PETROLUUM PRODUCTS NOT BE COVERED UNDER ANY EXEMPTION GIVEN THE HIGH COMMERCIAL NATURE OF SUCH PRODUCTS AND THE DISTORTIONARY IMPACT ON THE LOCAL MARKET.***

59. [Suggests the following change as regards paragraph 61:]

*61. From an administrative perspective, a system where the exemption is processed manually at the time it is requested should be discouraged. A reimbursement or voucher method and the use of an automated **TAX AND** customs management system are generally to be preferred and Guideline 8 recommends the use of these methods.*

60. [Suggests the following change as regards paragraph 73:]

*73. Like paragraph 1 of Article 19 of the UN Model and OECD Model and like the two Vienna Conventions mentioned in the previous paragraph, Guideline 11 provides an exception that allows a recipient country to tax the remuneration paid to local personnel who are permanent residents or nationals of that country. That exception is intended to ensure that locally-recruited personnel (e.g. **ANY TECHNICAL OR NON TECHNICAL STAFF**, security guards hired for the duration of an ODA project) are not entitled to the same treatment as employees of a state sent to a foreign country.*

61. [As regards paragraph 74:]

*74. The Guideline does not address the treatment of employees of international organizations as there is less international consensus on this issue. ((On the one hand, it could be argued that such employees, when providing services in relation to an ODA project, should be treated like any employee of the states that are members of that international organization and that provide the funding of that organization)). On the other hand, tax treaties typically do not provide a special treatment for employees of international organizations. In any event, the tax treatment of **INTERNATIONAL** employees of international organizations in the states that are members of that organization is often regulated by the agreements under which these organizations are established.*

Suggest that the sentence in the brackets be eliminated as there isn't any consensus.

62. [As regards paragraph 75:]

75. Guideline 12 provides for an exemption from income taxation in a recipient country in a case where a person employed by a foreign enterprise exercises his/her employment in the recipient country for a short period of time in connection with an ODA project. That exemption is based on a rule found in almost all bilateral tax treaties and incorporated in paragraph 2 of Article 15 of the UN Model and the OECD Model.

Where there isn't any bilateral tax treaty the tax law could apply.

63. [Suggest the following changes to the opening part of paragraph 101:]

*101. Exempting the personal property **IMPORTED IN THE RECIPIENT COUNTRY** of such workers from indirect taxes, including import duties, is justified as long as their stay is merely temporary and is related to the ODA project. Since there is currently no*

*established international practice that specifically deals with import duty and tax exemption for **IMPORTED** personal effects and household goods of persons who are not travellers but at the same time do not necessarily intend to relocate their place of residence, this Guideline therefore recommended that such exemption be generally provided. This should be done subject to the following conditions:*