Department of Health and Human Services
DEPARTMENTAL APPEALS BOARD
Appellate Division

Potentia Namibia Recruitment Consultancy
Docket No. A-14-79
Decision No. 2607
December 17, 2014

DECISION

Potentia Namibia Recruitment Consultancy (Potentia) appeals the decision of the Centers for Disease Control and Prevention (CDC) disallowing $173,354 in federal funds expended for the budget period April 1, 2009 – March 31, 2010 under a cooperative agreement. The disallowance was based on an audit finding by the HHS Office of Inspector General (OIG) that Potentia used these funds to pay a value-added tax (VAT) to the government of Namibia. CDC's Grants Management Officer determined that the VAT was an unallowable expenditure under the terms and conditions of the cooperative agreement. Potentia appealed this determination to the CDC Agency Review Committee (ARC) pursuant to 42 C.F.R. Part 50, subpart D, and the ARC upheld the determination.

For the reasons explained below, we uphold the disallowance.

Background

During the relevant time period, Potentia was registered in Namibia as a for-profit organization. Application for Federal Assistance, 1st page, item 7 (attached to Potentia ltr. dated 1/28/10). Potentia provides management and recruitment services, including a variety of human resource management services, such as payroll. ARC record at 49.[1] Under Namibian law, Potentia was required to charge a VAT of 15% on all income from goods and services and pay it over to the Namibian Ministry of Finance. *Id*. at 20, 27, 52. The VAT is a form of consumption tax. *Id*. at 52.

[1] The OIG audit report, including the Appendix to the report, is at pages 42-72 of the ARC record.

CDC entered into a cooperative agreement with Potentia for the project period September 30, 2005 through September 29, 2010. ARC record at 61.[2] Under the cooperative agreement, Potentia was to provide services to support the efforts of the Namibian Ministry of Health and Social Services to combat the HIV epidemic in Namibia. *Id*. at 49.

The OIG audited the cooperative agreement for the budget period April 1, 2009 through March 31, 2010. ARC record at 50. The OIG found that Potentia used $173,354 of the $14,486,635 it received for this budget period to pay the VAT on its income from recruitment services and retainer fees provided under the cooperative agreement. *Id*. at 6, 50-52. CDC's Grants Management Officer disallowed these costs on the ground that the "HHS Grants Policy Statement incorporated into the award by reference states that value-added taxes are unallowable under foreign grants." CDC ltr. dated 1/23/14, at 1. The ARC upheld the disallowance without further explanation. ARC record at 16-17 (ltr. dated 4/9/14).

The terms and conditions of the award for the budget period at issue state that the award "is subject to the terms and conditions incorporated either directly or by reference in the following: …. The [H]HS Grants Policy Statement, including addenda in effect as of the beginning date of the budget period." ARC record at 62-63. The 2007 HHS Grants Policy Statement (GPS) then in effect states, in a section regarding grants to foreign organizations, that "costs that are generally allowable under grants to domestic organizations also are allowable under foreign grants, with the following exceptions:"

> *Customs and import duties*. These costs, which include consular fees, customs surtax, value–added taxes, and other related charges, are unallowable under foreign grants and domestic grants with foreign components.

HHS GPS at II-113-114.[3]

The terms and conditions also incorporate by reference 45 C.F.R. Part 74, the uniform administrative requirements issued by the Department of Health and Human Services for awards to entities including commercial organizations. ARC record at 62-63.

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[2] The award notice for the budget period 4/1/09-3/31/10 is at pages 61-66 of the ARC record.

[3] The 2007 GPS can be accessed from http://www.hhs.gov/asfr/ogapa/aboutog/ogpoe/grants_mgmt_policy_sources.html. CDC provided an excerpt from the GPS showing the quoted provision, but on different page numbers (GPS II-118-119). CDC Statement dated 6/26/14, Att. 1.

Analysis

The terms and conditions of the award for the budget period at issue clearly provide that value-added taxes are not an allowable cost. Although the GPS provision on its face applies to grants, the GPS states that "statutes, regulations, policies, and the information contained in this policy statement that are applicable to grants also apply to cooperative agreements, unless the award itself provides otherwise." GPS at ii. Accordingly, Potentia's use of funds awarded under the cooperative agreement to pay a VAT materially violated the terms and conditions of the award, and CDC was authorized to disallow the amount in question. *See* 45 C.F.R. § 74.62(a) (stating that "[i]f a recipient materially fails to comply with the terms and conditions of an award, …the HHS awarding agency may…Disallow (that is, deny…use of funds…for) all or part of the cost of the activity or action not in compliance.").

Potentia nevertheless advances several arguments in support of its position that the disallowance should be reversed. As we explain below, none of these arguments have merit.

Potentia argues that the VAT was an allowable cost of the cooperative agreement because it meets four tests specified in the GPS for determining the allowability of costs: "Reasonableness (including necessity)," "Allocability," "Consistency," and "Conformance." Potentia ltr. dated 9/30/14, at 1, citing GPS at II-25. Potentia appears to read the following language in the GPS to mean that any cost meeting these four tests is allowable: "These four tests apply regardless of whether the particular category of costs is one specified in the cost principles or one governed by other terms and conditions of an award. These tests also apply regardless of treatment as a direct cost or an indirect cost." *Id.* (quoting GPS). However, the plain meaning of this language is that even if the cost principles or other terms and conditions of an award identify a particular <u>type</u> of cost as allowable, an actual cost of this type, whether charged directly or indirectly, is not allowable unless it meets the four tests. Moreover, the GPS states that these tests are derived from the cost principles, which state that "to be allowable under an award, costs must meet [the four tests and other] general criteria" and also list "selected items of cost," many of which are unallowable or are allowable only under certain circumstances. 2 C.F.R. Part 230, App. A, ¶ A.2., App. B. Thus, the requirements for reasonableness, allocability, consistency, and conformance are applied only if a cost is otherwise allowable under the terms and conditions of an award, which the VAT was not.

Potentia also observes that the funding opportunity announcement (FOA) for the cooperative agreement is incorporated by reference in the "Special Terms and Conditions" of the award and contains a section on "Funding Restrictions" (section IV.5)

that makes no reference to the VAT.[4] Motion to compel production dated 8//14, at 1-2; ARC record at 63. However, nothing in the FOA states or even suggests that the funding restrictions listed there would be the only limitations on allowable costs. Nor does the FOA indicate that any limitations on allowable costs in other terms and conditions of the award would somehow be superseded by the FOA. Accordingly, since the GPS, which is also incorporated by reference in the terms and conditions of the award, expressly prohibits the use of funds for a VAT, Potentia could not reasonably infer from the absence of any such prohibition in the FOA that a VAT is an allowable cost of the award.

Potentia also asserts that CDC knew that Potentia was a for-profit organization that was required to pay VAT for the services it provided under the award absent an exemption as well as that Potentia had no sources of funding to pay the VAT other than the cooperative agreement. Motion to compel production dated 8/1/14, at 2. Accordingly, Potentia argues, there was "an unspoken term of the award" that if Potentia were not exempt from paying VAT on the services it provided pursuant to the cooperative agreement, "the respondent would take all reasonable steps available to it to ensure that the appellant did not . . . suffer material financial damages merely as a result of providing the services[.]" *Id*. at 3. We read this as an argument, albeit a meritless one, that CDC should be estopped from disallowing the cost of the VAT based on CDC's alleged knowledge of Potentia's obligation to pay VAT and its inability to do so without using award funds. Potentia does not point to any evidence that CDC actually knew before making the award that Potentia was not exempt from the VAT. But even assuming CDC had such knowledge as well as knowledge of Potentia's financial status, that would not be a basis for treating the VAT as an allowable cost of the award. It is well-established that "the government cannot be estopped absent, at a minimum, a showing that the traditional requirements for estoppel are present (i.e., a factual misrepresentation by the government, reasonable reliance on the misrepresentation by the party seeking estoppel, and harm or detriment to that party as a result of the reliance) and that the government's employees or agents engaged in 'affirmative misconduct.'" *Oaks of Mid City Nursing & Rehab. Ctr.*, DAB No. 2375, at 31 (2011), citing *Office of Personnel Management v. Richmond*, 496 U.S. 414, 421 (1990), and *Pacific Islander Council of Leaders*, DAB No. 2091, at 12 (2007) ("Equitable estoppel does not lie against the federal government, if indeed it is available at all, absent at least a showing of affirmative misconduct."). Here, Potentia does not even allege that CDC made a factual misrepresentation regarding the use of CDC funds for the VAT, much less that CDC made a factual misrepresentation that rose to the level of affirmative misconduct. Accordingly, there is no basis for estoppel.

[4] Neither party provided a copy of the FOA, which was published in the Federal Register on August 18, 2005 at 70 Fed. Reg. 48566-48573. *See* http://www.gpo.gov/fdsys/pkg/FR-2005-08-18/html/05-16373.htm.. We have added a copy of the FOA to the record as Board Exhibit 1.

Potentia suggests in the alternative that both it and CDC were either unaware that the terms and conditions of the award made a VAT unallowable or unaware that Potentia was not automatically exempt from paying a VAT for services rendered to CDC, so that there was "a material error of fact fundamental to the parties entering into the agreement." Motion to compel production dated 8/1/14, at 2-3. Potentia seems to be arguing that the term and condition at issue is void because neither party would have entered into the cooperative agreement had it been aware of these facts. Potentia's premise that neither party would have entered into the cooperative agreement under these circumstances is pure speculation on Potentia's part. Furthermore, the terms of the award, including the incorporation of the GPS restrictions, were available to Potentia before it chose to accept the award. Potentia can hardly claim a right to change the terms retrospectively if it failed to read the applicable terms before accepting the award. In any event, the Board's role here is to determine whether Potentia's use of funds to pay the VAT materially violated the terms and conditions of the award, not the state of mind of the parties when the award was offered and accepted.

Potentia also asserts that since it is obligated by Namibian law to charge the VAT, CDC, by disallowing the cost of the VAT, is "requiring [Potentia] to blatantly contravene Namibian law in order to carry out the required functions and services that assist the CDC Namibia office to achieve their goals." Potentia ltr. dated 5/5/14, at 1. However, the terms and conditions simply precluded Potentia from using funds from the award to pay a VAT on services provided by Potentia under the cooperative agreement and did not prohibit Potentia from charging a VAT on those services.

Potentia also points out that in December 2012, CDC issued a notice stating that "value-added taxes . . . are an allowable cost effective as of September 13, 2012 through September 12, 2013" for "non-host-governmental entities" (defined to include "foreign (non-governmental) entities") and that such entities "will be receiving an amended Notice of Award with revised terms and conditions which include this allowable cost." Potentia ltr. dated 5/5/14, at 1 and attached memorandum to CDC Grantees dated 12/5/12; Motion to compel production dated 8/1/14, at 2, citing ARC record at 67-68. According to Potentia, moreover, CDC later gave notice that "the VAT is now an allowable expense under these grants." Potentia ltr. dated 5/5/14, at 1. Potentia questions why "if in hindsight the original condition was found to be incorrect, …the CDC continue[s] to insist on sustaining an incorrect decision which, as an organization, it no longer enforces." *Id*. However, nothing in the record indicates that CDC determined that it lacked authority to impose a term and condition making the VAT an unallowable cost or that its imposing such a term and condition was otherwise "incorrect." Instead, it appears that in its December 2012 notice, CDC was simply exercising its discretion to treat the VAT as an allowable cost for certain recipients for a limited period of time beginning

September 13, 2012.[5] Potentia identified no basis on which we could find that CDC lacks legal authority to treat the VAT as an unallowable cost for the time period at issue here.

Finally, Potentia asserts that, instead of requiring it to repay CDC for the cost of the VAT, CDC could ask the Namibian government to refund the VAT that Potentia paid from award funds. Potentia ltr. dated 5/5/14, at 2. Potentia cites an August 9, 2013 letter from the Namibian Ministry of Finance (ARC record at 6-8) stating that under a bilateral and technical assistance agreement between Namibia and the United States, VAT may be refunded. *Id*. Potentia alleges that CDC has not pursued this option despite several requests by Potentia and has provided no reason for its inaction. *Id*. However, it is simply irrelevant that the Namibian government, operating under an international agreement, might refund the VAT. The Board does not have authority to order CDC to seek a refund of the VAT from the Namibian government. Moreover, as CDC notes, while a refund might affect the disallowance repayment options, it would not affect the disallowance itself.[6] *See* CDC Statement dated 6/24/14, at 7.

Conclusion

Based on the analysis above, we uphold the disallowance of $173,354.

/s/
Leslie A. Sussan

/s/
Constance B. Tobias

/s/
Sheila Ann Hegy
Presiding Board Member

[5] CDC states that this "deviation" to its "policy" was "only for the period covering September 13, 2012 through September 30, 2014 and only for certain grantees." CDC statement dated 6/26/14, at 5.

[6] Based in part on this rationale, the Presiding Board Member denied Potentia's motion to compel discovery of the "PEPFAR/CDC Technical Assistance Agreement for Namibia" and the "bi-lateral agreement between the United States of America and the Republic of Namibia." Ruling Denying Motion to Compel Discovery, August 29, 2014 (attached).

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Department of Health and Human Services
DEPARTMENTAL APPEALS BOARD
Appellate Division

Potentia Namibia Recruitment Consultancy
Docket No. A-14-79
August 29, 2014

RULING DENYING MOTION TO COMPEL DISCOVERY

I deny the appellant Potentia Namibia Recruitment Consultancy's motion to compel the respondent, the Centers for Disease Control and Prevention (CDC), to produce the following:

- The PEPFAR[1]/CDC Technical Assistance Agreement for Namibia and
- The bi-lateral agreement between the United States of America and the Republic of Namibia.

Background

The appellant appeals the April 9, 2014 decision of the CDC Agency Review Committee sustaining the disallowance of $173,354 in federal funds awarded under a cooperative agreement with CDC to combat HIV in Namibia. The appellant does not dispute spending the funds on value added taxes (VATs) to the Namibian government based on the cost of services provided under the agreement. CDC determined that value-added taxes under foreign grants are unallowable according to the HHS Grants Policy Statement CDC says was incorporated by reference in the notice of grant award.

The appellant by e-mail on July 8, 2014 requested the two documents from CDC, which declined to provide them to the appellant on the ground that they were not relevant "to whether value-added taxes could be paid with grant funds" and were not part of the record before the Agency Review Committee. The Board by letter dated July 18, 2014 granted the appellant the opportunity to submit a motion to compel production and to explain "in greater detail the relevance of the requested materials to showing that the claimed costs were allowable charges to the federal grant at issue in this proceeding or will otherwise provide a basis to reverse the disallowance." The appellant filed its motion to compel CDC to produce the two documents on August 1, 2014, and CDC filed its opposition to the motion on August 12, 2014.

[1] President's Emergency Plan for AIDS Relief.

Bases for the motion

The appellant argues that the two documents will show whether the grant contained an "unspoken term" that "the appellant would be specifically exempt from any VAT liability" arising from its providing the services required by the grant and that, "if the appellant were not so exempted, the respondent would take all reasonable steps available to it to ensure that the appellant did not, on account of no fault on the part of the appellant, suffer material financial damages" from having provided those services "while complying with the laws of Namibia." Motion at 3. The appellant also argues that the documents "contain information that will enable the appellant and the Board to assess what exactly was the true position with respect to, amongst others, the VAT liability of Namibian for-profit service providers to the US Government or its agencies on technical agreements generally and under PEPFAR specifically at the time of the relevant award." *Id*.

The appellant also laid out the merits case it intends to present based on the documents. The appellant argues essentially that CDC was aware that the appellant would be required to pay a VAT and had no other sources of funding with which to do so other than through the cooperative agreement with CDC. Motion at 2. Alternatively, the appellant infers that "[t]he parties were as a matter of fact unaware" either "that VAT was an unallowable expense" or "that the appellant was not automatically exempt from paying VAT to the Namibian Government" under agreements between the United States and Namibian governments. *Id*. at 2-3. The appellant bases those inferences on the fact that, after the HHS Office of Inspector General identified the appellant's VAT payments as unallowable, HHS approved two "class deviations" permitting payments of VATs with CDC awards during later periods. CDC Response to Notice of Appeal at 5-6; Agency Review Committee Record at 67-72. The appellant states that each of the two possible misunderstandings was "a material error of fact fundamental to the parties entering into the agreement." Motion at 2-3. The appellant has also indicated that the documents might show that CDC could seek recovery of the VAT from the Namibian government. *See* Notice of Appeal at 2 (stating that "CDC Namibia" could approach the Namibian Government to amend the current Technical Assistance Agreement to allow "VAT refunds to be claimed retrospectively since date of inception of the project.").

Discussion

As noted in the Board's July 18 letter, the Board will grant discovery only of specific items of information that the Board determines a party needs "to directly address a specific, dispositive issue in a case." In an appeal of a disallowance of federal funds awarded under grants and cooperative agreements, the dispositive issue is whether or not the disallowed costs were allowable charges to grant funds. As also noted in the Board's letter, the Board has long held that the grantee or recipient of federal funds bears the burden of demonstrating that its expenditures of federal funds are allowable, once the

federal agency has questioned the allowability of those expenditures. *Recovery Res. Ctr., Inc.*, DAB 2063, at 16 (2007). The Board is "bound by all applicable laws and regulations" and "must uphold a disallowance if it is supported by the evidence submitted and is consistent with the applicable statutes and regulations." 45 C.F.R. § 16.14; *W. Va. Dep't of Health & Human Res.*, DAB No. 2185, at 20 (2008). The Board "does not have jurisdiction to forgive a disallowance where the grantee does not contest the legal or factual basis of the disallowance but merely seeks equitable relief" and "did not argue that the costs in question are allowable as a matter of law or fact." *Harambee Child Dev. Council, Inc.*, DAB 1697, at 4 (1999).

Here, the appellant has not demonstrated that the two documents it seeks would help demonstrate that the disallowed expenditures were allowable charges to federal funds under the laws, regulations and terms of the award that were in effect at the time of the expenditures. The documents instead appear to be sought to support arguments that do not provide a legal basis for the Board to reverse the disallowance. The Board, for example, does not have authority to order CDC to seek recovery of the VAT from the Namibian government, or to require that CDC retroactively apply HHS policies that were not applicable when the expenditures were made. Even if CDC itself could forgive the disallowance or recover the funds from sources other than the appellant, the Board has no authority to order CDC to do so. Finally, the Board's Practice Manual states that "an appellant should first search its own files for any relevant documents." http://www.hhs.gov/dab/divisions/appellate/practicemanual/manual.html#20. Appellant asserts in its motion that it obtained its information about the content of the documents sought from the Namibian Receiver of Revenue within the Ministry of Finance. Motion at 3. This assertion suggests that even if appellant does not already have copies of these documents in its files, it has access to the documents or can obtain access from the named source. Thus, even assuming appellant had made a showing that the documents are relevant, it has not made a showing that not ordering the CDC to produce these same documents will impede appellant's ability to fairly present its case.

For these reasons, I decline to order CDC to produce the documents the appellant requested. I note that the parties, in briefing and responding to the appellant's Motion, have done considerable briefing on the merits of the case. Accordingly, **the parties should inform the Board within one week after receiving this ruling whether they will rest their cases on that briefing or would like to submit supplemental briefs** before the Board decides the matter, in which case the Board will set a briefing schedule.

/s/
Sheila Ann Hegy
Presiding Board Member

cc: Sudevi Ghosh
Senior Attorney, CDC (by email)