NINETY-FIFTH SESSION

Judgment No. 2255

The Administrative Tribunal,

Considering the complaint filed by Mr J.B. D. B. R. (hereinafter "the lead complainant") against the United Nations Educational, Scientific and Cultural Organization (UNESCO) on 19 June 2002, the Organization's reply of 10 September, the complainant's rejoinder of 12 November 2002 and UNESCO's surrejoinder of 19 February 2003;

Considering the complaint filed by Mr A.J. R. against UNESCO on 10 May 2002, the Organization's reply of 2 August, the complainant's rejoinder of 22 October 2002 and UNESCO's surrejoinder of 13 January 2003;

Considering the complaint filed by Mr P. W. against UNESCO on 15 May 2002 and corrected on 11 June, the Organization's reply of 9 September, the complainant's rejoinder of 29 October 2002 and UNESCO's surrejoinder of 10 February 2003;

Considering Articles II, paragraph 5, and VII of the Statute of the Tribunal;

Having examined the written submissions and decided not to order hearings, for which none of the parties has applied;

Considering that the facts of the case and the pleadings may be summed up as follows:

A. The complainants are nationals of the United States of America who, at the time of the material facts, were US residents employed by UNESCO at its New York Office.

By an Administrative Circular of 5 July 1999, UNESCO staff were informed that the Director-General had decided to amend Staff Rule 103.18(b). The result of this amendment was that the Organization's system for income tax reimbursement changed, with effect from the 1999 tax year, from being a "last-income" system to being a "first-income" system. Staff members who were US citizens or residents were specifically informed of this change by Circular Letter BOC/XC/5 of 25 January 2000.

In June and July 2000 the Organization informed the complainants that their tax reimbursement requests for 1999, which they had submitted on the basis of the last-income method of assessment, had been overestimated and that as a result two of the complainants had received overpayments.

On 3 and 5 July 2000, two of the complainants wrote to the Assistant Director-General for Management and Administration challenging the legitimacy of the amended Staff Rule 103.18(b). By a memorandum of 30 November 2000 the Organization's Comptroller urged the Acting Director of the New York Office to take steps to recover the overpayments. That same day, two complainants sent written protests to the Director-General seeking the annulment of the amendment to Rule 103.18(b) on the grounds that it violated the principle of tax exemption for United Nations system incomes and discriminated against US citizens. On 4 December 2000 they submitted written protests against the Comptroller's decision to recover overpayments. On 9 December 2000 the lead complainant submitted a protest against the calculation of his tax reimbursement for 1999. He too sought the annulment of the amendment. Having received no reply to these protests within the time limit stipulated in the Statutes of the Appeals Board, they filed notices of appeal on 8 and 9 February 2001, followed by detailed appeals on 2 and 7 March 2001. Their appeals were joined by the Appeals Board, which considered, in its Opinion and Recommendation of 21 December 2001, that the appeals should be allowed. However, the Director-General decided not to accept the opinion and recommendation of the Appeals Board and informed the complainants accordingly by letters of 20 and 21 March 2001, which constitute the impugned decisions.

B. The complainants argue that the new Rule 103.18(b) violates the fundamental principle of equalisation of pay

that exists throughout the United Nations system. Unlike the previous rule, by shifting the burden of higher marginal rates onto non-UNESCO income and distributing exemptions and deductions on a *pro rata* basis between UNESCO income and non-UNESCO income, the new rule places staff members who are liable for US income tax at a disadvantage in relation to those whose UNESCO income is exempt from taxation.

In addition, the new rule violates the principle that UN system income should be exempt from taxation, because the first-income method of assessment results in increased taxation of staff members' income. In support of their argument they refer to the Tribunal's Judgment 2032 and to the findings of the High Level Committee on Management of the United Nations System Chief Executives Board for Coordination (CEB) on this issue, which were published on 15 February 2002 under the reference CEB/2002/HLCM/R.6.

They also contend that the new rule violates their contractual and acquired rights and that it is unfair in its application, creating inequalities between similarly-situated staff members.

They ask the Tribunal to order the Organization to reinstate the previous version of Staff Rule 103.18(b), which used the last-income method for tax reimbursements; to order UNESCO to pay them amounts, that they specify, representing the difference between the reimbursements they would have received for 1999, 2000 and 2001 under the last-income method and the reimbursements they actually received for those years under the amended rule, or alternatively require it to recalculate their tax reimbursements for 1999, 2000 and 2001 using the last-income method of the reinstated version of Rule 103.18(b), and pay them any amounts due pursuant to such recalculations. They also ask the Tribunal to order UNESCO to calculate their reimbursements in future using the reinstated methodology of the previous version of the rule and to pay the sums claimed within 90 days of the delivery of the judgment. Two of the complainants also seek interest on the sums claimed, and one seeks the reimbursement of certain expenses associated with the proceedings and the conversion of two days' annual leave, taken for the purposes of the proceedings, into special leave with pay.

C. The Organization replies that the complaints are time-barred, since the complainants' initial protests were filed long after the new Rule 103.18(b) came into force. It denounces the filing of a second protest on 4 December 2000 as an attempt to circumvent the time limits for the internal appeal, the issue of the recovery of the overpayments being inextricably linked with that of the legality of Rule 103.18(b).

On the merits, the Organization refers to the Tribunal's Judgment 1224 and asserts that there is no uniform practice of tax reimbursement in the United Nations system. Consequently, the plea that the amended rule violates the fundamental principle of tax exemption is unfounded. UNESCO considers that it is up to States to grant tax exempt status to United Nations system income, whereas the Organization's responsibility is confined to tax reimbursement. UNESCO has met its obligation by reimbursing staff members who are subject to taxation.

It considers that the issue of the tax reimbursement method is a matter for the discretion of international organisations in which the Tribunal should not interfere. Referring to the case law, it denies that the new rule is discriminatory, given that the same reimbursement system is applied to all staff members who are subject to taxation. It also rejects the allegation of a breach of contractual and acquired rights, since the complainants' respective contracts contain no clause entitling them to a particular method of tax reimbursement, and the conditions defined in the case law for breach of an acquired right are not satisfied.

Lastly, the Organization refers to rulings by the Administrative Tribunal of the Organization of American States and by the World Bank Administrative Tribunal to support the view that a distinction should be drawn between the principle of reimbursement and the method of reimbursement, and that the latter does not constitute an acquired right.

D. In their rejoinders the complainants maintain that their complaints are receivable because the disputed amendment could not be challenged by them until individual decisions applying the amended rule to them were taken and they knew specifically how it would apply to them. They reiterate their arguments on the merits, emphasising that the new rule breaches an essential condition of employment in the international civil service by creating two classes of international civil servants within the United Nations system: those whose income is effectively reduced as a result of taxation, and those whose income is not.

E. In its surrejoinders the Organization maintains its position on all issues.

CONSIDERATIONS

1. The lead complainant, a citizen of the United States and a staff member of UNESCO since 1974, contests the amendment to Staff Rule 103.18(b) which took effect on 5 July 1999, changing UNESCO's method of reimbursement of income tax from a "last-income" methodology to a "first-income" methodology, as being discriminatory and unfair in its application to him.

2. Apart from certain minor differences in the factual background and the precise amounts of the tax refunds to which each complainant claims to be entitled, the issues raised in their respective complaints are identical. The Tribunal orders them joined.

3. Previously, Staff Rule 103.18(b) read as follows:

"The amount of the reimbursement shall be the difference between the tax payable on the staff member's total income, including UNESCO earnings, and the tax which would be payable on his income excluding UNESCO earnings."

4. That is the last-income method.

5. Rule 103.18(b) as amended incorporates the first-income method and reads as follows:

"The amount of reimbursement shall take into account all deductions, exemptions or exclusions to which the staff member is entitled under applicable tax laws. If the staff member has other income subject to tax by the same country, the amount of the reimbursement shall be the tax which would be payable if his income consisted solely and exclusively of the salary and emoluments received by him from UNESCO. In that case, any applicable deductions, exemptions or exclusions shall, where appropriate, be taken into account on a pro rata basis, except that where they relate to a specific category of income they shall not be prorated to the non-UNESCO income."

6. On 5 July 1999 Administrative Circular 2083 informed UNESCO staff of the amendment. By Circular Letter BOC/XC/5, dated 25 January 2000, staff members who are citizens or residents of the United States were specifically advised of the amendment.

7. On 12 June 2000 the lead complainant submitted a request for reimbursement of US federal income tax for the year 1999 to the Bureau of the Comptroller. He used the previous last-income methodology and calculated a tax refund of 5,773.66 United States dollars. On 16 June 2000 the Bureau of the Comptroller issued a "tax reimbursement computation" and claimed that the reimbursement due to him amounted only to 1,811 dollars pursuant to the amended rule's first-income methodology.

8. In a memorandum dated 5 July 2000, the lead complainant protested to the Assistant Director-General for Management and Administration. No direct reply to this protest was received but the Bureau of the Comptroller responded by recalculating the reimbursement at 2,629 dollars. This calculation is neither signed nor dated.

On 30 November 2000 the administration indicated to the two other complainants, each of whom had received a refund calculated in accordance with the former Staff Rule, that it would require repayment of all amounts allegedly overpaid. Accordingly, on 4 December they protested to the Director-General, but obtained no reply.

On 9 December 2000 the lead complainant protested to the Director-General, maintaining his original position that the reimbursement should be calculated in accordance with the old Staff Rule's second-income methodology. Since he did not receive a response within the time limit required by the applicable Staff Rule, he filed a notice of appeal with the Secretary of the Appeals Board on 9 February 2001 as did the two other complainants on 8 February 2001.

9. The appeals of all three complainants were joined and were heard on 3 December 2001. On 21 December 2001 the Appeals Board recommended in favour of the appellants, finding that the appeal was receivable, and that amended Staff Rule 103.18(b) violated the principle of non-taxation of UN system incomes and resulted in unequal treatment of those UNESCO staff members whose UNESCO incomes are subject to taxation. It held that:

"[...] The only valid method is to reimburse the difference between the amount actually paid and the amount the

staff member would have paid if the State had not taken into account UNESCO incomes."

10. The Appeals Board also found that the amendment violated the complainants' acquired rights.

11. By letters dated 20 and 21 March 2002, the Director-General decided not to follow the Appeals Board's recommendations. These are the impugned decisions.

Receivability

12. The Organization did not contest the receivability of the appeals to the Appeals Board and does not now contest that the complaints were timely filed in accordance with the Tribunal's Statute. Notwithstanding these facts, however, UNESCO now argues that the internal appeals to the Appeals Board were irreceivable and that accordingly, the complaints to the Tribunal are also irreceivable.

13. In Judgment 522, the Tribunal was faced with the identical situation and held:

"There can be no doubt that the appropriate, if not the only, time to take the point was before the Appeals Board, since it is the proceedings before the Board that are said to be out of time [...] and not the proceedings before the Tribunal itself. The Tribunal has therefore now to consider whether or not justice requires that the Organization should be given a second opportunity to take the point. Three factors ought to be considered. The first is whether the point is a clear and compelling one. The second is whether there is an adequate explanation of the Organization's failure to take it. The third is whether the complainant may be prejudiced by the Organizations's failure."

14. It would not be in the interest of justice to allow the defendant Organization to advance this argument at this stage. In addition to not providing any credible explanation for its failure to press the point before the Appeals Board, UNESCO's argument is not clear and compelling. The lead complainant protested the calculation of his reimbursement on 5 July 2000. Thereafter, there appear to have been some exchanges between the parties, and UNESCO in fact changed the calculation in the complainant's favour. The second reimbursement assessment is neither signed nor dated. On 30 November 2000 the Organization indicated, for the first time, that it intended to claim back refunds from two complainants who in its view had been overpaid. The lead complainant challenged the second reimbursement assessment on 9 December 2000, well within the time limit established by the applicable rules. No reply from the Director-General having been received within the statutory time limit, his protest was deemed to have received a negative reply in accordance with paragraph 7(c) of the Statutes of the Appeals Board. The complainant then appealed that deemed negative reply on 9 February 2001. Although the Organization argues that the contested action was taken on 5 July 1999, the complainant was not in a position to contest Administrative Circular 2083 issued on that date until an individual decision was rendered which actually applied the amendment of Rule 103.18(b) to him. Any appeal or complaint filed before that time would undoubtedly have been objected to by the Organization as being premature. Far from being compelling, the Organization's position is entirely without merit.

15. The complaints are receivable.

The merits

16. The complainants raise a number of arguments which, in the view that it takes of the matter, the Tribunal does not find necessary to comment on in detail. Thus the Tribunal will not comment on the allegations that the amended Staff Rule 103.18(b) is bad for vagueness, that the method of its being put into force was unfair, or that it is in breach of their acquired rights.

17. The complainants' further argument that the Rule is discriminatory, were it to be considered, would require examination in the light of the Tribunal's previous ruling in Judgment 1224 where the first and last-income methods were also an issue:

"8. The Tribunal's answer to her first plea is that in this particular area there is no common-system method which the [defendant organisation] is in law obliged to apply. The principle of equal treatment therefore does not necessarily mean equal treatment for the staff of the various international organisations, each of which is autonomous and applies its own rules and regulations to its staff. Nor is the [defendant organisation] required - as the Tribunal ruled in Judgment 1073 [...] under 5 - to 'achieve uniformity with United Nations Staff Regulations'."

18. While by its terms this passage only refers to alleged discrimination by comparison to employees of other organisations, it is arguable that it also applies to employees in the same organisation where their different circumstances result from the different laws to which they are subject. Be that as it may, the Tribunal does not find it necessary to deal definitively with the point in the light of what follows.

19. In addition to the points already mentioned, the complainants also argue that the amended Staff Rule violates the fundamental principle of the law of the international civil service by which the remuneration of such employees must be exempt from national taxation. They cite Judgment 2032, in which the Tribunal held that:

"Exemption from national taxes is an essential condition of employment in the international civil service and is an important guarantee of independence and objectivity. It cannot be made to depend upon the whim of national taxing authorities who will be understandably reluctant to admit any exceptions to their claims."

20. The fundamental principle of tax exemption is not denied by the Organization, which instead claims that the new Staff Rule respects and gives effect to it. It again relies on a passage from Judgment 1224:

"9. As for her second argument, the staff member's entitlement under the Staff Regulations is to refund of tax paid on [a staff member's] Agency earnings only, whatever his duty station. Since that is exactly what the complainant received, as did staff in Vienna, she was in no way discriminated against. The fact that she was denied the $70,000 exclusion because she was not resident outside the country was due to the requirements of United States tax law, not to discrimination by the Agency.

10. She puts forward several subsidiary objections.

(a) The last-income method, she says, is the only one to put staff members who are liable to tax on international income in the same position that they would be in if their international income were exempt from tax.

The Tribunal's answer is that what staff members are entitled to under the rules is a refund of tax paid on Agency earnings only."

[Emphasis added]

21. It is to be noted that these passages, although treated by UNESCO as being statements of law, are in reality grounded in a finding of fact implicitly made by the Tribunal. That finding is that the first-income method provided for a refund of tax paid on "Agency earnings only". It seems apparent that the Tribunal had no evidence before it to support such finding for there is no mention of it anywhere in the Judgment, including the summary of the arguments of both parties (see sections B, C, D, E, and F of Judgment 1224). Nor is the finding self-evident or axiomatic, as appears from the Tribunal's later judgment cited below.

22. The situation is quite different for Judgment 2032. There, the Tribunal had and relied upon evidence that showed beyond any dispute that the second-income method resulted in the complainant paying taxes which would not have been payable at all had he not received "exempt" income from the international organisation employing him (the OPCW). That can only mean that notwithstanding its "exempt" status, such income was attracting tax. The Tribunal said:

"Where a State imposes tax upon its nationals who are international civil servants in receipt of income - some of which is tax exempt and some of which is not - the only proper method of determining how much tax should actually be paid is to calculate the hypothetical amount which would be due if the exempt income had not been received. The complainant has done just that and has shown that if he had not been in receipt of income from the [Organisation] he would not have been subject to German tax on his (and his wife's) remaining income."

23. Since the date of the release of Judgment 2032 there has been further confirmation of the factual finding which it contained. In a report (CEB/2002/HLCM/R.6) dated 15 February 2002 by the High Level Committee on Management of the United Nations System Chief Executives Board for Coordination (CEB) dealing with this very subject we find the following:

"5. US nationals do not receive uniform treatment. The US government policy is not to treat UN income as exempt, but instead to provide relief via reimbursement schemes. Tax equalization and reimbursement schemes are

cumbersome substitutes for tax *exemption*. The use of these mechanisms treats US nationals employed by the UN differently from other nationalities, because the US government requires that UN-derived salaries and emoluments are added to [a] US staff member's other-source income for tax reporting purposes. When calculating tax reimbursement, some organizations consider UN-derived income as 'last income', while other organizations treat it as 'first income'. In those organizations with 'first income' agreements, a US national's non-UN income does not receive full benefit from exemptions and standard/itemized deductions and is also taxed at the highest marginal rate. [Emphasis added]

6. Annex I provides a simple illustration of the two tax reimbursement approaches. Based on a hypothetical case involving both UN-source and private-source income, the staff member who works in a 'first income' organization pays $9,475 (15,749-6,274) more tax than a staff member who works in a 'last income' organization. In addition, US staff member income is grossed up, which affects other tax related provisions as follows:

• Loss carry forward (for example on real estate or investments) is limited by the amount of adjusted gross income;

• Staff may become ineligible for educational assistance, e.g. for advanced degrees due to adjusted gross income;

• Staff members may not be able to take advantage of certain types of individual retirement accounts such as Roth IRAs. US staff members who work in 'last income' organizations are similar to UN staff members who are not US nationals, since the non-US staff members' income is exempt and not reportable to taxing authorities.

7. 'Tax free' income is one of the fundamental features of UN remuneration. This is a factor taken in to consideration when comparing the emoluments of the UN with other similar organizations and in attracting staff. Although the tax reimbursement process is intended to 'equalize' the US national staff member with respect to taxes on UN income, this is not the case for 'first income' organization."

Annex I to the report contains the following:

"Assume that a US staff member has the following taxable income:

Total UN salary and emoluments	$150,000
Non UN income	60,000
Less: Foreign income exclusion	-74,000
Less: Standard deductions and personal exemptions	-18,200
Taxable income	117,800

(1) If the US staff member worked in a UN organization that applied the policy that UN income is last income, the staff member's tax, after tax reimbursement from the organization of $21,526, would be approximately $6,274 calculated as follows:

Tax paid on total taxable income of $117,800 (using 1999 tax tables, filing jointly)	$27,800
Tax on UN income reimbursed to staff member	21,526
Net tax paid by the staff member on non UN income of $42,800 (60,000-18,200 of deductions/exemptions)	6,274

The tax paid by the staff member in this case is what would have been paid if the staff member had no UN income.

(2) If the US staff member worked in a UN organization with the policy that UN income is first income, the staff member's tax, after reimbursement by the organization of $12,051, would be approximately $15,749 calculated as follows.

Tax on total taxable income of $117,800	$27,800
UN income	150,000

Less: Foreign income exclusion	-74,000	
Less pro-rata share of standard deduction And exclusions (150,000/210,000 X 18200)	-13,000	
Sub-total taxable	63,000	
Tax on $63,000 UN income reimbursed to staff member		12,051
Net Tax paid by staff member		15,749

The net tax paid by the staff member in this case is $9475 higher than if the non-UN income were the only income. Thus, the staff member's UN income is effectively taxed by the additional amount." [Emphasis added]

24. Given these findings and the evidence upon which Judgment 2032 was based, the Tribunal concludes that Judgment 1224 was based upon a finding of fact, namely that the first-income method provided for exemption from tax on United Nations earnings only. It is clear that the parties failed to produce evidence to support that finding and the material presently before the Tribunal shows conclusively that, at least for the present complainants and for the complainant in Judgment 2032, that finding would not be correct. Reference should also be made to Judgment 2256, adopted at the present session.

25. The Tribunal concludes that Staff Rule 103.18(b) as amended breaches the fundamental principle under which the remuneration of international civil servants must be exempt from national taxes and consequently cannot be applied to the complainants. The complaints must be allowed and the Organization ordered to refund to them any and all taxes paid by them over and above what they would have paid on the application of the last-income method. The complainants are each entitled to their costs in an amount of 2,000 euros.

DECISION

For the above reasons,

1. The impugned decisions are set aside.

2. The Organization is ordered to recalculate the tax refunds the complainants are entitled to in accordance with the last-income method and to make any consequential repayments.

3. It shall pay each of them 2,000 euros in costs.

4. All other claims are dismissed.

In witness of this judgment, adopted on 15 May 2003, Mr James K. Hugessen, Vice-President of the Tribunal, Mrs Flerida Ruth P. Romero, Judge, and Mrs Mary G. Gaudron, Judge, sign below, as do I, Catherine Comtet, Registrar.

Delivered in public in Geneva on 16 July 2003.

James K. Hugessen

Flerida Ruth P. Romero

Mary G. Gaudron

Catherine Comtet