

ASIAN DEVELOPMENT BANK ADMINISTRATIVE TRIBUNAL

**Decision No. 2
(18 January 1994)**

**Ferdinand P. Mesch and Robert Y. Siy
v.
Asian Development Bank**

**E. Lauterpacht, Chairman
F.P. Feliciano, Member
M.D.H. Fernando, Member**

1. The Applicants, Mr. Ferdinand P. Mesch, a national of the United States of America, and Mr. Robert Y. Siy, a national of the Republic of the Philippines, are contesting the decision of the Asian Development Bank ("the Bank" or "ADB") not to reimburse income tax paid by the Applicants on their salaries and emoluments ("salaries") derived from employment with the Bank. The Applicant Mr. Mesch has been employed since 25 February 1980 as a Senior Counsel, Level 6, in the Office of the General Counsel under a regular appointment; the Applicant Mr. Siy has been employed under a similar appointment since 23 June 1989 as an Evaluation Specialist, Level 4, in the Post-Evaluation Office.

2. The Applicants' grievance is that their salaries, after deduction of income tax levied by the Governments of the United States of America and of the Republic of the Philippines, are below the amounts that have been set by the Bank as appropriate for their respective levels of employment. The Applicants contend that the Bank is thus in breach of its obligation to provide equal compensation for comparable work, which they interpret as "equal net-of-tax pay for equal work."

3(a) Gross salaries were paid by the Bank to the Applicants on exactly the same basis as other employees who were nationals of other countries, holding comparable posts and performing like functions. However, the net salaries of the Applicants after taxation were obviously less than the salaries retained by those of their colleagues who were not liable to taxation.

3(b) From the inception of the ADB, its principal comparator organization for the purpose of maintaining a competitive salary structure was the International Bank for Reconstruction and Development ("IBRD"). The IBRD determines the salaries of its own staff as if they were tax-exempt and, where income tax is payable, provides for reimbursement of tax paid thereon. Thus the IBRD not only assumes that staff salaries are formally tax-exempt; it also ensures that they are effectively so. In contrast to this, the ADB, though also determining the salaries of its professional staff as if they were tax-exempt, does not reimburse national income tax if levied and does not make any additional payment to ensure that result. Consequently, those professional staff members whose salaries are liable to such income tax receive less by way of remuneration (lower after-tax salaries) than do their counterparts at the IBRD.

3(c) Thus, in 1991 Mr. Mesch received a basic salary of US\$82,590, and allowances amounting to US\$17,755, on which he paid United States income tax of US\$3,739. Mr. Siy received a salary of US\$60,362, on which he paid Philippine income tax amounting to US\$18,718, leaving him with US\$41,644. During that period, the Bank's salary scales entitled a staff member at Level 4 to a minimum annual salary of US\$54,230. Mr. Siy, however, received much less - even less than the minimum of US\$43,910 fixed for staff two levels below. Further, his after-tax salary was more than 30% below the salary of his counterparts in the IBRD.

4. By memorandum dated 10 February 1992 to the Manager, Compensation and Benefits Division ("BPCB"), the Applicants claimed that they were entitled to receive "net-of-tax compensation", i.e., payment of an amount which, even after taxes had been paid, would be equal to their nominal gross salaries. Accordingly, they requested the Management of the Bank to reimburse the income tax paid by them. On 20 July 1992 the Management informed the Applicants that they were not entitled to such reimbursement. Requests for review of that decision were unsuccessful. On 3 September 1992 the Applicants were informed that the President of the Bank would agree, under Article II, Section 3(a) of the Statute of the Tribunal, to the Applicants submitting their Application directly to the Tribunal. Thereupon, this Application was filed on 11 September 1992.

5. The Applicants allege that the Bank's failure to observe the practice of "net-of-tax compensation" and to reimburse income tax paid by them:

- a. is in breach of the Bank's obligation to pay the Applicants salaries which are "equitable and competitive" i.e., internally as well as externally vis-à-vis its comparator organization, the IBRD;
- b. "results in non-observance of the fundamental and essential conditions of [their] terms of appointment" and is also in violation of relevant Administrative Orders - in particular, Administrative Order 2.04:
- c. "3.3 . . . Subject to reasonable variations that recognize difference in previous experience, length of service in the Bank, quality of performance and relevant factors, equal compensation will be provided to staff members performing comparable work."
- d. is contrary to "the body of international law governing all major public international organizations, derived from 'international custom, as evidence of a general practice accepted as law'; and
- e. undermines Articles 36.2 and 36.3 of the Articles of Agreement Establishing the Asian Development Bank ("the Charter").

6. The principal items of relief claimed by the Applicants are:

- a. "the adjustment of [their] salaries so that [their] full salaries are received on a net-of-tax basis and fall within the net-of-tax salary ranges for [their] respective levels";
- b. the reimbursement of "the additional amounts paid in taxes by [the Applicants] in order to set the Applicants' past salaries on a net-of-tax basis, plus interest at an appropriate annual rate on these amounts"; and
- c. that "the Bank should ensure that equal net-of-tax compensation is provided to staff members performing comparable work in order to implement correctly Section 3.3 of Administrative Order 2.04 and other policies that provide for equal pay for equal work."

7. The principal question raised by the Application is whether the terms and conditions of employment of the Applicants require the Bank to reimburse income tax levied on their salaries by the member States of which they were nationals.

8. The parties accept that the terms and conditions of employment of the Applicants are to be determined by reference to the Applicants' letters of appointment, the Bank's Charter, By-Laws, Administrative Orders and Regulations, Personnel Policy Statements and Handbooks.

The letters of appointment

9(a) The letter of appointment of Mr. Mesch stated that: "You may note that salaries of foreign professional staff are not subject to taxation by the Government of the Republic of the Philippines",

but made no reference to the subject of income taxation by the United States. The letter of appointment of Mr. Siy said nothing whatsoever on the subject of income taxation.

9(b) Thus the letters of appointment did not contain either representations that the Applicants would not (then or in the future) be subject to income tax in their respective home countries or undertakings to make any form of tax reimbursement; nor did these letters expressly provide that it was the policy or practice of the Bank not to make such reimbursement.

9(c) Both letters of appointment also stated that:

"As a staff member of the Bank, you will be subject to present and future administrative regulations for the governance of such staff."

The Charter and By-Laws

10. The Tribunal will next examine whether any of the Bank's internal documents establish a right to tax reimbursement. The first document to be considered in this connection is the Charter of the Bank.

11(a) Article 56.2 of the Charter provides:

"No tax shall be levied on or in respect of salaries and emoluments paid by the Bank to Directors, alternates, officers or employees of the Bank, including experts performing missions for the Bank, except where a member deposits with its instrument of ratification or acceptance a declaration that such member retains for itself and its political subdivisions the right to tax salaries and emoluments paid by the Bank to citizens or nationals of such member." Of 52 member States, 17 deposited such declarations, including the United States and the Republic of the Philippines. These two countries, however, are the only ones that actually levy income tax upon the salaries of their nationals employed in the Bank.

The Bank's By-Laws have been silent, from the inception of the Bank, as to reimbursement of income tax paid by staff or the payment of any allowance in lieu thereof.

11(b) It may be observed in passing that the corresponding provision of the Articles of Agreement establishing the IBRD ("the IBRD Charter") is Article VII, Section 9(b):

"No tax shall be levied on or in respect of salaries and emoluments paid by the Bank to executive directors, alternates, officials or employees of the Bank who are not local citizens, local subjects, or other local nationals."

Resolution 11 of the Board of Directors of the IBRD, adopted at its inaugural meeting on 16 March 1946, stated:

"Appropriate measures for the elimination or equalization of the burden of national taxes upon salaries and allowances paid [by the World Bank] are indispensable to the achievement of equity among its members and equality among its personnel."

Section 14(b) of the IBRD's By-Laws (prior to 1980) provided that:

"Pending the necessary action being taken by members to exempt from national taxation salaries and allowances paid out of the budget of the Bank, the Governors and the Executive Directors, and their Alternates, the President, and the staff members shall be reimbursed by the Bank for the taxes which they are required to pay on such salaries and allowances."

This was amended in 1980 to provide in lieu of such reimbursement:

"a tax allowance that the Executive Directors determine to be reasonably related to the taxes paid by them on such salaries and allowances."

Subsequent to that amendment the IBRD letter of appointment stated:

"If you are liable for the payment of national income taxes on the remuneration you receive from the World Bank, you will receive from the World Bank a tax allowance as determined by the Executive Directors of the World Bank."

Thus, tax reimbursement was an express condition of employment in the IBRD; that condition was based upon a principle expressly adopted by the IBRD, namely, that the elimination of national taxes on staff salaries, or the equalization of the burden, was indispensable to equality among staff members.

11(c) Relying on the discussions preparatory to the adoption of the ADB's Charter, the Applicants contend that the intention of those who drafted that Charter was that Article 56.2 would necessitate a net-of-tax compensation system and that the Bank would be obliged to reimburse national income tax on staff salaries as a consequence of accommodating States which reserved their right to tax. The Tribunal observes that no such intention appears on the face of Article 56.2 and, having examined the proceedings of the Preparatory Committees relied on by both parties, it has been unable to discern either any such intention or any contrary intention.

11(d) It is the contention of the ADB that although the Charter of the IBRD did not prohibit the levying of taxes by a member State on the salaries of its nationals, the IBRD expressly undertook, by resolution of its Board and by its By-Laws, an obligation to reimburse national income tax on staff salaries; that there were other international organizations which had a tax

reimbursement system; and that the ADB is different, having recognized by its Charter the right of member States to reserve the right to tax their nationals and having deliberately refrained in its By-Laws and resolutions from adopting any tax reimbursement system. The ADB further contends that the adoption of a system of tax reimbursement would be contrary to its Charter. However, the Tribunal notes that there is nothing in the Charter which prohibits the Bank from undertaking an obligation to reimburse national income tax on staff salaries. It is, therefore, necessary to examine the administrative regulations of the Bank, as well as other Bank documents setting out its personnel and salary policies, in order to ascertain whether the Bank has subsequently assumed or excluded any such obligation.

Personnel and salary policies

12(a) Administrative Instruction ADM-7 (dated 27 April 1967) set out as follows one of the "Basic Principles Governing Salary Administration":

"It is the policy of the Bank to provide equal compensation to staff members performing comparable work, subject to reasonable variations that recognize differences in previous experience, length of service in the Bank, quality of performance and similar factors." (Emphasis supplied).

12(b) Although this Instruction was replaced by Administrative Order No 2.04 of 30 May 1972, the same principle was maintained:

"3(b) Salaries will be maintained at levels competitive with those prevailing in comparable organizations and in the market from which the Bank seeks to recruit its staff.

3(c) . . . Subject to reasonable variations that recognize differences in previous experience, length of service in the Bank, quality of performance and relevant factors, equal compensation will be provided to staff members performing comparable work.

. . . .

7.4. The Director of Administration is responsible for ensuring that salary administration policies are applied equitably and consistently throughout the Bank." (Emphasis supplied).

Similar provision was made in subsequent revisions of Administrative Order 2.04 which now, in its latest form (as revised 1 November 1993, Administrative Order No. 3.01), provides:

"3(a) Salaries will be designed to attract and retain a highly qualified and competent staff and to motivate the highest standards of performance by all staff members.

3(b) Salaries will be maintained at levels competitive with those prevailing in comparable organizations and with due regard to the locational considerations of the Bank's Headquarters . . .

3(c) The Bank will systematically evaluate the relative levels of each position, the equitable remuneration for similar responsibilities internally and externally, and reward staff according to performance, length of service and other relevant factors.

3(d) Salaries will be administered in a manner that is both equitable and transparent to all staff." (Emphasis supplied).

12(c) The same principle of equality, though not stated in identical terms, is contained in the Personnel Policy Statement approved by the Board of Directors on 7 December 1990:

"(i) In its staffing, the Bank gives paramount importance to securing the highest standards of efficiency and technical competence

(ii) The Bank's salaries, allowances and benefits will be maintained at competitive levels with due regard to the locational considerations of the Bank's Headquarters

(vi) The Bank will systematically evaluate the relative levels of jobs, the equitable remuneration for similar responsibilities internally and externally, and reward staff according to performance, length of service and other relevant factors." (Emphasis supplied).

12(d) Nothing contrary to this principle of equality in salaries is stated in the Bank's Personnel Handbook for Professional Staff (effective 1 April 1991):

"4.2 Compensation

Remuneration Principles

The overall objective of the Bank's remuneration policy is to enable it to recruit and retain highly qualified and competent staff on a geographical basis which reflects the Bank's membership.

A competitive salary, paid in United States dollars, is offered to you, taking into account relevant qualifications and experience, within the salary range corresponding to the classification of your job. Salaries for new staff members are generally computed on the basis of comparability with other jobs and with other staff in service who have equivalent or similar qualifications and experience and who are at the same position level.

Salaries and benefits paid to expatriate staff are exempt from taxation by the Philippine Government in accordance with the provisions of the Headquarters Agreement. Under tax legislation in most countries, this remuneration is exempt from home country taxes as well.

Actual salary levels are regularly monitored and reviewed to ensure that the Bank retains its competitiveness within the international market and maintains a reasonable degree of comparability with similar international institutions, principally the World Bank Group. Based on these reviews, the Bank from time to time revises its salary ranges and individual salaries by means of a general salary increase (GSI), in the form of a percentage adjustment."

The same is true of the Bank's booklet entitled Staff Appointments with the Asian Development Bank, which refers also to regular salary reviews

"in order to ensure that the Bank retains its competitiveness within the international market and maintains a reasonable degree of comparability with similar institutions (principally, the World Bank Group)." (Emphasis supplied).

12(e) With the exception of United States and Philippine nationals, all professional staff of the Bank receive salaries which are tax-exempt and which are, therefore, equal to the salaries of their colleagues performing comparable work in the Bank, and are also comparable with the salaries of their counterparts in the IBRD.

Other documents

13(a) On 10 October 1975 the President of the Bank sent a telex to the United States Secretary of the Treasury when he became aware that the House of Representatives of the United States was considering a proposal to eliminate the foreign earned-income exclusion (of about US\$20,000) then available to the American staff of the Bank. He stated:

"The Bank, unlike certain other international organizations, is not in a position to reimburse national taxes assessed against its staff members, and the Bank salary structure is based on the assumption that staff salaries are not subject to national income taxation.

"The effect of the proposed legislation would be to reduce the net salaries of Americans on our staff sharply. I feel it would depress the relative living standard of Americans compared to their associates. This will seriously affect our ability to attract and hold highly qualified Americans on our staff and I am concerned that it will inevitably have an adverse impact on the American presence in the Bank."

The Bank thus recognized that the levy of income tax on salaries of American staff would create a significant inequality.

13(b) The Applicants also rely on a memorandum dated 18 September 1981 from the General Counsel and the Director, Budget, Personnel and Management Systems Department ("BPMSD"), to the President of the Bank regarding a proposal by the United States Department of the Treasury ("Treasury") to make funds available to the Bank for the partial reimbursement of 1980 United States taxes paid by American staff members. According to that memorandum, in response to requests made by the Bank to the United States Government to provide relief for the American staff, the United States Treasury determined that it had authority to make such reimbursement. Thereafter, an Agreement was concluded and the Treasury paid US\$500,000 to the Bank to be used for such reimbursement. That Agreement described these payments as "Salary Equalization Payments." Although it was not the Bank which provided the funds for these payments, the Tribunal considers that this Agreement demonstrates that the United States Government and the Bank recognized that tax reimbursement was both legitimate and proper to restore equality in respect of salaries of professional staff.

Conclusions

14. The resulting position may be summarized as follows. The Charter, By-Laws and Board Resolutions did not establish any obligation of the Bank in respect of the reimbursement of income tax levied on staff salaries; equally, however, those documents did not prohibit the adoption of any such obligation. Likewise, although the letters of appointment issued by the Bank to professional staff did not include any express undertaking to reimburse income tax,

nevertheless they did not specifically exclude that prospect. There was thus no pronouncement by the Bank as to the exclusion of tax reimbursement. Moreover, the letters of appointment sent to staff members made the Bank's administrative regulations part of the contract between the Bank and the staff members. Accordingly, from 1967 onwards, the principle of equal compensation for comparable work (contained in Administrative Instruction ADM-7) was part of the terms and conditions of all staff members; and by 1972 the Bank acknowledged the need to apply salary policies equitably throughout the Bank. Thereafter, the Bank accepted, in principle and in practice, that its professional staff were entitled to "equitable remuneration" both internally (in relation to their colleagues in the Bank) and externally (i.e., bearing "a reasonable degree of comparability" with the remuneration of their IBRD counterparts).

15. The Tribunal observes that the comparison of compensation levels on the practical plane necessarily involves a consideration of the net benefits, after tax if any, to the recipient. Therefore, it cannot be said that a given salary which, in the hands of one recipient, is taxable is the same as an identical figure which, in the hands of another, is not. Accordingly, the failure to consider the incidence of taxation is inconsistent with the principle of "equal compensation for comparable work."

16. The Tribunal is conscious that the implementation of this principle will increase the overall amounts that the Bank must pay to the professional staff. However, that is not a reason for rejecting the logical operation of the principle of equality. The ultimate financial consequences of the proper application of the principle of equal compensation for comparable work, to which the Bank has subscribed since its earliest days, are something that can only be worked out between the Bank and its Members.

17. In balancing in the present case the equities as between the Bank and its staff, the Tribunal considers that more weight should be given to the interests of the employee than to those of the employer, if only because the Bank could have so structured its terms of employment as to exclude expressly the prospect of equal pay for comparable work and could thus have excluded the need for tax reimbursement. But it never did so. Any ambiguity or uncertainty in this respect, wherever appearing in documents emanating from the Bank must, therefore, be resolved *contra proferentem* and in favor of the staff.

18. The Tribunal accordingly holds that the terms and conditions of employment of the Applicants require the Bank to reimburse income tax levied on their salaries.

19. In view of its conclusion on this question, the Tribunal does not need to consider the further questions that have been posed and examined by the parties, namely:

Whether there is a principle of international law, custom or practice which imposes an obligation on international organizations to reimburse national taxes levied on salaries of their professional staff and, if so, whether the Bank was bound by it?

Whether the levy of national taxes by member States on the salaries of Bank staff undermines the provisions of Articles 36.2 and 36.3 "36.2 The Bank, its President, Vice-President(s), officers and staff shall not interfere in the political affairs of any member, nor shall they be influenced in their decisions by the political character of the member concerned. Only economic considerations shall be relevant to their decisions. Such considerations shall be weighed impartially in order to achieve and carry out the purpose and functions of the Bank.

36.3 The President, Vice President(s), officers and staff of the Bank, in the discharge of their offices, owe their duty entirely to the Bank and to no other authority. Each member of the Bank shall respect the international character of this duty and shall refrain from all attempts to influence any of them in the discharge of their duties." of the Charter and, if so, was there an obligation on the Bank to reimburse such taxes levied by member States in order to prevent those Articles being undermined"?

20. The Tribunal observes, however, that although there are notable differences in the mechanisms adopted by the United Nations and its Specialized Agencies, the IBRD, the International Monetary Fund, the Inter-American Development Bank, and some other international organizations, they all succeed in achieving effective equality among comparable staff members of the organization in respect of after-tax salaries.

Relief

21. The Tribunal must now consider the relief to which the Applicants are entitled. While there is, no doubt, force in the argument that the Applicants are entitled to reimbursement of taxes from the beginning of their respective periods of employment with the Bank, it appears to the Tribunal that such a solution entails so many practical difficulties - especially in view of the implications of the Tribunal's decision for other members of the professional staff in situations comparable to those of the Applicants - that it must be excluded. Self-evidently, it would only be with the greatest difficulty that the financial arrangements of the Bank could be adjusted to cover the re-opening of its salary payments for many years back.

22. Moreover, although it was a term or condition of employment of each of the Applicants that he was entitled to reimbursement of income tax levied on his salary, the Bank's obligation of reimbursement in each case could have arisen only upon a reasonably prompt claim being made, accompanied by proof of payment of such tax. The Tribunal observes that despite the fact that the Applicant Mr. Mesch commenced employment with the Bank on 25 February 1980, and the Applicant Mr. Siy did so on 23 June 1989, it was not until 10 February 1992 that the Applicants made their first formal representations to the Bank seeking reimbursement of taxes. Payment of tax in respect of the year 1990 would, in the normal course, have been made in 1991. The Tribunal considers, therefore, that it would be reasonable and equitable to entertain the Applicants' claims for reimbursement of tax paid for the years 1990 and 1991, but that the claims made in respect of previous years are belated and cannot be entertained.

23. It hardly needs saying that the concept of "tax reimbursement" means reimbursement only for income tax actually payable and paid in respect of salaries received from the Bank. Each Applicant's entitlement to such reimbursement in each case must be restricted to the amount of income tax payable and paid by him on the assumption that the salary received from the Bank constituted his total income. Further, in determining the reimbursable amount of income tax paid by each Applicant, any tax credits or benefits to which he is entitled under his national tax system must be applied first in respect of his salary from the Bank.

Decision:

For these reasons the Tribunal unanimously decides that:

- a. in principle, the terms and conditions of employment of the Applicants entitle them to reimbursement (computed in the manner stated in paragraph 23) of income tax levied and paid on their salaries;

- b. the Bank shall reimburse the Applicants the income tax levied and paid on their salaries beginning with the year 1990 together with interest at 5% per annum from 10 February 1992 in respect of the years 1990 and 1991; and
- c. all other claims of the Applicants are dismissed.