SEVENTY-FOURTH SESSION

In re O'DELL

Judgment 1224

THE ADMINISTRATIVE TRIBUNAL,

Considering the complaint filed by Miss Marlene O'Dell against the International Atomic Energy Agency (IAEA) on 16 January 1992 and corrected on 3 March, the IAEA's reply of 12 May, the complainant's rejoinder of 29 July, the Agency's surrejoinder of 6 October, the complainant's communication of 19 October and the Agency's comments thereon of 10 November 1992;

Considering Article II, paragraph 5, of the Statute of the Tribunal, Regulation 5.02(a) and Rules 5.02.1(D) and 12.01.1(D)(1) of the Agency's Provisional Staff Regulations and Staff Rules;

Having examined the written submissions and decided not to order hearings, which neither party has applied for;

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

A. The complainant, a United States citizen, first joined the IAEA in 1957. After a break in service from 1961 she rejoined in 1968 and now serves in its New York office as a liaison and public relations officer at grade P.3.

Regulation 5.02(a) of the Agency's Provisional Staff Regulations exempts its officials from payment of national income tax on salaries and post adjustment allowances. The regulation goes on:

"Should such taxes be levied on the salaries or allowances paid by the Agency, they will, unless otherwise specified in the letter of appointment, be reimbursed by the Agency."

The Agency's practice in the matter of tax reimbursement is described in Judgment 1140 (in re Rosen) under A. From 1965 to 1970 it followed the so-called "first-income" method, whereby it refunded tax payable on institutional income alone, taking account of all applicable exemptions and deductions. In 1970 it adopted the "last-income" method, whereby the amount it refunded in taxes was equal to the difference between the sum payable in taxes when institutional income was included and the amount payable when such income was not included. In 1981 the United States Government declared that it would pay back to the Agency the amounts of tax refunded to staff only if the Agency treated institutional income as "first income" and outside income as "last income". From then until 1989 the Agency continued to apply the last-income method while waiting for the United Nations Administrative Committee on Co-ordination, known as the ACC, to work out new arrangements applicable throughout the United Nations common system.

The ACC's efforts having come to nothing, the Agency and the Government signed a new agreement on 5 April 1989. It prescribed a modified first-income approach under which exemptions and deductions could be pro-rated. The method was brought in as of 1 January 1989 and announced to the Agency's staff by circular SEC/NOT/1263 dated 5 May 1989.

On 9 April 1990 the complainant got a cheque for the outstanding amount the Agency owed on her 1989 income. In a letter of 23 April 1990 to the Director of its Legal Division she pointed out what she saw as the unfairness of a sevenfold increase in her tax liability and asked him to review the matter and advise her. In his reply of 17 December 1990 the Director told her that the cardinal principle of the IAEA's policy was "equality among an organization's staff members" and cited one other international organisation whose New York staff got the same treatment.

By a letter of 26 February 1991 she appealed to the Director General under Rule 12.01.1(D)(1) on the grounds that SEC/NOT/1263 was intended to apply only to staff employed outside the United States. The acting Director General rejected her appeal on 9 April. On 22 May 1991 she went to the Joint Appeals Committee. In its report of 4 October 1991 the Committee found no evidence of discriminatory treatment and recommended rejecting her appeal. The acting Director General endorsed the Committee's recommendation in a letter to her of 9 October 1991. That is the decision she impugns.

B. The complainant submits that the Agency's approach is discriminatory since it denies her the earned-income exemption of 70,000 United States dollars which Agency employees not assigned to the United States do get. If her duty station had been Vienna her tax liability for outside income would have come to only $941. But just because she is stationed in New York she had to pay $4,067, an effective rate of 36.5 per cent of her private income of $11,123. Though the Appeals Committee held that her higher tax liability was due, not to discrimination by the Agency, but to United States tax law there is, she submits, no law which taxes a private income as low as hers at the rate of 36.5 per cent.

She also fared less well than other United States citizens serving in the United Nations or other New York liaison offices, which were still applying rules like those the Agency used to follow. Had she had the same treatment should would have been liable for a mere $318 in State and local taxes on her outside income.

Only the last-income method puts staff members who must pay income tax on their international income in the position they would be in if their international income were duly exempt from tax. The Agency yielded to pressure from the United States Government, which had been refusing for years to pay back the Agency's tax refunds.

The Agency was in breach of the rule against retroactivity: though it applied the new policy as from 1 January 1989 it did not announce it until 5 May 1989, too late to let staff protect their interests by shifting to tax-free investments.

The complainant asks the Tribunal to order the Agency not to apply the first-income method to her and to refund to her any sums she paid in tax over and above what other New York staff in like circumstances paid.

C. In its reply the IAEA submits that even if other United Nations organisations applied the last-income method - and at least one other does not - equal treatment would not require the Agency to apply it to her. The principle of equal treatment does not require that staff in different organisations be given the same treatment.

The first-income method is not discriminatory: it merely eschews the unfairness of granting disproportionate benefits to officials with high outside incomes. It applies to all Agency staff alike, whatever their duty station. Since the complainant also has to pay a "self-employment tax" which goes towards United States social security benefits, the IAEA further refunds to her the employer's contribution of 50 per cent, thereby granting her an entitlement that United States citizens stationed abroad do not get.

The Agency contends that its decision to go back to the first-income method shows none of the flaws she alleges but rests on sound considerations of policy, among them the need to put the IAEA on a secure financial footing at a time when the total of tax refunds the United States refused to pay back was mounting.

Lastly, the IAEA maintains that notification of the change to the new method was timely. Since it came before any advance payments for the 1989 tax year, it left the complainant ample time in which to take steps to safeguard her private income. She might even have lodged an appeal in 1989.

D. In her rejoinder the complainant develops her earlier pleas and answers those put forward in the reply. As the only citizen of the United States whom the Agency employed in that country she was the only official to suffer the discriminatory effects of its approach. It was unfair that her duty station should determine how much she had to pay in tax. That the Agency may have had to bow to pressure from the Government did not make the new policy "sound". Nor was she given "timely" notice of the change, since she could at best have gained partial protection if she had acted as soon as the circular reached her, in May 1989. As for the obligation to pay a self-employment tax, she rejects the assumption that payment into two compulsory pension systems must be better than payment into one: having to pay for United States social security merely made her disposable income in 1989 some $3,600 lower than it would have been had she been employed at headquarters. She presses her claims.

E. In its surrejoinder the Agency seeks to refute the arguments in the rejoinder. It maintains that the adoption of the first-income method was a proper exercise of its discretion and that it is not bound to follow the example of any other United Nations body. Any "discrimination" the complainant may suffer as to her outside income is due to United States tax law. As to her allegations of breach of the rule against retroactivity, it urged her to sort out her private investments when there were still nine months of the tax year left in which to do so.

F. Further submissions by the parties discuss a ruling by the United States Supreme Court on the nature of certain

benefits under United States social security.

CONSIDERATIONS:

1. The United States tax system requires all citizens to declare their income and pay tax thereon insofar as it is not subject to any exemption, deduction or exclusion.

2. The Agency used to refund tax payable on Agency earnings alone. That is known as the first-income method. In 1970, however, the United Nations broke away from that method and decided to refund the difference between the total tax payable on income including United Nations earnings and the total tax payable on income excluding such earnings. That is the last-income method. In the same year the Agency amended its rules so as to adopt the last-income method, setting a maximum limit of 26,000 United States dollars on taxable outside income.

3. Up to 1974 the IAEA paid refunds out of its regular budget. In that year the United States concluded an agreement with the Agency for the return of any sums it had paid to its staff in reimbursement of United States tax. In 1975 the Agency removed the limit of $26,000.

4. In 1981 the United States unilaterally terminated the agreement on repayment and it did not conclude a new one until 5 April 1989. The new agreement was based on a modified firstincome method and the Agency announced it to the staff by circular SEC/NOT/1263 of 5 May 1989.

5. For the purpose of calculating taxable income the tax policy of the United States ordinarily permits the exclusion of up to $70,000 of "foreign-earned" income, i.e. income earned by the citizen while resident abroad. That exclusion is not available to United States tax payers who are resident in the country. The effect is that an IAEA official who is both a citizen of and resident in the United States pays more in tax on Agency earnings, and at a higher rate, than one who, though a United States citizen, is not resident in the country. But the Agency pays back to all staff members, whatever their duty station, United States tax they have paid on their earnings from it. That is in accordance with Regulation 5.02(a) of the Provisional Staff Regulations, which provides that the Agency shall reimburse taxes levied on earnings from it unless the letter of appointment states otherwise.

6. The complainant is a United States citizen whom the Agency employs in its office in New York. Her claim arises out of the taxation by the United States of her private income, which, she says, has been "forced ... into the top tax bracket". Because she lives and works in the United States she is denied the exemption from tax of up to $70,000 in foreign income which is granted to citizens who are resident overseas. What she is challenging is a final decision of 9 October 1991 by the acting Director General of the Agency to refuse her the benefit of the last-income method in reckoning the reimbursement of her United States income tax for 1989.

7. Her main pleas are the following.

(1) Because she is denied the benefit of the last-income method that is applied to staff of the United Nations and some other international organisations, she has been discriminated against.

(2) Because she is denied the exclusion of up to $70,000 of foreign-earned income she is again discriminated against in comparison with Agency staff stationed in Vienna.

8. The Tribunal's answer to her first plea is that in this particular area there is no common-system method which the Agency 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 Agency required - as the Tribunal ruled in Judgment 1073 (in re Munro No. 2) under 5 - to "achieve uniformity with United Nations Staff Regulations".

9. As for her second argument, the staff member's entitlement under the Staff Regulations is to refund of tax paid on his 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. The Agency was entitled to change from a method which was to the benefit of those with outside income to a method that refers only to Agency income. Before that change it had sustained a loss of over $500,000 in the tax years 1983 to 1988. The former method went beyond the Agency's obligations under the rules.

(b) It was under pressure, she maintains, from the United States Government that the Agency adopted the modified first-income method.

That is mere comment rather than argument. The Agency is an autonomous international organisation, it is entitled to enter into an agreement with any government, and there were sound financial reasons for concluding the agreement with the United States Government in this instance.

(c) It was improper, argues the complainant, to apply the new policy in May 1989 for the tax year 1989 because by the time the policy was announced it was no longer possible for staff to change their investments so as to protect them against the effects of the new policy, for example by switching to investments exempt from Federal, State and city taxes.

The system is that the Agency reimburses tax to staff at the start of each year following the end of the tax year, though there is provision for advance payment if pre-payment of tax is required: see Rule 5.02.1(D). The final settlement is made at the beginning of the year following the tax year after a final tax return is made, taking into account any such advance payments there may have been.

According to the Agency time was left in the tax year for staff to take steps to mitigate the consequences for any private income they had.

The Tribunal accepts that contention. Besides, even though the complainant implies that she could have protected herself by making other investments had she known of the change earlier, she does not appear to have done so at any stage during the tax year 1989 after the issue of circular SEC/NOT/1263.

DECISION:

For the above reasons,

The complaint is dismissed.

In witness of this judgment Miss Mella Carroll, Judge, Mr. Pierre Pescatore, Judge, and Mr. Michel Gentot, Judge, sign below, as do I, Allan Gardner, Registrar.

Delivered in public in Geneva on 10 February 1993.

Mella Carroll
P. Pescatore
Michel Gentot
A.B. Gardner

Updated by PFR. Approved by CC. Last update: 7 July 2000.