ADMINISTRATIVE TRIBUNAL OF THE INTERNATIONAL MONETARY FUND

JUDGMENT No. 2007-1

Ms. Christina Daseking-Frank v. IMF
Mr. Gamal Zaki El-Masry v. IMF
Mr. Christian Josz v. IMF
Mr. Carlos Alberto da Cunha Leite v. IMF
Ms. Binta Terrier v. IMF

Introduction

1. On January 22, 23 and 24, 2007, the Administrative Tribunal of the International Monetary Fund, composed of Judge Stephen M. Schwebel, President, and Judges Nisuke Ando and Michel Gentot, Associate Judges, met to adjudge the case brought against the International Monetary Fund by five of its staff members.

2. Applicants, in identical Applications, contest the decision taken by the IMF Executive Board on April 14, 2006 to revise the methodology by which staff salaries are determined, as well as the implementation of that amended system in the 2006 compensation round. In particular, Applicants challenge (i) changes to the respective sector weights applied in calculating salaries in the comparator (United States and French/German) markets, i.e. by increasing the public sector weight and decreasing the private industrial sector weight, while maintaining unchanged the private financial sector weight but lowering its "pitch," (ii) implementation of a 3-year cycle for assessing the "international competitiveness" of salaries of Grade A9–B2 staff, i.e. by undertaking a full assessment of the international comparator markets every third year and relying (with discretion to apply certain exceptions) upon published indices of United States data for each of the other two years, and (iii) vesting the Executive Board with discretion (subject to specified constraints) to adjust Fund salaries upward or downward when they fall within the "testing range" for international competitiveness as well as when they fall outside of that range.

3. Applicants maintain that the amendment of the compensation system is contrary to the internal law of the Fund and general principles of international administrative law. In Applicants' view, the Executive Board's decision violates a fundamental condition of their employment, i.e. the Fund's obligation under the Articles of Agreement to maintain an internationally diverse staff of the highest quality, fails to comply with the Fund's rules-based compensation system, and reflects an improper motive to reduce staff compensation. Applicants further contend that the process of amendment was not based on a proper consideration of relevant facts and, accordingly, the decision was arbitrary and constitutes an abuse of discretion. Finally, Applicants maintain that the contested decision resulted in a downward adjustment of the Fund's staff compensation for 2006 and that the further exercise of discretion in the future will erode the

international competitiveness of Applicants' salaries, allegedly in violation of the terms and conditions of their employment.

4. Respondent, for its part, maintains that the Executive Board's decision was a proper exercise of its discretionary authority, which had as its principal aim maintaining the international competitiveness of Fund salaries. In Respondent's view, the decision did not violate any fundamental condition of Applicants' employment and was not improperly motivated. Furthermore, the Fund maintains that the decision was taken as a result of a process of study and deliberation in which key stakeholders were consulted. Finally, as to the application of the revised compensation system in the 2006 compensation round, the Fund asserts that Applicants have not demonstrated any abuse of discretion and that speculation about future abuse does not provide a basis for legal challenge in the present case.

The Procedure

5. On July 17, 2006, Applicants, members of the governing board of the Staff Association Committee ("SAC"), filed five identical Applications with the Administrative Tribunal. The Applications were transmitted to Respondent on the following day. As the Applications raised identical issues of law and fact, Respondent was invited to file a single Answer to the five Applications. On July 18, 2006, pursuant to Rule IV, para. (f),[1] the Registrar circulated within the Fund a notice summarizing the issues raised in the Applications.

6. On September 1, 2006, Respondent filed its Answer to the Applications. On October 3, 2006, the President of the Tribunal, pursuant to Rule IX, para. 1[2] of the Rules of Procedure, granted Applicants' request for an extension of time to file their Reply, which was submitted on October 31, 2006. The Fund's Rejoinder was filed on December 4, 2006.

The Factual Background of the Case

7. The relevant factual background may be summarized as follows.

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[1] Rule IV, para. (f) provides:

> "Under the authority of the President, the Registrar of the Tribunal shall:
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> ...
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> (f) upon the transmittal of an application to the Fund, unless the President decides otherwise, circulate within the Fund a notice summarizing the issues raised in the application, without disclosing the name of the Applicant, in order to inform the Fund community of proceedings pending before the Tribunal; ..."

[2] Rule IX, para. 1 provides:

> "The Applicant may file with the Registrar a reply to the answer within thirty days from the date on which the answer is received by him, unless, upon request, the President sets another time limit."

History of the Fund's Compensation System Prior to 2004

8. In parallel with the World Bank, a formal system for salary adjustment was not implemented by the IMF until 1979. Prior to that time, according to Respondent, "[s]alary adjustments were made more or less annually, on an *ad hoc* basis, without an underlying pre-determined methodology or set of considerations." Following the Report of the Joint Fund/Bank Committee on Staff Compensation Issues ("Kafka Committee"), in 1979 the Fund adopted a system of staff compensation providing for periodic review based on surveys of comparator organizations, using the United States as the primary market for professional grades, tested against non-U.S. comparators. Discretion was retained, however, for the Executive Board to set salaries at a level differing from that indicated by the comparator markets.

9. With regard to "international competitiveness," in the words of a subsequent Staff Bulletin describing the 1979 system's later revision:

> "As an international organization, required by its Articles of Agreement to recruit staff on a wide geographic basis, it was clearly essential that salaries based on the U.S. comparator market were sufficiently competitive to achieve that purpose. However, the system provided little guidance on how the international competitiveness of Fund salaries was to be maintained."

(Staff Bulletin No. 89/10 (May 22, 1989), p. 2.)

10. In 1984, Terms of Reference were established for a Joint Bank/Fund Committee of Executive Directors on Staff Remuneration ("JCC"). The Committee was to bear in mind *inter alia*: "(a) the importance of ensuring, with due regard to cost, the continuing ability of the two institutions to recruit and retain staff of the highest caliber appropriate to job requirements; [and] (b) the international character of the staff." (EBAP/84/195, Supp. 2.)

11. As an outcome of the JCC's review, the Fund embarked upon a new compensation system effective May 1, 1989. As announced to the staff by Staff Bulletin No. 89/10 (May 22, 1989), p. 1 "… some of the JCC's recommendations were endorsed [by the Executive Board], and others were modified on the basis of the comments and suggestions of management." Among the main features of the system implemented in 1989 was to retain the U.S. market as the primary comparator for professional grades, with secondary markets (French and German) to be used to test the U.S. market's international competitiveness. Sector weights (which previously had given equal weight to public and private sectors) were revised to apportion the weights at one-third public sector, one-third private financial sector, and one-third private industrial sector. Compensation was linked to the 75th percentile of comparator markets, but this element, advised the Staff Bulletin, "will need to be kept under review." (Staff Bulletin No 89/10, pp. 7-9.) The payline for grades A1-A8 was set by extrapolating downward from the A9-B5 payline, with a mechanism for checking the outcome against comparator markets. (Id., p. 10.)

12. With respect to the testing range for "international competitiveness," the Staff Bulletin explained:

> "[The JCC] recommended … the establishment of a 'testing range' for the margin of international competitiveness between 10 and 20 percent. Specifically, the recommendation was as follows:
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> > '… if the selected U.S. comparator market fell below the 10 percent margin or progressed beyond the 20 percent margin of the test markets for a number of grades, this would demonstrate the need for an evaluation of international competitiveness. In deciding whether any action was required, in the context of annual salary reviews, and on the nature and the extent of such action, a number of considerations would be taken into account, including the extent to which the margin has been eroded or surpassed, recruitment and retention experience, and exchange rate developments.'"

(Id., p. 5.)

13. Following implementation of the revised system in 1989, the Fund continued to review and revise its compensation rules, through a process that included preparation of papers by human resources staff, comments from the Staff Association Committee, and deliberations of the Executive Board. In April 1999, the Fund implemented changes that included revision of the apportionment of sector weights to 35 percent for the public sector, 25 percent for the private industrial sector, and 40 percent for the private financial sector. In January 2000, sector weights were again re-allocated, and a new source adopted for U.S. market data.

14. An element of the system adopted in 1989 that, however, remained unchanged until it was amended in January 2005 was the rule for testing the "international competitiveness" of the Fund's payline (established on the basis of U.S. comparators) by reference to the French/German market. That rule provided for "automaticity" of the salary adjustment when the U.S.-indicated payline fell within a "testing range" of 10-20 percent above the payline established by the French/German comparators. Accordingly, under that system, the Executive Board did not have discretion to adjust the Fund's salary structure when the initial payline fell within the "testing range" for international competitiveness. By contrast, when the U.S.-indicated payline placed the initial Fund payline either above or below the "testing range," discretion could be exercised to make either an upward adjustment (when the payline fell below the 10 percent testing range floor) or a downward adjustment (when the payline fell above the 20 percent testing range ceiling). According to Respondent's summary, in thirteen of the seventeen years in which the automaticity rule was in effect, the initial U.S.-indicated adjustment placed the Fund payline outside the 10-20 percent testing range; in eleven of those thirteen years, the Executive Board exercised discretion to adjust the salary structure either upward or downward.

15. For five consecutive years, i.e. 2000-2004, when the U.S.-indicated payline fell above the 20 percent ceiling of the testing range, the Executive Board did not ratify the full increases indicated by the U.S. market and adjusted the salary structure downward in exercise of the discretion accorded under the system. Moreover, in 2004, a number of the Members of the

Executive Board indicated that they could no longer support the overall compensation system and called for its review.

Employment, Compensation and Benefits Review ("ECBR")

16. On July 30, 2004, the Managing Director, responding to concerns from some Members of the Executive Board, informed the Board of plans for a broad review of the Fund's "employment strategies, the salary system and benefits, and the coordination of compensation decisions and the budget process." This review was to become known as the Employment, Compensation and Benefits Review ("ECBR"). Among the issues to be examined was:

> "… how we can best measure and maintain the **competitiveness of our compensation and benefits systems**. While continuing with a rules-based approach, we will look into all aspects of our relationship with the comparator markets, and how we should take into account total compensation—salaries and benefits together—and employer costs of benefits."

(Managing Director's Speaking Notes on the Compensation Review; Informal Briefing for the Executive Board, July 30, 2004.) (Emphasis in original.) The ECBR went forward under the auspices of a Steering Committee chaired by the Director of the Human Resources Department ("HRD"), and an outside consulting firm was engaged to provide an initial study. The Managing Director noted in his Speaking Notes to the Executive Board: "The Steering Committee will also consult extensively with the Staff Association Committee. It is our intent that this exercise be transparent." (Id.)

17. The Terms of Reference for the ECBR stated that the review was designed to support a number of objectives, including that the Fund:

> "● Employ high-quality staff of diverse nationalities and skills.
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> …..
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> ● Provide compensation that is competitive with the market at different grades and skills, so as to support recruitment and retention, while being as economic and cost-effective for the Fund as possible.
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> ….
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> ● Make consistent decisions on salaries and budgets within a predictable, rules-based process."

(ECBR Terms of Reference.)

18. On September 6, 2004, the Managing Director addressed a message to the staff, which included the following points relating to the international competitiveness of Fund salaries:

> "… it is understood that, when deciding to join the Fund, many staff and their families have been uprooted and have, thereby, relinquished family ties and other opportunities in their home countries. Thus, it is essential for the Fund to maintain a compensation and benefits system that is internationally competitive and attractive, in order to ensure that the organization is able to attract and retain staff of the highest caliber.
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> ….
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> Regarding the compensation system, … the core principles that underlie the design of the existing system will not be changed. Specifically, the compensation system will continue to provide for periodic structural increases in salaries that are designed to ensure that staff salaries remain internationally competitive, taking into account relevant comparator markets."

(Message from Managing Director to Staff on Compensation Review and Grandfathering, December 6, 2004.)

19. On July 28, 2005, the Chair of the Steering Committee transmitted to the Executive Board the Report of the consultants, noting that the Report additionally was being provided to the Staff Association Committee and posted on the Fund's intranet where it would be accessible to all staff. (Memorandum to Members of the Executive Board from Chair, ECBR Steering Committee, July 28, 2005.) Among the Report's conclusions was that the Fund's salary structure was "overcompetitive" at lower grades and "undercompetitive" at higher grades.

20. According to the Steering Committee Chair, the Committee would next prepare "its own assessment of the issues." (Id.) In the process of preparing this assessment, the Steering Committee undertook consultations with what it termed "key stakeholders," including representatives of the SAC. Staff views were assessed through departmental comments on the outside consultants' Report, through "town hall" meetings, and via a dedicated electronic mailbox. During 2005, the Steering Committee additionally held informal briefings and seminars with the Executive Board in which SAC representatives had the opportunity to participate. (Employment, Compensation and Benefits Review – Overview Paper, Prepared by the Steering Committee, January 6, 2006.)

21. In January 2006, the Steering Committee issued two papers setting out its formal recommendations to the Executive Board, including to "align the Fund payline more closely to the market by steepening the Fund payline between Grades A12 and B2, and bending the Fund payline downward from Grade A12 to Grade A9." The Steering Committee additionally proposed a 4-year cycle for adjustments to the salary structure. (Id.) In a Companion paper, the Committee provided an extensive, detailed review of the compensation system, emphasizing that it should "continue to be comparator-based .... [and] rules-based:"

> "● **The compensation system should continue to be comparator-based.** The Fund makes compensation

> comparisons with pay levels in selected member countries as an effective means of ensuring that Fund salaries are, in fact, internationally competitive. This market-based approach remains valid: by linking the level of its salaries to those paid in relevant comparator markets, the Fund can provide compensation that is competitive but not over-competitive.
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> - **The compensation system should continue to be rules-based.** A salient feature of the compensation system over the past 15 years has been its objective, rules-based methodology in which the composition of the comparator markets, the formulae for aggregating market data, and the procedures governing decisions on salary adjustments have been clearly defined. This approach remains desirable because it avoids the contentiousness of earlier approaches by providing definitive results in accordance with an established methodology while allowing judgment to be exercised within defined parameters."

(Employment, Compensation, and Benefits Review – Companion Paper, prepared by the Steering Committee, January 6, 2006, pp. 43-98.) The paper additionally proposed a system for adjustments when the Fund's payline fell within the 10-20 percent testing range. This proposal was presented for consideration as an alternative to retaining as part of the 2006 enactment the amendment to the system that the Executive Board had adopted in January 2005 (see below).

22. During the first quarter of 2006, as the outcome of the ECBR's review of the compensation system neared decision by the Executive Board, the process was punctuated by exchanges of views between the SAC and the Managing Director, as well as formal "Summings Up" of the Board meetings. These interchanges were circulated to the staff of the Fund and have been made part of the extensive record before this Tribunal.

23. On January 17, 2006, the SAC responded in detail to the Steering Committee's proposals with specific alternatives of its own. The SAC further stated:

> "10. **We welcome the maintenance of a rules-based compensation system that seeks to preserve the competitiveness of our salaries vis-à-vis both the U.S. and the international comparator markets.** A market-based comparison is the only mechanism that can ensure objectivity, fairness, and cost effectiveness. At the same time, we understand that Executive Directors require some discretion to smooth annual salary increases also within the 10-20 percent margin for international competitiveness. Here, however, we stress that this margin is a feature of the compensation system for all staff and should not be portrayed as an expatriate benefit.[2]

> 11. **We believe that the main features of the proposal are sound and strike an acceptable balance.** A quadrennial comprehensive review appears reasonable, provided it is targeted to preventing misalignments vis-à-vis our established comparator markets and does not transform into a 'mini-ECBR' every four years. We also have sympathy for attempts to simplify the process and generate some administrative savings in those years when the salaries are proposed to be determined on the basis of an index. In addition, we find the arguments for inclusion of supplementary market information (international financial centers, academia, and selected international organizations) and for decompression of the B3-B5 grade structure generally persuasive. **That said, we are concerned about some specific recommendations where modifications are warranted and see considerable risks in those areas that remain to be fleshed out.**
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> [2]In this context, it is also important to note that salary adjustments in the past have not always preserved the minimum margin of 10 percent (for example in 1996-97). Moreover, while the international competitiveness test is important, the last time salaries were adjusted *upward* because they would have otherwise fallen below the testing range was in 1994. In 2000-04, the competitiveness test resulted in *downward* adjustments to the salary increase indicated by the U.S. market—implying a loss, not a benefit, to the staff."

(SAC Reactions to ECBR Proposals (EBAP/06/02), January 17, 2006.) (Emphasis in original.)

24. A series of Board meetings was held in early 2006, at which consideration was given to implementation of the aspects of the ECBR relating to the compensation system. The Managing Director, reporting to the staff on the meeting of March 3, 2006, noted that the consultants' Report had found that the Fund was overcompetitive at lower grades and undercompetitive at higher grades. Accordingly,

> "…the steering committee proposed, and I endorsed, proposals that would over time change the slope of the payline, raising salaries at the higher grades and lowering salaries at the lower grades. The Board could not reach agreement on this, making the legitimate point that the Fund is a public sector institution, with greater security of tenure and lower levels of risk than in the private sector. Specifically, it was not ready to accept changes that would result in significant pay increases at the higher grades."

(Message from the Managing Director on the ECBR Board Meeting, March 3, 2006.)

25. On April 13, 2006, the Managing Director issued a further statement on the proposed decisions. Noting that the SAC had had the opportunity to present its views at the January 25 and March 3 Board meetings, he expressly responded to several points. First, as to the proposed changes to sector weights and financial sector pitch, the Managing Director stated:

"Management's central objective in reforming the compensation system has been to produce a simpler and more transparent system that links Fund salaries more closely to market levels." Second, regarding the Board's discretion to adjust the payline upward or downward, he noted:

> "The Board has discretion to set salaries below the levels warranted by comparison with the Fund's primary comparator market (the U.S.) only when the competitiveness margin over non-U.S. markets exceeds 10 percent. When this margin is met, the Board has discretion to set salaries below U.S. levels – but only if it deems that such a move would not impair the international competitiveness of Fund salaries."

The Managing Director further observed: "Directors will recall that Management's proposal is to incorporate the same features regarding the exercise of discretion as agreed by the Board in January 2005 but in the context of the broader comparator-based review….[and that]…The issue for the Board is to decide whether the risk of the Board adopting an unsound salary policy that would undermine the competitiveness of Fund salaries is sufficiently large that there is a need to rule out this scenario by further constraining the Board's room for maneuver." Finally, as to the issue of relying upon published indices of U.S. comparator markets in Years 2 and 3 of the salary cycle, he noted that the proposed indexation mechanism included safety clauses; he additionally advised: "... staff will conduct further work on the properties of [the ECI-based] index in the coming months and also explore whether other established/published series could provide a better indicator." (Statement by the Managing Director on Employment, Compensation and Benefits Review – Proposed Decisions, Executive Board Meeting 06/36, April 14, 2006.) (BUFF/06/67.)

January 2005 Amendment to the Compensation System and *Baker et al. v. IMF*

26. On January 24, 2005, while the ECBR was in progress, and in anticipation of setting salaries during the 2005 compensation round, the Executive Board enacted amendments to the staff compensation system that had the effect of expanding the circumstances under which the Board could exercise discretion by making adjustments when the payline indicated by the United States market fell within the "testing range" for international competitiveness as well as when it fell above or below that range.[3]

27. The legality of the January 2005 enactment was challenged in this Tribunal by seven staff members, Baker et al. The Fund responded with a Motion for Summary Dismissal, contending that the Baker Applicants had not been "adversely affected" by the amendment, as required to maintain an application under Article II of the Tribunal's Statute. The Fund maintained that the

[3] The text of the January 2005 enactment is set out in Baker et al., Applicants v. International Monetary Fund, Respondent (Dismissal of the Applications as Moot), IMFAT Judgment No. 2006-4 (June 7, 2006) ("Baker II"), para. 10.

amendment had had no adverse financial effect in the 2005 compensation round[4] and that the Applicants had not established any other adverse effect resulting from the contested decision.

28. In Baker et al., Applicants v. International Monetary Fund, Respondent (Admissibility of the Applications), IMFAT Judgment No. 2005-3 (December 6, 2005) ("Baker I"), the Tribunal denied the Fund's Motion, concluding that the Applicants in that case were "adversely affected," for purposes of maintaining their Applications pursuant to Article II, Section 1(a) of the Statute, on the ground that the January 2005 decision had "some present effect" on the Applicants' position and "[t]hat effect is inherent in the wider discretion that the Executive Board has assumed in respect of salary adjustments which, in the absence of further action by the Executive Board, will be applied in 2006." (Para. 21.) Accordingly, the pleadings resumed on the merits of that case.

29. Subsequently, however, the January 2005 enactment was superseded in April 2006 by a further Executive Board decision, described below. Accordingly, in Baker et al., Applicants v. International Monetary Fund, Respondent (Dismissal of the Applications as Moot), IMFAT Judgment No. 2006-4 (June 7, 2006) ("Baker II"), the Tribunal dismissed as moot the pending Applications of Baker et al. on the ground that the contested January 24, 2005 decision would no longer be applied and therefore did not continue to have any "present effect." (Para. 22.) At the same time, the Tribunal observed: "Insofar as the April 2006 scheme maintains elements of discretion regarding the extent to which the Executive Board may make downward adjustments in staff compensation, Applicants and other staff members retain their right to bring fresh Applications challenging that scheme." (Para. 22.) It is the April 14, 2006 enactment and its implementation in the 2006 compensation round that Applicants Daseking-Frank et al. challenge in this case.

The April 14, 2006 Decision of the Executive Board

30. The April 14, 2006 Executive Board decision by its express terms "… supersedes all previous decisions concerning the staff compensation system." The decision adopts paragraphs 4-52 of EBAP/06/38 (March 31, 2006),[5] the introductory paragraphs of which summarize its principal provisions:

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[4] Following the Executive Board's January 24, 2005 decision, two data errors were discovered in the comparator information utilized in the 2004 compensation review. The retroactive adjustment of the Fund's 2004 salary structure to correct for these errors had the following effect: the structural increase called for by the amended compensation system, as approved in the 2005 compensation round, did not differ from the increase that would have been called for under the system existing prior to its January 2005 amendment. Baker et al., Applicants v. International Monetary Fund, Respondent (Admissibility of the Applications), IMFAT Judgment No. 2005-3 (December 6, 2005) ("Baker I"), paras. 11-12.

[5] The April 14, 2006 decision also modified aspects of the expatriate benefits provided to eligible staff members. EBAP/06/38, paras. 53-65. *See also* Staff Bulletin No. 06/11 (June 13, 2006) ("Changes to Education Allowance Policy and New Education Allowance Ceilings for the 2006/2007 Academic Year") and Staff Bulletin No. 06/13 (July 25, 2006) ("Changes to Home Leave Policy"). Applicants have not challenged the expatriate benefits provisions of the revised compensation system.

"**II. Principal Provisions of the Revised Staff Compensation System**

4. This section sets out the proposed provisions of the revised compensation system. Under the revised system, the annual compensation reviews will be conducted, and the annual adjustments to the salary structure will be made, on the basis of a three-year review cycle: (i) in the first year of each cycle, comparator-based reviews will take into account full comparisons of compensation levels in the designated comparator markets for Grades A9-B2 and A1-A8 and other relevant considerations, including, in the case of Grades A9-B2, the assessment of international competitiveness; and (ii) in the intervening years, the structural adjustments will be based on an index of private and public sector salary increases in the United States. Taking into account each year's approved adjustment to the salary structure, resources will be allocated annually for individual, performance-related merit increases.

5. Although the new compensation system will include features that are similar to the existing system, some of these features require modification given the fact that they will be operating within a different overall framework. For example, there will be new level comparisons between each Fund grade and the corresponding compensation rate in comparator markets and the possibility of grade-by-grade adjustments; and the evaluation of international competitiveness will take place in the context of a broader comparator market review.

6. It is intended that the provisions set out below would become effective upon their approval by the Executive Board. They would govern the 2006 and subsequent annual compensation reviews."

31. Referring to the Articles of Agreement of the Fund, the decision sets out the "basic objectives and principles" of the revised compensation system as follows:

"A. Basic Objectives and Principles

7. The central objectives of the Fund's staff compensation system are derived from Article XII, Section 4 (d) of the Articles of Agreement, which provides that, subject to the paramount importance of securing the highest standards of efficiency and of technical competence, the appointment of staff should 'pay due regard to the importance of recruiting personnel on as wide a geographical basis as possible.' To give effect to this provision, the Fund's compensation system seeks to be:

a. highly competitive in the national markets and market sectors in which the Fund competes for staff, and effective in supporting the recruitment and retention of a diverse, multinational staff meeting the highest standards of quality and professionalism;

b. structured and administered in a way that provides effective incentives for high standards of performance;

c. internally equitable and consistent; and

d. cost effective in its design and operation.

8. In addition to these objectives, two principles will guide the operation of the compensation system:

- **The system is comparator-based**. Periodic reviews of market comparability, based on an established set of relevant comparator markets and designated benchmark levels of compensation in those markets, will provide the basis for ensuring that the Fund's salary structure and staff salaries are maintained at competitive levels in relevant markets.

- **The system is rules-based**. The major provisions of the system, including the definition of the comparator markets and the procedures used to determine the annual salary adjustments, will be clearly defined so that the annual reviews will be conducted in accordance with an established methodology, while still allowing management and the Executive Board to exercise judgment, within defined parameters, in setting salary levels."

Reproduced below are those elements of the contested decision that are most pertinent to the consideration of the issues of the case.

32. Part B of the April 14, 2006 Executive Board decision sets out the parameters for the "comparator-based" review for A9-B2 positions, which is to take place in Year 1 of the 3-year compensation cycle:

"B. Grades A9-B2: Comparator-Based Reviews

....

Definition of Comparator Markets and Market Paylines

....

Countries

12. The primary comparator market, which will serve as the principal basis for setting and adjusting the level of the A9–B2 salary structure, will be the United States market. To ensure that the A9–B2 salary structure is internationally competitive, the competitiveness of the Fund payline, as indicated by the U.S. market, will be tested against an international market. …

....

Market Sectors

14. The selection of specific market sectors and the weight assigned to each in aggregating the sector data in a single market payline are designed to ensure that Fund salaries are maintained at competitive levels that support recruitment and retention from all areas of national employment markets in which the Fund competes for staff. Each national comparator market will include three sectors, which will be assigned the indicated weights:

- **Public sector**, with a 50 percent weight;
- **Private financial sector**, with a 40 percent weight; and
- **Private industrial sector**, with a 10 percent weight.

....

Market pitch

28. Compensation in the comparator markets will be measured and the level of the comparator market paylines (i.e., the reference level to which the Fund relates its salaries) will be set at: (i) the 75th percentile of the U.S. industrial sector and of each sector in the international (i.e., French and German) comparator market; (ii) a level 10 percent above the mean of the U.S. public sector; and (iii) on the following sliding scale between the 75th percentile and the mean of the U.S. financial sector ….”

33. Of particular significance to the consideration of the issues of the instant case are those provisions that govern “international competitiveness” and provide for adjustments to the level of the Fund’s payline:

"Provisions Governing International Competitiveness and Adjustments to the Level of the Fund Payline Indicated by Alignment with the U.S. Market

33. In accordance with the rules described in the subsection above, after grade-by-grade adjustments have been made, the result will be a provisional A9–B2 payline that is aligned, on the basis of the MSE measurement method, with the U.S. market. An adjustment to the average level of this provisional A9-B2 payline will be permitted, but is not required, on the basis of an evaluation of international competitiveness in accordance with the rules set forth below.

34. When evaluating international competitiveness, consideration will be given to such factors as recent recruitment and retention experience, the extent to which the margin over the international test market (described below) has been eroded or surpassed, and effects of tax and exchange rate developments on the level of the international market payline.

35. Adjustments based on the above considerations will be subject to the following:

(a) The targeted margin that will be considered an appropriate degree of international competitiveness will be a range that is 10–20 percent above the designated level of salaries in the international comparator market.

(b) When alignment of the Fund's A9–B2 payline with the U.S. market would produce a Fund payline that, on a staff-weighted average, falls outside the target range for international competitiveness, the provisional A9–B2 payline could be adjusted either (i) upward if the Fund payline would otherwise fall below the 10 percent floor of the range or (ii) downward if the Fund payline would otherwise fall above the 20 percent ceiling of the range. An upward adjustment from a position below the 10 percent floor could raise the A9–B2 payline to a level either below or above that threshold. However, a downward adjustment from a position above the 20 percent ceiling that would position the payline below that threshold would be constrained by the rules applicable within the target zone described in (c) below.

(c) When alignment of the A9–B2 payline with the U.S. market, or a discretionary downward adjustment under (b) above, would produce a Fund payline that, on average, falls within the 10–20 target range for international competitiveness,

> any downward adjustment could not result in a staff-weighted average level of the A9–B2 payline that is less than the higher of (i) a level equal to 10 percent above the level indicated by the international comparator market, and (ii) a level resulting from a staff-weighted average percentage structural increase at least equal to the percentage increase in the Washington metropolitan area Consumer Price Index for the 12 months ending in January.[8]
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> 36. In the event that adjustments are made as a result of an evaluation of international competitiveness, such adjustments would normally be applied uniformly to the Fund's A9–B2 payline; however, different adjustments could be made to individual grades (with offsetting adjustments to other grades) if this is considered necessary for reasons of international competitiveness.

[8] The CPI floor would only apply in circumstances where there is a downward adjustment of the Fund payline indicated by alignment with the U.S. market within the target range of international competitiveness. Accordingly, the floor would not apply when (a) the downward adjustment would still place the Fund's payline above the 20 percent floor or (b) the alignment of the Fund's payline with the U.S. market would place the payline within the target range and no downward adjustment is sought. If warranted by considerations of international competitiveness, an upward adjustment from a level within the target range would be permitted. "

34. Part C of the April 14, 2006 Executive Board decision designates procedures for the "indexation-based" reviews that are to be applied in Years 2 and 3 of the 3-year compensation cycle:

> **"C. Grades A9-B2: Indexation-Based Reviews**
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> 37. In the indexation-based reviews, which will be carried out in years 2 and 3 of each three-year cycle, the structural adjustments (which will be uniform across all grade levels) will be determined in accordance with an index that incorporates annual rates of compensation increases in the public and private sector of the United States. Except as provided below, the international test market would not be taken into account in determining the size of these adjustments.
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> ....
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> **Application of the indexation formula**
>
> 42. In years 2 and 3 of the compensation system cycle, the Grade A9-B2 salary structure (range minima, midpoints, and maxima)

> will be increased uniformly by the amount indicated by the increase in the chosen salary index.
>
> 43. Management may propose to the Board an upward adjustment to the salary increase indicated by the index if one or more of the following conditions is met:
>
> - there is compelling evidence to suggest that movements in the index are unrepresentative in a material way of general salary trends in the U.S. comparator market;
>
> - changes in U.S. tax policy make it likely that there will be significant increases in net salaries at the Fund at the time of the next comparator-based review; or
>
> - movements in the euro-dollar exchange rate create significant competitiveness problems for staff recruitment that warrant remedial action prior to the next comparator-based review."

(EBAP/06/38.)

The April 17, 2006 Decision of the Executive Board

35. On April 17, 2006, the Executive Board adopted a further decision, giving effect to the newly revised compensation system for the 2006 round. (EBAP/06/44.) Respondent has summarized the effect in 2006 as "a steepening of the Fund's payline and an overall reduction in the A9-B2 salary structure of 0.7 percent on average, with the midpoints at Grades A9-A13 reduced and those for Grades A14–B2 increased." The salary adjustments for 2006 also included transitional arrangements, ensuring that no staff member would experience an actual reduction in salary for 2006.[6]

36. Additionally, in 2006, the U.S.-indicated payline for Grades A9-B2 established an average margin of 8 percent above the French-German comparator payline. Accordingly, as the Managing Director noted in his Statement for the Executive Board Meeting, "[w]hen the competitiveness margin is less than 10 percent, the rules of the compensation system allow, but do not require, an increase in the payline above U.S. levels; an evaluation of the international competitiveness of Fund salaries is the basis for any such adjustment." Therefore, advised the Managing Director, "[w]e considered the case for raising the Fund payline above the levels indicated by alignment with the U.S. market, but decided on this occasion that such adjustment

[6] "The revised salary structure proposed for Grades A1-B5 (Attachment III) would be put into effect on May 1, 2006. Given that the changes to the salary structure involve a combination of reductions (Grades A1-A13) and increases (Grades A14-B5), it is necessary to establish transitional arrangements for: (a) staff members' performance-based salary adjustments in 2006; (b) avoiding salary reductions for staff whose existing salaries are above the new and lower maxima of their salary ranges; and (c) ensuring that all staff will have the possibility of receiving a salary increase in 2006." (EBAP/06/44, para. 32.)

was not needed to maintain the Fund's competitive position." (Statement by the Managing Director on Staff Compensation—2006 Review, Executive Board Meeting, April 19, 2006.) (BUFF/06/70 Revised.)

37. In support of the decision not to adjust the payline upward, the Managing Director cited the following factors:

> "● the Fund's recruitment/retention experience in 2005 did not point to competitiveness problems that need to be addressed by an adjustment of the entire salary schedule;
>
> ● experience suggests that modest deviations from the 10-20 percent target margin do not significantly impair recruitment/retention; the margin was also below 10 percent during the mid-1990s, but the Fund remained competitive and was able to expand professional staffing very substantially;
>
> ● the euro depreciation that explains much of the decline in the competitiveness margin between the 2005 and 2006 reviews has since largely reversed itself."

(Id.)

38. The SAC, for its part, rejected Management's analysis and, in its own statement to the Board, urged it to exercise its discretion to make an upward adjustment to the U.S.-indicated payline:

> "**We are troubled by the 2006 compensation proposal which already confirms our serious concerns about the new system at the time of its first application.** We remain convinced that the downgrading of the salary structure, particularly at key recruitment and retention grades, will have an adverse effect on the Fund's ability to attract international staff of the highest quality .... we cannot imagine more compelling circumstances for management to propose, and the Board to endorse, an upward adjustment to an otherwise negative structural salary increase."

(SAC Statement on 2006 Review of Staff Compensation (EBAP/06/44), April 17, 2006.) (Emphasis in original.)

Direct Review of Regulatory Decisions

39. Pursuant to Article VI, Section 2[7] of the Statute of the Administrative Tribunal, an application challenging the legality of a "regulatory decision"[8] may be filed with the Tribunal within three months of its announcement or effective date. There are no channels of administrative review to exhaust in respect of regulatory decisions being challenged directly. *See* Baker I, para. 13.

40. The contested decision of the Executive Board amending the compensation system was taken on April 14, 2006 and announced to the staff on the same day. By a second decision, of April 17, 2006, the Board, on the basis on the amended system, set the staff salaries for the 2006 compensation round.

41. On July 17, 2006, Applicants filed their Applications with the Administrative Tribunal.

Summary of Parties' Principal Contentions

Applicants' principal contentions

42. The principal arguments presented by Applicants in their Applications and Reply may be summarized as follows.

1. The April 14, 2006 decision of the Executive Board is arbitrary and an abuse of discretion in both lowering the benchmark for Fund salaries and widening the Fund's discretion to adjust staff compensation downward.

2. The decision to lower the benchmark for Fund salaries violates the Fund's obligation under the Articles of Agreement to hire an internationally diverse staff of the highest quality.

3. The decision fails to comply with the principles of the Fund's rules-based compensation system, the internal law of the Fund, and general principles of

[7] Article VI, Section 2 provides:

> "An application challenging the legality of a regulatory decision shall not be admissible if filed with the Tribunal more than three months after the announcement or effective date of the decision, whichever is later; provided that the illegality of a regulatory decision may be asserted at any time in support of an admissible application challenging the legality of an individual decision taken pursuant to such regulatory decision."

[8] Article II, Section 2.b. provides:

> "b. the expression 'regulatory decision' shall mean any rule concerning the terms and conditions of staff employment, including the General Administrative Orders and the Staff Retirement Plan, but excluding any resolutions adopted by the Board of Governors of the Fund."

international administrative law, thereby violating Applicants' terms and conditions of employment.

4. The new compensation system weakens the Fund's ability to attract and retain international staff of the highest quality, in conflict with the Articles of Agreement and the stated objectives of the system.

5. Specific elements of the amended compensation system, such as reducing the financial sector "pitch" and increasing the relative weight of public v. private sector comparators, have weakened the competitiveness of Fund salaries, particularly at those grades that are key to recruitment and retention.

6. The amendment was improperly motivated and reflects an intention to reduce the benefits of staff members.

7. During the indexing years, Fund salaries will follow only the U.S. market without consideration of international comparators, resulting in erosion of the international competitiveness of Fund salaries.

8. The guarantee of international competitiveness of Fund salaries is a fundamental and essential condition of employment of the staff that must continue to be ensured within the context of any rules-based compensation system adopted by the Executive Board.

9. The April 14, 2006 decision of the Executive Board to widen its discretion resulted in a downward adjustment in staff compensation for 2006, having a direct negative impact on the financial interests of the staff. Further such exercises of the Board's discretion will erode the level of salary required to maintain Applicants' salaries at internationally competitive levels.

10. Through its consistent practice, the Fund has restricted its discretion to change the following rules for maintaining international competitiveness:

    a. the comparator market weights and pitch;

    b. an annual comparator-based review taking into account international comparators; and

    c. "automaticity" within the testing range.

11. The new rules permit the Executive Board to deprive Applicants of the certainty inherent in a rules-based system.

12. The mere possibility of upward discretion does not provide an adequate safeguard for preserving international competitiveness of Fund salaries.

13. The contested decision was not based on a proper consideration of the relevant facts and not reasonably related to the objectives it is intended to achieve.

14. Applicants seek as relief:

    a. rescission of the Executive Board's decision of April 14, 2006 "to widen its discretion to adjust staff salaries downwards;"

    b. declaration as null and void the Executive Board's decision of April 17, 2006 implementing the amended system in the 2006 compensation round, and retroactive determination of the 2006 compensation on the basis of the pre-January 2005 system; and

    c. legal costs.

Respondent's principal contentions

43. The principal arguments presented by Respondent in its Answer and Rejoinder may be summarized as follows.

1. In exercising its authority to amend the terms and conditions of employment, the Executive Board did not transgress any legally binding norms.

2. Decisions regarding the appropriate methodology for determining salary adjustments are within the discretionary authority of the governing organs of international organizations and are not to be second-guessed by administrative tribunals.

3. Applicants' challenge to the new system is essentially over issues of methodology rather than legal principles.

4. The contested decision did not contravene the requirement of the Fund's Articles of Agreement that the Fund hire an internationally diverse staff of the highest quality. That principle does not mandate a particular type of compensation system or a specific market relationship or level.

5. The decision did not abrogate any fundamental or essential conditions of Applicants' employment.

6. None of the following provisions of the revised compensation system infringes any fundamental condition of Applicants' employment:

    a. changes to comparator market weights and pitch;

    b. annual comparator-based review that takes into account international comparators only every third year, while relying on U.S. indices for the other two years;

    c. the constrained use of discretion rather than "automaticity" within the "testing range" for international competitiveness.

7. The fact that the new system may result in a lower salary structure than the previous system does not mean that it is not competitive or derogates from any legal requirements.

8. The Fund has never made a formal commitment to the staff to maintain the rules of the compensation system unchanged, and the fact that a particular feature of the compensation system has been in place for a certain period of time does not mean that the organization has made a legal commitment not to abolish or modify that feature.

9. Under the revised compensation system, the determination of Fund salaries continues to be based on the application of a detailed and predictable methodology, based on relevant and well-defined comparator markets.

10. Applicants' challenge to the application of the new system in the 2006 compensation round is tantamount to challenging a feature of the system that has been in place since 1989.

11. Speculation now as to how discretion attributed to itself by the Executive Board might potentially be abused in the future does not provide a legal basis for Applicants' challenge in the present case.

Consideration of the Issues of the Case

Did the IMF Executive Board abuse its discretion by its enactment on April 14, 2006 of a revised system for the annual adjustment of Fund salaries?

44. The Applications of Daseking-Frank et al. present the Tribunal with the question of what constraints operate to circumscribe the "… broad, although not unlimited, power of the organization to amend the terms and conditions of employment" (Report of the Executive Board to the Board of Governors on the Establishment of an Administrative Tribunal for the International Monetary Fund, hereinafter "Report of the Executive Board," p. 17) and whether those constraints have been transgressed by the April 14, 2006 decision of the Executive Board.

45. The analysis that follows considers whether the principles of "international competitiveness" of Fund salaries and of a "rules-based" compensation system are fundamental elements of Applicants' conditions of employment. It considers as well whether particular features of the compensation system challenged by Applicants are either themselves fundamental conditions of employment, established by the consistent practice of the IMF, and therefore not subject to unilateral amendment, or whether the particular revisions to these features violate the principles of international competitiveness or of a rules-based system. The Tribunal lastly turns to the question of whether the Executive Board otherwise abused its discretion in enacting the contested decision, as by failing to take proper account of the relevant facts or by adopting a decision that was not reasonably related to the objectives that it seeks to achieve or was improperly motivated.

General principles governing review of regulatory decisions of the Fund

46. The Tribunal consistently has recognized the broad principle that "[t]he management of the Fund necessarily enjoys a managerial and administrative discretion which is subject only to limited review by this Tribunal." Mr. "R", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 2002-2 (March 5, 2002), para. 65. Moreover, the Tribunal has observed that "[t]his deference is at its height when the Tribunal reviews regulatory decisions (as contrasted with individual decisions), especially policy decisions taken by the Fund's Executive Board." Ms. "J", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 2003-1 (September 30, 2003), para. 105. The Executive Board is the highest decision-making authority within the Fund whose decisions are subject to review by the Administrative Tribunal.[9]

47. With respect to the Tribunal's competence to review the Fund's regulatory decisions, the Commentary on the Statute states:

> "As applied to the review of regulatory decisions, the case law of administrative tribunals in general demonstrates that although there exists a competence to review regulatory decisions, the scope of that review is quite narrow. There are broad and well-recognized principles protecting the exercise of authority by the decision-making organs of an institution from interference by a judicial body. The Fund tribunal would have to respect those principles in reviewing the legality of regulatory decisions."

(Report of the Executive Board, p. 19.) Moreover,

> "... the tribunals have reaffirmed, in a variety of contexts, that they will not substitute their judgment for that of the competent organs and will respect the broad, although not unlimited, power of the organization to amend the terms and conditions of employment."

(Id., p. 17.)

48. At the same time, the Commentary also recognizes that the Fund's authority to amend terms and conditions of employment is circumscribed:

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[9] *See* Article II, Section 2.b. of the Statute, and related Commentary: "The statute excludes from the tribunal's competence resolutions taken by the organ establishing the tribunal, that is, the Board of Governors." (Report of the Executive Board, p. 15.)

Pursuant to Article XII, Section 3 of the IMF Articles of Agreement, the Executive Board "shall be responsible for conducting the business of the Fund, and for this purpose shall exercise all the powers delegated to it by the Board of Governors." Accordingly, the Executive Board is the central decision-making organ of the IMF. *See* F. Gianviti, "Decision-Making in the International Monetary Fund," in Current Developments in Monetary and Financial Law, Vol. 1 (1999), pp. 31-67, at p. 50.

> "With respect to employment-related matters, the internal law of the Fund includes both formal, or written, sources (such as the Articles of Agreement, the By-Laws and Rules and Regulations, and the General Administrative Orders) and unwritten sources. These sources of internal law apply to, and circumscribe, the exercise of discretionary authority by the Executive Board in prescribing the terms and conditions of Fund employment."

(Id., pp. 17-18.) Accordingly, with respect to such amendments, the Commentary explains:

> "The Fund, like all international organizations, has reserved to itself broad powers to alter the terms and conditions of employment on a prospective basis.[7] However, an important limitation on the exercise of this authority would be where the Fund has obligated itself, either through a formal commitment or through a consistent and established practice, not to amend that element of employment. In the absence of such a commitment by the Fund, there would be no basis for a finding by the tribunal that a decision changing an element of employment violated the rights of the staff. Moreover, even where the organization has voluntarily undertaken such a commitment, subsequent developments, such as urgent and unavoidable financial imbalances, may authorize certain adjustments if they are reasonably justified.[8]
>
> ---
>
> [7] One basic limitation on an organization's power of amendment is the protection of acquired or vested rights, whether or not expressly provided for in the staff regulations. However, even this limitation has been very narrowly construed and interpreted as essentially synonymous with the principle of non-retroactivity. In other words, an amendment cannot deprive a staff member of any benefit or emolument that has been earned or accrued before the effective date of the change. Accordingly, respect for acquired rights would not preclude the organization from prospective alterations in the conditions of employment.
>
> [8] *Gretz*, UNAT Judgment No. 403 (1987)."

(Id., pp. 18-19.)

49. The Administrative Tribunal has recognized that the Fund's policy-making discretion extends to making choices between more than one reasonable alternative. In Mr. "R", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 2002-2 (March 5, 2002), the Tribunal considered the application of an overseas Office Director who challenged as discriminatory the enhanced benefits denied to him but afforded to the Fund's Resident Representative posted in the same city. The Tribunal noted that Mr. "R"'s contentions "… are far from frivolous. On the contrary, they are natural and understandable." (Para. 62.) Nonetheless, it concluded:

> "63. But however comprehensible the Applicant's position, this judgment call was not his but that of Fund management to make.

> After extended consideration, and rejection of a recommendation by the Director of Human Resources that the Applicant be afforded the housing allowance, the Fund decided that the further very material benefits enjoyed by the Resident Representative in Abidjan (and all other Resident Representatives, but no Office Directors) should not be extended to the Applicant. The manner of arriving at the decision taken was deliberate and within the Fund's managerial authority.
>
> 64. The Fund's management gave consideration to more than one option, and made the decision that it made. The distinction in the benefits accorded to Resident Representatives and Office Directors was rational, related to objective factors, and untainted by any animus against the Applicant. The allocation of differing benefits to different categories of staff was, in this case, reasonably related to the purposes of these benefits, in particular, the incentive to recruitment of Resident Representatives that is provided by the overseas assignment allowance."

Finally, concluded the Tribunal:

> "65. The management of the Fund necessarily enjoys a managerial and administrative discretion which is subject only to limited review by this Tribunal. If it is the Fund's considered decision that differences in the functions and recruitment of Resident Representatives and Office Directors justify a consequential difference in the benefits accorded those officials--even while uniquely serving in the same city overseas--it is not for the Tribunal to overrule that decision. This conclusion applies as well to the refusal of the Fund to make an exception to its policy in favor of the Applicant. While, in the view of the Tribunal, the granting of such an exception in this case would have been reasonable, the Fund's decision not to make an exception … is also reasonable and one within the ambit of the Fund's managerial discretion."

50. The Tribunal's Judgment in Mr. "R" is pertinent to current concerns. In upholding the Fund's decision, the Tribunal noted that the manner of arriving at the decision had been "deliberate" and taken "after extended consideration." The distinction in benefits was "rational, related to objective factors, and untainted by any animus." The allocation of differing benefits was "reasonably related to the purposes of these benefits," in particular the "incentive to recruitment" for particular posts.

51. Applying similar reasoning, in Ms. "G", Applicant and Mr. "H", Intervenor v. International Monetary Fund, Respondent, IMFAT Judgment No. 2002-3 (December 18, 2002), this Tribunal denied a challenge to an Executive Board decision allocating eligibility for expatriate benefits according to visa status. Significantly, the Tribunal concluded that the

"substance of the Fund's choice is rational and defensible" even in light of the Tribunal's observation that "perhaps even more so, was its earlier selection of the nationality criterion." (Para. 80.) The Tribunal cited de Merode (see below) for the proposition that the care with which a decision is taken should be taken into account by the Tribunal:

> "77. It may be recalled that, in the case of Mr. "R", the fact that Respondent studied and then rejected the proposition that there should be complete parity of benefits between overseas Office Directors and Resident Representatives was given weight. Similarly, in de Merode, the World Bank Administrative Tribunal observed that in reviewing the exercise of legislative powers of an international organization to make changes to the terms or conditions of employment, '…the care with which a reform has been studied and conditions attached to a change are to be taken into account by the Tribunal.' (paragraph 47.)"

52. In considering whether the method of allocating expatriate benefits discriminated impermissibly among categories of staff, the Tribunal in Ms. "G" examined whether there was a "rational nexus" between the "goals of the expatriate benefits policy" and the "method for allocating these benefits," and noted that such a nexus "does not require that there be a perfect fit between the objectives of the policy and the classification scheme established, and …. may rest upon generalizations:"

> "79. The Tribunal in the case before it must assess whether there is a rational nexus between the goals of the expatriate benefits policy--i.e. to compensate staff for costs associated with maintaining and renewing ties with their home countries (through home leave and education allowances), to facilitate their repatriation following service with the Fund, and to recruit and retain a diverse staff sustaining the international mission of the Fund--and its method for allocating these benefits. It is noted that the Tribunal's reasoning in Mr. "R" suggests that a 'rational nexus' does not require that there be a perfect fit between the objectives of the policy and the classification scheme established, and indeed that the categories employed may rest upon generalizations.
>
> 80. In the view of the Tribunal, the Fund's choice of a visa criterion for allocation of expatriate benefits is reasonable. The procedure of selecting it was not arbitrary but deliberate. The substance of the Fund's choice is rational and defensible. So, perhaps even more so, was its earlier selection of the nationality criterion. But if in the exercise of its undoubted legislative authority and managerial discretion the Executive Board chooses a visa policy in 1985, reconsiders and reaffirms that policy in 1994, and refines that policy as of 2002, these decisions in the exercise of its managerial authority cannot be overridden by this Tribunal

> when they are rationally related to the mission and objectives of the Fund, in particular as regards expatriate benefits. …."

53. The foregoing elements of the jurisprudence of the IMF Administrative Tribunal will be later called upon in assessing whether the Fund's Executive Board abused its discretion in enacting the contested decision of April 14, 2006.

Fundamental conditions of employment and the framework of *de Merode*

54. In de Merode, Lamson-Scribner, Reese, Reisman-Toof, Ruberl, and Shapiro v. The World Bank, WBAT Decision No. 1 (1981), the World Bank Administrative Tribunal considered the applications of six staff members challenging decisions taken by the Bank's Executive Board in 1979 to alter the methodologies applied to tax reimbursement and salary adjustment of staff members. The de Merode applicants contended that the contested decisions resulted in salaries as much as 29 percent lower than they would have been under the previous system of salary adjustment. Similarly, four of the six complained of "substantial reductions in their gross income" (para. 12) resulting from changes in the method of calculating tax reimbursement.

55. The WBAT identified the question presented in de Merode as follows: "Does the World Bank have the power – and, if so, within what limits – unilaterally to change the conditions of employment of its staff?" (Para. 15.) The reasoned response of the WBAT to that question is of considerable significance and it will be set out in detail.[10] Both the Daseking-Frank Applicants and the International Monetary Fund have invoked de Merode in support of their respective arguments.

56. The WBAT held that "[t]he practice of an organization may …, in certain circumstances, become part of the conditions of employment…. The integration of practice into the conditions of employment must … be limited to that of which there is evidence that it is followed by the organization in the conviction that it reflects a legal obligation…." (de Merode, para. 23.)

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[10] In the de Merode Decision, the WBAT commented on the significance of the jurisprudence of sister tribunals in the formulation of international administrative law:

> "28. …. While the various international administrative tribunals do not consider themselves bound by each other's decisions and have worked out a sometimes divergent jurisprudence adapted to each organization, it is equally true that on certain points the solutions reached are not significantly different. It even happens that the judgments of one tribunal may refer to the jurisprudence of another. Some of these judgments even go so far as to speak of general principles of international civil service law or of a body of rules applicable to the international civil service. Whether these similar features amount to a true corpus juris is not a matter on which it is necessary for the Tribunal to express a view. The Tribunal is free to take note of solutions worked out in sufficiently comparable conditions by other administrative tribunals, particularly those of the United Nations family. In this way the Tribunal may take account both of the diversity of international organizations and the special character of the Bank without neglecting the tendency towards a certain rapprochement."

57. The WBAT's Decision in de Merode directly influenced the drafting of the Statute of the IMF Administrative Tribunal. The Commentary on the Statute, expressly citing de Merode, recognizes as one of two unwritten sources of the internal law of the Fund "…the administrative practice of the organization [which] may, in certain circumstances, give rise to legal rights and obligations." (Report of the Executive Board, p. 18.) *See also* Ms. "B", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 1997-2 (December 23, 1997), para. 37.

58. Additionally, the WBAT noted, "[i]t is a well-established legal principle that the power to make rules implies in principle the right to amend them. This power flows from the responsibilities of the competent authorities of the [organization]." (de Merode, para. 31.)

> "36. The existence of the Bank's power unilaterally to change conditions of employment rests on its implied power to pursue fully and efficiently the purposes and objectives for which it was created. …. The existence of objective rules of a general and impersonal character implies not only the power of the organization to change these rules, but also a power to decide that the new rules should apply immediately to personnel already employed."

(Id.)

59. Moreover, the WBAT in de Merode drew a crucial distinction between what it termed "fundamental and essential" elements of the conditions of employment, which cannot lawfully be amended on a unilateral basis by the organization, and those elements that are less fundamental or essential and, accordingly, are open to amendment, subject to review under an abuse of discretion standard:

> "42. The Tribunal considers that in examining the numerous and varied elements of the conditions of employment, a major distinction must be drawn. Certain elements are fundamental and essential in the balance of rights and duties of the staff member; they are not open to any change without the consent of the staff member affected. Others are less fundamental and less essential in this balance; they may be unilaterally changed by the Bank in the exercise of its power, subject to the limits and conditions which will be examined later. ….
>
> 43. .... Sometimes it will be the principle itself of a condition of employment which possesses an essential and fundamental character, while its implementation will possess a less fundamental and less essential character. …."

60. This distinction between "principle" and "implementation," was essential to the WBAT's disposition of the decisions contested in de Merode and, as will be seen, is equally applicable to the analysis of the Applications pending before this Tribunal.

Does the contested decision of the Executive Board violate the terms and conditions of Applicants' employment by abrogating any of its fundamental conditions?

61. The Tribunal now turns to the question of what elements of the Fund's compensation system are, in the terms of de Merode, "fundamental and essential" and whether these elements have been violated by the decision challenged in this case.

The principles of "international competitiveness" and of a "rules-based" compensation system

62. Applicants maintain that by enacting revisions to the Fund's system of staff compensation the Executive Board abused its discretion by violating the principle of international competitiveness of Fund salaries, a principle that they contend is both a fundamental condition of their employment and a stated objective of the compensation system. Furthermore, Applicants maintain that the amended system violates the principle of ensuring a rules-based compensation system.

63. The express terms of the Executive Board decision contested by Applicants in this case state: "The central objectives of the Fund's staff compensation system are derived from Article XII, Section 4(d) of the Articles of Agreement, which provides that, subject to the paramount importance of securing the highest standards of efficiency and of technical competence, the appointment of staff should 'pay due regard to the importance of recruiting personnel on as wide a geographical basis as possible.'" (EBAP/06/38, para. 7.) This principle repeatedly was given voice throughout the ECBR process. For example, in a message to the staff of December 6, 2004, the Managing Director stated:

> "Regarding the compensation system, … the core principles that underlie the design of the existing system will not be changed. Specifically, the compensation system will continue to provide structural increases in salaries that are designed to ensure that staff salaries remain internationally competitive, taking into account relevant comparator markets."

(Message from Managing Director to Staff on Compensation Review and Grandfathering, December 6, 2004.) Moreover, as shown above, the goal of international competitiveness was also expressly stated in earlier revisions of the Fund's system for setting salaries, for example, in 1989. (*See* JCC Terms of Reference; Staff Bulletin No. 89/10.)

64. Accordingly, it is clear from the record, and Respondent has not disputed, that a principal aim of the Fund's compensation system at least since 1979 has been to maintain international competitiveness. It may be maintained that "there is evidence that [this practice] is followed by the organization in the conviction that it reflects a legal obligation" (de Merode, para. 23), or as the Commentary on the Statute of the IMF Administrative Tribunal explained:

> "The Fund, like all international organizations, has reserved to itself broad powers to alter the terms and conditions of employment on a prospective basis.[footnote omitted] However, an

> important limitation on the exercise of this authority would be where the Fund has obligated itself, either through a formal commitment or through a consistent and established practice, not to amend that element of employment."

(Report of the Executive Board, p. 18.)

65. The conclusion that international competitiveness of Fund salaries is, or has become, a fundamental condition of staff employment flows from two sources. First, the principle has, by dint of interpretation, been found to inhere in Article XII, Section 4(d) of the Articles of Agreement. Second, the Fund consistently and expressly has incorporated the principle of international competitiveness in its methodology for adjusting staff salaries.

66. The principle of international competitiveness is said to be found in the Articles of Agreement and practice of the Fund. Article XII, Section 4(d) of the Fund's Articles of Agreement provides:

> "Section 4. *Managing Director and staff*
>
> …
>
> (*d)* In appointing the staff the Managing Director shall, subject to the paramount importance of securing the highest standards of efficiency and of technical competence, pay due regard to the importance of recruiting personnel on as wide a geographical basis as possible."

67. At the same time, it must be recognized that an interpretation that the Articles of Agreement of the Fund require any particular mode of staff recruitment or any particular measure of staff compensation, competitive or otherwise, is not self-evident. The Articles of Agreement do not refer to competitive recruitment or competitive compensation of the staff of the Fund. They do not refer to the matter of staff compensation at all. They do no more than provide that, "In appointing the staff the Managing Director shall, subject to the paramount importance of securing the highest standards of efficiency and technical competence, pay due regard to the importance of recruiting personnel on as wide a geographical basis as possible." The Tribunal is not aware of any contention that the Fund's *modus operandi* prior to 1979 transgressed the Articles of Agreement or the entitlements of the staff even though international competitiveness had not been adopted as governing the compensation of the staff.

68. The essence of the very provision expressed by Article XII, Section 4(d) of the Fund's Articles of Agreement governs the appointment of the staff of all of the Organizations of the United Nations family. The language of the governing provisions of their charters and constitutions concerning the appointment of staff is virtually identical. But, apart from the IMF and the World Bank, it does not appear that any of those Organizations interpret their identical constitutional provisions to require that their salaries be internationally competitive with the private financial and industrial sectors. Some of the participants in the United Nations Common System, such as the International Labour Organisation, the United Nations Development Programme (UNDP) and the United Nations Conference on Trade and Development

(UNCTAD), employ numbers of qualified economists, and apparently succeed in recruiting them despite the fact that the salaries and pensions of the staffs of the Organizations of the United Nations Common System are much lower than those of the staffs of the Fund and the Bank.

69. There is of course a tenable interpretation of the Fund's Articles of Agreement that supports the pattern of staff recruitment and compensation that it has employed, namely, that staff of "the highest standards of efficiency and technical competence" cannot be recruited unless they are offered salaries and other inducements that are competitive not only with other public sector organizations, national and international, but are competitive with private financial and industrial sectors. In view of the fact that the Fund and the Bank, unlike other members of the United Nations family, concentrate their activities in the sphere of international financial and investment operations, that position is a plausible one, whose weight is enhanced by its acceptance by the Fund and the Bank at least since the adoption of the Kafka Report. It is a position that may be said to find support in "evidence that [this practice] is followed by the organization in the conviction that it reflects a legal obligation." (de Merode, para. 23.) It is pertinent to recall that Article III of the Statute of the Administrative Tribunal provides that "[t]he Tribunal shall be bound by any interpretation of the Fund's Articles of Agreement decided by the Executive Board, subject to review by the Board of Governors in accordance with Article XXIX of that Agreement." The Executive Board, since 1979, appears to have interpreted the Articles of Agreement to mean that the Fund is required to maintain a system of staff recruitment implementing the principle of "international competitiveness" of Fund salaries.

70. But this interpretation cannot be said to be a position that is expressly required by the terms of the Articles of Agreement; it is, at most, a reasonable, but not a necessary, interpretation of the Articles. Nor may it be assumed that, in point of fact, the Fund could not recruit staff of the highest standards of efficiency and technical competence if the terms it offered were competitive only with public sectors, or if the weight of the public sector were predominant.

71. Another principle governing the Fund's compensation system since 1979 is that it is to be "rules-based." The ECBR Steering Committee noted that a "salient feature of the compensation system over the past 15 years has been its objective, rules-based methodology in which the composition of the comparator markets, the formulae for aggregating market data, and the procedures governing decisions on salary adjustments have been clearly defined." Furthermore, the April 14, 2006 decision itself states:

> "**The system is rules-based**. The major provisions of the system, including the definition of the comparator markets and the procedures used to determine the annual salary adjustments, will be clearly defined so that the annual reviews will be conducted in accordance with an established methodology, while still allowing management and the Executive Board to exercise judgment, within defined parameters, in setting salary levels."

(EBAP/06/38, para. 8.) In Applicants' view, the question is whether the system in fact does fulfill its stated objectives.

72. Invoking the distinction between "principle" and "methodology," Respondent maintains that the relevant provision of the Articles of Agreement "… has never been understood as mandating a particular type of compensation system or a specific market relationship or level, but rather has accommodated the various systems established by the Board to meet evolving policy priorities and changing circumstances." Applicants acknowledge that since the establishment of the Fund, the Executive Board has indeed made significant changes to the compensation system and concede that "Respondent rightly notes" that while the requirement may be met in different ways, the question is whether the particular system at issue meets the essential elements of Article XII, Section 4(d).

73. The Tribunal observes that it is clear from the history of the Fund's compensation system that it has been far from static.[11] Even following implementation of an amended system in 1989, the Fund continued to review and revise its compensation rules. Likewise, as noted above, other international organizations with virtually identical governing provisions for staff recruitment have implemented them in differing ways. The Tribunal accordingly concludes that the Fund has always been, and remains, entitled to reconsider and re-shape the rules-based system for adjustment of staff salaries that it instituted in 1979.

74. With respect to the principle of international competitiveness, as Respondent correctly points out, "… there is no specific or objective test as to what level of salaries may be regarded as 'internationally competitive.' It is a matter of judgment not only as to the meaning of this standard, but also how it is to be achieved." Ultimately, the question of whether the Fund's compensation system, as revised by the Executive Board in April 2006, maintains international competitiveness is an empirical question, subject only to limited review by the Administrative Tribunal. At most, the Tribunal may examine whether the decision has been taken in accordance with appropriate consideration of the relevant facts, for example, the recruitment and retention data that periodically are collected and analyzed by the Fund.

75. What characterizes the practice of the IMF in giving effect to international competitiveness is that (i) comparators are drawn from selected markets in which the Fund competes for talent, and (ii) these comparisons are updated from time to time to reflect changes in those markets and in the Fund's needs for staffing. Judgments as to which particular markets to target, in what countries, and what weight shall be attached to public v. private sectors, as well as the weight to accord the various comparators, are complex policy decisions which, when reasonably based, are beyond the competence of the Tribunal to reconsider. Indeed, these are questions upon which reasonable persons, reasonably informed, may differ; indeed, experts may differ.

Challenges to specific provisions of the amended system

76. The Tribunal now turns to whether any of the individual provisions of the revised compensation system that Applicants challenge are "fundamental or essential" conditions of employment, i.e. whether the Fund has "… obligated itself, either through a formal commitment or through a consistent and established practice," (Commentary on the Statute, Report of the

[11] *See* The Factual Background of the Case.

Executive Board, p. 18) or whether they are subject to amendment in accordance with international administrative jurisprudence on the review of regulatory decisions for abuse of discretion.

77. Applicants have specifically challenged the following elements of the 2006 amendment to the system of setting staff salaries: (i) changes to the respective sector weights applied in calculating salaries in the comparator (United States and French/German) markets, i.e. by increasing the public sector weight and decreasing the private industrial sector weight, while maintaining unchanged the private financial sector weight but lowering its "pitch," (ii) implementation of a 3-year cycle for assessing the "international competitiveness" of salaries of Grade A9–B2 staff, i.e. by undertaking a full assessment of the international comparator markets every third year and relying (with discretion to apply certain exceptions) upon published indices of United States data for each of the other two years, and (iii) vesting the Executive Board with discretion (subject to specified constraints) to adjust Fund salaries upward or downward when they fall within the "testing range" for international competitiveness as well as when they fall outside of that range.

78. As to the challenged features of the compensation system, the Fund maintains that it has never made a formal commitment to the staff to maintain the rules of the compensation system unchanged, and the fact that a particular feature of the compensation system has been in place for a certain period of time does not mean that the organization has made a legal commitment not to abolish or modify that feature. Moreover, that the system is "rules-based" does not imply that the rules may never be amended. As explained in the Executive Board's decision of April 14, 2006, that the system is "rules-based" means that it "will be clearly defined so that the annual reviews will be conducted in accordance with an established methodology…."

79. In the view of the Tribunal, none of the specific provisions of the compensation system challenged by Applicants represents revision of an element of the system that was a fundamental or essential condition of their employment. Indeed, the contested provisions reflect elements of the system that have been subject, not infrequently, to amendment in the past. Changes to the sector weights and market pitch have been implemented on a number of occasions during the course of the Fund's history.[12] Accordingly, in the words of de Merode, para. 78, these provisions are "not sacrosanct and could be modified from time to time."

80. As to the 3-year cycle for assessment of international competitiveness and reliance on published indices of U.S. data during Years 2 and 3 of the cycle, Applicants concede that "… the Fund is not under a legal obligation to make a full review of the compensation system every year…" Nonetheless, they contend that implementation of the revised procedure abrogates the principle of international competitiveness because, in their view, the indices themselves are unreliable and the "escape clauses," which allow them to be overridden (see above, at para. 34), provide inadequate protection.

81. The Tribunal does not find itself in a position to say that the provisions of the revised compensation system that govern the 3-year cycle for assessment of international

[12] *See* The Factual Background of the Case.

competitiveness of Fund salaries have not been taken with an appropriate consideration of the relevant facts or do not bear a reasonable relation to the objective of maintaining international competitiveness.

82. The Tribunal observes that much of Applicants' concern relating to the individual elements of the compensation system focuses on the "risk" of their leading to a lack of international competitiveness in the future. For example, in respect of the 3-year cycle for evaluating comparator markets, Applicants maintain, "… the international competitiveness of Fund wages *could be* significantly eroded substantially over the course of the indexation years." (Emphasis supplied.) The issue of the risk of abuse of discretion is addressed below in relation to Applicants' challenge to the expansion of the Executive Board's discretion to adjust the Fund's payline when it falls within the testing range.

The widening of discretion and the risk of its abuse

83. In their Applications, Applicants cast their request for relief as "rescission of the decision taken by the Fund's Executive Board on April 14, 2006 *to widen its discretion to adjust staff salaries downwards*." (Emphasis supplied.) Accordingly, a key element of Applicants' complaint is the contention that the Fund's Executive Board, by revising the compensation system so that it may (subject to specified constraints) adjust the Fund's payline upward or downward when it falls within the "testing range" for international competitiveness, as well as when it falls outside of that range, has arrogated to itself an undue degree of discretion that is subject to abuse.

84. As described above,[13] one of the changes wrought by the January 2005 amendment and retained in the April 14, 2006 decision contested by Applicants in this case was to eliminate "automaticity" within the testing range, a feature of the Fund's compensation system from 1989 until its January 2005 amendment. The elimination of automaticity was maintained in the April 2006 decision challenged by Applicants in this case. Applicants contend that the resultant discretion may be the subject of future abuse by the Executive Board. Respondent, by contrast, maintains that any decision taken by the Board in the context of an annual compensation exercise will itself be subject to legal challenge, thereby providing a check on potential abuses of discretion and that "[s]peculation as to how that discretion might potentially be abused does not provide a legal basis for Applicants' challenge in the present case." Applicants reply that (a) this type of issue is ripe for its review, and (b) the Board, by applying the amended system in 2006, already has abused its discretion.

85. Applicants allege that the Board granted itself discretion to change the rules "at will and without analysis," and that automaticity within the testing range had been "at the core" of the pre-January 2005 system. Applicants observe that, by its April 14, 2006 decision, the Executive Board granted itself discretion above the level previously deemed necessary to ensure that salaries remain internationally competitive. The Managing Director, in explaining this proposed provision to the Executive Board, commented: "The issue for the Board is to decide whether the *risk* of the Board adopting an unsound salary policy that would undermine the competitiveness of Fund salaries is sufficiently large that there is a need to rule out this scenario by further

[13] *See* The Factual Background of the Case.

constraining the Board's room for maneuver." (Statement by the Managing Director on Employment, Compensation and Benefits Review – Proposed Decisions, April 14, 2006) (BUFF/06/67) (Emphasis supplied.)

86. The Tribunal observes, however, that the discretion at issue is, as Respondent describes it, "constrained." The following constraints, which are themselves based upon considerations of international competitiveness, apply to the Board's authority to make adjustments to the Fund's payline when it falls within the testing range:

> "34. When evaluating international competitiveness, consideration will be given to such factors as recent recruitment and retention experience, the extent to which the margin over the international test market (described below) has been eroded or surpassed, and effects of tax and exchange rate developments on the level of the international market payline."

(EBAP/06/38, para. 34.)

87. Additionally, the Tribunal notes that in respect of their challenge to the expansion of the Board's discretion to adjust salaries when the Fund's payline falls within the testing range of 10-20 percent above the U.S.-indicated payline, Applicants invoke Baker I "with regard to the harm suffered by Applicant[s]." However, because the Baker Applications were later dismissed as moot as a result of the Board's April 2006 decision, the Tribunal did not reach the merits of the question of whether the expansion of discretion within the testing range represented an abuse of discretion, but only that Applicants had an actual stake in the controversy to pursue such a claim. Baker I, para. 17, quoting Ms. "G", para. 61, reads:

> "… the 'intendment of [the "adversely affected"] requirement is simply to assure, as a minimal requirement for justiciability that the applicant has an actual stake in the controversy:
>
> > "…the tribunal would not be authorized to resolve hypothetical questions or to issue advisory opinions." (Report of the Executive Board, p. 13.)'"

The concept of "adversely affected" as that term applies to the admissibility of a claim before the Tribunal must not be conflated with an abuse of discretion on which Applicants might prevail on the merits. As exemplified by the case of Ms. "G", Applicant was "adversely affected" and therefore had standing to challenge an Executive Board decision that denied expatriate benefits to her and others with her visa status. Nevertheless, the Tribunal denied her Application on the merits, holding that the challenged policy and the Fund's refusal to make exception in her case was within the managerial discretion of the Fund.

88. International administrative tribunals have recognized that provision for the exercise of discretion within a system does not invalidate the system, and that the exercise of that discretion within its governing parameters leads to solutions no less legally valid than another. As the WBAT observed in von Stauffenberg, Ganuelas, and Leach v. The World Bank, WBAT Decision No. 38 (1987), para. 95:

> "Since the Kafka system and de Merode leave to the Bank a margin of discretion, the same technical data are capable of leading, after interpretation and an exercise of judgment, to a variety of solutions, that is to say, to several rates of adjustment, none any less legally valid than any other."

See Sebastian (No. 2) v. International Bank for Reconstruction and Development, WBAT Decision No. 57 (1988) ("The very fact of allowing the grading and reviewing bodies a wide range of discretion does not by itself invalidate the scheme."), quoted favorably in Ms. "Y" (No. 2), Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 1998-1 (December 18, 1998), para. 55 (upholding challenge to Discrimination Review Exercise: "The hallmark of these procedures was their flexibility …. Hence, the procedures contemplated a considerable degree of latitude for the review teams in undertaking either investigation," and note 32, citing Sebastian, "The very fact of allowing [decision-making bodies] a wide range of discretion does not by itself invalidate the scheme.")[14] *See also* In re Berthet (No. 2), ILOAT Judgment No. 1912 (2000), Consideration 15 ("… the staff can only be protected against arbitrariness if the criteria used in deviating from the suggested orientation of the external index are objective, adequate and known to the staff").

> Having concluded that the amended system of setting staff salaries does not violate any fundamental elements of the conditions of Applicants' employment, did the Executive Board otherwise abuse its discretion by enacting the contested decision?

89. Having concluded that the particular methodology by which the Fund maintains the international competitiveness of staff salaries is not a fundamental or essential element of Applicants' employment, what constraints do apply to its amendment?

90. The WBAT in de Merode articulated the following test for abuse of discretion in adopting changes to the non-fundamental terms and conditions of employment:

> "47. …. The Bank would abuse its discretion if it were to adopt such changes for reasons alien to the proper functioning of the organization and to its duty to ensure that it has a staff possessing 'the highest standards of efficiency and of technical competence.' Changes [to non-fundamental elements of the conditions of employment] must be based on a proper consideration of relevant facts. They must be reasonably related to the objective which they are intended to achieve. They must be made in good faith and must

[14] The Tribunal went on to test whether application of the Discrimination Review Exercise in the case of the individual complainant was carried out within the parameters allowed by this discretion. Ms. "Y" (No. 2), Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 1998-1 (December 18, 1998). *See also* Ms. "W", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 2005-2, (November 17, 2005); Ms. "Z", Applicant v. International Monetary Fund, Respondent, IMFAT Judgment No. 2005-4 (December 30, 2005).

> not be prompted by improper motives. They must not discriminate in an unjustifiable manner between individuals or groups within the staff. Amendments must be made in a reasonable manner seeking to avoid excessive and unnecessary harm to the staff. In this respect, the care with which a reform has been studied and the conditions attached to a change are to be taken into account by the Tribunal."

Quoted in Ms. "Y" (No. 2), paras. 47-49 (concluding that the challenged Discrimination Review Exercise was "undertaken as a result of reasoned consideration by the Fund's administration, based on recommendations made in an extensive study," the procedures adopted for the DRE appear to have been "rationally related to its purposes" and therefore implementation of the DRE was a proper exercise of the Fund's discretionary authority). S*ee also* Mr. "R", para. 59 (citing de Merode, para. 47, and concluding "... the fact that Respondent studied and then rejected the proposition that there should be complete parity of benefits between overseas Office Directors and Resident Representatives supports the view that the contested policy decision has not been taken arbitrarily.") *Accord* Ms. "G", para. 77; s*ee also* Mr. "R", para. 64:

> "The Fund's management gave consideration to more than one option, and made the decision that it made. The distinction in the benefits accorded to Resident Representatives and Office Directors was rational, related to objective factors, and untainted by any animus against the Applicant. The allocation of differing benefits to different categories of staff was, in this case, reasonably related to the purposes of these benefits, in particular, the incentive to recruitment of Resident Representatives that is provided by the overseas assignment allowance."

91. Applying these standards, the Tribunal turns to the question of whether the contested Executive Board decision of April 14, 2006 was an abuse of the Fund's discretion to modify the methodology by which it implements the principles of international competitiveness and a rules-based compensation system.

> Was the contested decision based on an appropriate consideration of the relevant facts and reasonably related to the objectives that it seeks to achieve?

92. Applicants contend that in enacting the revised compensation system, the Executive Board "cast aside" the findings of the comprehensive review of the compensation system so that the new system fails to "reflect the outcome of the analysis and discussion that took place within the context of that review" and "does not mirror the stated and indeed mandated objectives of adopting a new compensation system." Accordingly, Applicants maintain, the contested decision of the Executive Board was not based on an appropriate consideration of relevant facts and is not reasonably related to the objectives it seeks to achieve. Accordingly, in Applicants' view, the decision was arbitrary and an abuse of discretion.

93. Respondent, by contrast, maintains that the course of the Executive Board's decisionmaking was a deliberative one, which included consultation with the staff of the Fund and its representatives. Respondent maintains:

> "… it is both appropriate and necessary for legislative organs to reach such compromises in order to carry out their policy-making responsibilities, and the fact that the particular result reached may not reflect the original proposal, or blends elements of disparate proposals, does not demonstrate in any way that the organ abused its discretion in taking the decision."

94. The Tribunal recalls that the ECBR process entailed, first, a comprehensive review of the Fund's compensation system by an outside consulting firm, and that next the Steering Committee prepared its "own assessment of the issues." The staff of the Fund, individually, and through its representatives in the SAC, exercised multiple opportunities to voice opinions and proffer alternative proposals, as did the Fund's Management, through its Managing Director. The Executive Board's ultimate decision did not mirror precisely any one of these different proposals or points of view, but rather reflected a process of compromise and deliberation. This fact, however, does not mean that the decision failed to take proper account of the relevant facts or that the provisions adopted are not reasonably related to the objectives that they seek to achieve.

95. As set out above at para. 23, the SAC (as well as Management) varied in its views over time. For example, responding to the Steering Committee's proposal for a 4-year cycle for review of international comparators (which is to be contrasted with the 3-year cycle ultimately adopted and challenged in this case), the SAC in its January 17, 2006 statement commented: "A quadrennial comprehensive review appears reasonable, provided it is targeted to preventing misalignments vis-à-vis our established comparator markets and does not transform into a 'mini-ECBR' every four years." Furthermore, as to granting the Board discretion to make adjustments within the "testing range," the SAC opined: "…. we understand that Executive Directors require some discretion to smooth annual salary increases also within the 10-20 percent margin for international competitiveness." (SAC Reactions to ECBR Proposals (EBAP/06/02), January 17, 2006.) *See also* "The Chairman's Summing Up, Employment, Compensation, and Benefits Review, Executive Board Meeting 06/12, February 7, 2006" (BUFF/06/30) (chronicling diversity of opinion among Executive Directors).

96. When reviewing challenges to decisions of the Executive Board in establishing or amending the terms and conditions of employment, principles of separation of powers between the Tribunal and the policy-making organs of the Fund are also pertinent:

> "***ARTICLE III***
>
> **(third sentence)**
>
> **Nothing in this Statute shall limit or modify the powers of the organs of the Fund under the Articles of Agreement, including the lawful exercise of their discretionary authority in the taking of individual or regulatory decisions, such as those**

> **establishing or amending the terms and conditions of employment with the Fund.**
>
> The third sentence of Article III incorporates, as part of the governing instrument of the tribunal, the concept of separation of power between the tribunal, on the one hand, and the legislative and executive organs of the institution, on the other hand, by stating that the establishment of the tribunal would not in any way affect the authority conferred on other organs of the Fund under the Articles of Agreement. This provision would be particularly significant with respect to the authority conferred under Article XII, Section 3(a), which authorizes the Executive Board to conduct the business of the Fund, ...
>
> This provision is consistent with well-established case law in which judicial bodies have repeatedly affirmed their incapacity to substitute their own judgments for those of the authorities in which the discretion has been conferred.[11] Thus, although a tribunal may decide whether a discretionary act was lawful, it must respect the mandate of the legislative or executive organs to formulate employment policies appropriate to the needs and purposes of the organization. Similarly, a tribunal is not competent to question the advisability of policy decisions.[12]
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> [11.] See generally S.A. de Smith, *Judicial Review of Administrative Action*, at 278-79 (4th ed. 1980).
>
> [12.] See *von Stauffenberg*, WBAT Reports, Dec. No. 38 (1987), at para. 126; *Decision No. 36*, NATO Appeals Board (1972), Collection of the Decisions (1972).

(Report of the Executive Board, p. 20.)

97. As Respondent emphasizes, the structure of the compensation system adopted in 2006 reflects consultation with all pertinent stakeholders, the Board's drawing upon the information before it in taking its decision, and the compromises that characterize a legislative process. Similarly, in de Merode, the WBAT observed that solutions to the problem had been considered first by way of a study that the Bank had commissioned by an outside firm and then by the Joint Committee on Staff Compensation Issues (Kafka Committee), which considered several possible alternative solutions. On the basis of the Kafka Committee Report, the Bank's Executive Directors introduced the new system, which, noted the WBAT, was "subject to two conditions which had not been proposed by the Kafka Committee." (Paras. 65-69.) *Cf.* Ms. "G", paras. 45-53 (noting that a Working Group on Expatriate Benefits had assessed five possible bases for allocating expatriate benefits and later differing proposals had been made by SAC and HRD).

98. The WBAT further noted that "… the tax allowances under the new system would only be 'reasonably related' to the taxes effectively paid by each staff member in such a way that, in

the terms of the Circular, 'the tax allowances will rarely exactly equal the taxes payable – it may be more, it may be less.'" (de Merode, para. 71.)

> "76. … A balance has to be struck among various factors (equity, simplicity, cost) which sometimes contradict one another: rigorous exactness cannot be achieved save at the price of complications; a simple solution can only be achieved at the cost of approximation. On all these questions it was by a reasoned judgment and after a balance of considerations that the competent authorities of the Bank preferred one formula to another, being conscious that none could be perfect in all respects."

(Id., para. 76.) *See also* Ms. "G", para. 79 (nexus between goals of expatriate benefits policy and method for their allocation "does not require that there be a perfect fit between the objectives of the policy and the classification scheme established, and … may rest upon generalizations").

99. It is also significant that earlier iterations of the Fund's staff compensation system reflect a similar process by which recommendations were gathered and debated. For example, with respect to the system implemented in 1989, "… some of the JCC's recommendations were endorsed [by the Executive Board], and others were modified on the basis of the comments and suggestions of management." (Staff Bulletin No. 89/10 (May 22, 1989), p. 1.)

100. This Tribunal has held that the fact that one decision is recommended to a decision-making authority and a different decision ultimately is taken does not of itself vitiate the reasonableness of that decision. *See* Mr. "R", para. 63 (decision taken "after extended consideration, and rejection of a recommendation by the Director of Human Resources.") Accordingly, that the Executive Board's decision reflects compromise among varying positions and did not track all of the recommendations of the Steering Committee does not establish, as Applicants contend, that it was not reasonably taken on the basis of relevant facts.

101. As described above, this Tribunal on more than one occasion has recognized that the Fund's policy-making discretion extends to making choices between more than one reasonable alternative. *See* Mr. "R", para. 65 and Ms. "G", para. 80 (quoted above at paras. 49-52). *See also* Crevier v. International Bank for Reconstruction and Development, WBAT Decision No. 205 (1999):

> "17. During the discussion and preparation of the pension reform, a number of alternatives were considered instead of the Rule of 50, including an early retirement window that would have allowed for staff members to retire on an unreduced pension during a limited period of time. This alternative was favored by the Staff Association but was not retained because it was believed by management that it would encourage a number of valuable staff members to retire early in order to take advantage of this limited opportunity. It is not within the competence of the Tribunal to consider which alternative would have been best or more effective to attain the desired objectives of the reform. This is a matter that

> is solely within the discretion of the Board of Directors. The Tribunal is empowered only to decide whether the solution retained in Article 3.3 of the SRP can be applied lawfully to the Applicant in the light of his rights as a staff member."

102. In de Merode, the WBAT further recalled that several aspects of the method of calculation of tax reimbursement had been unilaterally amended by the Bank before 1979 and therefore the method of computation of reimbursement established in 1946 on the basis of the standard deduction was "not sacrosanct and could be modified from time to time:" (Para. 78.)

> "82. …. The only change effected is in the replacement of the standard deduction method with another method. The Bank was entitled to do this even if the gross income of certain United States staff members has been reduced as a result, and even if the reimbursement in excess of taxes which they previously received is diminished or altogether disappears. All these non-essential elements in the conditions of employment were subject to unilateral amendment by the Bank."

(Id.)

103. The WBAT concluded *inter alia* that "… the objective of the Bank was not to reduce the income of a particular category of staff members by reason of their nationality but to ensure a better functioning of the institution by a more equitable personnel policy. This did not involve an abuse of discretion or a misuse of powers on the part of the Bank." (Para. 85.)

104. The WBAT in de Merode went on to observe that the Tribunal could not "substitute its judgment for that of the Bank" in choosing the revised system for tax reimbursement. "That the average deduction system also presents some inconveniences is certain. As the Kafka Report brought them into the open, the Executive Directors were fully aware of them. As was the case in 1946, the 1979 decision represented a considered choice taking into account the various relevant factors." (Para. 86.)

105. Accordingly, in the light of these precedents, this Tribunal concludes that the Fund's Executive Board acted within its authority and in an appropriate exercise of that authority in its consideration of the relevant facts bearing upon the revised compensation system.

Was the contested decision improperly motivated?

106. Applicants contend that the amendment of the staff compensation system reflects an "intention to reduce the benefits of staff members." Respondent, for its part, maintains that "the fact that the new system may result in a lower salary structure than the previous system does not mean that the new system is not competitive or derogates from any legal prescriptions."

107. In the view of the Tribunal, that the amendment of the system for setting staff salaries may have "weakened" their competitiveness is not tantamount to a failure to adhere to the principle of "international competitiveness," especially where, as here, there is clear evidence in the record that the amendment was taken as a result of studied consideration leading to the

conclusion that the Fund's payline had been "misaligned" with comparator markets, resulting in its being "overcompetitive" at particular grade levels. As the Steering Committee's Companion Paper explained, "… by linking the level of its salaries to those paid in relevant comparator markets, the Fund can provide compensation that is competitive but not overcompetitive."

108. International administrative tribunals, considering challenges to the amendment of terms of employment, have upheld revisions that resulted in lower staff compensation when they likewise were motivated by such legitimate concerns. For example, in de Merode, the WBAT observed that the change in the methodology for carrying out the principle of tax reimbursement was to correct the problem of over-reimbursement, a problem that had evolved under the pre-existing methodology over time with changed circumstances:

> "64. Gradually, doubts arose as to the adequacy of this system in new economic conditions .... The possibility of reimbursement in excess of taxes paid, which in 1946 had been thought of as remaining infrequent and unimportant, in fact had become increasingly frequent and more important. Correspondingly, the cost of the system became constantly heavier for the Bank."

Similarly here, the Fund over time made an assessment that the compensation system was no longer fulfilling its objectives in the optimum fashion.

109. Moreover, international administrative tribunals have held that taking account of cost considerations in amending terms and conditions of employment is not an improper motive. For example, in Kepper v. International Finance Corporation, WBAT Decision No. 149 (1996), the applicant contested the Bank's delay in implementing a new system of post allowances, contending that the delay had resulted in reduced compensation to him. The WBAT concluded: "Among the factors pertinent to a change in policy and the timing thereof are considerations of cost-effectiveness, budget, administration and transition. The Respondent did not abuse its discretion in weighing the budgetary implications, concerning both extent and timing, of the proposed change in the post allowance index against the benefits to be derived therefrom." (Para. 26.) *See also* de Merode, para. 87 ("The choice of a particular method of tax reimbursement may properly be determined by several factors: equity, ease of administration, cost, comprehensibility, confidentiality. Thus the cost of any particular system is one of several factors which the organization may take into account.")

110. Accordingly, the Tribunal concludes that the fact that the Fund, as the result of study and deliberation, sought to correct for "overcompetitiveness" in certain elements of its system for setting staff salaries does not establish that the decision taken was improperly motivated.

Did the Executive Board abuse its discretion, by its decision of April 17, 2006, applying the revised system of adjusting staff salaries to the 2006 compensation round?

111. While in their Applications Applicants identify the Executive Board's decision of April 14, 2006 as the contested decision, they further contend that the Board's subsequent decision of April 17, 2006, applying the revised system for adjustment of staff salaries to the 2006 compensation round, also was illegal. Accordingly, Applicants maintain that the effect in 2006

both illustrates the illegality of the April 14 decision and itself constitutes an abuse of discretion. Applicants in their Reply request as additional relief that the Tribunal "… declare the decision taken on April 17, 2006, in application and implementation of the April 14, 2006 decision, to be null and void, and to order the Fund to apply the pre-January 2005 compensation system in retroactively determining the salary increase for the 2006 compensation round."

112. Applicants maintain that implementation of the amended system in 2006 "did, in fact, transgress the limits of the discretionary power of the Fund's Executive Board." There appear to be two elements to Applicants' complaint regarding the 2006 compensation round. First, Applicants contend that the changes in the methods for setting the Fund's payline, e.g., changes in sector weights and financial market pitch, operated to decrease the payline as compared with the increase that would have been indicated under the previous system. It is not disputed that this effect occurred and was a consequence of the operation of the newly adopted compensation system.[15] Accordingly, this element of the complaint is indistinguishable from Applicants' challenge to the April 14 decision considered above.

113. Accordingly, the gravamen of Applicants' complaint in respect of the 2006 compensation round is that because the U.S.-indicated payline was only 8 percent above that indicated by the French/German comparators, i.e. below the floor of the "testing range," the Board had discretion to raise the payline above the level indicated by the U.S. market but it chose not to do so. As Respondent correctly notes, the discretion at issue in the 2006 round is the same that was available to the Board under the pre-existing system; the expansion of discretionary authority implemented by the 2006 amendment applies when the initial payline falls within, not outside of, the "testing range" as it did in 2006. Accordingly, Respondent asserts that Applicants' challenge to the implementation of the new system in 2006 is tantamount to challenging a feature of the system that has been in place since 1989.

114. Nonetheless, Applicants assert that the fact that the first application of the revised system resulted in a Fund payline only 8 percent above that of the European market is "… strong evidence that the mere *possibility* of upward discretion does not provide an adequate safeguard for preserving the international competitiveness of Fund salaries." (Emphasis in original.) Accordingly, Applicants argue that "… there is sufficient evidence that armed with its recently adopted discretionary authority, the Board has already begun to veer in the direction of systematically disregarding those crucial factors that are required to be taken into account in order to ensure that staff salaries continue to be internationally competitive."

115. Applicants take issue, in particular, with the Fund's interpretation of the 2005 recruitment and retention data. Similar views were presented by the SAC to the Executive Board at the time of its decision (see above, para. 38). At the same time, Management articulated the grounds upon which its recommendation was based, taking account of a series of relevant factors, including recruitment and retention data and exchange rate developments (see above, at paras. 36-37). It is

[15] The Fund summarized the effect in 2006 as "a steepening of the Fund's payline and an overall reduction in the A9-B2 salary structure of 0.7 percent on average, with the midpoints at Grades A9-A13 reduced and those for Grades A14–B2 increased." Transitional arrangements assured that no staff member would experience a reduction in salary.

also to be recalled that, under the pre-existing system, upward adjustments were taken only in six of the eight years in which the initial Fund payline fell below the 10 percent floor of the testing range. As the WBAT has observed, "… the same technical data are capable of leading, after interpretation and an exercise of judgment, to a variety of solutions,… none any less legally valid than any other." (von Stauffenberg, para. 95.)

116. Having regard to the foregoing considerations, the April 17, 2006 decision setting the staff salaries for the 2006 compensation round was, in the view of the Tribunal, not taken in disregard of the relevant facts and it does not constitute an abuse of the Executive Board's discretion.

Decision

FOR THESE REASONS

The Administrative Tribunal of the International Monetary Fund unanimously decides that:

The Applications are denied.

Stephen M. Schwebel, President

Nisuke Ando, Associate Judge

Michel Gentot, Associate Judge

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Stephen M. Schwebel, President

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Celia Goldman, Registrar

Washington, D.C.
January 24, 2007