

FSM SUPREME COURT TRIAL DIVISION

SANAJATAMITRA BASU,	)	CIVIL ACTION NO. 2019-029
	)	
Petitioner and Plaintiff,	)	
	)	
vs.	)	
	)	
EUGENE AMOR, in his official capacity as	)	
the Secretary of Finance, Government of	)	
the Federated States of Micronesia, and	)	
the FSM NATIONAL GOVERNMENT,	)	
	)	
Respondents and Defendants.	)	
_____	)	
SANAJATAMITRA BASU,	)	CIVIL ACTION NO. 2021-014
	)	
Plaintiff/ Counterdefendant,	)	
	)	
vs.	)	
	)	
CARLSON D. APIS, in his official capacity	)	
as the Secretary of Transportation,	)	
Communications, and Infrastructure for the	)	
Federated States of Micronesia, and the	)	
FSM NATIONAL GOVERNMENT,	)	
	)	
Defendants/Counterclaimants.	)	
_____	)	

ORDER DENYING DISMISSAL OF COUNTERCLAIM

Larry Wentworth  
Associate Justice

Decided: June 7, 2022

APPEARANCES:

For the Plaintiff: Michael J. Sipos, Esq.  
P.O. Box 2069  
Kolonia, Pohnpei FM 96941

For the Defendants: Lori J. Williams, Esq.  
Assistant Attorney General  
FSM Department of Justice  
P.O. Box PS-105  
Palikir, Pohnpei FM 96941

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## HEADNOTES

### Civil Procedure – Motions – Unopposed

The failure to oppose a motion is generally deemed a consent to the motion, but even if there is no opposition, the court still needs good grounds before it can grant the motion. Basu v. Amor, 23 FSM R. 589, 591 (Pon. 2022).

### Administrative Law – Judicial Review; Civil Procedure – Parties

By law, the Secretary of Finance and Administration is the only named defendant in a judicial review of a tax assessment decision. Basu v. Amor, 23 FSM R. 589, 592 n.2 (Pon. 2022).

### Taxation – Wages and Salaries Tax

There is a statutory exemption from FSM taxation for non-citizens, who are employed by an international organization, foreign contractor, or other foreign entity performing services or otherwise conducting business in furtherance of a foreign aid agreement entered into by the FSM. Basu v. Amor, 23 FSM R. 589, 593 n.3 (Pon. 2022).

### Contracts – Third-Party Beneficiary

The determining factor as to the rights of a third-party beneficiary is the intention of the parties who actually made the contract. Basu v. Amor, 23 FSM R. 589, 595 (Pon. 2022).

### Contracts – Third-Party Beneficiary

The question whether a contract was intended for the benefit of a third person is generally regarded as one of construction of the contract. The parties' intention in this respect is determined by the contract's terms as a whole, construed in the light of the circumstances under which it was made, and with the apparent purpose that the parties are trying to accomplish. Basu v. Amor, 23 FSM R. 589, 595 (Pon. 2022).

### Contracts – Third-Party Beneficiary

If a third-party beneficiary is so described as to be ascertainable, it is not necessary that he be named in the contract in order to enforce the contract. Basu v. Amor, 23 FSM R. 589, 595 (Pon. 2022).

### Contracts – Third-Party Beneficiary

A third party beneficiary can only recover if he is an intended beneficiary of the contract; he cannot recover if he is only an incidental beneficiary of that contract. A third-party beneficiary's right to sue upon a contract depends, as a rule, upon whether the contract is for his direct benefit or whether his benefit under it is merely incidental, indirect, or consequential. Basu v. Amor, 23 FSM R. 589, 595 (Pon. 2022).

### Contracts – Third-Party Beneficiary; Taxation – Wages and Salaries Tax

A senior project manager hired by the FSM to work on Asian Development Bank loan projects is not an intended third-party beneficiary of ADB Special Operations Loan Regulations, which makes the loan principal and interest exempt from taxation; or of the ADB Loan agreement, which prohibits withdrawals from the Loan Account for any local taxes, when those agreement were not made for the project manager's direct benefit. He is only an incidental beneficiary of the ADB contract and the ADB regulations Therefore the court cannot conclude from either provision that the contracting parties intended that the project manager hired by the FSM, was meant to be exempt from FSM income taxes. Basu v. Amor, 23 FSM R. 589, 595 (Pon. 2022).

### Taxation – Gross Revenue Tax; Taxation – Wages and Salaries Tax

A tax on the income of a senior project manager hired by the FSM, after he has earned it, does violate the Asian Development Bank loan agreement's prohibition of withdrawals from the Loan Account for any local taxes because the withdrawal from the loan account pays the senior project manager's compensation, and, after that, the senior project manager is liable to pay his own taxes (either through employer withholding if his pay is subject to the wage and salary tax or by his own payment if he is subject

to the gross revenue tax). Basu v. Amor, 23 FSM R. 589, 595-96 (Pon. 2022).

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### COURT'S OPINION

LARRY WENTWORTH, Associate Justice:

On April 14, 2022, the petitioner and plaintiff, Sanajatamitra Basu, filed his Motion to Dismiss Counterclaim for the Failure to State a Claim upon Which Relief May Be Granted. No opposition has been filed. The failure to oppose a motion is generally deemed a consent to the motion, FSM Civ. R. 6(d), but even if there is no opposition, the court still needs good grounds before it can grant the motion. Senda v. Mid-Pacific Constr. Co., 6 FSM R. 440, 442 (App. 1994). Good grounds do not exist. The motion is denied. The reasons follow.

#### I. BACKGROUND FACTS

The FSM Omnibus Infrastructure Development Project ("OIDP"), and the Asian Development Bank ("ADB") loans to finance it, were authorized by statute. FSM Pub. L. No. 14-46, §§ 1-3, 14th Cong., 2d Reg. Sess. (2005). The statute provided that "[l]oan proceeds may be used only as set forth in the Loan agreements between the Federated States of Micronesia ("FSM") and the Bank." One loan agreement attachment provided that "[n]o withdrawals from the Loan Account shall be made in respect of any local taxes." ADB Loan No. 2099-FSM, sch. 3, para. 2 (June 28, 2005). The ADB also recommended or required that a senior project manager be hired for the OIDP's management and administration.

The FSM Department of Transportation, Communications and Infrastructure ("TC&I") contracted with Basu, a citizen of India, to be the consultant and senior project manager for the OIDP. Under the contract, Basu reported to the TC&I Assistant Secretary, assisted TC&I in planning and implementing infrastructure projects effectively and efficiently, and provided TC&I with management support for the OIDP and other projects. The contract stated that "[n]othing in this Contract shall be construed as establishing any relationship other than that of independent contractor between the EA<sup>1</sup> and the Consultant, or the Firm if the Consultant is engaged through a firm." Contract para. G-14 (footnote added). Basu was not engaged through a firm, and his contract was funded entirely from the OIDP loan. The contract started January 13, 2014, and ran until July 12, 2015.

Basu was paid \$10,000 a month. Each month, he submitted an invoice for that amount to the TC&I Assistant Secretary. TC&I then approved it and executed a payment voucher for that amount which was sent to FSM Finance for payment. Finance did not deduct or withhold any taxes or sums from the monthly \$10,000 payments. These payments were made entirely from the ADB OIDP loan money. After this contract ended on July 12, 2015, it was followed by a second contract, with identical provisions, that ran from August 1, 2015, to July 31, 2016. A third, identical contract followed. It ran from September 1, 2016, to August 31, 2017. Throughout these contracts, Basu continued to be paid \$10,000 monthly and no wages and salaries taxes were withheld or deductions made. Nor did Basu himself pay any taxes to the FSM on this income.

After Basu's third consultant and senior project manager contract ended, Basu had a three-month contract at the year's end and then another employment contract with the FSM, the last of which ended on September 30, 2019. It included a term that obligated the FSM to pay for Basu's costs of return after the contract term ended. The usual payroll taxes were withheld from Basu's income under these contracts.

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<sup>1</sup> "EA" refers to the "Executing Agency," which "is the organization or government agency of the Government with which the Consultant signs the Contract." Contract para. D-7.

On January 9, 2019, the FSM Assistant Secretary of Finance and Administration, the head of that department's Division of Customs and Tax Administration, sent Basu a letter assessing Basu's tax liability for his first three contracts at \$33,805, plus \$16,828.80 in penalties and \$6,830.10 in interest, for a total of \$57,463.90. Basu denied liability. The Assistant Secretary's March 25, 2019 follow-up letter acknowledged that Basu had a contract with TC&I, stated that the ADB loan agreement was irrelevant, emphasized that recipients of wages and salaries are, under 54 F.S.M.C. 124, subject to a tax on that income, and informed Basu that, given his unwillingness to pay, the Assistant Secretary would ask the Finance Division to withhold 50% from Basu's paychecks until the tax debt was paid in full. The Assistant Secretary's second follow-up letter (Apr. 10, 2019) rejected another Basu response and noted that Basu's contract was with TC&I and not ADB, thus making his income subject to FSM tax.

In response to the Assistant Secretary's request, the Finance Division deducted \$12,731.93 from Basu's 2019 paychecks for pay periods #15 through 19. It also deducted (withheld) Basu's entire paycheck for pay period #20, which Basu believed amounted to an additional \$4,959.32 "credit" towards his alleged tax debt, for a total of \$17,691.25. Finance also did not pay Basu's return costs under his contract ending on September 30, 2019. At the time, TC&I officials supported Basu's position, and the FSM Department of Justice, in a September 23, 2019 letter, sided with the Assistant Secretary.

## II. CIVIL ACTION 2019-029 INITIAL JUDICIAL REVIEW

On December 23, 2019, Basu filed Civil Action No. 2019-029 as a petition for judicial review of a tax assessment and as a complaint for violation of civil rights and for declaratory relief.<sup>2</sup> Basu alleged that the tax assessment on his "independent contractor" earnings was unlawful because that income was tax exempt; that the deductions for that tax assessment were thus unlawful; and that therefore his civil rights were violated. He sought a declaration that the tax assessment was unlawful, that no penalties and interest could apply, that the deductions from his 2019 earnings to pay that tax assessment were wrong, and that the FSM could take no further action against him based on that assessment. He also sought an order that the FSM reimburse him for those deductions, pay pre-judgment interest, pay his attorney's fees and costs, and any further compensation he was entitled to under his just-expired contract.

The defendants' answer denied Basu's grounds and prayer for relief. They then moved to compel an administrative hearing and asked that the case be stayed until that administrative process was done. Regarding it as futile, Basu opposed an administrative hearing. Basu then moved for summary judgment, which the defendants opposed because independent contractors are not tax exempt and the ADB loan terms did not change that result.

Since Basu had not had an administrative hearing before the Secretary of Finance and Administration, the court ordered that he have one, and that if Basu was still aggrieved after the Secretary's decision, he could then seek judicial review. Basu v. Amor, 22 FSM R. 557, 568 (Pon. 2020) (citing 54 F.S.M.C. 156(1)). The administrative hearing went forward.

## III. SECRETARY AMOR'S ADMINISTRATIVE DECISION

On August 29, 2020, Secretary Eugene Amor ruled that the exemption from local taxes mentioned in the ADB loan agreements, that financed Basu's employment, did not apply to wages and salaries income taxes; that Basu was obviously an FSM employee because his employment contract was with the FSM national government; that Basu was thus subject to the FSM wages and salaries tax under Title 54; that the

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<sup>2</sup> These claims are made against both the Secretary of Finance and Administration and the Federated States of Micronesia, although, by law, only the Secretary of Finance and Administration can be named as the defendant in a judicial review of a tax assessment decision. 54 F.S.M.C. 156(1); Fuji Enterprises v. Jacob, 20 FSM R. 279, 281 (Pon. 2015) (since statute requires that, in an action for judicial review of a tax assessment, the Secretary of Finance be the sole named defendant; deletion of other named defendants is proper).

wages and salaries tax is collected by the employer withholding the required amount when paying the employee [54 F.S.M.C. 131]; that this was not done when Basu was paid; that the amount of Basu's unpaid wage and salary tax was correctly assessed; that the employer (the FSM) is initially liable for the wages and salaries tax not withheld from Basu's pay (plus penalties and interest [54 F.S.M.C. 134]); and that the government may recover from Basu the sums that should have been withheld from his salary only once his employer, the FSM, had first paid that amount out of its own funds [54 F.S.M.C. 135(3)].

Secretary Amor further found that Basu's position was not tax exempt; that his employment contract was drafted by the ADB and negotiated between TC&I and Basu; that the ADB's position was that only local taxes (not income taxes) are exempted; that the Department of Foreign Affairs was not involved in negotiating Basu's contract; that the government's standard practice was to exempt consultants who contract directly with international organizations like the ADB<sup>3</sup> and to tax consultants who contract with the FSM government; and that the amount not paid to Basu at the end of his last FSM contract was \$1,163.25 (last paycheck of \$500.15 and \$663.10 for Basu's airfare to Chuuk).

In March 2021, TC&I paid the amount that, in Finance's view, should have been withheld from Basu's TC&I pay for his ODP consulting contracts, thus allowing TC&I to make, under 54 F.S.M.C. 135(3), an indemnity claim against Basu for \$33,805.

#### IV. CIVIL ACTION NO. 2021-014

On May 7, 2021, Basu filed a new lawsuit, docketed as Civil Action No. 2021-014, this time against the Secretary of Transportation, Communication, and Infrastructure, Carlson D. Apis, and the FSM. Basu now sought a declaratory judgment that his income under his initial consultancy contracts was tax-exempt; or if not tax-exempt, that it was the FSM's contribution to the ADB ODP project; or that the FSM had waived the right to tax Basu's income because it had not informed the ADB that it intended to; or that promissory estoppel barred collecting these taxes from Basu; or that either the statute of limitations or laches barred the FSM's claim in whole, or in part; that the amount was wrong; or that he was an independent contractor against whom the wages and salaries tax does not apply.<sup>4</sup> Basu also sought damages for the tortious breach of his employment contract and for conversion, including economic damages and punitive damages for both those causes of action, plus attorney's fees and costs.

The defendants answered and asserted a counterclaim of \$33,805 for the wage and salary tax amount it believed should have been withheld from Basu's consultancy contracts, but was not, and which TC&I had now itself paid from its own funds and for which it now sought indemnity from Basu.

#### V. BASU'S FORMER SUMMARY JUDGMENT MOTION

Basu then moved, in Civil Action No. 2019-029, for summary judgment based on Secretary Amor's administrative ruling, which Basu conceded was partially adverse to him. Basu contended that Secretary Amor correctly ruled that Basu was not liable for penalties and interest, but had not addressed Basu's claim that the FSM's unjustified taking of money from his later non-tax-exempt paychecks to pay the unlawful tax

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<sup>3</sup> This policy complies with the statutory exemption from FSM taxation for non-citizens, who are "employed by an international organization, foreign contractor, or other foreign entity performing services or otherwise conducting business in furtherance of a foreign aid agreement entered into by the Federated States of Micronesia." 54 F.S.M.C. 112(13)(k). Early in the litigation, Basu asserted that he was a tax-exempt foreign aid organization employee under this statute, but seems to have been abandoned that position after the court, *Basu v. Amor*, 22 FSM R. 557, 565 (Pon. 2020), and the Secretary concluded that, based on Basu having contracted with the FSM, he was not.

<sup>4</sup> Many of Basu's claims in Civil Action No. 2021-014 will, presumably, stand as what are, in effect, affirmative defenses to the defendants' counterclaim.

assessment, violated the law since the FSM had not paid the taxes assessed, which the Secretary had just ruled that the FSM needed to do in order to have any claim against Basu for unpaid taxes. Basu asserted that Amor then unlawfully reissued the same assessment against him (minus the penalties and interest). Basu asserted that he was entitled not only to an order that this taking was unlawful but also to an order that Basu's earned salary and withheld benefits, totaling \$18,854.57, should be immediately returned to him (plus 9% interest from the date of each taking and reasonable attorney's fees).

The defendants acknowledged that Secretary Amor lacked the authority to recover from Basu any unpaid taxes, unless and until Basu's employer (the FSM) had first been required to pay, out of its own funds, the amounts it should have initially withheld from its employee's (Basu's) pay (plus the added employer's penalties and interest). The defendants asserted, and Basu did not dispute, that, after appropriation by Congress, the defendants had paid the taxes that they believe should have been withheld from Basu's pay, plus the employer's penalties and interest for not having done so when paying Basu.

The defendants asserted that this was an affirmative defense, which Basu had to overcome to obtain summary judgment, and, in separate Civil Action No. 2019-029 motions, moved for leave to file an amended answer and to file a supplemental pleading to add this affirmative defense and to also assert a counterclaim to recover from Basu the sum (\$33,805) that should have been withheld from Basu's pay, but was not [with a \$18,854.57 credit for the sums that the FSM has already taken and still retains and that Basu wants returned].

Basu contended that nothing should have been withheld because the evidence showed (but was ignored in the administrative proceeding) that he had not been an FSM employee, but had been an independent contractor. Basu further argued that the Civil Action No. 2019-029 defendants should not, and need not, be granted leave to amend and supplement their Civil Action No. 2019-029 pleadings because those defenses and counterclaims were already raised in Civil Action No. 2021-014 by that case's defendants. Basu asserted that he should be granted summary judgment in the entirety in Civil Action No. 2019-029; that immediate payment of that judgment should be ordered; that Civil Action No. 2019-029 should then be closed; and that Civil Action No. 2021-014 could proceed as a separate case, with the FSM's affirmative defenses and counterclaims to be considered therein and adjudicated in due course. In Basu's view, consolidation was unnecessary because Civil Action No. 2019-029 should result in an immediate judgment in his favor, and the FSM could proceed with its defenses and counterclaims in Civil Action No. 2021-014 as it saw fit.

Basu disputed the Secretary's finding that he was, from the start, an FSM employee. Basu asserted that he was instead an independent contractor. Basu further argued that, in his lawsuit(s), he pled only that he owed no wages and salaries tax and neither raised nor included the issue of whether, as an independent contractor, he owed any gross revenue tax, so that was irrelevant.

The court could not agree. Civil Procedure Rule 54(c), commands that "[e]xcept as to a party against whom a judgment is entered by default, every final judgment shall grant the relief to which the party in whose favor it is rendered is entitled, even if the party has not demanded such relief in the party's pleadings." Thus, if Basu were to prove, that for tax purposes, he was an independent contractor, the court would then have to grant him whatever relief he would then be entitled to based on the difference (if any) between his alleged wages and salaries tax liability and his actual gross revenue tax liability, even if he had not demanded that relief in his two complaints.

The court granted partial summary judgment on Basu's claim that, when the FSM retained Basu's \$18,854.57, Basu bore no liability for wages and salaries tax since his putative employer (TC&I) had neither withheld any wages and salaries tax nor paid those sums itself out of its own funds and that therefore, as a matter of law, the FSM's later retention of the \$18,854.57, was unlawful, and remained unlawful until that amount was paid out of the employer's [the FSM's] own funds. *Basu v. Amor*, 23 FSM R. 429, 433 (Pon. 2021) (citing 54 F.S.M.C. 135(3)). The court otherwise denied Basu's summary judgment motion because

material facts were genuinely in dispute, since, under the common law rules, a factual inquiry is usually necessary to determine whether someone is an employee or an independent contractor. *Id.* at 432-33. And, because the cases involved the same property, the court ordered the cases consolidated to avoid the possibility of inconsistent decisions, to expedite the matter's ultimate resolution, and to avoid expensive and unnecessary duplication. *Id.* at 433.

#### VI. BASU'S CURRENT MOTION TO DISMISS COUNTERCLAIM

Basu now moves to dismiss the Civil Action No. 2021-014 counterclaim. Basu contends that the Civil Action No. 2021-014 defendants' counterclaim fails to state a claim upon which the court can grant relief because the ADB Special Operations Loan Regulations, Article VII, § 7.01 (Jan. 1, 2006) makes the loan principal and interest exempt from taxation; because the ADB Loan No. 2099-FSM, schedule 3, paragraph. 2 (June 28, 2005) prohibits withdrawals from the Loan Account for any local taxes; and because the ADB Special Operations Loan Regulations, Article VI, § 6.01 (Jan. 1, 2006) required that a borrower (the FSM in this case) and the ADB cooperate and exchange views to ensure that the loan purposes are accomplished and Basu asserts that taxation of his compensation was a matter on which views had to be exchanged, but were not. Basu further contends that these are contracts between the ADB and the FSM and that he was an intended third-party beneficiary of these contractual provisions which, in his view, require that his ADB ODP consultancy compensation be tax-exempt.

As mentioned above, *supra* note 3, the court has previously rejected other theories meant to prove that Basu's pay was tax-exempt. It must now reject this one.

The determining factor as to the rights of a third-party beneficiary is the intention of the parties who actually made the contract. Mailo v. Penta Ocean Inc., 8 FSM R. 139, 141 (Chk. 1997). "The question whether a contract was intended for the benefit of a third person is generally regarded as one of construction of the contract." *Id.* (quoting 17A AM. JUR. 2D *Contracts* § 441, at 464 (1991)). The parties' intention in this respect is determined by the contract's terms as a whole, construed in the light of the circumstances under which it was made and with the apparent purpose that the parties are trying to accomplish. *Id.*

Basu is not named as a beneficiary in any of the contracts of which he contends he is the intended beneficiary. But if a third-party beneficiary is so described as to be ascertainable, it is not necessary that he be named in the contract in order to enforce the contract. Mailo, 8 FSM R. at 141-42. Basu, even though he was the senior project manager and consultant, that position is not described as to be ascertainable as an intended beneficiary of the contracts.

A third party beneficiary can only recover if he is an intended beneficiary of the contract; he cannot recover if he is only an incidental beneficiary of that contract. FSM Dev. Bank v. Mudong, 10 FSM R. 67, 75 (Pon. 2001). "The right of a third-party beneficiary to sue upon a contract depends, as a rule, upon whether the contract is for his direct benefit or whether his benefit under it is merely incidental, indirect, or consequential." 17A AM. JUR. 2D *Contracts* § 443, at 467 (1991).

The court cannot conclude that the ADB Special Operations Loan Regulations, Article VII, § 7.01 (Jan. 1, 2006), which makes the loan principal and interest exempt from taxation; and the ADB Loan No. 2099-FSM, schedule 3 (June 28, 2005), which prohibits withdrawals from the Loan Account for any local taxes, were made for Basu's direct benefit. The court also cannot conclude from either provision that the contracting parties intended that the senior project manager's income, or that income any person the FSM hired to work on the ADB loan projects, was meant to be exempt from FSM income taxes. Basu is only an incidental beneficiary of the ADB contract and the ADB regulations.

Furthermore, a tax on Basu's income after he has earned it is not a tax on the loan principal or interest in violation of the ADB Special Operations Loan Regulations, Article VII (or the Article VI requirement to exchange views). Nor does a tax on Basu's income, after he has earned it, violate the ADB Loan No.

2099-FSM, schedule 3's prohibition of withdrawals from the Loan Account for any local taxes. The withdrawal from the loan account pays the senior project manager's (Basu's) compensation. After that, the senior project manager, Basu, is liable to pay his own taxes (either through employer withholding if his pay is subject to the wage and salary tax or by his own payment if he is subject to the gross revenue tax).

VII. CONCLUSION

ACCORDINGLY, Basu's motion to dismiss the counterclaim because he is an intended third-party beneficiary of the ADB Loan No. 2099-FSM or of the ADB Special Operations Loan Regulations is denied.

VIII. SCHEDULE FOR FURTHER PROCEEDINGS

NOW THEREFORE IT IS HEREBY ORDERED that the following schedule is set for these consolidated cases:

- 1) the parties shall make all their discovery requests no later than August 15, 2022;
- 2) all discovery shall be completed no later than September 5, 2022; and
- 3) all pretrial motions shall be filed and served no later than September 26, 2022.

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