

HONG KONG COURT CONFIRMS IMPLIED TERM OF EMPLOYMENT

In a judgment that will have repercussions for all employers in Hong Kong, the Hong Kong Court of First Instance rejected arguments that the courts are strictly bound by legislation and express terms of an employment contract. Calling Hong Kong's employment protection "minimal" and recommending that the courts "exercise judicial creativity" to "maintain a fair balance" between employers and employees, it upheld an employee's claim that an implied term prevented her employer from dismissing her to avoid paying a bonus.

Introduction

Many employees, particularly in Hong Kong's financial sector, receive some form of bonus. These bonuses often form a large part of the total remuneration package and can represent very significant sums.

Given the amounts at stake, disputes arising out of bonuses are common. Where employees are terminated close to bonus time, there may be allegations that this was done to avoid paying a bonus. The Employment Ordinance (the "**Ordinance**") does not contain any express anti-avoidance provisions aimed at employers who do this if the bonus is discretionary, and it is generally accepted that employers in Hong Kong have considerable latitude when it comes to terminating employment. Employees have sought to incorporate implied anti-avoidance terms into their contracts, but the issue has not previously been definitively determined by the Hong Kong courts. However, in *Tadjudin Sunny v Bank of America, National Association* [2014] HKCFI 2313; HCA 322/2008 the Court considered whether an anti-avoidance term should be implied into an employee's employment contract so as to prevent the employer engaging in tactics to deprive her of her bonus.

Background

The Plaintiff, Ms. Sunny Tadjudin, was an analyst at the Bank of America from 2000-2007. Her contract provided that her employment could be terminated by either party giving one month's notice in writing or paying one month's salary in lieu of notice. The contract also provided that she was eligible to be considered for a bonus under the Bank's performance incentive programme, subject to her being in employment with the Bank at the time it came to decide upon and pay bonuses. The Plaintiff received bonuses from 2000-2006, but her employment was terminated by the Bank in August 2007. She was not paid any bonus or pro-rata bonus for that year.

The Plaintiff claimed damages for wrongful termination of her employment on the basis that it was done with the intention of depriving her of a bonus for 2007. The Plaintiff also sought damages for perverse, irrational and bad faith evaluations of her performance for 2005, 2006 and 2007.

The Key Arguments

The Plaintiff argued that several terms were implied into her contract of employment, including the term of anti-avoidance. The anti-avoidance term, argued the Plaintiff, operated to prevent the Bank from exercising its contractual right to terminate her employment because the reason for her dismissal was to prevent her from being eligible for the bonus.

The Bank's core argument against the implied anti-avoidance term was that it was inconsistent with both the express terms of her employment contract as well as sections 6 and 7 of the Ordinance, which give employers the statutory right to terminate their employees' employment by giving the agreed notice or making a payment in lieu. The Bank argued that, because the Ordinance already provides a statutory framework with protection against dismissal in certain circumstances, the Court must infer that the legislature did not intend to provide additional remedies extending to the circumstances in the Plaintiff's case. The Bank relied heavily on English case law which emphasised the primacy of legislation.

The judge rejected this argument on the basis that the implied anti-avoidance term was reasonable, equitable and necessary to give business efficacy to the employment contract, and capable of clear expression.

The judge noted that the UK's employment legislation is very comprehensive compared to Hong Kong's. He also noted that employees in the UK are protected against unfair dismissal, whereas in Hong Kong the protection is merely against what he called "*dismissal to save costs*". He concluded that the "*two regimes are not comparable*", then made the following important observations:

The absence of legislation in this area is precisely the reason why the court should not hesitate to exercise judicial creativity to develop the law by implying a suitable term into the contract of employment to maintain a fair balance of the interests of the employer and those of the employee. In maintaining that fair balance, the court should keep pace with the changes in employment terms in the employment market, particularly as in this case in how the remuneration package is structured. There is no reason why in the near absence of statutory employment protection, the development of the common law should not be allowed to take its course.

Was the Implied Term Breached?

Having found that an anti-avoidance term should be implied into the Plaintiff's contract; the next issue was whether the Bank was in breach of the implied term.

The Court applied a subjective test by considering whether the Bank had a genuine reason for termination or a genuine belief that it had a valid reason. In particular, it considered the conduct of the Plaintiff's manager, Mr. John Liptak. At the end of June, 2007, Mr. Liptak (acting on behalf of the Bank) issued an official warning letter to the Plaintiff and placed her on a Performance Improvement Plan (the "**PIP**"). The PIP set out specific goals which the Plaintiff was required to meet. The warning letter stated that if the Plaintiff failed to make immediate improvement as specified in the plan, the Bank would take further disciplinary actions including summary dismissal.

On the facts, the Court found that the PIP process was "*manifestly not conducted in good faith*" and that Mr. Liptak was "*being oppressive, fault finding and looking for pretext to fail the Plaintiff in her performance of the PIP*", which was ultimately a "*pretext to terminate the Plaintiff's employment*". Accordingly, the Bank did not have a valid reason to terminate her employment.

The Court inferred from Mr. Liptak's "*malicious*" behavior towards the Plaintiff that he intended all the foreseeable consequences that termination would bring, including depriving the Plaintiff of her eligibility of being considered for a bonus. Mr. Liptak's intentions and knowledge were imputed to the Bank (presumably on the basis of vicarious liability). That intention, the Court found, along with Mr. Liptak's intention to get rid of the Plaintiff, was one of the dominant intentions or purposes of the dismissal.

It was therefore held that the Bank intended all the foreseeable consequences that termination would bring, including depriving the Plaintiff of her eligibility to be considered for the 2007 bonus.

The Plaintiff did not succeed on her similar claims in relation to her 2005 and 2006 bonuses.

Damages

The Plaintiff was awarded damages of HK\$3,900,000. The Court rejected the Plaintiff's argument that her damages should be assessed on the basis that the discretionary bonus was formulaic, but was prepared to assess her loss by putting *"itself in the employer's shoes and consider what decision, acting rationally and not arbitrarily or perversely, the employer would have reached as to the amount of the bonus to be paid"*. The Judge then looked at previous years' bonuses and came up with a comparable figure for the Plaintiff's 2007 bonus.

On the questions of costs, the Court (rather unusually) awarded the Plaintiff 85% of her costs even though she succeeded on only one claim and failed on two. The Court reasoned that even though she failed in relation to her claims relating to the 2005 and 2006 bonuses, the evidence relating to them provided background facts that were necessary for her to prove her claim for the 2007 bonus.

The Plaintiff took seven years to achieve this result, and overcame an application by the Bank to strike-out her claims (in the course of which the Court of Appeal signalled that the implied anti-avoidance term was arguable). The Bank has filed an appeal against this decision.

Key points to take away for employers and employees

For Employees:

This case confirms that there are limitations on the otherwise very broad grounds for termination set out in the Ordinance. Employees who are dismissed just ahead of their bonus date may be able to identify conduct which gives rise to breach of the implied anti-avoidance term.

For Employers:

Be wary of terminating employees as a result of personality conflicts with management, and need to be vigilant about managers who may be pursuing a personal vendetta against an employee. It is also important that appraisals are not 'slanted' in order to justify dismissal.

In General:

The case also seems to open the door to further judicial expansion of employee protection beyond the Ordinance, and (depending on the outcome of any appeal) we expect to see this decision deployed in disputes between employers and employees.

LEGISLATION UPDATE

Apart from the significant case mentioned above, there have been a number of changes made to employment-related legislation in late 2014 and early 2015. We summarise the key changes below.

Statutory Paternity leave

Starting from 27 February 2015, male employees are entitled to three days of paternity leave. Employers are obliged to grant this if the employee:

- is the child's father;
- is employed under a "continuous contract"⁽¹⁾ immediately before taking the leave;
- has given the employer advance notice of his intention to take paternity leave in accordance with the Employment Ordinance; and
- (if required by the employer) has provided the employer with a signed written statement stating that (a) he is the father, (b) the mother's name, and (c) the expected or actual date of delivery.

When can an employee take paternity leave?

The three days of paternity leave can be taken consecutively or separately in the period beginning four weeks before the expected date of delivery of the child and ending 10 weeks after the actual birth of the child.

Is paternity leave paid?

If an employee has been employed under a continuous contract for 40 weeks or more immediately before taking statutory paternity leave, he will also be entitled to receive paternity leave pay so long as he provides the supporting documents (e.g., birth certificate) specified in the Employment Ordinance.

Paternity leave pay is calculated as 80% of the daily average of the wages earned by the employee during the 12 months (or actual period of employment if shorter) immediately preceding:

- the first day of paternity leave (if leave is taken consecutively); or
- the first day paternity leave is taken (if leave is not taken consecutively).

Are there penalties for employers who don't comply?

An employer who fails to grant paternity leave or effect paternity leave pay to an eligible employee is liable to prosecution and, upon conviction, to a fine of HK\$50,000.

Practical points

Employers should ensure that company policy on paternity leave is up to date and compliant. Companies may consider developing a standard form for paternity leave applications. Employees should be given clear guidelines as to how they can apply for paternity leave and the procedure they should follow.

Contracts (Rights of Third Parties) Ordinance

The Contracts (Rights of Third Parties) Ordinance (the "Ordinance") was passed into law on 5 December 2014 and is expected to come into effect in late 2015. Although this is not strictly employment legislation, it has an effect on employment contracts, particularly for employers who are part of a wider group of companies.

What is the effect of the Ordinance?

Previously, a third party did not have any right to enforce the terms of a contract unless it was a party to the contract. For example, if an employee used confidential or proprietary information belonging to an affiliate of her employer (as opposed to the employer) in breach of a separation agreement, the affiliate had no right to directly take action against the employee. The Ordinance now allows third parties to enforce such terms in certain circumstances.

¹ An employee is regarded as being employed under a continuous contract if he has been employed continuously by the same employer for four weeks or more, with at least 18 hours worked in each week.

Under what circumstances can a third party enforce a term of a contract?

A third party who is expressly identified in a contract may enforce a term of the contract if:

- the contract expressly states that the third party has such a right, or
- the term that the third party wishes to enforce confers a benefit on the third party.

Are there exclusions?

Yes, the Ordinance specifically excludes a third party from enforcing a term of a *contract of employment* against an employee. However, a third party is not excluded from enforcing a term of a contract of employment against an employer.

A third party is also not excluded from enforcing a term of an *employment-related contract* (e.g. a separation agreement or stand alone confidentiality agreement) against a party to the contract.

Can the parties opt out of the application of the Ordinance?

Yes, parties are free to expressly contract out of the provisions of the Ordinance so that a third party cannot rely on the Ordinance to enforce the terms of the contract to which he is not a party. This intention to contract out of the Ordinance must be clearly expressed.

Practical points

Both parties will need to consider whether to expressly include a clause allowing third parties to exercise rights or to expressly include them and ensure that contracts are carefully drafted so that third party rights (or limitation of third party rights) are clearly expressed.

Sex Discrimination Ordinance

On 12 December 2014, the Sex Discrimination Ordinance was amended to protect goods and services providers from sexual harassment by their customers or prospective customers. This includes any unlawful sexual harassment which occurs on a Hong Kong registered ship or aircraft outside Hong Kong. For employers in the goods and services sector (where there is frequent direct interaction between staff and customers), this means that you may be liable if your customers harass your employees. We recommend that employers develop internal policies on handling sexual harassment complaints and provide its staff with the relevant training in this area.

Labour Tribunal Ordinance

On 24 December 2014, the Labour Tribunal Ordinance and its subsidiary legislation were amended in order to:

- clarify that the Labour Tribunal (the “Tribunal”) has the power to deal with all types of monetary claims relating to employment claims (including unliquidated damages which are to be assessed by the Tribunal in accordance with legal principles);
- align the time limit (i.e. six years) for enforcing Tribunal awards or orders with other civil claims; and
- give the Tribunal enhanced case management powers (such as making orders for payment of security for an award or order, where a party can show that it would be “just and expedient” to do so). If a party fails to provide the security as ordered by the Tribunal, the Tribunal has the power to dismiss that party’s claim, stay the proceedings, or enter judgment against that party.

The Tribunal may order a party to give security if:

- there is a real risk that payment of an award or order will be obstructed or delayed (e.g.. because there is a real risk that the party will dispose of or remove from Hong Kong assets belonging to that party); or
- a party has conducted proceedings in a manner that delays the determination of the case, or where a party’s conduct otherwise constitutes an abuse of the process; or
- a party has, without reasonable excuse, failed to comply with any award, order or direction.

Employees' Compensation Ordinance

On 4 February 2015, the Legislative Council passed a resolution to increase the compensation levels under the Employees' Compensation Ordinance for work accidents happening on or after 5 March 2015. The minimum compensation for death has been raised from HK\$340,040 to HK\$375,950 and the minimum compensation for permanent total incapacity has been raised from HK\$386,110 to HK\$426,880. The monthly earnings ceiling for calculating compensation for death and permanent total incapacity has been raised from HK\$23,580 to HK\$26,070.

Other increases relate to (i) the minimum monthly earnings for calculating employees' compensation, (ii) the maximum amount of compensation for employees requiring attention by another person, (iii) the maximum amount of funeral expenses, (iv) the costs of supplying, fitting, repair and renewal of a prosthesis or surgical appliance, and (v) the surcharge on late payment of compensation.

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