Baker McKenzie.

Hong Kong Employment Law Update

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Case Reviews

Amendment to employment contract void due to lack of consideration

Wu Kit Man v Dragonway Group Holdings Limited 02/06/2017, HCLA15/2016

In brief

The Court of First Instance (**Court**) held that an addendum amending an employee's contract of employment by requiring the employer to pay the employee a bonus of HKD 350,000, was void as the addendum was only beneficial to the employee and the employee had not provided sufficient consideration for the addendum to be binding.

Background and decision

Wu Kit Man (**Wu**) was hired by Dragonway Group Holdings Limited (**Dragonway**) in May 2015 to assist with preparing Dragonway for listing on the Hong Kong Stock Exchange. In October 2015, the parties signed an addendum stating that:

"If the Company or its holding company ceased the listing plan or you leave the Company for whatever reason before 31 December 2016, a cash bonus of HKD 350,000 will be offered to you within 10 days after the cessation or termination and in any event no later than 31 December 2016."

Wu left Dragonway on 21 December 2015 and had successfully argued at the Labour Tribunal that the addendum was valid and binding and she was entitled to the cash bonus of HKD 350,000. Dragonway appealed on the following three grounds:

- the Labour Tribunal had failed to consider the underlined part of the bonus clause which required the bonus to be paid "in any event no later than 31 December 2016" and therefore Wu's claim had been submitted prematurely. This ground was rejected by the Court, it was clear the phrase "in any event no later than 31 December 2016" was intended to ensure that even if Wu left less than 10 days before 31 December 2016, she would still receive her bonus no later than 31 December 2016. The relevant time limit for the bonus was 10 days, not 31 December 2016;

- Wu had not disclosed her previous criminal record before accepting Dragonway's offer of employment, and due to this misrepresentation, her employment contract and the addendum were void. This ground was rejected by the Court. The Court reiterated that under common law, employees are under no obligation to disclose a criminal record; and

- the addendum lacked consideration and therefore was not a valid contract. This ground was accepted by the Court.

Lack of consideration

The Court stated that if any amendment to a contract only benefits one party, the amendment would be invalid due to lack of consideration. The Court held that the addendum which granted Wu the right to receive the bonus did not require Wu to fulfil any further conditions to receive the bonus, it only required her to continue to carry out her existing role which was to assist with preparing Dragonway for listing. On that basis, the addendum lacked consideration and was invalid. The Court ordered Wu to repay the cash bonus of HKD 350,000.

Takeaway points

- **Execute as a deed:** to avoid any dispute over consideration, any amendments to an employment contract should be executed as a deed, as a deed does not need consideration to be binding on the parties.

- **Need consideration from both parties:** employers are often concerned with ensuring they are providing appropriate consideration to the employee so that a contract is valid. This case reminds employers to be equally aware of whether the contract benefits the employer as well as the employee, e.g. is the employee is taking on more responsibilities etc.? If in doubt, use a deed as explained above.

- **No common law duty to disclose criminal records:** if you want to ensure prospective employees disclose any criminal records, you must ask the employee directly as there is no common law duty to disclose such records, or you must include disclosure of any criminal record as a condition in the employment contract.

Civil servant successful in claiming benefits for same-sex spouse

Leung Chun Kwong v. Secretary for the Civil Service and another 28/04/2017 HCAL 258/2015

In brief

A male civil servant was successful in overturning the Secretary for Civil Service's decision not to award spousal benefits to his husband, even though same-sex marriage is not recognised in Hong Kong.

Background and decision

Mr Leung was employed as an immigration officer by the Government, with his employment contract being subject to the Civil Service Regulations (**CSRs**). Mr Leung married his partner, Mr Adams, in New Zealand in 2014.

Under the CSRs, Mr Leung and his "family" are entitled to certain welfare benefits, including medical and dental care, provided by the Government. The definition of "family" in the CSRs referred to "the officer's spouse". After getting married in New Zealand, Mr Leung applied to the Civil Service Bureau to change his marital status and obtain these welfare benefits for Mr Adams. The Secretary for the Civil Service (**Secretary**) did not recognise the change of status and denied the benefits to Mr Adams, stating that same-sex marriage fell outside the meaning of "marriage" under the CSRs. The Secretary claimed that, under the CSRs, "marriage" should be taken to mean

“marriage” as set out in section 40 of the Marriage Ordinance, “a formal ceremony recognised by the law as involving the voluntary union of life of one man and one woman”.

Separately, Mr Leung applied to have his income jointly assessed with Mr Adams as a married couple for tax purposes. The Commissioner of Inland Revenue rejected his application, stating that same-sex marriage was not regarded as a valid marriage for the purposes of the Inland Revenue Ordinance.

Mr Leung applied for judicial review of both decisions, arguing they were discriminatory against him based on his sexual orientation and in breach of his right to equality under (i) Article 25 of the Basic Law (ii) Article 1(2) and 22 of Hong Kong Bill of Rights and (iii) common law. Article 25 of the Basic law states that all Hong Kong residents shall be equal before the law. Article 1(2) and 22 of the Hong Kong Bill of Rights prohibit discrimination of any kind but binds government and public authorities only. The cases were heard together by the same judge.

Benefits decision

The Court of First Instance (**Court**) held that the Secretary's decision on benefits amounted to unlawful discrimination. The Court noted that Hong Kong law does not recognise same-sex marriage, that Mr Leung could not enter into a heterosexual marriage given his sexual orientation and that the difference in treatment accorded to the him was therefore based, at least indirectly, on his sexual orientation. The Court held that there was no sufficient justification for the differential treatment of the applicant as there was nothing illegal or unlawful in granting the same spousal benefits to, and indirectly recognising, an overseas same-sex married couple. The denial of spousal benefits to homosexual couples who were legally married under foreign laws would not undermine the integrity of the institution of marriage in Hong Kong or protection of the institution of the traditional family. It is important to note that it appears from the judgment that the CSRs did not explicitly incorporate the definition of marriage found in the Marriage Ordinance, and the definition of "family" in the CSRs referred only to "spouse". As a result, the Secretary was not entitled to rely on the statutory definition of "marriage" in the Marriage Ordinance to withhold benefits.

Tax decision

The Court found that the tax decision was lawful, as the definition of “marriage” included in the Inland Revenue Ordinance, which governs the assessment of income for tax purposes, could not be construed to cover same-sex marriages, as it refers to a spouse as being "a husband or wife".

Distinction between decisions

The discrepancy in the decisions is based on the interpretation of the underlying documents in both cases. It appears that the Court's reasoning in the benefits decision was based on the fact that the CSRs only referred to "spouse" which could therefore be more widely interpreted to include same sex spouses. The CSRs did not explicitly incorporate the Marriage Ordinance's definition of "marriage" (which is between a man and a woman only). Therefore the Secretary's decision not to award the benefits could not be based on the statutory definition of "marriage" in the Marriage Ordinance. It was instead based on the fact that the marriage was a same-sex marriage,

and this was differential treatment based on sexual orientation which was unlawful.

The tax decision was found to be lawful because any joint assessment for tax purposes must be made under the Inland Revenue Ordinance (this was explained in guidelines given employees). Therefore, the tax decision was correct as a matter of construction of statute, as the definition of "marriage" found in the Inland Revenue Ordinance does not include same-sex marriages. However this appears to be a narrow interpretation of the wording of the Inland Revenue Ordinance. The Inland Revenue Ordinance defines "marriage" as "any marriage recognised by the law of Hong Kong or any marriage whether or not recognised, entered into outside Hong Kong according to the law of the place where it was entered into and between persons having capacity to do so…". "Spouse" is defined to mean "a husband or wife". Neither of these definitions restrict the concept of marriage to being just between a husband and wife.

The Secretary is appealing the Court's decision. Over 27,000 individuals, 80 civil groups and five lawmakers signed a petition urging the Secretary to appeal the decision, arguing the ruling could have a profound impact on other housing and welfare policies.

Takeaway points

- **Protection against discrimination even without specific legislation:** the case shows that even without specific legislation to prohibit discrimination due to sexual orientation, employees can be protected under the Basic Law and the Hong Kong Bill of Rights which include high level, overarching protection against discrimination generally. It begs the question, could this legislation be used by employees to protect against other discrimination not currently protected by legislation in Hong Kong, such as age or religion?

- **Potential for further same-sex spouse claims:** it is possible that more same-sex couples will bring similar claims in both the public and private sector. These claims may be more successful in the public sector as claimants will be able to rely on the provisions set out in Hong Kong Bill of Rights (which explicitly binds government and public authorities only) as well as the Basic Law. It will also depend on the wording included in the underlying benefits documentation, but employers should not assume that terms such as "spouse" or "family" are restricted to heterosexual couples only.

- **Increased recognition of LGBT rights:** the case may mark the beginning of a shift towards greater protection for LGBT rights and could increase the chance of specific LGBT legislation being introduced.

Recent UK decision on legal privilege may have consequences in Hong Kong

SFO v ENRC [2017] WLR(D) 317

In a recent UK case, the Serious Fraud Office (**SFO**) obtained a declaration that certain documents prepared during investigations by solicitors and forensic accountants into the activities of a UK-incorporated multinational corporation (the **Company**) were not subject to legal professional privilege

vis-à-vis the regulator. The English court in *SFO v ENRC* ruled that the Company must hand over to the SFO, among other things, notes of interviews with employees. The impact of this UK decision may have consequences for Hong Kong employers, as confidential documents that must now be disclosed in the UK could potentially be available to regulators in other jurisdictions. For a full discussion of the potential implications for Hong Kong see our full alert here.

First company director sentenced to imprisonment after defaulting on MPF contributions

On 10 July 2017 a company director was sentenced to 21 days' imprisonment for failing to comply with a court order to pay outstanding Mandatory Provident Fund (**MPF**) contributions and surcharges. The Mandatory Provident Fund Schemes Authority brought civil claims against the employing company to recover outstanding MPF contributions and surcharges of around HKD 380,000. Although partial payment was subsequently made, a large part of the outstanding contributions remained unpaid and the employer pleaded guilty in June 2017

Under the Mandatory Provident Fund Schemes Ordinance (the **MPFSO**), any employer who, without reasonable excuse, fails to make a timely payment of mandatory contributions commits an offence and can be fined up to HKD 450,000 and face up to four years' imprisonment. It is also an offence if an employer fails, without a reasonable excuse, to comply with a court order to pay outstanding MPF contributions and surcharges. Employers can be fined up to HKD 350,000 and face up to three years' imprisonment. When the employer is a company, then any officer (i.e., director or manager) may also be liable if that person knew or ought to have known about the breach.

Takeaway points

- **Director liability for MPF default:** although convictions for defaulting on MPF contributions and breaching the MPFSO do happen, this is the first case in which a company director has been sentenced to imprisonment. The case should serve as a reminder to employers that defaulting on MPF contributions can have serious consequences.

Expat employees may benefit from UK employment law protection

Green v SIG Trading Ltd UKEAT/0282/16/DA

In brief

The UK Employment Appeals Tribunal (**EAT**) has found that an employee working in a foreign country but employed by a UK company, may benefit from UK employment law protection if the employment contract is explicitly stated to be governed by English law.

Background and decision

Mr Green was employed as a Managing Director of a UK company, SIG Trading Ltd (**SIG**), and was responsible for managing SIG's business in Saudi Arabia. He had lived in the Middle East for many years and had no home in the UK. Mr Green reported to a manager in UK, was employed under a UK

contract which included references to UK employment law protections, and was paid in British pounds.

SIG decided to close its business in Saudi Arabia resulting in Mr Green being made redundant. He subsequently brought a claim for unfair dismissal under the UK's Employment Rights Act. In the first instance, the Employment Tribunal (**ET**) concluded that Mr Green was an expat employee who had a stronger connection to Saudi Arabia than the UK and therefore the ET had no jurisdiction to hear the claim. Mr Green appealed.

The EAT allowed the appeal, basing its decision primarily on the fact the employment contract was expressly stated to be subject to English law. The ET had disregarded this relevant factor, based on SIG's argument that the employment contract was governed by English law for convenience (as SIG did not have a standard form employment contract for Saudi Arabia). The EAT held that the governing law the parties had agreed to be bound by was a material factor and could not be dismissed based on SIG's subjective explanation. The EAT held that the ET's judgment was "unsafe" and the case should be remitted to the ET for reconsideration.

Hong Kong case law

This case should be read in context with the two major Hong Kong decisions which considered whether expat employees should be subject to English or Hong Kong law. *HSBC Bank Plc v Wallace [2007]* involved an employee, Mr Wallace, who had been seconded from the UK to HSBC in Hong Kong for several years. Following a dispute between the parties, the Hong Kong Court of First Instance held that Mr Wallace's employment contract was subject to English law, primarily because Mr Wallace's employment contract expressly stated it was governed by English law.

Cantor Fitzgerald Europe v Jason Jon Boyer & Others [2012] involved several employees who had been seconded from UK to work for the Hong Kong branch of Cantor Fitzgerald, an investment bank. Their employment contracts included governing law clauses which stated English law applied "save for any mandatory employment laws of Hong Kong". The Court held that certain sections of the Employment Ordinance were overriding and grant protection to employees even if their employment contracts were governed by foreign law. The judge in Cantor Fitzgerald disagreed with the reasoning in the HSBC case that a foreign law clause could override the Employment Ordinance.

Takeaway points

- **Governing law clause is important:** the case confirms that the governing law clause is an important factor when deciding which law employees will be subject to. Employers should take care to ensure the clause reflects the intention of the parties, however even if a Hong Kong employee has a foreign governing law clause, this does not necessarily stop the employee being able to claim Hong Kong employment law protection.

- **Expat employees may be entitled to dual protection:** employees working overseas with English governing law clauses may be more likely to initiate proceedings in the UK courts as this case suggests they may benefit from UK employment law protection regardless of their location. However, Hong Kong case law demonstrates that expat employees are

likely to also benefit from certain mandatory provisions in the Employment Ordinance, even if their contracts are governed by foreign law, meaning expat employees from the UK may enjoy dual protection. Employers should carefully draft their employment or secondment agreements to avoid employees getting the best of both worlds.

Company director fined for default on Labour Tribunal award

On 25 July 2017 a company director was prosecuted by the Labour Department for defaulting on sums awarded to employees by the Labour Tribunal under the Employment Ordinance. The company had failed to pay the awarded sums of HKD 130,000 within 14 days after the payment date specified in the Labour Tribunal award under the Employment Ordinance. The director was subsequently convicted for his consent, connivance or neglect in the above offences, fined HKD 60,000 and ordered to pay the outstanding amount of HKD 130,000 in total to two employees that day (25 July 2017).

Under the Employment Ordinance, if the Labour Tribunal requires the employer to pay any specified amount (such as wages, end of year payment, maternity leave pay and severance payment, etc.) and the employer wilfully and without reasonable excuse fails to do so within 14 days, the employer is liable to a fine of up to HKD 350,000 and imprisonment for three years. Where this offence is committed by a corporate body, with the consent, connivance or neglect of any director, manager, secretary or other similar officer that person may be convicted as well.

Takeaway points

- **Labour Tribunal awards must be paid on time:** the decision sends a message to employers, including individual directors, that they must pay sums due to employees within the timeframe set by the Labour Tribunal.

UK case limits the "blue pencilling" test

Tillman v Egon Zehnder Ltd [2017] EWCA Civ 1054

In brief

In the recent UK case of *Tillman v Egon Zehnder Ltd [2017]*, the Court of Appeal held that (1) a restrictive covenant preventing an employee from being "interested in" a competing business prevented the employee from holding even a minor shareholding in a competing business, and was therefore unreasonably wide and unenforceable; and (2) the words "interested in" could not be "severed" (e.g. removed) from the restrictive covenant to allow the balance of the covenant to be enforceable. This decision may have implications for employers in Hong Kong who use restrictive covenants, as the Hong Kong courts have traditionally applied UK case law to assess covenant enforceability.

Background and decision

The employee, Ms Tillman, was Co-Head of the Financial Services Group for Egon Zehnder, a headhunting firm based in the UK. In January 2017, Ms Tillman resigned, hoping to start work for a competitor firm.

Her contract of employment contained the following six month non-compete:

> "13.2 You shall not without the prior written consent of the Company directly or indirectly, either alone or jointly with or on behalf of any third party and whether as principal, manager, employee, contractor, consultant, agent or otherwise howsoever at any time within the period of six months from the Termination Date:
>
> …
>
> 13.2.3 directly or indirectly engage or be concerned or interested in any business carried on in competition with any of the businesses of the Company or any Group Company which were carried on at the Termination Date or during such period."

The question arose as to whether the above restriction prevented Ms Tillman from starting work with her new firm for six months after termination.

High Court

Ms Tillman argued that the restriction was an unreasonable restraint of trade because the words "interested in" prevented her from becoming even a minor shareholder in a competitor, which was unnecessary for the protection of the Company's interests after termination and made the restrictive covenant unreasonably wide.

The High Court found in favour of the employer. It held that the non-compete was not intended to deal with shareholdings as it did not expressly refer to them. The fact there was another clause in the contract which expressly dealt with shareholdings during employment supported this view. The High Court held that it was right to favour a construction which validated rather than invalidated the clause. Accordingly, the covenant was upheld and an injunction was granted against Ms Tillman, preventing her from starting work at the competitor for six months. Ms Tillman appealed the decision.

Court of Appeal

The Court of Appeal overturned the High Court's decision. The Court of Appeal held that it was established in case law, dictionaries and every day language that "interested in" could refer to a person holding shares in a company. The fact that the covenant did not expressly refer to shareholdings, and another clause in the contract did, was not important. The Court of Appeal then considered whether the words "interested in" could be severed from the clause to render it enforceable. It held that parts of a single covenant cannot be severed, and that severance can only take place where there are separate covenants. The Court of Appeal set out the three part test, established in case law, that must be fulfilled for severance to apply:

(1) the unenforceable provision must be capable of being removed without the necessity of adding to or modifying the wording of what remains;

(2) the remaining terms must continue to be supported by adequate consideration; and

(3) the removal of the unenforceable provision must not so change the character of the contract that it becomes "not the sort of contract that the parties entered into at all".

The Court of Appeal held that any severance or "blue pencilling" which removes part of a covenant to render it enforceable, would be to change the character of the contract.

Hong Kong impact

The Hong Kong courts follow the same three part test set out above when considering restrictive covenant severance. Hong Kong case law, like the prior UK case law, supports the idea that where a discrete phrase within a particular covenant is held to be unreasonable, individual words or phrases may be severed, provided that what is left is enforceable without the need to modify the wording and the intention of the contract is not changed.

Takeaway points

- **Blue pencil test no longer applies:** previous case law had led to the expansion of "blue pencilling" i.e. removing certain words or sentences to allow the covenant to be enforceable. The decision in *Tillman v Egon Zehnder Ltd [2017]* casts doubt over whether the practice will continue in the UK. It remains to be seen whether Hong Kong courts will follow in the same direction.

- **Careful restrictive covenant drafting:** restrictive covenants which are not carefully tailored to the circumstances may be deemed too wide and therefore unenforceable. Employers should revisit the wording of covenants in their contracts to ensure they are not too widely drafted and, if possible, are structured to allow for severance if necessary.

Legislative Developments

Proposed Employment (Amendment) Bill 2017 gives employees right to reinstatement

On 5 May 2017 the Government gazetted the Employment (Amendment) Bill 2017 (**Bill**) and on 17 May 2017 it was introduced to the Legislative Council. The Bill, if approved, would allow the Labour Tribunal to make an order for reinstatement or re-engagement of an employee who has been unreasonably and unlawfully dismissed without the need to first secure the employer's agreement. The Tribunal must consider the order to be reasonably practicable and secure employee consent only.

The maximum sum an employer will have to pay for failing to reinstate or re-engage an employee is HKD 72,500. This amount will be additional to the monetary remedies payable to the employee as ordered by the Labour Tribunal under the Employment Ordinance.

Currently, employees can seek a court order for reinstatement or re-engagement of their employment if they have been unlawfully and unreasonably dismissed but the Tribunal will only make such an order if the employer and the employee agree to it. The option as it stands is rarely used in employment disputes as usually the employment relationship has broken down to a point where it is unworkable to reinstate or re-engage the employee. It remains to be seen whether the option would be used more

frequently if the Bill comes into force in its current form. There is a risk that it would be used by employees in exit negotiations to demand higher termination packages.

The Bill is largely the same as the Employment (Amendment) Bill 2016 that was introduced into the Legislative Council in March 2016 which lapsed at the end of the 2012-16 Legislative Council term, except that the maximum penalty an employer must pay has been increased from HKD 50,000 to HKD 72,500.

Government proposes working hours protection for those earning HKD 11,000 or less

On 13 June 2017 Hong Kong's Executive Council passed proposals to regulate working hours for employees who earn HKD 11,000 or less a month. This follows the Standard Working Hours Committee's report to Government in January 2017, which recommended that legislation regulating standard working hours be introduced for low-income employees. For these low-income employees, it will be mandatory for employers to pay them overtime wages at rates no less than their regular wages, with written contracts stating the standard working hours. The employer and employee would decide an acceptable number of standard working hours. Some 550,000 workers stand to benefit from the new legislation. The decision has drawn criticism from trade union bodies who argue most employees in Hong Kong will not be covered. The Government has proposed that an amendment bill will be presented to the Legislative Council by the second half of 2018 and implemented by the end of 2020 or early 2021.

Government's MPF offset abolishment proposals approved by Executive Council

On 23 June 2017, Hong Kong's Executive Council approved the Government's proposal to progressively abolish the Mandatory Provident Fund offset mechanism for severance payments and long service payments. Click here see our full alert on the matter.

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