

## Is this clawback clause in the employment contract effective?

### Description

I was asked a few days ago by an expat working in Shanghai in regard of his difficult situation:

he was relocated from United States to Shanghai two years ago; upon relocation, he signed an expat arrangement agreement with the parent company in which he agreed to work for the China subsidiary for up to three years; he was offered with good package of benefits including housing allowance, kid education tuition and a car for his daily life use; he signed a very simple contract with the Shanghai entity in order to obtain the work permit; in the middle of the last year, after no positive response from the parent company for renewing the employment, he resigned from his position.

To his surprise, his superior was angered by his resignation, and further the boss quoted a clause in the contract with the parent company to the effect that the employee shall return all costs of working in China if the employee voluntarily resigns prior to the expiry of the employment term.

Further, there are no clauses in the labor contract with the Shanghai entity relating to those benefits at all though the Shanghai company had been paying these benefits all the time.

This is a typical arrangement for expats who serve high-ranking positions in their Chinese operations. The dispute will often cause serious grievance on the employee as they have much more than their job to take care of, since they need to take care of their family that come with him or her into China.

Now can the employer succeed in taking back those benefits offered to the employee in the past by instituting legal proceeding *in China*?

#### 1. Applicable Laws

First of all, as always in the case of a foreign-related dispute, the first thing that shall be determined is the applicable law. In this case, the Chinese labor related laws shall only be applicable in cases where the employment relationship is created in China. In Article 2 of China Labor Contract Law, it is provided that this Law applies to employment relationship created between employers within the territories of China and their employees. In other words, employment contract signed between a foreign company (incorporated in foreign jurisdictions) and an employee working in China falls out of the ambit of China Labor Contract Law and related labor rules. But the labor contract signed by the employee with the Shanghai entity shall be governed by China labor laws.

#### 2. Benefits being Part of the Labor Contract with Shanghai Entity

Though the benefits are not stipulated in the labor contract with the Shanghai company, since the Shanghai company has been paying such benefits, it shall be deemed at law that the parties, the Shanghai company and the expat employee, have agreed by conducts on the terms regarding the benefits. In other words, courts will read relevant terms into the labor contract with the Shanghai company.

Though this interpretation favors the employees, I would definitely suggest that expat employees shall insist that all benefits and welfare offered by companies shall be stipulated clearly in the contract with the local company, so in the case of dispute, employees will be better protected with clear agreements on the issue in dispute.

### 3. Benefits Paid in the Past not Refundable

First of all, the clawback clause did not appear in the labor contract with the Shanghai entity. It is groundless for the Shanghai company to ask the expat employee to refund those benefits.

Assuming that there is such a clawback clause of taking back the benefits offered to expat employee in the labor contract with the Shanghai company, would this kind of clause be upheld in Chinese laws? The answer is quite clear: NO.

Such clawback clause in essence is a liquidated damages clause. But the Chinese Labor Contract Law has made it clear that there are only two occasions where liquidated damages clause is allowed to be stipulated against the employees: (1) breach of non-competition obligation; (2) breach of service period after receiving professional and technical training. In other words, other liquidated damages clauses to the detriment of employees are not allowed and therefore null and void.

While this is the case, it is worth a note that Shanghai High People Court has indicated in its own interpretation of the China Labor Contract Law that benefits that are prepaid to employees as part consideration for employee's commitment on service term can be taken back in proportion in light of the unperformed period. Such local interpretation is often observed by local courts in Shanghai.

All in all, in consideration of the possible [employment dilemmas](#) that may confront expat employees working in China, it is important that expats that are coming to China for employment shall be careful in negotiating terms with their employers before setting their feet on Chinese soil. Professional legal advice on employment issues such as severance pay, overtime pay, income taxes shall be sought to protect your interests relating to the employment in China.

However, expats that have relevant arrangement agreements with parent companies outside China shall seek local legal advice back in the jurisdiction where the parent company is located in relation to whether the parent companies will be able to get an upper hand in the said jurisdictions.

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#### **Author**

admin