

Landmark labor case: Scope of ordinary wages

On December 18, 2013, the Supreme Court of Korea held that the ordinary wages of employees of KB Auto Tech include fixed bonuses regularly paid. The decision impacts all employers in Korea, as ordinary wages are used to calculate overtime and compensation for unused annual leave, which may in turn impact severance pay. The following is a summary of the relevant issues.

Scope of ordinary wage prior to the decision

In Korea, an employer generally provides four types of payments to its employees for their services: base salary, overtime, bonus (fixed or variable), and other allowances (e.g., meal allowances etc.).

Prior to the Supreme Court's decision, the Ministry of Labor had released guidelines which recognized base salary and certain fixed allowances paid monthly as being included in ordinary wages. Pursuant to such guidelines, in calculating overtime payment based on ordinary wages, many companies excluded fixed bonuses which were paid every two months, quarterly or bi-annually. Contrary to the guidelines however, the lower courts in a few cases had held fixed bonus, whether paid monthly or not, should be included in ordinary wages if such bonus is paid regularly to all employees.

Scope of ordinary wage clearly defined after the decision

According to the Court's decision, all fixed payments that are provided to all employees on a regular basis (regardless of regularity) must be included when calculating ordinary wages. As a result, any fixed payments regularly made to employees, such as fixed bonuses and meal allowances, must now be included in ordinary wages.

The Court excluded bonuses that are conditional on being employed at the time of payment, and certain seasonal payments (e.g., summer vacation pay) and welfare benefits based on the reason that

those payments and benefits were not necessarily available to all employees on a regular/pro-rata basis.

The Court also ruled that any collective bargaining agreement or labor-management agreement that attempts to exclude regular payments from ordinary wage are void for being in violation of the mandatory provisions of Korean law.

However, the Court expressly noted that if an employer is able to prove that there is an agreement between the employer and the labor union stipulating that the fixed bonus is excluded from ordinary wages, and that paying employees for the past will cause a substantial detriment to management or major threat to the existence of the company due to the unexpected financial burden as a result of having to pay employees, employees' claim for underpayments can be denied based on principles of good faith. Unfortunately, the Court did not provide any further guidance as to what would constitute "substantial detriment or major threat".

Implications

Employers will need to ensure that ordinary wages are accurately calculated and that payments for overtime and severance payments are adequately paid. Importantly, employers are exposed to potential claims in relation to overtime and compensation for annual leave not having been calculated accurately and paid in previous years. Employees could also claim that any severance that was paid was too low. Relevantly, under the statute of limitations an employee can only make a claim with respect to the three years immediately preceding his/her claim.

In principle, employers are responsible to make good any underpayments. However, the Court's limited exception based on principles of good faith noted above is likely to be the source of ongoing debate.

Aftermath

In light of the Court's decision, potential claims from employees are in theory huge in terms of amount and number of claims. Employers should expect tough negotiations with its employees and their respective labor unions as the employees will feel empowered by the Court's decision. We recommend that employers thoroughly review their pay schemes, internal rules and regulations, employment agreements and labor-management agreements to accurately budget for the maximum liability the company faces for the previous three years and also the likely increase in ordinary wages for all employees and its collorary implications.

We are happy to discuss various means to limit exposure to the possible liabilities employers face as a result of the decision.

Should you have any questions regarding any of the foregoing, please feel free to contact us at any time.

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