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Employment-Context Choice-of-Law Clauses

Challenge:

Multinationals often insert choice-of-law clauses (usually calling for home-country law) into cross-border employment agreements. But more often than not these clauses backfire, forcing the employer to comply with the extra rules of an additional legal regime.

In our last *Global HR Hot Topic* (August), on "Whose Laws Reach Border-Crossing Employees?," we discussed the general rule that employment protection laws of the place of employment apply even notwithstanding a choice-of-law clause by which parties to an employment (or employee compensation) agreement purport to select the law of some foreign jurisdiction with a nexus to the employment. When a border-crossing employee selects the law of some jurisdiction outside the host country—even a jurisdiction with a genuine nexus to the employment—the selection is usually powerless to block host-country "mandatory rules." And in the employment context, host-country "mandatory rules" include most regulation of the workplace, such as for example laws relating to: pay rate, overtime, payroll, mandatory benefits, hours, rest periods, vacation/holidays, health/safety, labor unions/collective representation, discrimination/harassment/"moral" abuse, employee-versus-contractor classification, restrictive covenant/non-compete/trade secret rules and dismissals—firing procedure, notice, severance pay and releases.

The problem with an employment-context choice-of-law clause is that it implicates tougher employment laws of the selected jurisdiction without blocking the mandatory application of tougher employment protection laws ("mandatory rules") which apply by force of public policy in the *host* jurisdiction. Both sets of laws end up protecting the employee. The employee gets to "cherry pick" whichever rules offer better protections. The multinational employer now has to comply with two sets of employment protection laws, rather than just one. A choice-of-home-country-law clause can therefore backfire and *restrict* employer flexibility: The employee gets the best of both worlds while the employer suffers the worst of both worlds. Indeed, where a choice-of-law clause pulls in an additional set of employee protection laws that otherwise would not have reached the employee, the employer often ends up arguing later that the selected jurisdiction's law does not itself reach abroad *even notwithstanding* the choice-of-law clause (because the selected jurisdiction's law has no

Best Practices Tip:

Resist the urge to insert a choice-of-law clause into a cross-border employment agreement unless the clause simply calls for the law of the place of employment or unless special circumstances exist protecting the employer from the clause backfiring.

Each monthly issue of *Global HR Hot Topic* focuses on a specific challenge to globalizing HR and offers state-of-the-art ideas for ensuring best practices in international HR management and compliance. White & Case's International Labor and Employment Law practice helps multinationals globalize business operations, monitor employment law compliance across borders and resolve international labor and employment issues.

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extraterritorial reach, and the selected jurisdiction's domestic conflict-of-law rules call for the law of the host country, not the rules of the selected jurisdiction). *See, e.g., Gravquick A/S v. Trimble Nav. Int'l*, 323 F.3d 1219,1223 (9th Cir. 2003); *Wright v. Adventures Rolling Cross Country*, case no. C-12-0983 EMC., US D.C. N.D. Cal., Order of 5/3/12. The employer in effect has to impeach its own choice-of-law clause. *See, e.g., Wright, supra* (American employer argues clause in its own cross-border employment agreement saying "you are considered to be a California resident, subject to California's tax laws and regulations" is *not* a California choice-of-employment-law clause). Of course, in these situations, the employer should have omitted or narrowed the home-country choice-of-law clause in the first place.

Another drawback to choice-of-foreign-law clauses in employment agreements is that these provisions can needlessly complicate employment litigation, imposing significant additional costs. When disputes implicating choice-of-foreign-law clauses land in local employment tribunals, local judges inevitably wrestle with complex proof-of-foreign-law issues (often involving expensive expert testimony and translations) before coming to the usual conclusion that local employee protection laws apply anyway, by force of public policy. *See, e.g., Duarte v. Black and Decker,* [2007] EWHC 2720 (QB)(UK)(1/07); *Samengo-Turner v. Marsh & McLennan,* [2007] EWCA Civ. 723 (UK)(7/07).

But even given the drawbacks of choice-of-foreign-law clauses in employment arrangements, these clauses remain stubbornly common. Multinationals like them. Presumably, at least in some exceptional contexts, a choice-of-foreign-law clause in an expat arrangement might be a wise strategy. So let us examine five possibly exceptional situations often claimed to render a choice-of-foreign-law clause advantageous to an employer of border-crossing employees: (1) Europe's Rome I regulation; (2) Global Employment Companies and non-mandatory benefits; (3) restrictive covenants; (4) forum selection clauses; and (5) the "trick-the-expat" strategy.

1. **Europe's Rome I Regulation:** European Union member states are subject to a choice-of-law in contracts regime called the Rome I Regulation, which (per Rome I Regulation article 24) "replaces" the earlier 1980 Rome Convention. For some reason, many European employment lawyers persist in talking about the Rome regime (Rome I and its predecessor Rome Convention) as if it somehow lets expat choice-of-law clauses block the mandatory application of host-country employment law. A March 2005 article by German lawyers, for example, says the Rome regime leaves European workers "free to agree upon the law of the country that shall be applicable to the employment contract" and an October 2003 article by French lawyers characterizes the Rome regime as leaving "the parties to an employment contract…free to choose the governing law." Indeed, when the Rome I regulation replaced the predecessor Rome Convention, some European lawyers argued that Rome I more effectively empowers choice-of-law clauses to block the mandatory application of host-country employment protection laws.

   But this analysis is wrong. The texts of both the original 1980 Rome Convention and now the Rome I Regulation affirm our general rule that, in an employment or other contract, the "overriding mandatory provisions of the law of the forum" apply notwithstanding any choice-of-law clause. Rome I defines "overriding mandatory provisions" as laws "the respect for which is regarded as crucial by a country for safeguarding its public interests." Rome I Reg. at art. 9(2)(1); *cf.* art. 21 (choice-of-law clause cannot override any rule "manifestly incompatible" with "public policy" of "forum" court). The Rome I Regulation mandates that a choice-of-law clause in an employment agreement cannot "depriv[e] the employee of the protection afforded to him by provisions that cannot be derogated from by agreement under the law that, in the absence of choice, would have been applicable." Rome I art. 8(1). Rome I also declares that a choice-of-law clause cannot override the law of any "country" "more closely connected with" the "circumstances [of employment] as a whole." Rome I arts. 8(1), (4). These Rome I Regulation provisions merely restate firmly entrenched principles of the predecessor Rome Convention at its articles 3(3), 6, 7.

   In short, under the Rome regime, terminated expats in Europe—even Americans and other non-European expats (*see* Rome I Reg. art. 2)—lucky enough to have a choice-of-foreign-law clause in their agreements follow our usual rule: They get to select the law more favorable to them, either their selected (chosen) country *or* the law of the country "in which the employee habitually carries out his work" (Rome I Reg. art. 8(2))—or both. Labor courts in Europe decide cases consistent with this analysis all the time. For example, French appeals courts in Grenoble and Paris have overridden choice-of-law clauses calling for Texas and German law by invoking the Rome Convention to impose the French employment code on expats working in France.

2. **Global Employment Companies and non-mandatory benefits:** We have seen that host-country employee protection laws—laws relating to pay rate, overtime, payroll, mandatory benefits, hours, rest periods, vacation/holidays, health/safety, labor unions/collective representation, discrimination/harassment/"moral" abuse, employee-versus-contractor classification, restrictive covenant/non-compete/trade secret rules and dismissals (firing procedure, notice, severance pay, releases)—tend to be "mandatory rules" applicable by force

of local public policy. Parties cannot contract around or opt out of them. The other side of this coin is that an expat's contractual choice of foreign law might succeed in blocking host-country law if it is confined to those human resources laws that *steer clear* of employee protection statutes and "mandatory rules."

Indeed, parties to a cross-border employment relationship can effectively select home-country laws that govern *discretionary* human resources topics outside the realm of local "mandatory rules." In fact, this principle grounds "global employment companies"—so-called GECs, multinational entities set up to employ a corps of a multinational's career expatriates working worldwide—and this principle explains why choice-of-home-country-law clauses are common in international compensation and equity award agreements.

Yet only a small subset of employment laws is discretionary, steering clear of mandatory employment protections. The employment law topics most likely to be discretionary and susceptible to a choice-of-foreign-law clause tend to be equity plan rules, executive compensation doctrines, and some (but not all) regulation of non-mandatory benefits, like rules on voluntary pensions, certain tax and social security totalization treaties, and some (but not all) rules applicable to discretionary bonuses.

While selecting the law of a host or headquarters country can be vital in designing a GEC or a cross-border compensation or equity agreement for highly compensated expats, remember that this exception is limited to the discretionary employment law topics that steer clear of "mandatory rules." Even a choice-of-law clause confined to a high-ranking executive's bonus plan, equity award agreement or compensation arrangement will not divest host-country "mandatory rules." When multinationals get this wrong, they lose in court, *See, e.g., Duarte v. Black and Decker,* [2007] EWHC 2720 (QB)(UK)(1/07); *Samengo-Turner v. Marsh & McLennan,* [2007] EWCA Civ. 723 (UK)(7/07); *cf. Ruiz v. Affinity Logistics,* 667 F.3d 1318 (US 9th Cir. 2012). *Duarte* and *Samengo-Turner*, two landmark UK decisions, involved whether a US state choice-of-law clause (one case involved a New York law clause and the other a Maryland law clause) in executive compensation arrangements requires a UK court to defer to US state law in interpreting a *restrictive covenant* enforced in the UK. The facts in each case involved some twists, but at the end of the day, both UK courts predictably ruled that UK, not US state, public policy and "mandatory rules" control restrictive covenants enforced on UK soil—even where the employer packs the restrictive covenant into a complex compensation or equity award.

3. **Restrictive covenants:** The *Duarte* and *Samengo-Turner* cases highlight the special challenges of restrictive covenants (non-competes, non-solicits, confidentiality and employee inventions commitments) in cross-border employment. Laws that enforce restrictive covenants tend to be "mandatory rules" that apply by force of public policy, and so the restrictive-covenant-interpretation rules of a place of employment or forum court tend to apply by operation of law. For example, a California court is highly unlikely to respect a New York or English choice-of-law clause to enforce an employment-context non-compete against a defendant whose place of employment is California. With post-term restrictive covenants, the practical enforcement issue usually comes down to complying with the mandatory restrictive covenant rules and public policy of the *jurisdiction where the employer seeks enforcement*. This often ends up being the place where the employee goes off to breach the covenant, and may be neither the home nor the host country. *See* our *Global HR Hot Topic* of July 2012, "Non-Competes and Other Restrictive Covenants in the Cross-Border Context."
4. **Forum selection clauses:** We have been addressing choice-of-*law* clauses that invoke a *legal* regime other than that of the forum country. A separate but similar issue is choice-of-*forum* clauses that seek to require parties to litigate any disputes before some selected forum—arbitration or a foreign jurisdiction's courts. The challenge with employment-context forum selection clauses is that outside the US, special-jurisdiction labor courts tend to enjoy mandatory jurisdiction over employees who work locally (just as, within the US, special-jurisdiction workers' compensation agencies, unemployment compensation agencies, equal employment agencies and the NLRB tend to enjoy mandatory jurisdiction that choice-of-forum clauses cannot block). Outside the US, clauses in expat agreements and compensation/equity plans purporting to select some forum other than local host-country labor tribunals rarely block the jurisdiction of host-country labor judges—unless, perhaps, the parties sign a forum selection clause *after* a dispute arises, or unless the host country is one of a handful of jurisdictions, like Malaysia, with statutes authorizing employment arbitration. In London today, many American financial services expats may be working under arbitration clauses of dubious enforceability.
5. **The "trick the expat" strategy:** An expat consultant at a major HR consulting firm used to recommend inserting into Americans' expat assignment agreements a US choice-of-law and choice-of-forum clause, *even though* those clauses are extremely unlikely to block local host-country employee protection laws and labor court jurisdiction. His theory: Some American expats, particularly those posted into poor

countries, may be so innately skeptical of overseas justice that a choice-of-US-law (or forum) clause might dissuade at least less sophisticated American expats from asserting inalienable legal rights granted by their new host country. This consultant predicted that American expats might believe a US choice-of-law/forum law clause means what it says, that any dispute must be resolved under the employer-friendly regime of US employment-at-will. A choice-of-law clause might blind at least a less sophisticated expat to the fact that "mandatory rules" of the current place of employment grant unwaivable substantive and procedural rights better (for the expat) than what American law provides.

But these days, expats are increasingly sophisticated and increasingly likely to research their rights on the Internet. They are increasingly likely, therefore, to figure out that choice-of-law and choice-of-forum clauses in the cross-border employment context are largely powerless to block host-country "mandatory rights." Expats posted to rich countries are particularly likely to figure out that host-country law guarantees them employee-friendly labor rights.

This said, though, in some cases a home-country law or forum selection clause is said somehow to act as an acknowledgment between an expat and an employer that their mutual intent, even if non-binding, is to resolve disputes under home-country rules. Some expatriates might accept that—even if the law does not force them to.

Conclusion

One question comes up time after time in administering international human resources: *Whose laws reach border-crossing employees?* The general rule is that because employee protection laws are "mandatory rules" applicable by force of public policy, host-country employment law—the law of the current place of employment—tends to apply by operation of law. In addition—but not instead—home-country laws sometimes *also* apply, such as where a home-country statute has "extraterritorial reach" or where the parties contractually selected their home-country law. While the law of the current place of employment tends to apply regardless of most other factors, the issues here are nuanced, particularly when the parties signed a choice-of-foreign-law clause.

Analyze border-crossing choice-of-law questions in the employment context strategically. Never *over*estimate the power of an employment-context choice-of-law clause.