

Labor Issue related to Branch Manager's Severance Pay (Less Paid; Not including Incentive in Average Wage)

Bongsoo Jung, Korean labor law at KangNam Labor Law Firm

I. Case Summary

Company B is a Korean branch of a newspaper sector company whose head office is located in a foreign country. The company was divided into four business entities in 2002 for the purpose of efficient accounting management. Each entity operates independently in different locations. The business entities are classified as: 1) Report Team, 2) Digital News, 3) Newspaper Distribution, and 4) Advertisement. The business head of each entity was appointed to the representative of respective entity. The Petitioner (hereinafter referred to as "Employee") joined Company B as a sales manager in September 2000 and worked as a branch manager of the Advertisement business entity starting 2002 until he quit in July 2007. The Employee was the representative director of the entity which maintained only two other employees, a number that was too small to be applicable to severance pay under the Labor Standards Act. Although the company granted a legal severance pay to the Employee in consideration of his contributions during his tenure, the amount did not meet the accumulation rate (1.5 times) of severance pay verbally promised to the Employee at the time of his hiring.

The company also failed to reflect individual sales incentive bonus in its calculation of average wages for severance pay. When the Employee appealed to the company for a re-calculation of his severance pay, the company refused to accept his demand. Hence, the Employee submitted the application for delayed payment of severance pay to the Ministry of Labor via the labor attorney in August 2007.

II. Company B's Claim

1. Company B (hereinafter referred to as "Company") is not liable for severance pay because it hires only two employees and does not submit to any rules or agreement stipulated for the payment of severance pay in the Rules of Employment, labor contract or verbal contract. As already conveyed to the branch manager (the Employee), the Company intends to pay the amount of severance pay calculated by multiplying the average wages to the number of service years

during the time of his resignation. This amount will factor in his contributions made to the company during his tenure. Provided, however, that all legal liability shall expire between the Company and the Employee in accordance with payment of severance pay.

2. The incentive bonus requested by the Employee is not wage to be included in average wages under the Labor Standards Act. Even if the bonus was assumed to be included in average wages, the incentive bonus requested by the Employee was paid in March 2007 in remuneration for labor service in 2006. The requested bonus cannot be included into average wages, because it was not paid in return for labor service for the last three months prior to the Employee's retirement date in July 2007.

III. Employee's Claim

1. The Employee was hired as a sales manager of Company B on September 1, 2000, and had maintained office continued to work until he quit on July 31, 2007. The wages are comprised of basic monthly basic pay and the annual incentive bonus. The basic monthly basic pay was paid once every month, and the incentive bonus of a similar amount was given every March for the last 7 years based upon the payment criteria of the incentive bonus contracted previously by sales result. When the Employee resigned from the Company, his severance pay did not calculate the individual sales incentive bonus into the average wages and failed to reflect the accumulation rate (1.5) of consecutive service year.
2. There were 16 employees in Company B when the Employee was hired, and the Company has maintained the similar number of employees so far. The Company was divided into four business entities in 2002 for the purpose of better accounting management. Each business was established as independent entities: 1) Report Team, 2) Digital News, 3) Newspaper Distribution, and 4) Advertisement (2 persons). The business head of each entity was appointed to the representative of each entity. However, practically, the above two entities of the Newspaper Distribution business and Advertisement business had been operating in the same building until recently and the above four entities have been managed by a single accounting team. The president of the foreign head office has directly directed, ordered and supervised four business entities, and the Human Resources management has been controlled under an Asia regional head office in

000 country. Even though the president of the company worked in the workplace of less than 5 employees, he was pursuant to the definition of an employee under the Labor Standards Act.

3. During the hiring stage, Company B verbally promised Employee an accumulation rate (1.5 times) of severance pay. Two former employees were granted with their adjusted severance pay upon retirement. Without employees' consent, however, the Company decided to abolish the application of an accumulated rate into severance pay. This new adjustment should be made null and the Company shall pay the Employee his severance pay with the accumulated rate.
4. The Employee received an additional 120 million won as incentive bonus in March 2007 as a result of his good sales from the previous year. The Company did not reflect individual sales incentive bonus to the calculation of average wages for his severance pay, insisting that the incentive bonus is not applicable to average wages. However, as the incentive bonus reflects individual sales performance, not the corporate business performance, the Employee's individual sales incentive bonus shall also be included into the calculation of his average wages.

IV. Related Administrative Interpretations and Judicial Ruling

1. In case where there are different entities per business under one company (Administrative interpretation: Retirement benefit team 4126, Oct 11, 2007):
 - ➔ In case where an identical employer operates more than one business or workplaces at different locations, if the branch offices, sales offices and unit plants are operated under an identical organization and management without independent operations, the related entities are regarded as one business or one workplace. This means that the total number of employees at all entities shall be counted together in pursuant to the labor laws. However, if each entity maintains different structures and operates independently in terms of business location, accounting and human resources management, each entity shall be considered as independent business or workplace. Accordingly, whether severance pay is applicable or not shall be considered according to the specifics.

2. In case where the company unilaterally revises accumulated rate of severance pay to non-accumulated rate (Administrative interpretation: same as the above):

➔ Even though there had been no mention of severance pay stipulated in the contents of the labor contract (no existence of the Rules of Employment), the Company had promised the Employee a severance pay with accumulated rate of service years and had applied the system for a considerable period to its former employees. In this case, the Company shall take measures to receive employees' consent in order to revise the content, especially in the case of unfavorable revision to its employees.

3. Administrative guides and judicial rulings in relation to sales incentive bonus

○ **Bonus part in the Calculation Rules of Ordinary Wages**

(Article 476 of Regulation of the Ministry of Labor, January 22, 2002)

< In case bonus is wage >

In case where payment conditions, amounts, and payment rate are regulated in the Rules of Employment, or where employees are paid routinely and expected to get paid: regular bonus, exercise support fee, etc.

< In case bonus is not wage >

In case where payment is not paid routinely, but paid temporarily or conditionally in accordance with the company's profit by means of the employer's discretion and favor: Business incentive bonus, special incentive bonus, production incentive bonus, rewards, and incentive

○ **Individual sales incentive bonus that has been paid regularly and periodically shall be included to average wages. (Seoul District Court, June 21, 2007, 2006 na 20978)**

"The Company's salary system consists of basic annual salary and incentive annual salary. The basic annual salary is paid monthly, and the incentive annual salary is paid in January as a lump sum payment based upon the valuation of sales target and outcome for the corresponding year. The Company pays a severance pay that reflects basic annual salary without including incentive annual salary. Insisting that the Company should include incentive annual salary into the calculation of average wages because incentive annual salary belongs to wage, the Employee has requested a re-calculation of his severance pay to the Company. When his application was rejected, he filed the suit against the Company."

➔ "Whether the items of the pay may be identified as wages reflected into the calculation of average wages shall consider the following criteria: 1) They shall be

paid regularly and periodically; 2) They are mandated by the employer according to collective bargaining, Rules of Employment, salary regulation, labor contract, and habitual practice; or 3) Employees identified under general conditions shall be paid uniformly. In these cases, these items of pay shall be considered as wages regardless of their titles.” The incentive annual salary was ruled as wages.

4. How to include bonuses paid through one year into the amount subject to the calculation of average wages (Feb. 24, 2003, Wages 68207-120)

In cases where payment rate of bonuses is established per annum and paid for the period exceeding one month, the total amount of bonus paid for a certain month shall not be included into the calculation of average wages. The bonuses shall be calculated by dividing the total amount of bonuses paid to a relevant employee— during the twelve-calendar months before the day on which a cause for calculating his average wages occurs— by the total number of calendar months, which is 3/12 times the total amount of bonuses paid per year.

V. Conclusion

The Company and the employee have been interrogated by the Labor Supervisor since the application for delayed payment of severance pay was filed to the labor office in August 2007, The Employee has also submitted a Q&A reference (see the above administrative interpretation): Company B’s four independent entities are identified as one company, and that the abolition of accumulated rate of service year in severance pay shall be made null because the Company did not receive employees’ consent. During this process, the Company proposed that although it will not admit the total amount of incentive bonus received in return for work of 2007, it will accept in the average wages 5/12 portions of incentive bonus related to incentive bonus the Employee had received in March 2007 in return for the labor service of the previous year. The Employee accepted the company’s proposal and received an additional amount (60 million won in addition to statutory severance pay) calculated based upon new average wages. After this settlement, the Employee repealed the application for delayed payment of severance pay to the labor office.