SPC Guiding Case No. 184: Ma Xiaonan v. Beijing Sohu New Power Information Technology Co., Ltd. (Non-compete Dispute)

Dan Young Business Consultancy — www.danyoungcpa.com

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Keywords

Civil / non-compete restriction / duration / invalidity of agreement

Holding

Where an employer and a worker agree in a non-compete clause that the period for applying for arbitration and bringing a lawsuit arising from a dispute over performance of the non-compete clause shall not be counted toward the non-compete period, such an agreement falls within the circumstance prescribed in Article 26, paragraph 1, item (2) of the Labor Contract Law — namely, the employer exempting itself from its own statutory liability or excluding the worker's rights — and shall be found invalid.

Basic Facts

Ma Xiaonan joined Beijing Sohu New Power Information Technology Co., Ltd. ("Sohu New Power") on September 28, 2005, and the parties' final labor contract ran from February 1, 2014 to February 28, 2017, under which Ma Xiaonan served as a senior director. On February 1, 2014, Sohu New Power (Party A) and Ma Xiaonan (Party B) entered into a Non-Competition Agreement, clause 3.3 of which provided: "... The non-compete period shall commence on the date of Party B's resignation and shall not exceed 12 months at most; the specific number of months shall be calculated based on the non-compete compensation actually paid by Party A to Party B. However, if a dispute arises from performance of this Agreement and arbitration or litigation is initiated, the period of adjudication of the arbitration and litigation shall be deducted from the aforementioned non-compete period; that is, the period during which Party B must perform the non-compete obligation shall, after deducting the period of adjudication of the arbitration and litigation, not be shorter than the number of months of non-compete agreed above." On February 28, 2017, the labor contract expired and the labor relationship between the parties terminated. On March 24, 2017, Sohu New Power issued to Ma Xiaonan a "Notice Regarding the Requirement to Perform the Non-Compete Obligation and to Receive Non-Compete Economic Compensation," requiring him to abide by the Non-Competition Agreement and to fully and properly perform the non-compete obligation. After resigning from Sohu New Power, Ma Xiaonan began a cooperative relationship with Youku in mid-March 2017, and later left Youku at the end of April 2017, thereby breaching the Non-Competition Agreement. Sohu New Power applied to the Beijing Labor and Personnel Dispute Arbitration Commission for arbitration, requesting confirmation that Ma Xiaonan breached the non-compete obligation and should return double the non-compete compensation, continue to perform the non-compete obligation, compensate for losses, and pay attorney fees. The Arbitration Commission rendered Award Jing Lao Ren Zhong Zi [2017] No. 339: (1) Ma Xiaonan shall return, in one lump sum, double the non-compete compensation paid by Sohu New Power for March and April 2017, totaling RMB 177,900; (2) Ma Xiaonan shall continue to perform the non-compete obligation owed to Sohu New Power; (3) the remaining arbitration claims of Sohu New Power were dismissed. Ma Xiaonan refused to accept the award and, within the statutory period, brought a lawsuit before the Haidian District People's Court of Beijing.

Judgment

On March 15, 2018, the Haidian District People's Court of Beijing rendered Civil Judgment (2017) Jing 0108 Min Chu No. 45728: (1) Ma Xiaonan shall, within seven days from the effective date of the judgment, return to Sohu New Power double the non-compete compensation for March and April 2017, totaling RMB 177,892;

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(2) it was confirmed that Ma Xiaonan was not required to continue performing the non-compete obligation owed to Sohu New Power. Sohu New Power refused to accept the first-instance judgment and appealed. On August 22, 2018, the Beijing First Intermediate People's Court rendered Civil Judgment (2018) Jing 01 Min Zhong No. 5826: the appeal was dismissed and the original judgment affirmed.

Reasoning

The effective judgment of the court held: The focus of the dispute in this case was the question of the legal application of the non-compete period agreed in clause 3.3 of the Non-Competition Agreement. Sohu New Power argued on appeal that clause 3.3 of the Agreement was valid and that Ma Xiaonan's non-compete period was the actual period of adjudication of the arbitration and litigation in this case plus 12 months, based on the time actually incurred and not exceeding two years; however, the court did not accept that argument.

I. Review of the non-compete agreement

Although the law permits an employer and a worker to agree on a non-compete obligation, it simultaneously imposes mandatory provisions on the content of the parties' non-compete agreement. In other words, by means of provisions of a mandatory nature, the law expressly limits the scope of personnel to whom the non-compete obligation applies, the field of competition, and the duration of the restriction, and requires that the non-compete agreement not violate laws and regulations, in order to protect the employer's trade secrets and maintain fair competition and market order, while also preventing the employer from improperly using the non-compete system to cause excessive harm to the worker's freedom to choose employment.

II. Validity of the agreement to "deduct the period of adjudication of arbitration and litigation"

In this case, Sohu New Power agreed in clause 3.3 of the Non-Competition Agreement that Ma Xiaonan's non-compete period should deduct the period of adjudication of arbitration and litigation. That agreement in effect required Ma Xiaonan to perform the non-compete obligation for a period equal to: the period of adjudication of the arbitration and litigation procedures plus the number of months of non-compete compensation actually paid (up to a maximum of 12 months). From the perspective of the worker's freedom to choose employment, although the law imposes statutory limits on the period of adjudication of arbitration and litigation procedures, in a specific case that period is not a concretely determinate period; using that period as content of the non-compete agreement is inconsistent with the legislative purpose that non-compete clauses should be specific and definite. In addition, given the particularity of labor dispute cases, a considerable number of cases need to go through the "one arbitration, two trials" procedure. The above agreement meant that, once a dispute arose between the worker and the employer, the worker's non-compete period would be extended to an unpredictable and quite lengthy period, even reaching two years. In substance, this placed the worker's freedom to choose employment in a pending state for a certain period. On the other hand, from the perspective of the worker's right to judicial relief, if the worker initiated arbitration and litigation because a dispute arose from performance of the Non-Competition Agreement with Sohu New Power, then pursuant to clause 3.3 of the Agreement, the worker would still be required to perform the non-compete obligation during the period of adjudication of the arbitration and litigation, resulting in an extension of the worker's non-compete period. This would place the worker in the dilemma of "if he seeks judicial relief, his non-compete period is extended; if he does not seek judicial relief, his rights and interests are harmed," thereby restricting, to a certain extent, the worker's right to judicial relief. For the employer, clause 3.3 of the Agreement enabled Sohu New Power, without any need to negotiate with the worker, to unilaterally and indirectly extend the worker's non-compete period by initiating arbitration and litigation, thereby to a certain extent exempting itself from its statutory liability. In summary, the court held that the part of clause 3.3 of the Non-Competition Agreement providing that the non-compete period should deduct the period of adjudication of arbitration and litigation — namely, "However, if a dispute arises from performance of this Agreement and arbitration or litigation is initiated ... the period during which Party B must perform the non-compete obligation shall, after deducting the period of adjudication of the arbitration and

litigation, not be shorter than the number of months of non-compete agreed above" — fell within the circumstance prescribed in Article 26, paragraph 1, item (2) of the Labor Contract Law, namely the employer exempting itself from its own statutory liability or excluding the worker's rights, and should be invalid. Pursuant to Article 27 of that Law, where a labor contract is partially invalid without affecting the validity of the other parts, the other parts shall remain valid.

III. Determination of the non-compete period in this case

Accordingly, pursuant to the still-valid part of clause 3.3 of the Non-Competition Agreement, Ma Xiaonan's non-compete period should be determined based on the number of months of non-compete compensation paid to him by Sohu New Power, and should not exceed 12 months at most. Given that Sohu New Power had already paid Ma Xiaonan non-compete compensation for a total of 12 months from March 2017 to February 2018, Ma Xiaonan's non-compete period had already expired, and he was not required to continue performing the non-compete obligation owed to Sohu New Power.

Relevant Legal Provisions

Article 23, paragraph 2, Article 24, and Article 26, paragraph 1 of the Labor Contract Law of the People's Republic of China.

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