

## China's New Labour Contract Regime: An Engaging Puzzle?



### 1. Introduction

The *People's Republic of China Labour Contract Law* (“中华人民共和国劳动合同法”) (“**Labour Contract Law**” or the “**new law**”) was promulgated by the Standing Committee of the National People's Congress (“NPC”) on 29 June 2007 with effect from 1 January 2008.

The Labour Contract Law represents the most significant reworking of Chinese labour law for more than 10 years, i.e. since the promulgation of the *People's Republic of China Labour Law* (“中华人民共和国劳动法”) (the “**1995 Labour Law**”), effective from 1 January 1995. It impacts on labour contracts entered into both before and after its effective date.

Two drafts of the Labour Contract Law were released in December 2005 and December 2006 and during the consultation process, many foreign entities, including the European Chamber of Commerce, the American Chamber of Commerce and the U.S.-China Business Council, participated and lobbied strongly against some provisions of the draft law that were described as unduly burdensome on foreign invested enterprises (“**FIEs**”). In March 2006, the NPC also issued a call for public comment: over 190,000 comments were received from the public via letters and the internet. The law was finally enacted on 29 June 2007, at a time when China was subject to intense criticism for failing to effectively enforce its existing labour legislation, in the light of national scandals involving slave labourers in brick kilns and coal mines in the provinces of Shanxi and Henan.

The Labour Contract Law is designed to encourage long-term employment relationships, to enhance the protection of workers' rights and to give employees' representatives more influence in the workplace. These broad objectives of the new law have been unanimously applauded as a commendable effort by the international business community and, apparently in response to the latter's concerns, the Chinese authorities have watered down many of the most onerous provisions found in previous drafts. In fact, many provisions of the new law simply restate provisions of other existing laws or lower level rules and regulations. On the other hand, the new law does increase the costs for employers doing business in China and grants to employees and trade unions self-help remedies which were previously unavailable.

The main issue for employers, however, as with countless pieces of legislation in China, remains one of enforcement. In this respect, the primary fear of FIEs is that the law will be enforced in an inconsistent and asymmetrical manner, notably more vigorously against them than domestic companies. This might, in certain cases, result in a competitive disadvantage for the more law-abiding enterprises.

We highlight below some of the key provisions of the Labour Contract Law. As many of its provisions are drafted in quite vague terms, it is expected that implementing regulations will be promulgated before the end of this year to offer more guidance for all parties involved, i.e. employers, trade unions, employees, administrative authorities and labour arbitration tribunals.

## 2. Impact on existing contracts

The Labour Contract Law expressly provides that contracts entered into before its effective date (1 January 2008) will remain valid after that date.<sup>1</sup>

However, the transitional arrangements applicable to contracts entered into before 1 January 2008 are not entirely clear. In other words, it is not entirely clear whether, after 1 January 2008, the current law or the new law will apply to contracts entered into before that date.

On the one hand, the new law clearly explains what will happen in three cases, namely: (i) the obligation to enter into written contracts for employment relationships that were formed without written contracts before 1 January 2008; (ii) the obligation to offer open-term contracts after two renewals of fixed-term contracts; and (iii) the amount of severance compensation that employers must pay on terminating labour contracts after 1 January 2008. The specific solutions formulated by the new law in these three cases are set out below in Sections 4, 6 and 10.2(e) respectively.

On the other hand, the new law is not entirely clear as to which of the current or the new law will apply in certain other situations. One example of this is the performance after 1 January 2008 of non-competition agreements entered into before 1 January 2008 (the maximum term for non-competition clauses is three years under the current law, but only two years under the new law). We believe that the provision which states that contracts entered into before 1 January 2008 will remain valid after that date means that such contracts will remain valid in accordance with the law in force at the time of the conclusion of the contract, but it would have been helpful if the new law had said as much. Furthermore, labour arbitration tribunals which have a monopoly jurisdiction over Chinese labour disputes may have a different interpretation of the transitional regime under the Labour Contract Law, and implementing regulations may amend or provide further nuances to the basic transitional regime prescribed by the new law.

## 3. Company rules and policies

Under the current 1995 Labour Law, internal company rules and policies on matters such as labour remuneration, working hours, rest and leave periods, labour health and safety, insurance and welfare benefits, employee training, labour

<sup>1</sup> *People's Republic of China Labour Contract Law* ("中华人民共和国劳动合同法"), promulgated by the Standing Committee of the National People's Congress on 29 June 2007 with effect from 1 January 2008, Article 97.

<sup>2</sup> *People's Republic of China Labour Law* ("中华人民共和国劳动法"), promulgated by the Standing Committee of the National People's Congress on 5 July 1994 with effect from 1 January 1995, Article 4. See also: *Interpretation of the Supreme People's Court on Several Issues About the Application of Laws for the Trial of Labour Disputes*, issued on 16 April 2001, Article 19: "internal company rules and policies are enforceable only if: (i) they were adopted through democratic procedures; (ii) they do not violate laws and administrative regulations; and (iii) they have been publicized to the workers."

discipline and quota management are subject to minimal requirements.<sup>2</sup> However, a minority of employers used internal rules and policies as a general channel for unilaterally imposing unpopular, and in some cases illegal, provisions that prejudiced the rights of employees. In an effort to fight such practices, the new law imposes more specific and onerous obligations in this respect.

Under the Labour Contract Law, in order to adopt or amend company rules and policies, employers must discuss with the employees' representatives' congress or with all their employees. After considering the latter's proposals and comments, employers must engage in negotiations with the trade union or the employees' representatives' congress (in an earlier draft, any change to the internal company rules had to be *approved* by the employees' representatives or trade union). Finally, after company rules and policies are adopted or revised, employers must notify them to employees or put them on public display.<sup>3</sup> If an employee suffers a loss because an internal rule or policy is illegal, the employer will be issued a warning by the labour administrative authorities and will have to compensate the employee for any losses suffered.<sup>4</sup> In such circumstances, the employee also has the right to terminate the contract and receive compensation.<sup>5</sup>

## 4. Individual labour contracts

Like the 1995 Labour Law, the Labour Contract Law requires employers to enter into written employment contracts containing various mandatory clauses with all employees (except part-time employees), and to make all contractual amendments in writing.<sup>6</sup>

In order to penalise what remains a problem, particularly amongst small and medium sized enterprises, the new law also gives more "teeth" to the obligation to enter into written agreements. Specifically, it provides that if an employer fails to sign a written agreement with an employee within one month, he must pay him double wages for the period of the violation.<sup>7</sup> Furthermore, if the period of violation extends to one year, the employer will be deemed to have signed an open-term contract,<sup>8</sup> which is more difficult to terminate.

For employment relationships established prior to 1 January 2008 without a written contract, the employer must sign a written contract before 1 February 2008,<sup>9</sup> otherwise the penalties provided by the new law will apply.

## 5. Trade unions and collective contracts

Under existing laws and regulations, workers in China are not allowed to form independent unions. The sole officially approved labour union is the All-China Federation of Trade Unions ("ACFTU"), which is run by the Chinese Communist

<sup>3</sup> *Id.*, Article 4.

<sup>4</sup> *Id.*, Article 80.

<sup>5</sup> *Id.*, Article 38.

<sup>6</sup> *Id.*, Article 10, 17, 35 and 69; 1995 Labour Law, Articles 16 and 19.

<sup>7</sup> *Id.*, Article 82.

<sup>8</sup> *Id.*, Article 14(iii).

<sup>9</sup> *Id.*, Article 97.

Party; company-based trade unions are in fact branches of this state-run union. Since the ACFTU has traditionally been more concerned with monitoring workers in order to avoid social unrest than to advocate workers' rights, workers often had to negotiate their wages and benefits with their employers individually rather than through collective bargaining or collective contracts. However, the promulgation of the Labour Contract Law and recent high profile campaigns to force household names such as Wal-Mart to unionise their China operations may be sending a signal that the Chinese authorities are now determined to see trade unions play a more proactive role in the workplace.

As under previous legislation, employers and employees may enter into collective contracts with trade unions with respect to matters such as labour remuneration, working hours, rest periods and leave, labour health and safety, social welfare insurance and benefits.<sup>10</sup> Trade unions are expressly given the statutory role to protect the lawful rights and interests of employees and to supervise employers' compliance with the labour contracts system.<sup>11</sup>

Trade unions are also granted three more specific roles under the Labour Contract Law.

Firstly, as under the current 1995 Labour Law, in order to enter into collective labour contracts, employers must first circulate a draft of the contract to the employees' representatives' congress (or all employees) for deliberation and adoption.<sup>12</sup> Employers must then enter into the contract with a trade union representing all the employees (or, if no trade union has been formed, with the representatives elected by the employees under the guidance of the trade union at the level above) and obtain the approval of the relevant labour administrative authority.<sup>13</sup> A new feature of the Labour Contract Law is the possibility for trade unions at the industry level (in industries such as construction, mining, and food and beverage services), rather than at the enterprise level, to negotiate with the representatives of employers.<sup>14</sup> Under the new law, industry-level trade unions will also be able to enter into industry-wide contracts or area-level contracts, and such contracts will be binding on employers and employees within the industry or area concerned.<sup>15</sup>

Second, as explained below in Section 10.2(c), trade unions have some bargaining power with respect to collective lay-offs of employees.

Thirdly, in disputes related to breaches of collective contracts, trade unions themselves are entitled to apply for arbitration or to file a suit.<sup>16</sup> This appears to be an addition to their more passive role of providing support and assistance to employees who apply for labour arbitration or bring suits.<sup>17</sup>

## 6. Term of labour contracts: fixed-term v. open-term

Labour contracts are divided into three categories with respect to their term: (i) fixed-term; (ii) open-term; and (iii) term equal to the time taken for the completion of a specific task.<sup>18</sup>

Under the new law, employers are permitted to sign fixed-term contracts with their employees<sup>19</sup>, but they are legally obliged to offer open-term contracts to employees who have been consecutively working with them for 10 years or more, who have worked for over one year without a written contract or who have completed two successive fixed-term contracts.<sup>20</sup> This requirement is in line with the objective of the new law to encourage long-term employment relationships.

The obligation to offer open-term contracts to employees who have completed two successive fixed-term contracts is arguably one of the novel aspects of the new law whose impact will be greatest on employers. It is not clear from the text of the law whether employers must automatically offer open-term contracts to their employees after two renewals of fixed-term contracts, or if they may opt not to renew the contract at all (presumably the latter). This uncertainty needs to be resolved as it may potentially have an impact on the HR decisions of employers.

In any event, in these three instances, if the employer fails to enter into an open-term contract, he or she will be liable to pay the employee double his or her salary for each month during which the breach of the law continues.<sup>21</sup>

Labour contracts entered into before 1 January 2008 are retrospectively, rather than retroactively, subject to the new law, which means that the employer may renew them twice after 1 January 2008 before he or she must offer an open-term contract.<sup>22</sup>

## 7. Probation

The Labour Contract Law maintains the principle that maximum probationary periods for newly-recruited employees vary according to the agreed term of the employment contract. The maximum probationary periods are however shortened as follows:<sup>23</sup>

| Contract Term                        | Maximum Permitted Probationary Period |
|--------------------------------------|---------------------------------------|
| 3 months - 1 year                    | 1 month                               |
| 1 year - 3 years                     | 2 months                              |
| 3 years or more / open-term contract | 6 months                              |

<sup>10</sup> *Id.*, Article 51; *comp.* 1995 Labour Law, Article 33.

<sup>11</sup> *Id.*, Article 78.

<sup>12</sup> *Id.*, Article 51; *comp.* 1995 Labour Law, Article 33.

<sup>13</sup> *Id.*, Article 54 ; *comp.* 1995 Labour Law, Articles 33 and 34.

<sup>14</sup> *Id.*, Article 53.

<sup>15</sup> *Id.*, Articles 53-54.

<sup>16</sup> *Id.*, Article 56.

<sup>17</sup> *Id.*, Article 78.

<sup>18</sup> *Id.*, Article 12.

<sup>19</sup> *Id.*, Article 13.

<sup>20</sup> *Id.*, Article 14(iii).

<sup>21</sup> *Id.*, Article 82.

<sup>22</sup> *Id.*, Article 97.

<sup>23</sup> *Id.*, Article 19.

In this respect, many employers may find that a two months' probationary period is a relatively short period of time to fully evaluate the suitability of a mid-to-high level executive employed for slightly less than 3 years. In addition, employers are limited to imposing only one probation period in relation to any given employee, apparently even where the employee is promoted to a new post involving substantially different duties (a decision which usually warrants a new evaluation of the employee's qualifications for the job). No probationary periods are allowed for part-time employees.<sup>24</sup>

During the probationary period, the employer must pay a salary that cannot be lower than the lowest salary for someone holding a similar position within the employer, nor can it be lower than 80% of the salary agreed upon in the labour contract or the local minimum salary rate.<sup>25</sup>

Finally, while employees may terminate a labour contract during the probationary period simply by giving 3 days' notice, the employer can only do so on limited grounds under the Labour Contract Law.<sup>26</sup>

## 8. Non-competition clauses

The Labour Contract Law is far more restrictive than the current law with respect to non-competition clauses.

Firstly, the new law only recognises the validity of non-compete restrictions imposed upon senior management, senior technical staff and other employees whose work involves confidential information.<sup>27</sup>

Second, the new law shortens the maximum non-compete period from 3 years to 2 years calculated from the expiration or termination of the contract.<sup>28</sup>

Thirdly, the new law provides that employers must pay compensation in monthly instalments to employees during the post-termination period for their compliance with non-compete obligations.<sup>29</sup> It is not clear what an acceptable standard is for such post-termination compensation payments: the standard proposed in earlier drafts, i.e. 50% of the normal salary during the non-compete period, has not been maintained in the final promulgated version.

In view of the limited validity period of non-competition clauses, employers developing new technologies may find it increasingly necessary to limit the number of employees who have access to intellectual property or trade secrets. Employers should also consider taking advantage of the express provision of the new law which allows them to stipulate liquidated damages for the breach of non-competition clauses (liquidated damages clauses are forbidden in labour contracts for all other breaches, except to recoup certain professional training costs).<sup>30</sup>

<sup>24</sup> *Id.*, Article 70.

<sup>25</sup> *Id.*, Article 20.

<sup>26</sup> *Id.*, Articles 21, 39 and 40(i)-(ii).

<sup>27</sup> *Id.*, Articles 23-24.

<sup>28</sup> *Id.*, Articles 23-24.

<sup>29</sup> *Id.*, Article 23.

<sup>30</sup> *Id.*, Article 25.

<sup>31</sup> *Id.*, Article 11.

## 9. Abuses by employers

The Labour Contract Law prohibits various abuses committed by a minority of employers in China in relation to the formation and enforcement of labour contracts. These include refusing to enter into written contracts,<sup>31</sup> confiscating employees' ID cards,<sup>32</sup> requiring employees to provide financial security,<sup>33</sup> imposing liquidated damages (except in permitted cases),<sup>34</sup> using fraud or coercion or taking advantage of an employee's vulnerability (in order to secure a labour contract or amendments thereof),<sup>35</sup> exempting themselves from liability or excluding the rights of employees<sup>36</sup> and compelling employees to work overtime, whether overtly or in a disguised fashion.<sup>37</sup>

These abuses, depending on the circumstances, are generally sanctioned either by the invalidity of the contract or by payment of compensation. Other instances of abuses by employers allow employees to terminate the labour contract.

## 10. Termination of labour contracts

The chapter on the rescission and termination of labour contracts is the Labour Contract Law's most comprehensive. It addresses cases involving termination by the employee and termination by the employer (including collective dismissals, severance compensation and unlawful termination).

### 10.1 Termination by Employees

In contrast to the position of employers, who cannot dismiss employees at will or on simple notice in any circumstances, employees are entitled to terminate labour contracts by giving 30 days' notice (or 3 days' notice during the probationary period).<sup>38</sup> In such cases, employees are not entitled to severance payments. This broadly reflects the current legal position except for the new provision on termination during the probationary period.

Employees are also entitled to terminate labour contracts and receive severance pay in different circumstances, including where the company rules and policies are illegal and damage their interests, or where the employer fails to provide the labour protection or working conditions agreed in the contract, fails to make full and timely payment of remuneration or fails to pay social welfare insurance premiums.<sup>39</sup> These are essentially new rights for the employee.

Finally, as under the current 1995 Labour Law, employees are entitled to terminate labour contracts without notice and receive severance compensation when employers compel them to work by means of violence, threats or illegal restrictions on personal freedom, or issue unlawful instructions or demand that they perform unsafe work which endangers their personal safety.<sup>40</sup>

<sup>32</sup> *Id.*, Article 9.

<sup>33</sup> *Id.*, Article 9.

<sup>34</sup> *Id.*, Article 25.

<sup>35</sup> *Id.*, Article 26(i).

<sup>36</sup> *Id.*, Article 26(ii).

<sup>37</sup> *Id.*, Article 31.

<sup>38</sup> *Id.*, Article 37.

<sup>39</sup> *Id.*, Articles 38(1) and 46.

## 10.2 Termination by Employer

The Labour Contract Law maintains the same position as the current 1995 Labour Law, which is that an employer cannot terminate an employment relationship at will. In other words, there must always be a legally recognised ground for termination.

### (a) Termination Without Notice or Severance

Summary dismissal, i.e. termination without notice and without severance pay, is permitted for what are considered to be egregious breaches by employees, including serious violation of the company rules and policies, corruption or dereliction of duties (causing severe damage to the employer's interests), or where the employee fails to meet the recruitment requirements during the probationary period, has used fraud to cause the employer to sign the employment contract or is concurrently employed by another employer (severely affecting the performance of his duties).<sup>41</sup> The last two grounds for summary dismissal did not exist under previous laws and regulations and are introduced for the first time in the Labour Contract Law.<sup>42</sup>

These limitations on termination without notice do not apply to part-time workers, who may be terminated at any time without compensation.<sup>43</sup>

### (b) Termination With Notice

Employers may also unilaterally terminate employees on 30 days' notice (or the payment of one month's severance in lieu) on any of the following grounds: (i) the employee, following an illness or a non-work related injury, is unable to perform the original job or the replacement position arranged by the employer<sup>44</sup>; (ii) the employee is proven incompetent even after training or transfer to a new position; and (iii) there is a material change in the objective circumstances prevailing at the time the labour contract was entered into such that the contract can no longer be performed and the parties cannot agree on the required amendments.<sup>45</sup> Once again, this maintains the current position under the 1995 Labour Law.

In addition, as explained below in Section 10.2(d), certain categories of employees are protected from termination of their employment contracts.

### (c) Collective Dismissals

Under the 1995 Labour Law, mass lay-offs were permitted only in certain limited circumstances, i.e. legal reorganisation due to conditions of near bankruptcy or serious difficulties in productions or

operations.<sup>46</sup>

The Labour Contract Law expands the grounds upon which mass lay-offs (i.e. dismissal of 20 or more employees or over 10% of an employer's total workforce) may be carried out. In particular, mass lay-offs are also allowed where an employer still needs to lay off employees after switching mode of production, introducing a major technological innovation, adjusting its business model, or due to a material change in objective economic circumstances.<sup>47</sup>

On the other hand, the Labour Contract Law makes it more difficult on a procedural level to lay off employees. Specifically, it obliges employers to solicit the opinion of the trade union (or all their employees) at least 30 days before proceeding to the lay-off.<sup>48</sup> Where the employer is in violation of any laws or provisions of the labour contract, the trade union may require the employer to rectify his conduct and employers must notify the trade union in writing of any outcome in this regard.<sup>49</sup> It is not entirely clear whether this is a purely consultative process or whether the trade union or the employees have a right to veto the dismissal. An earlier draft of the Labour Contract Law explicitly required employers to obtain the approval of the state-controlled union before collective dismissals could take place.

Under the new law, when proceeding to lay-offs, employers must retain in priority certain categories of employees, i.e. those who have entered into relatively long fixed-term labour contracts, those who have entered into open-term contracts and those who are the sole employed person in a family comprising elderly persons or minors.<sup>50</sup> This provision was heavily criticised by the American Chamber of Commerce which said that it represented a return to the era of the "iron rice bowl", and clearly conflicted with the needs of enterprises to improve efficiency when poor performances and heavy losses were endangering their future. It does make it difficult for an employer to re-employ on the basis of merit and performance. If an employer wishes to recruit new workers within six months of making the collective dismissal, he must give notice to the dismissed employees and recruit them in priority to new hires.

The Labour Contract Law also obliges employers to report the lay-offs to the local labour administrative authorities,<sup>51</sup> possibly giving the authorities an opportunity to intervene and mediate.

<sup>40</sup> *Id.*, Article 38(2); *comp.* 1995 Labour Contract Law, Article 32.

<sup>41</sup> *Id.*, Article 39.

<sup>42</sup> 1995 Labour Law, Article 25.

<sup>43</sup> Labour Contract Law, Article 71.

<sup>44</sup> If the employee suffers from an occupational disease or a work-related injury (and is confirmed to have lost, completely or partially, the capacity to work), the employer must not terminate his contract: *id.*, Article 42.

<sup>45</sup> *Id.*, Article 40.

<sup>46</sup> 1995 Labour Law, Article 27.

<sup>47</sup> Labour Contract Law, Article 41. This provision may be invoked when the major assets of the employer are transferred to a third party or in the case of other forms of major restructuring that make employees effectively redundant.

<sup>48</sup> *Id.*, Article 41.

<sup>49</sup> *Id.*, Article 43.

<sup>50</sup> *Id.*, Article 41.

(d) Employees Protected from Termination

Certain categories of employees are protected from termination of their employment contracts where there are grounds justifying a dismissal under Article 40 on giving 30 days' notice (or the payment of one month in lieu) or under Article 41 where a collective lay-off takes place, but this does not exclude a dismissal "for cause" under Article 39 (which sets out the most egregious breaches by employees). The class of protected employees includes any employee who: (i) is suffering from occupational illness and was not given a proper health examination before leaving the position, or is in a diagnosis or medical observation period for an occupational illness; (ii) has lost or partially lost the ability to work due to a work related injury or diseases; (iii) is within the statutory period for medical treatment; (iv) is pregnant, in confinement or nursing; or (v) has worked uninterruptedly for 15 years with the same employer and is less than 5 years away from statutory retirement age.<sup>52</sup>

Categories (i) and (v) are new categories that were not included in the former legislation,<sup>53</sup> although the latter is a reformulation of the so-called "double ten" rule set out in the 1995 Labour Law and its suite of related regulations.

The Labour Contract Law also contemplates the possibility for the authorities to adopt laws or regulations adding new categories of employees protected from termination.<sup>54</sup>

(e) Severance Compensation

Under the new law, employers must pay severance compensation in the following circumstances:

- (i) Where an employee terminates a labour contract and is entitled to receive compensation, as explained above in Section 10.1;
- (ii) Where both parties agree to terminate a labour contract after the employer took the initiative to raise termination;
- (iii) Where the employer terminates a labour contract on 30 days' notice as set out in Section 10.2(b) above;
- (iv) Where the employer proceeds to carry out a collective dismissal due to the necessity to restructure the enterprise in accordance with the *People's Republic of China Enterprise Bankruptcy Law*;
- (v) Where a fixed-term labour contract reaches its term, except if the employer offers contractual terms that are no less favorable than the existing terms, and the employee refuses to agree to renew the labour contract;

(vi) Where the employer is declared bankrupt in accordance with the law, or has his business licence revoked, is ordered to shut down or is closed down, or decides to go into early dissolution; or

(vii) In any other circumstances prescribed by laws or administrative regulations.<sup>55</sup>

Item (v) above places a particularly heavy burden on employers, who will systematically have to pay severance when they decide not to renew fixed-term contracts. This is another mechanism used by the new law to discourage the tendency of employers in China towards establishing short-term employment relationships.

The amount of compensation that must be paid depends on the number of years worked with the same employer, but is calculated (as under the current law) on the basis of one month's salary for each year of service. For the purpose of this calculation, one month's salary means the employee's average monthly salary for the 12 months prior to the termination. In addition, under the new law, a period of less than six months gives rise to an entitlement to half a month's salary, and any period between six months and one year is counted as a full year.<sup>56</sup> The Labour Contract Law, on the other hand, also introduces two caps on the amount of severance compensation. Firstly, in all cases, severance compensation is capped at 12 months' salary. Second, if the monthly salary is greater than three times the average monthly salary of employees in the employer's area for the previous year, the severance compensation is capped at three times this average monthly salary. An interesting feature of the new law is that this last provision may make it far less onerous for enterprises to terminate labour contracts with highly-paid employees, including expatriate executives.

Finally, the new law establishes a basic transitional regime applicable to contracts entered into before 1 January 2008 (i.e. the effective date of the new law) and terminated after that date. For such contracts, the general rule is that the number of years for which severance compensation is payable must be counted from 1 January 2008;<sup>57</sup> however, where laws and regulations in effect prior to 1 January 2008 obliged employers to pay severance compensation with respect to the period prior to 1 January 2008, they must pay compensation accordingly.

(f) Unlawful Termination

If an employer terminates a labour contract in violation of the Labour Contract Law, the employee

<sup>51</sup> *Id.*, Article 41.

<sup>52</sup> *Id.*, Articles 42 and 45.

<sup>53</sup> Cf. 1995 Labour Law, Article 29.

<sup>54</sup> Labour Contract Law, Articles 42 and 45.

<sup>55</sup> *Id.*, Article 46.

<sup>56</sup> *Id.*, Article 47.

<sup>57</sup> *Id.*, Article 97.

has the right to demand that the employer continue to perform his contractual obligations (i.e. reinstate him).<sup>58</sup> If relationships have broken down, this is not really a practical option and the threat or fact of suing for reinstatement is often a tactic used by the employee to enhance the severance terms offered by the employer.

If the employee does not require the employer to reinstate him, the employer will be liable to pay damages equal to double severance,<sup>59</sup> i.e. two months' salary for every year worked with the employer. This clarifies a long-standing issue as to the standard of compensation where a labour contract is terminated unlawfully.

## 11. Special employees: part-time employees and temporary agency employees

The Labour Contract Law recognises two categories of special employees, i.e. part-time employees and temporary agency employees.

### 11.1 Part-time Employees

Under the new law, part-time employees are defined as employees who work not more than four hours per day or 24 hours per week for the same employer. This constitutes a reduction from the criteria under the previous legislation, whereby part-time employees were those who work not more than five hours per day or 30 hours per week for the same employer.

As mentioned above, the obligations of employers towards part-time employees are far less onerous than towards regular employees, i.e. they may be engaged based on an oral agreement<sup>60</sup> and they may be terminated at will without compensation.<sup>61</sup>

On the other hand, they must not be subject to any probationary period,<sup>62</sup> they must be paid every 15 days or less<sup>63</sup> and they are subject to local minimum hourly wage regulations.<sup>64</sup>

### 11.2 Temporary Agency Employees

There is currently no comprehensive body of rules governing the use of temporary employees from dispatch agencies or secondment programs. The new law provides a relatively detailed legal regime for dispatch agencies and for the entity ultimately benefiting from the work of the employees, called the "employing entity".

Dispatch agencies are considered as "employers" under the new law and they must enter into written contracts with employees for a fixed-term of at least two years.<sup>65</sup> Labour dispatch must generally only be used for positions of a temporary, auxiliary or replacement nature.<sup>66</sup>

Dispatch agencies must pay compensation on a monthly basis and, even when employees are not working, they must compensate them on the basis of equal pay for equal work<sup>67</sup> and, in any event, at a rate not lower than the local minimum salary.<sup>68</sup> Where an employing entity uses employees hired by a dispatch agency located in another area, the working conditions and remunerations of the employees must be provided in accordance with the standards of the area where the employing entity is located.<sup>69</sup> Dispatched workers are also entitled to organise or to participate in trade unions within their dispatch agency or their employing entity.<sup>70</sup>

Dispatched workers are not entitled to terminate their contracts at will but only with the agreement of the employing entity or on certain objective grounds essentially where the conduct of the employing entity is abusive or unlawful.<sup>71</sup> Finally, concerning termination by the employer, the employing entity is entitled to return the dispatched worker to the dispatch agency, and the latter to terminate his contract, for the same reasons as for other employees, e.g. for cause or due to non-work related illness or lack of competence, but not for economic reasons (i.e. material change in the objective circumstances under which the labour contract was entered into).<sup>72</sup>

## 12. Conclusion

Overall we see the Labour Contract Law as something of a "mixed bag". There are certain aspects that are sensible and practical in nature (such as clarifying that payment in lieu is acceptable instead of notice when a contract can be terminated on 30 days' notice), and others that rightly address certain common types of unacceptable abuses by employers. Some of the changes do have a quite marked financial impact, such as the requirement to renew on equivalent terms or pay compensation at the end of a fixed-term contract, which to a large extent removes the previous flexibility enjoyed by responsible employers in China.

Many fundamental aspects of the existing employee-friendly legal regime are preserved in that it remains the case that in China employers have to fit a termination into a legally stipulated ground, rather than being able to dismiss at will or on simple notice.

Whilst credit needs to be given to the various Chinese authorities who appear to have genuinely engaged with and taken on board many of the concerns of foreign investors and Chambers of Commerce in relation to previous drafts (e.g. previous drafts required employee representative groups or unions to agree to all changes to internal policies and rules), one cannot escape the feeling that due to the authorities' desire to protect the weakest and most vulnerable groups of employees, responsible and generally law-abiding employers have ended up paying the price for the abusive conduct of a small minority.

<sup>58</sup> *Id.*, Article 48.

<sup>59</sup> *Id.*, Article 87.

<sup>60</sup> *Id.*, Article 69.

<sup>61</sup> *Id.*, Article 71.

<sup>62</sup> *Id.*, Article 70.

<sup>63</sup> *Id.*, Article 72.

<sup>64</sup> *Id.*, Article 72.

<sup>65</sup> *Id.*, Article 58.

<sup>66</sup> *Id.*, Article 66.

<sup>67</sup> *Id.*, Article 63.

<sup>68</sup> *Id.*, Article 58.

<sup>69</sup> *Id.*, Article 61.

<sup>70</sup> *Id.*, Article 64.

<sup>71</sup> *Id.*, Article 65.

<sup>72</sup> *Id.*, Article 65. See also Section 10.2 above.

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