

# Employment law in China – an overview



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## Introduction

China's strong economy, large manufacturing base and burgeoning consumer market make it an irresistible place for many Western companies to do business. This in-brief provides a snapshot of some of the key aspects of Chinese employment law.

Our Hong Kong office was opened to meet a growing demand from many of our clients for coordinated employment and immigration/global mobility support across the Asia Pacific region (including China).

This publication provides general guidance only: expert advice should be sought in relation to particular circumstances. Our Hong Kong office can source Chinese law advice through its links with local firms in China.

## The employment law landscape

Prior to the economic restructuring and privatisation that occurred in China from around 1979, there were in effect no private employers and virtually no employment law. This has now well and truly changed. Alongside the growth of private employment, recent years have seen increasing levels of employment regulation to address the complexities of this type of relationship which also tends to involve a more mobile, expensive and demanding workforce.

Employment law in China is based on a statutory, civil law system, and there is no formal system of binding case law precedent. Employment law tends to be very pro-employee. There is no "at will" employment and termination of employment is only possible on specific statutory grounds, which in practice can be difficult to satisfy. There are also national and local layers of employment law. Local laws clarify the national ones by providing more detail. Enforcement of the national law can vary, sometimes significantly, from region to region. For example, enforcement in Shanghai tends to favour employers over employees to a greater extent than it does in other regions.

(see the "Terminating employment" section below). Since 2008, a so-called "two fixed terms rule" has applied, under which an employer must automatically provide an employee with an open term contract where they have signed a fixed-term contract twice in succession. An ambiguity in the wording of the two fixed terms rule has led to different interpretations in different locations. For example, in Shanghai, currently an employer can decide not to renew the contract at the end of both the first and second fixed term and must only provide an open term contract if it chooses to renew the employment and the employee requests for an open term contract after that point. In contrast, elsewhere in the country, including Beijing, only the first fixed term is "safe" because at the end of the second fixed term, the employer must automatically provide an open-term contract unless the employee decides not to renew the employment or requests for another fixed term contract.

Labour dispatch or "agency" type arrangements are very popular with employers (where workers are engaged through a third party agency rather than employed directly). However, this area is becoming increasingly regulated. The number of dispatch workers is restricted to 10% of the employer's total workforce, and such workers can only be engaged to fill temporary, auxiliary or substitute positions. The rules are more relaxed for ROs because they cannot hire local staff directly so must engage staff through agencies.

Probationary periods are commonly used and their duration is prescribed by statute depending on the employee's term of the employment. They can be for up to six months and cannot generally be extended.

## Commencing employment

### Structuring the employment relationship

In general, a foreign entity must establish some sort of formal business presence in China in order to engage employees. This presence could be a subsidiary, with the most common subsidiary vehicle being a so-called Wholly Foreign-Owned Enterprise ("WFOE"). It may also be a Representative Office ("RO"). In contrast to a WFOE, a RO has no formal legal identity in China itself as it is merely an extension of the foreign entity. While a WFOE can directly engage Chinese employees, a RO cannot - it must hire employees through a recognised employment or "labour dispatch" agency.

### Types of employment

The three main types of employment are open-term (i.e. a permanent contract), fixed-term and project-related contracts.

Fixed-term contracts are popular because Chinese law provides only limited grounds for an employer to unilaterally terminate an employment contract

### The employment contract

Full-time employees must have written employment contracts in Chinese. The penalties for not putting a written contract in place swiftly can be severe. If there is no written contract signed within 30 days of employment commencing, the employee is entitled to double pay until there is one. If a signed, written contract is still not in place a year after employment started, the employee will automatically become employed on an open-term basis (although at that point their right to receive double pay ends). Part-time employees can be employed under written or oral contracts.



## Work rules

Work rules are very important in China. Every employer must have them and they typically cover issues such as disciplinary procedures, termination grounds and pay. An employer must follow a consultation procedure before introducing new work rules or changing existing rules. Employees or their representatives do not, as part of consultation, have a right to veto the employer's proposals but merely have a right to provide an opinion. The consultation procedure generally takes one to two weeks to complete although there is no set period. Consultation on work rules can be overlooked by employers in practice. However, it is critical to follow the consultation procedure if the rules are to be effectively enforced against employees if there is a dispute.

## Key minimum employment rights

### Working time

There are three working hours systems: standard, flexible and comprehensive.

The standard working hour system is the default system for all employees (and by far the most common). It provides for standard working hours of no more than 8 hours per day and 40 hours per week. Overtime is payable for hours in excess of this standard amount, ranging from 150% to 300% of the employee's pay depending on whether the overtime is carried out on a working day, rest day or public holiday. Employees cannot generally be required to work more than three hours' overtime per day or 36 hours per month. This limit is quite restrictive by regional standards and many employers, particularly in labour intensive industries such as manufacturing, struggle to comply with it in practice.

The flexible system allows duties to be performed on a flexible schedule, and the comprehensive hours system allows an averaging of working hours over a specific period. These systems are limited to specific positions that are not suitable for the standard working hour system – for example, certain types of shift work and seasonal work. Employers wanting to implement these systems must first obtain approval from the local labour authority.

### Leave

An employee who has worked continuously for at least one year is entitled to paid annual leave of between five and 15 days depending on their total years in the workforce (not their length of service with their current employer). Employees should take their full annual leave entitlement in the year in which it is accrued. If an employer prevents an employee from doing so due to business reasons, the employer may be required to pay the employee double pay for unused annual leave unless the employee consents to carry this over. There are 11 statutory public holidays.

Female employees are entitled to 98 calendar days' paid maternity leave and extended maternity leave (usually 30 days, subject to local regulations) and male employees are now entitled to paternity leave in most major cities, the details of which vary across locations as there is no national provision covering paternity rights.

Employers are not required to allow employees to take a certain number of fully paid sick days for short term and common complaints such as colds and flu, although many do. Employees who need medical treatment because they are ill or suffering from a non-work-related injury are entitled to statutory medical treatment leave of between three and 24 months, depending on their length of service. A reduced rate of pay generally applies during medical treatment leave, which varies by location.

### Wages and social insurance

Employers must at least pay a minimum wage to employees. The relevant labour authority in each location sets its own minimum wage, which applies to all employees regardless of their age and experience.

China has a mandatory social security and welfare system under which employers and employees must contribute to funds including pension, medical and unemployment insurance. The employer is also required to contribute to occupational injury insurance and maternity insurance. The exact funds and level of contributions required vary across locations. By way of example, from 2020 employers in Shanghai were required to contribute 27.16-28.52% of the employee's pay to social insurance while the employee was required to contribute

10.5%. The level of the pay used for the purposes of calculating contributions is capped at certain levels which vary from region to region.

## Terminating employment

There is no "at will" employment, and termination of employment must be for cause. There is a list of statutory grounds for termination, and it is not possible for an employer and employee to agree to grounds that are not set out in statute. Unlike many other countries in the region, all employees are protected from unlawful dismissal, regardless of their seniority.

There is also a statutory minimum notice period of 30 days if the employer gives notice. An employer may pay in lieu of this notice period. The employee may resign by giving a notice period of 30 days (or 3 days during the probationary period).

The threshold for dismissing an employee lawfully is high. For example, statutory grounds that would allow an employer to dismiss an employee without notice include serious neglect of work duties causing substantial damage to the employer, and material breach of the work rules. Grounds upon which an employer may dismiss with notice include the employee being incompetent even after training and other assistance has been given by the employer, and a material change in circumstances which means that performance of the contract is impossible. In addition, the employer should first notify the trade union before unilaterally terminating employment, although the union has no right to veto the termination decision.

Given the high threshold that must be met in order to lawfully dismiss, in practice many employers instead pursue a termination by way of a mutual agreement with the employee.

Collective redundancies (where 20 or more employees or more than 10% of the employer's workforce are to be made redundant) are rare in practice. In such situations, it is more common for employers to seek a mutual agreement with the employee over termination.

In general, an employee is entitled to statutory severance if their employment is terminated by notice, mutual agreement or as a result of

collective redundancy. Statutory severance is one month's pay for each year worked, with pay in respect of service years since 2008 being subject to a statutory cap.

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## Discrimination

Discrimination protection in China is developing at pace though is still relatively nascent when compared to other countries. Discrimination against employees on grounds of nationality, ethnicity, race, gender and religious belief is unlawful. There are also protections for applicants during the recruitment process on additional grounds such as sex. However, the legal remedy in this respect of unlawful discrimination is limited, which means that in practice discrimination claims are relatively rare. Although the discrimination framework is not as developed as employers may be accustomed to in North America and Europe, the pressure on the government to develop the legal framework in general is likely to result in more discrimination regulation in coming years.

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## Protecting the business

Non-compete restrictions of no more than two years may be applied to senior employees or other employees who have access to confidential information. In order for a non-compete restriction to be enforceable, an employer must pay the employee a monthly amount during the non-compete period. The monthly amount varies from region to region but is generally between 30% and 60% of the employee's normal monthly salary during 12 months before the termination or expiration of employment. Non-solicitation and non-poaching restrictions are common but may not be enforceable in practice, and like elsewhere,

employers face practical difficulties in terms of proving an employee's breach.

Although a duty of confidentiality is implied into the employment contract, it is advisable for employers to include express confidentiality obligations as well.

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## Resolving disputes

Employment litigation is common in China. The time limit for an employee to file an employment claim with a labour arbitration committee (broadly the equivalent to the UK's employment tribunal) in respect of an employment dispute is generally one year. The system is relatively informal and fast - the law provides that cases should be completed within 45 days of the date that the claim is accepted by the relevant labour arbitration committee. An arbitration award may be appealed to the higher courts within 15 days of receipt. Arbitration is free of charge, while litigation in higher courts involves only nominal filing and hearing fees which are exempted by courts in many regions. Free of charge mediation is encouraged as a first step, although it is not compulsory.

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## Employee representation

An employer is not strictly required to establish trade unions in the workplace. In practice, however, there is an expectation that every workplace will have at least one trade union and many employers come under heavy pressure from authorities to establish unions. If there is a trade union in the workplace, the employer must contribute an amount equal to 2% of its total payroll in China to that union.

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## Data protection

There is no comprehensive national legislation in respect of data protection and no general expectation of privacy in the workplace such that there is in much of North America and Europe. However, the law does require that an employee's personal data be kept confidential and not be made public without the employee's written consent. During the past several years, data protection requirements in scattered laws and regulations (especially in terms of cyber security) are also developing gradually.

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