

a closer look: the new labour contract law

■ The Standing Committee of the National People's Congress adopted the Law on Employment Contracts of the People's Republic of China ("LCL") on 29 June 2007 and this came into effect on 1 January 2008. The LCL, which consists of 98 articles within eight chapters, emphasises the legal protection of employees' rights and offers better guidance on the employment relationship, compared with the old Labour Law.

The key provisions in the LCL include the following:

1. *Corporate rules and policies*

The making of rules by a company which have a direct bearing on the interests of employees (such as rules relating to work hours, rest and leave policies, training, etc) and any changes to such rules, are required to be carried out through consultation with the labour union or employee representatives on an equality basis. The relevant rules must be made public or notified to the employees.

2. *Employment contracts*

The LCL recognises three types of employment contracts, namely:

- (i) fixed term contracts (where the date of termination is stated);
- (ii) open-ended contracts (where there is no stated termination date); and
- (iii) project-based contracts.

The LCL clearly reflects a greater

preference for open-ended labour contracts. An open-ended contractual relationship will be deemed to be established between an employer and an employee if the employer does not enter into a written labour contract within one year from the date the employer actually starts using the employee. Further, LCL requires employers to enter into an open-ended labour contracts with employees in certain circumstances (such as the contract is renewed for the third time, continuous employment with the same employer for more than 10 years), unless the employees request otherwise. If the employer fails to enter into an open-ended contract with an employee in violation of the LCL, the employer is required to pay the employee double the monthly wage commencing from the time that the employer should have executed an open-ended contract.

Moreover, if an employer fails to enter into a written labour contract within one month of the employee start date, the employer must pay the employee two times the employee's monthly wage for every month without written contract.

3. *Probation period*

LCL standardises the permissible length of probation periods. The length of the probation period varies according to the length of the labour

contracts, with a maximum probation period of six months. During the probation period, employees are entitled to the minimum wage level specified in the LCL. Employees are required to give three day's notice of termination to employers without reason, while the employers must give valid reasons for termination of employment of employees (valid reasons may be, for instance, incompetence or serious violations of the rules of the employer, etc)

LCL further provides that an employer may not impose more than one probation period on a given employee.

4. *Liquidated damages payable by employee*

LCL stipulates that an employee is liable for liquidated damages in the following situations:

(i) *Training agreements*

If employers provide special training fees for employees to take professional technical training, they may enter into an agreement with the employee requiring employees to commit to work for an agreed period. If the employee resigns before completing the agreed service period, the employer may recoup from the employee liquidated damages which should not exceed the pro-rata share of the training expenses related to

the uncompleted portion of the agreed period of service. However, LCL does not specify the definition of professional technical training.

(ii) Non-competition and confidentiality provision

LCL permits labour contracts to include provisions relating to maintaining the confidentiality of the trade secrets of an employer. This provision is only applicable to employees with a confidentiality obligation such as senior management, senior technical personnel, etc. LCL allows two years as the maximum duration for non-compete restrictions after termination/recission of an employment contract but requires that during this two-year restriction period, the “old” employer shall pay the former employee financial compensation on a monthly basis. However, LCL does not specify the minimum amount of such compensation.

LCL also provides that if the employee breaches the non-compete restriction provisions, he shall be liable to the employer for liquidated damages.

5. Severance pay for employees

LCL broadens the circumstances under which an employer is required to make severance payment to an employee. Compared with the old Labour Law, LCL introduces new circumstances for making severance payment, namely (i) upon expiration of a fixed-term contract unless an employee refuses to renew the contract despite being offered the same/better terms than those in the expired contract; and (ii) termination is due to bankruptcy, suspension of business license, being ordered to close down or premature dissolution.

The amount of severance payment

shall be calculated by reference to the employee’s length of service. The standard severance payment is one month’s wage for each year of employment, where:

- (i) the monthly wage is based on the employee’s average monthly wages for the twelve months prior to cessation of his employment; and
- (ii) any working period of not less than six months but less than one year shall be counted as one year while any working period of less than six months shall be taken as half a year.

However, LCL limits the rate for severance payment to:

- (i) three times the (officially published) average monthly salary of an employee in the city where the employer is located; and
- (ii) the maximum length of service allowed for the purpose of calculating severance payment is 12 years of service.

Termination in violation of the LCL may trigger the right of an employee to be re-employed or give rise to a sum for additional compensation by the employer equivalent to twice the statutory compensation.

6. Redundancies

LCL expands the range of events that justify terminations because of redundancy. Difficulties in production and/or business operations, changes in economic conditions, etc are all circumstances which could be relied upon to justify redundancies.

In summary, LCL has been formulated in order to develop stable and harmonious employment relationships and to promote a sense of stability among employees by giving legal protection to various employee rights and benefits.

However, it is expected that LCL will

have a major impact on the operation of the employer. First of all, an employer may face increased operating costs relating to human resources in order to fully comply with the LCL (such as costs of reviewing and revising if necessary the current employment documents and policies, etc). For certain employers which may not have fully complied with the old law, such cost increases may be significant. Secondly, the employer may have reduced flexibility in choosing its own employment terms for its employees. For example, employers may find it difficult to enter into short term labour contracts with employees because if the same contracts are renewed, the employees have the right to request for conclusion of the open-ended labour contracts. Thirdly, LCL imposes more responsibilities on an employer who breaches an employment contract or LCL. On the other hand, provisions on non-competition and confidentiality should improve protection of the employer’s trade secrets and intellectual property. Fourthly, severance payments are required to be paid to employees in a large number of situations including where the employer is bankrupt. Fifthly, labour unions will play an increasingly important role in employee-related issues such as formulation of corporate rules and termination procedures, etc.

Finally, as certain provisions of the LCL are expressed in general terms and some of the terms are ambiguous, we hope that implementation regulations will be issued in a timely manner so as to assist employers, especially foreign investors, in complying with the LCL. ■

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