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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.

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 by an employer is only possible on specific statutory grounds, which in practice can be difficult to satisfy. In addition to the national level law, there are also local layers of employment law at provincial and municipal level. Local laws are intended to interpret and clarify the national ones by providing more detail. Interpretation and enforcement of the national law can vary, sometimes significantly, from region to region. For example, Shanghai tends to take a more practical and commercial view that is more favourable to employers than most other regions.

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"). An alternative is to have a Representative Office ("RO"). In contrast to a WFOE, an RO has no formal legal identity in China and is far more limited in its permitted activities. 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 (in effect 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 (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 had two consecutive previous fixed-term contracts. However, the two fixed terms rule is applied differently in different locations. For example, in Shanghai 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 at 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 expressly requests another fixed term contract.

Labour dispatch or "agency" type arrangements (where workers are engaged through a third-party agency rather than employed directly) used to be very popular with employers. However, this area has become more regulated and more restricted. The dispatch arrangement can only be used to fill temporary, auxiliary or substitute positions and the total number of dispatch workers must not exceed 10% of the employer's total workforce. These restrictions do not apply to ROs because they cannot hire local staff directly and are legally required to engage staff through agencies.

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

The employment contract

Full-time employees must have written employment contracts in Chinese. The penalties for not putting a written contract in place promptly can be severe. If an employer fails to put in place a 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, handbooks and policies are very important in China to provide additional detail on legal entitlements and organisational expectations. They typically cover issues such as conduct, leave, disciplinary procedures and termination grounds. An employer must follow a consultation procedure before introducing new work rules or changing existing rules. There is no fixed format or set timing for the consultation process, but employers should generally allow one to two weeks. Employees or their representatives do not have a right to veto the employer's proposals but are entitled to provide comments and recommendations which the employer must duly consider. It is critical to undertake a consultation process, otherwise the rules may not be deemed valid and enforceable for the purposes of a dispute.

Key minimum employment rights

Working time and overtime

In principle, all employees are entitled to be paid overtime (or in some circumstances given time off in lieu). However, there are exemptions from this basic requirement under specific working hour schemes.

The standard working hour system is the default system for all employees (and the most common). It provides for standard working hours of no more than eight hours per day and 40 hours per week. Overtime is payable for hours in excess of this, ranging from 150% to 300% of the employee's pay depending on whether the overtime is carried out on a normal working day, rest day or public holiday. Employees generally cannot be required to work more than three hours' overtime per day or 36 hours per month. This is a standard which many employers struggle to comply with in practice.

The flexible working hours system can be used for more senior personnel and allows for regular salary to cover any additional hours worked. The comprehensive hours system allows employees to work longer hours without overtime compensation, provided their average overall working hours fall within the statutory threshold. This arrangement is often used by employers to cover peak demand periods and seasonal or shift work. Employers wanting to implement these systems must first obtain approval from the local labour authority. The exact formalities and requirements vary by location.

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 employee is unable to do so for work-related 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 a basic 98 calendar days' paid maternity leave. Typically, there is also an extended maternity leave entitlement depending on the location. In Shanghai this is currently 30 days with further possible extensions in specific circumstances. Male employees are now entitled to paternity leave in most major cities. The amount varies by location and is currently 7-10 days in Beijing.

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. While the entitlement is designated as medical treatment leave, in practice this applies equally to common illness and complaints such as colds and flu. A reduced rate of pay may apply during medical treatment leave, depending on the duration of the leave and other circumstances. Again, there are location specific nuances and practices.

Wages and social insurance

Employers must pay at least pay the 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 various funds including pension, medical and unemployment insurance. The employer is also required to contribute to occupational injury insurance and maternity insurance funds. The exact funds and level of contributions required vary widely by location and reflect the relative affluence of the place and average incomes. However, there is generally a local or regional cap on the amount of salary used for the purposes of calculating contributions.

Terminating employment

There is no concept of "at will" employment. Employers cannot terminate unilaterally simply by giving notice and must have a ground prescribed by law. In essence, an employer can terminate without notice or severance in certain for cause situations, or with notice (or payment in lieu of notice) in certain other specific and limited circumstances.

The threshold for lawfully dismissing an employee is generally high. For example, statutory grounds that would allow an employer to dismiss an employee for cause include serious neglect of work duties causing substantial damage to the employer, and serious breach of the work rules. Grounds upon which an employer may dismiss with notice include: the employee being incompetent even after training and/or a change of role; inability to return to work after medical treatment leave has expired; and a material change in circumstances which means that performance of the contract is impossible. There is no right to terminate for poor performance unless this can be shown to constitute incompetence.

There is also a right for employers to implement a so-called mass lay-off if they suffer serious financial, technological or organisational issues. This requires a minimum of 20 employees or more than 10% of the employer's workforce. The proposed terminations must be reported to the local labour bureau and a consultation process undertaken with all employees ahead of implementation.

Given the challenges of making lawful terminations, it is common for employers to seek a mutual agreement with employees over termination, involving a settlement package which is in excess of statutory severance and entitlements. Statutory severance is broadly one month's pay per year of service, but with a local cap on pay for this purpose.

Discrimination

China has an array of national legislation and local rules setting out basic principles on discrimination protection. Protected attributes include nationality, ethnicity, race, gender, religious belief, disability, household registration location and certain infectious diseases. Despite these principles, the legislation lacks detail and clear definitions, especially with regard to practical implementation and legal remedies. For this reason, discrimination complaints and claims are not common. Nevertheless, there is societal pressure and increased government focus in this area, with important recent developments in relation to sexual harassment - employers now have clear and express obligations regarding safeguarding, systems, training and investigations. Aside from legal ramifications, reputational risk is also a key factor, with increased sensitivity in connection with allegations relating to foreign companies operating in China.

Protecting the business

Non-compete restrictions of up to two years may be applied to senior staff and other employees who have access to confidential information. In order for a non-compete restriction to be enforceable, an employer must pay the employee compensation on a monthly basis during the restricted period. Under national law the payment must be at least 30% of the employee's salary, although certain locations impose a higher standard. Non-solicitation and non-poaching restrictions are not covered in legislation but are common in practice and generally accepted provided that the restrictions are clear and reasonable.

Although employees have a general duty of confidentiality, it is advisable for employers to include express confidentiality obligations in employment documentation.

Resolving disputes

Employment disputes are common in China, especially given the restrictive nature of the law on termination. Claims generally must be referred to the relevant local arbitration commission in the first instance but can be appealed to the People's court. The time limit for an employee to bring a claim is generally one year from the date that the employee knows or should have known of the alleged infringement. For disputes over remuneration with current employees, the one-year limitation period commences on the date of termination. The labour arbitration system is informal and relatively quick. The law provides that cases should be completed within 45 days of the date that the claim is accepted by the relevant labour arbitration commission, although the process can take longer in practice. Mediation is often encouraged as a first step but is not compulsory.

Employee representation

National level legislation provides that employers should set up a labour union within the company if requested to do so by a specific threshold of employees, although the exact position on this remains uncertain. In certain locations, employers have come under pressure from local authorities to establish unions. If a labour union is established, the employer must contribute an amount equal to 2% of its total payroll in China to that union, many foreign companies seek to resist pressure to establish unions on the basis that they already have sophisticated HR systems and protections for employees.

Data protection

Employment legislation sets out the basic principle that employers have an obligation to keep employee personal data confidential and not make this public without the employee's written consent, but no further detail or guidance. However, the recent new Personal Information Protection Law ("PIPL") now sets out a more comprehensive and universal framework in this area, which will apply to the employment context. Under the PIPL employers must obtain the individual's consent for the collection of personal information, unless they can show that the information is necessary for the performance of the contract or required by law. Technically, consent is also required for the cross-border transfer of personal information, which would include transfers of employee data by multinational companies for HR administration purposes. As this is a sensitive, complex and developing area, companies should consider carefully the documents and procedures they have in place for their China operations.

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