China Employment Law Update

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Annual Leave Rules Clarified

In a notice issued on April 15, 2009, the Ministry of Human Resources and Social Security (MOHRSS) clarified that service with previous and current employers should be counted to determine whether employees have 12 "consecutive months" of service and therefore are entitled to paid annual leave. In practice, this clarification means that employees who have at least 12 months of consecutive service with previous employers will immediately be eligible for paid annual leave with new employers if there is no break in employment between employers.

This clarification conflicts with a Guangdong provincial regulation issued on January 23, 2009, providing that employees are entitled to annual leave only after they have accrued 12 months of service with their current employers.

The MOHRSS notice also specifies what types of documents may be used by employees to evidence service years, such as social insurance payment records and employment contracts.

In a related development, Zhejiang provincial regulations issued on March 31, 2009 give employers the right to extend expired or terminated contracts in order to require employees to use up annual leave and therefore avoid a requirement to pay 200% compensation for unused leave. The Zhejiang regulations also indicate that employees on the flexible working hours system are not entitled to compensation for unused annual leave.

Unions Flex Muscle at Wal-Mart China

Local unions reportedly played a key role in Wal-Mart's scrapping of a plan to eliminate assistant manager positions at all stores in China.

In mid April 2009, approximately 2,000 managers were reportedly offered three options: (a) transfer to a new store (usually in a remote area of the country) at the same salary; (b) stay with the current store but be demoted to a lower position with lower pay; (c) leave the company with a severance package.

The managers considered the proposal to be an illegal mass layoff, and reportedly contacted store branch unions nationwide. Employees at the

headquarters of Wal-Mart China in Shenzhen complained to the local branch of the All China Federation of Trade Unions (ACFTU), and dozens of the affected employees staged a protest at the headquarters. Under pressure from the Shenzhen ACFTU, Wal-Mart China agreed to postpone the implementation of the plan nationwide and to negotiate the terms of the plan with employee representatives under the guidance of the Shenzhen ACFTU. Details of the collective bargaining process were not made public, but on April 17, 2009, Wal-Mart China announced that it had decided to abandon the original proposal.

However, Wal-Mart reportedly has rolled out a new reduction plan. Under this plan, more than 9,000 employment contracts nationwide will not be renewed upon expiration. The affected employees reportedly are mainly those who hold positions that the company plans to eliminate, or those whose performance is unsatisfactory. No further actions from employees have yet been reported, but since fixed-term employment contracts are normally allowed by law to expire without statutory termination grounds, the employees may find it difficult to challenge the company's decision, as long as Wal-Mart has complied with legal and contractual obligations.

Shenzhen Reduces Required Non-Competition Compensation

The monthly amount of non-compete compensation an employer must pay to a former employee in Shenzhen was reduced from two-thirds to one-half of the former employee's average monthly salary pursuant to regulations adopted on May 21, 2009. The reduction was contained in amendments to the Regulations of Shenzhen Special Economic Zone on the Protection of Technical Secrets of Enterprises (深圳经济特区企业技术秘密保护条例).

If an employer fails to make non-compete compensation, the new regulations give an employee the right to demand the unpaid non-compete compensation in a lump sum or to terminate the non-compete agreement. The new regulations, however, do not expressly permit an employer to waive a non-compete restriction at its discretion.

Under the new regulations, an employer who knowingly hires an employee who is under a non-compete restriction may be subject to joint and several liability with the employee for liquidated damages in addition to actual damages for the breach of any confidentiality obligation by the former employee. In addition, administrative fines up to RMB 50,000 can be imposed against the employee and up to RMB 200,000 against the employer.

Overtime Calculation Base Reduced in Shenzhen

Amounts that employers must pay for overtime will likely decrease in Shenzhen as a result of rules passed on May 21, 2009.

Amendments to the Regulations of the Shenzhen Municipality on the Wage Payment Regulations (深圳市员工工资支付条例) will limit the calculation base for overtime pay to the "base wage" only. The Shenzhen regulations currently require employers to include allowances and other subsidies in the calculation base for overtime pay. The amendments will bring the Shenzhen regulations in sync with national law, which limits the calculation base for overtime wages to the base wage (not including allowances and other subsidies).

Senior Managers Automatically Exempted From Overtime in Shenzhen

Senior managers are automatically exempted from overtime requirements in Shenzhen as a result of regulations effective on May 13, 2009. The new rules exempt "senior management personnel" from the need to apply for approval to implement flexible working hours. Among the personnel exempted are general managers, deputy general managers, financial controllers and persons who are defined as "senior management personnel" in a company's articles of association.

The new rules also expand the job positions that are eligible to be approved for flexible working hours system to include employees whose salary exceeds 300% of the city's average monthly salary (which is currently at RMB 3,621) and who can arrange their own working hours and rest time.

Companies in Shenzhen should thus review and amend the companies' articles of association where appropriate, and apply for flexible working hours system.

Enterprise Income Taxes and Individual Income Taxes Can Be Cross Checked

The State Administration of Taxation issued a notice on May 15, 2009, intended to prevent tax evasion by employers. Under the notice, tax authorities can cross-check the salaries and wages claimed by employers for enterprise income tax purposes against withheld individual income taxes.

Companies should ensure that individual income taxes are properly withheld and paid to the local tax bureaus, and that such taxes match up with the salary expenses claimed for enterprise income tax purposes. If there is a huge discrepancy, the tax officials may conduct an on-site inspection of an enterprise to examine and verify the amount of wages paid to employees, or hand over the case to the audit department for a tax audit. Depending on the nature of the case, problems that arise as a result of the inspection will be handled by the state tax bureau or local tax bureaus.

Shanghai Court Rules Base Salary May Not Include Overtime Pay or Social Insurance Contributions

In March 2009, the Changning District Court in Shanghai ruled that an employer may not include overtime pay, or the employer portion of social insurance premiums, as part of an employee's monthly salary. The case involved a real estate company that had signed employment contracts with seven migrant workers, in which the employees agreed that their regular monthly salary would include both overtime claims and their comprehensive insurance premiums. No such contributions were ever made and the seven employees later brought a suit against the company, claiming back payment for overtime pay and social insurance contributions.

The court held in favor of the employees, and ordered the employer to make back payments of overtime pay to the seven employees and to make up social insurance contributions. Employers should thus not try to include overtime pay and social insurance contributions in their employee's regular salary payments.

Court Rules "Foreign Expert" Not Entitled to Full Labor Law Protections

A court in Suzhou reportedly ruled on May 7, 2009, that a Singaporean teacher employed as a "foreign expert" was not entitled to full labor law protections and benefits extended to PRC national employees.

The Suzhou Industrial Park District People's Court relied on the Measures for the Administration of Wages and Living Treatment for Foreign Cultural and Educational Experts (外国文教专家工资和生活待遇管理办法) to reject a claim filed by Sze-Ying Sim against the Suzhou Singapore International School. Ms. Sim had undergone surgery shortly before the expiration of her contract in July 2008. She had reportedly claimed that her employment contract should be extended for the same period enjoyed by PRC national employees who are on medical leave.

Court Clarifies "Equal Pay for Equal Work"

A district court in Jiangsu province recently ruled that the "equal pay for equal work" rule did not require that employees holding the same position be paid equally. Instead, employers are permitted to compensate employees holding the same job differently depending on factors such as their skills and productivity.

An employee, identified as Mr. Hu, filed a work injury claim against his employer, an unidentified machine company. Mr. Xu argued that his insurance benefits should be based not on his own wages (which were close to the minimum wage), but on that of a co-worker, which were substantially higher (by almost 300%). The Haian District People's Court rejected Mr. Hu's claims and ruled that the employer could justify the lower salary and benefits for Mr. Xu, because his abilities and productivity were lower than the other employees.

In a related case in Beijing, employees who were employed by a staffing services company, and seconded to work at Datang International Power Generation, claimed that they were entitled to the same salary as the employees who were directly hired by the power company because there were no differences in their positions, years of service, and productivity. The case was brought before a labor arbitration commission in May 2008, and was reportedly settled.

Nonetheless, the case indicates that employers may be required to offer the same compensation to both directly and indirectly hired employees if both groups of employees perform the same work. Equal pay for equal work for seconded employees is guaranteed under the ECL. Companies that, often for headcount reasons, use agency workers next to direct hires must be prepared to differentiate between these two groups, in order to avoid equal pay and discrimination claims.

Unmarried, Pregnant Employee Cannot be Terminated

A people's court in Zhejiang province found that an unmarried, pregnant employee cannot be terminated on the basis of her violation of China's mandatory family planning rules.

The employee, identified only by the pseudonym of "Xiao Li," was employed by an unidentified company in Zhejiang province. The employee was terminated October 2007, after she informed her employer that she was pregnant, but not married.

A labor arbitration tribunal reportedly upheld her dismissal on the grounds that her pregnancy (as an unmarried woman) violated family planning rules and therefore denied her protection under the Labor Law. In February 2008, the local people's court reversed the arbitration

decision and reinstated Xiao Li, finding that the company did not have statutory grounds to terminate her and that the Labor Law and ECL in fact applied to her. The court reportedly noted that violations of family planning rules could be handled separately from the employment issues.

After the child was born, the unmarried employee was again terminated in September 2008, for being absent without leave. The employee reportedly took an unauthorized leave after her request for maternity leave was denied. In January 2009, the employee sued the company again, claiming that she was illegally denied statutory maternity leave, and was entitled to unpaid salary, severance, and social insurance benefits. After the labor arbitration tribunal ruled partially in her favor, she appealed again to the same people's court.

On appeal, the court found that she again had been unlawfully terminated and awarded her RMB 30,000 in severance. The court ruled that the employee was entitled to maternity leave and social insurance payments, but not her regular salary during such leave period.