

Update On China Labor Contract Law: China Promulgates Implementing Regulations To Labor Contract Law

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The China Labor Contract Law (“CLCL”), which took effect on January 1, 2008, has generated much confusion and controversy among employers since its adoption on June 29, 2007. On September 18, 2008, China’s State Council released the long-awaited Implementing Regulations of the China Labor Contract Law (the “Regulations”), which took effect on the same date. The Regulations have been formulated to resolve legislature ambiguities, clarify uncertainty, and provide practical guidance to the implementation of some controversial provisions in the labor contract law, such as the mandatory written contract requirement, “open-ended” contract, severance pay and compensation.

First, the Regulations strengthen and clarify the mandatory written contract requirement. To establish a labor relationship, an employer must sign a written labor contract with an employee. Under the Regulations, if an **employee** refuses to sign the contract within the first month of employment with an employer, the employer shall terminate the labor relationship. Although the employer must compensate the employee for his or her actual services during that period, it is not required to pay severance pay to the employee. If the employee refuses to sign a written labor contract with the employer more than one month, but less than one year from the date of the employee’s commencement of employment, the employer shall terminate the labor relationship and pay severance to the employee.

If the **employer** fails to sign a written labor contract with the employee more than one month but less than one year from the date of the employee’s commencement of employment, the employer shall be required to pay the employee double wages per month and shall sign a written labor contract with the employee. The time for calculating the double wages per month starts from the next day after a one-month period from the commencement date, and concludes on the day before the written labor contract is signed. If the employer fails to sign a written labor contract with the employee more than one year from the date of the employee’s commencement of

employment, the employer shall be required to pay the employee double wages per month and shall be deemed to have signed an open-ended labor contract with the employee. The employer shall prepare an open-ended written labor contract with the employee immediately.

Second, the Regulations seek to clarify some confusion and misunderstanding on the open-ended labor contract concept and its applications. China's Labor Contract Law encourages the use of open-ended labor contracts. The CLCL entitles an employee who has been employed for 10 consecutive years to sign an open-ended labor contract. The CLCL is ambiguous as to the calculation of the 10-year period. The Regulations make it clear that the consecutive 10-year working period shall start from the date when the employee commences work for the employer, including a service term prior to January 1, 2008, the effective date of the CLCL. Before the Regulations were enacted, some employers transferred their employees among group entities or different affiliates to avoid creation of open-ended contracts because of the 10-year working period rule. The Regulations specifically addressed this by stating that if an employee has arranged to work for a new employer that is not of the employee's own selection, the service term with the former employer shall be counted toward the service term with the new employer.

Some employers erroneously believe that the open-ended labor contract is a life-time contract, or an "Iron Bowl," and cannot be terminated by either party. The Regulations list 13 circumstances where the employee may terminate an open-ended labor contract and another 14 circumstances where the employer may terminate an open-ended labor contract. These circumstances also apply to the termination of a fixed-term labor contract as well as a project-based labor contract. The employer and employee, however, may not agree on other conditions for the termination of the labor contract except for the circumstances listed under Article 44 of the CLCL.

Third, the Regulations provide further clarity on certain issues relating to severance pay and compensation. For example, the Regulations make it clear that an employer shall pay severance pay to an employee who has signed a project-based labor contract when the project has been completed. The monthly wage for severance pay calculation purposes shall include hourly or piece wages, bonuses, allowances, subsidies and other currency incomes. If the average wage of an employee is less than the local standard for minimum wage, the local standard for minimum wage shall prevail. Note that if an employer terminates a labor contract in violation of the CLCL and has paid a penalty to the employee according to Article 87 of the CLCL, the employer shall not be required to pay severance pay.

Fourth, the Regulations clearly state that any disputes in connection with the conclusion, execution, amendment, termination or expiration of a labor contract shall be handled in accordance with the Law on the Mediation and Arbitration of Employment Disputes.

As the Regulations went into effect immediately upon their promulgation, it is

suggested that employers train their senior-level employees and human resources personnel to be familiar with the Regulations and their best practices as soon as possible. Employers should also review and update the employer's internal rules and regulations or human resources policies, especially in the open-ended contract, severance pay and compensation areas.

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