

# A Summary of the Labor Contract Law of the People's Republic of China

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Thirteen years ago, the *Labor Law of the People's Republic of China* ("Labor Law") was released, which is a fundamental law to govern employment relationships between employers and employees in China. The Labor Law has indeed played a very important role in such sector in the past 13 years. However, with the development of the Chinese economy and society, more and more labor issues, which may not be completely or well dealt with under the current Labor Law, have occurred. As a result, a few years ago, the legislative department started to create a new labor law to cope with this situation. After a few rounds of review and revision, the *Labor Contract Law of the People's Republic of China* ("Labor Contract Law") was eventually promulgated by the 28th Session of the Standing Committee of the 10th National People's Congress on June 29, 2007 and took effect as of January 1, 2008. The following is a summary to facilitate your understanding of the Labor Contract Law.

## OVERVIEW

The Labor Contract Law consists of 8 chapters including 98 clauses, which are the General Principles, the Conclusion of Employment Contract, the Performance and Amendment of Employment Contract, the Rescission and Termination of Employment Contract, the Special Provisions, the Supervision and Examination, the Legal Liabilities and the Supplementary. There are three sub-chapters under the chapter of Special Provisions, i.e. the Collective Employment Contract, the Secondment of Labor and the Non-Full-Time Employment.

As compared with the Labor Law and other laws, the secondment of labor and non-full-time employment are systemically covered in the Labor Contract Law. Another key part in the Labor Contract Law is the amendment of the provisions relating to non-fixed-term employment contracts, which is one of the hottest and the most argumentative topics of the Labor Contract Law and even has resulted in a number of lay-offs in China prior to the effective date of the Labor Contract Law.

## Effect on Prior Employment Contracts

Based on Article 97 of the Labor Contract Law, this law has no retrospective effect. Existing employment contracts entered into prior to the effectiveness of the Labor Contract Law shall be performed in accordance with its original provisions. Of course, renewal and amendment of an existing employment contract must comply with the Labor Contract Law.

## CHAPTER 1: GENERAL PRINCIPLES

Like other laws, the General Principles of the Labor Contract Law points out its legislative intention and application scope. According to Article 2 of the Labor Contract Law, this law shall govern the enterprises, individual economic organizations or private non-enterprise units on the one hand, and the employees on the other hand, to establish employment relationships and to conclude, perform, amend, rescind or terminate employment contracts. The conclusion, performance, amendment, rescission and termination of the employment contracts between the government departments, institutions or social organizations and its employees are also governed by this law.

In addition, the General Principles also stipulate the roles of labor unions and the labor administrative departments of the People's Governments at the county level and above. The labor administrative departments of the People's Governments at the county level and above, together with labor unions and employer representatives, shall establish a comprehensive tripartite mechanism for the coordination of employment relationships for the purpose of jointly studying and resolving major issues concerning employment relationships. The labor unions shall assist and guide employees in the conclusion of employment contracts with their employers and the performance thereof in accordance with the law and establish a collective negotiation mechanism with employers in order to safeguard the lawful rights and interests of the employees.

## **CHAPTER 2: CONCLUSION OF THE EMPLOYMENT CONTRACT**

To establish an employment relationship, a written employment contract shall be concluded by an employer and an employee. The employment relationship is established as of the date of employment. A written employment contract must be concluded within a month from the date of employment. If the employer refuses to conclude a written employment contract with the employee, the employer must pay double wages on a monthly basis to the employee during the period without a written employment contract, and if such a written contract has not yet been concluded within a year from the date of employment, a non-fixed-term employment contract shall be deemed to have been concluded between the employer and the employee.

### **Types of Employment Contracts**

Employment contracts are divided into three types by their terms, i.e. fixed-term employment contract, non-fixed-term employment contract and employment contract with the term to expire upon completion of a certain job. Where there is any of the following circumstances, except when an employee proposes to conclude a fixed-term employment contract, if the employee proposes or agrees to renew or conclude an employment contract, the type of employment contract shall be a non-fixed-term contract:

- (1) The employee has consecutively worked for the employer for no fewer than 10 years;
- (2) When the employer initially implements an employment contract system or state-owned enterprise re-concludes the employment contract during its reform restructuring, the employee has consecutively worked for the employer for no fewer than 10 years and there is fewer than 10 years to the date of legal retirement of the employee; or
- (3) The employer and the employee have consecutively concluded a fixed-term employment contract twice and there is no statutory breach situation committed by the employee, the employer and the employee still agrees to renew the existing employment contract.

In addition, as mentioned above, if a written contract has not been concluded within a year from the date of employment, a non-fixed-term employment contract shall be deemed to have been concluded between the employer and the employee.

As a consequence of the conclusion of a non-fixed-term employment contract, without statutory circumstances occurring (as set out in the section of “Rescission by the Employer” below), the employer may not fire the employee, who has a non-fixed-term employment contract with the employer.

### **Probationary Period**

According to the Labor Contract Law, an employer and an employee may agree on a probationary period in an employment contract. Where the term of an employment contract is more than 3 months but less than 1 year, the probationary period may not exceed 1 month; where the term of an employment contract is more than 1 year but fewer than 3 years, the probationary period may not exceed 2 months; where the term of an employment contract is more than 3 years or non-fixed, the probationary period may not exceed 6 months; where the term of an employment contract is fewer than 3 months or to expire upon the completion of a certain job, there shall not be any probationary period. The same employer and the same employee can only agree on a probationary period one time. The probationary period shall be included within the term of the employment contract. Where there is only a probationary period without any other period agreed in an employment contract, such probationary period shall be invalid and construed as the term of the employment contract.

If the employee is shown to be unqualified for the employment requirements or commits certain defaults stipulated by the Labor Contract Law in the probationary period, such as serious violation of the rules of the employer or committing a criminal offence, the employer can rescind the employment contract with explanations for such rescission.

### **Confidentiality and Non-competition**

The employer and the employee may agree in the employment contract on certain confidentiality provisions with respect to business trade secrets and intellectual property. The employer and the employee with the duty of confidentiality may also stipulate non-competition clauses in the employment contract or the confidentiality agreement. Employees with responsibility of non-competition shall be limited to the senior officers, senior technical employees and other employees with a duty of confidentiality. The period of non-competition may be during the period of the employment and for up to 2 years after the termination of the employment contract.

In addition, the employer shall pay the employee compensation during the non-competition period on a monthly basis. Where the employee breaches the provisions of non-competition of the employment contract, he/she shall pay the amount agreed upon as penalty to the employer pursuant to the employment contract.<sup>1</sup>

### **Special Training Expenses**

If the employer provides the expenses for the employee's special training, the employer and the employee accepting the above special training can agree on a certain service period in a separate contract. Where the employee violates the service period provision, he/she must pay a penalty to the employer in accordance with the agreed provision. But the amount of total penalty shall not exceed the training expenses provided by the employer, and the actual penalty paid by the employee shall not exceed the amount of training expenses to be amortized over the unperformed service period.

### **Invalidity of the Employment Contract**

An employment contract shall be invalid or partially invalid under any of the following circumstances:

- (1) A party causes the other party to conclude an employment contract that is contrary to that party's true intention by means such as deception, coercion or taking advantage of the other party's difficulties;
- (2) The employer disclaims its statutory liabilities or denies the employee's rights in the employment contract; or
- (3) Any mandatory provision of laws or administrative statutes is violated by the employment contract.

The invalidity or partial invalidity of an employment contract shall be determined by a labor administration authority, a labor dispute arbitration institution or the People's Court.

## **CHAPTER 3: PERFORMANCE AND AMENDMENT OF THE EMPLOYMENT CONTRACT**

The employer and the employee shall fully perform their respective duties in accordance with the provisions of

employment contract. Where the employer undergoes a merger or separation or otherwise is acquired, the existing employment contract between the employer and the employee shall still be valid and be consecutively performed by the employer who inherits the rights and duties of the former employer. Like other contracts, the employer and the employee may amend the employment contract in writing with mutual consent.

## **CHAPTER 4: RESCISSION AND TERMINATION OF THE EMPLOYMENT CONTRACT**

### **Rescission**

Based on mutual consent, the employer and the employee may rescind the employment contract. Under the following circumstances, an employee or an employer may rescind the employment contract unilaterally.

#### **1. Rescission by the Employee**

The employee may rescind the employment contract unilaterally, where any of the following circumstances occurs:

- (1) The employer fails to provide agreed labor protection or labor conditions pursuant to the employment contract;
- (2) The employer fails to fully and timely pay the employee's remuneration;
- (3) The employer fails to contribute social insurance premiums for the employee pursuant to the law;
- (4) The rule or system formulated by the employer violates the provision of law or regulation, and which damages the employee's interests;
- (5) The employer causes the employee to conclude or amend the employment contract against the employee's true intention by means of fraud, coercion or taking advantage of the employee's unfavorable position; or
- (6) Other circumstances stipulated by laws and regulations.

Where the employee proposes to rescind the employment contract, he/she shall notify the employer with 30 days advance written notice. During a probationary period,

<sup>1</sup> The Labor Contract Law is silent on other forms of relief for employers with respect to the breach of the non-competition provision of the employees other than compensation. However, in accordance with the Anti Unfair Competition Law of the People's Republic of China and the Relevant Provisions of Prohibiting from Infringing Business Trade Secrets, if an employee discloses, utilizes or permits other party to utilize his/her employer's business trade secrets accessed to him/her which breaches the provision of contract or the requirement of confidentiality on business trade secrets, the competent Industry and Commerce Authority can demand such employee to stop the infringement. This is an administrative remedy rather than a judicial one under Chinese law.

the advance notice period can be limited to 3 days. However, where the employer forces the employee to work by means of violence, coercion or illegal restriction of personal freedom, or the instruction of the employer violates the rules of safety operation or the employer forces the employee to work in danger, which endangers the employee's personal safety, the employee may rescind the employment contract immediately without any advance notice.

## **2. Rescission by the Employer**

### **a. Rescission for the Employee's Fault**

The employer may rescind the employment contract unilaterally, where any of the following circumstances occurs:

- (1) The employee is proven not to satisfy the employment criteria during the probationary period;
- (2) The employee seriously breaches the rules or system of the employer;
- (3) The employee commits serious dereliction of duty or practices graft, which causes material damage to the employer;
- (4) The employee has established an employment relationship with another employer simultaneously, which causes material impact on the completion of current work assignment, or he/she refuses to rectify the situation when demanded by the employer;
- (5) The employee causes the employer to conclude or amend the employment contract against the employer's true intention by means of fraud, coercion or taking advantage of the employer's unfavorable position; or
- (6) The employee has been determined to have criminal liability pursuant to law.

### **b. Rescission for Non-Fault**

Where there is any of the following circumstances, the employer may rescind the employment contract with 30 days advance written notice to the employee or by paying the employee an additional 1 month remuneration in lieu of prior notice:

- (1) The employee is ill or non-work-related injured, and upon the expiration of the stipulated medical period, he/she can not engage in the original assignment or other work assigned by the employer;

(2) The employer is incompetent and remains incompetent after training or a position transfer; or

(3) The basic circumstances for the conclusion of the employment contract have significantly changed, which makes the performance of the employment contract impracticable, and the employer and the employee can not agree on the amendment of the employment contract after negotiation.

### **c. Economic Lay Off**

Where there is any of the following circumstances and the employer needs to reduce staff by 20 or more or by a number that is fewer than 20 but accounts for more than 10 percent of all employees of the employer, the employer shall explain to the labor union or all employees 30 days in advance. The employer may reduce the workforce after considering the opinions from the labor union or all employees and reporting the retrenchment plan to the labor administrative authority in charge:

- (1) The employer undergoes restructuring pursuant to the Enterprise Bankruptcy Law;
- (2) The employer is confronted with severe difficulties in production or operation;
- (3) The employer undergoes a switch of production, significant technology change or adjustment of operation mode and there is still a need for reduction even after the amendment of employment contracts; or
- (4) The basic economic circumstances for the conclusion of the employment contract have significantly changed, which makes the performance of the employment contract impracticable.

However, where there is any of the following circumstances, the employer may not rescind the employment contract with such employee as mentioned above:

- (1) The employee has engaged in work exposed to occupational disease hazards without a pre-termination of employment occupational health check or the employee who is suspected to have contracted an occupational disease is still in the period of diagnosis or medical observation;
- (2) The employee has contracted an occupational disease or injury during work and has been confirmed to have lost or partly lost the capacity to work;

- (3) The employee is in the statutory medical period of his/her illness or non-work-related injury.
- (4) The female employee who is in the period of pregnancy, maternity or breastfeeding;
- (5) The employee has consecutively worked for the employer for no fewer than 15 years and it is fewer than 5 years away from his/her statutory retirement age; or
- (6) Other circumstances stipulated by laws and regulations.

When the employer unilaterally rescinds an employment contract pursuant to the above provisions, the employer shall notify the labor union of the reason in advance. If such rescission breaches the law, regulation or provision of the employment contract, the labor union may require the employer to rectify. The employer shall study the labor union's opinions and notify the labor union of its decision in writing.

#### **Termination of the Employment Contract**

Where there is any of the following circumstances, an employment contract shall be terminated:

- (1) The term of the employment has expired;
- (2) The employee is eligible to exercise his/her basic pension insurance entitlement in accordance with the law;
- (3) The employee is dead, or declared dead or missing by the People's Court;
- (4) The employer has been declared bankruptcy pursuant to the applicable law;
- (5) The business license of the employer has been revoked, or the employer has been ordered to close down or has decided to dissolve prematurely; or
- (6) Other circumstances stipulated by laws and administrative statutes.

#### **Compensation for Rescission or Termination of the Employment Contract**

Where there is any of the following circumstances, the employer shall compensate the employee:

- (1) The employment contract is rescinded by the employee unilaterally due to the employer's fault as described above;
- (2) The employer proposes the rescission of the employment contract to the employee and obtains the employee's consent;
- (3) The employer rescinds the employment contract pursuant to the provision of "Rescission for Non-Fault" described above;
- (4) The employer rescinds the employment contract pursuant to the provision of "Economic Lay Off" described above;
- (5) The employment contract has expired, except if the employer agrees to renew the employment contract with the same or better conditions for the employee but the employee does not agree to renew;
- (6) The employment contract is terminated for the employer's bankruptcy, revocation of its license or dissolution; or
- (7) Other circumstances stipulated by laws and administrative statutes.

The amount of the compensation shall be calculated on the basis of the employee's work period for the employer. The standard of compensation is one month's wage for each one year of employment. Any work period of more than 6 months but less than 1 year will be counted as 1 year, and the employer shall pay a half month's wage to the employee as compensation for any work period of fewer than 6 months.

If the employee's monthly wage is more than 3 times the average monthly wage of the preceding year announced by the People's Government of the municipality directly under the Central Government or the municipality divided into districts where the employer is located, the standard for compensation shall be calculated as three times the average monthly wage. The maximum compensation period the employer must pay to the employee is 12 years. The "monthly wage" mentioned above means the employee's average month's wage of the 12 months prior to the rescission or termination of the employment contract.

If the employer rescinds or terminates the employment contract in violation of the Labor Contract Law and the

employee demands continued performance of such employment contract, the employer shall continue to perform it. Where the employee does not make such demand or the continued performance of employment contract is impracticable, the employer must compensate the employee in an amount twice as much as the above compensation standard.

## **CHAPTER 5: SPECIAL PROVISIONS**

### **Collective Employment Contract**

On behalf on all employees, the labor union may conclude a collective employment contract with the employer to stipulate the remuneration, work hours, rest periods and off days, safety and health, insurances and benefits related to the workplace. If a labor union has not been established in the employer, the high-level labor union shall guide the representative elected by all employees to conclude a collective employment contract with the employer.

In regions below the county level, the industrial labor union of construction, mining or catering service etc. may conclude an industrial collective employment contract or a regional collective employment contract with the representative of the enterprise.

The standards of remuneration, work conditions and other conditions stipulated in the collective employment contract shall be no lower than the minimum standards stipulated by the local People's Government, and the standards of remuneration, work conditions and other conditions agreed in the employment contract shall be no lower than corresponding standards or conditions stipulated in the collective employment contract.

The draft of the collective employment contract shall be submitted to the meeting of employee representatives or all employees for discussion and adoption. Upon the conclusion of the collective employment contract, such contract shall be submitted to the labor administrative authority, and if the labor administrative authority has no objection within 15 days from receipt of such contract, the collective employment contract shall forthwith take effect.

A legally concluded collective employment contract shall be binding on the employee and the employer. An industrial or regional collective employment contract shall be binding on the employee and the employer of the locality in such industry or region. Where there

is a dispute raised over a certain standard which is not stipulated in the employment contract or relevant stipulation is not clear, the employer and the employee can renegotiate such standard, but if mutual consent can not be reached, the provision of the collective employment contract with respect to such standard shall govern.

### **Labor Secondment**

A labor secondment company can dispatch its employees to work for other employers. In this case, the labor relationship is established between the seconded employee and the labor secondment company. The labor secondment company shall conclude a fixed-term employment contract with a term of more than 2 years and pay the employee on a monthly basis. During the period in which there is no work assigned to the employee, the secondment company shall still pay wages to the employee on a monthly basis pursuant to the lowest wage standard stipulated by the local People's Government.

The secondment company provides labor secondment service to other employers, and such employers shall be responsible for (1) implementing the state labor standards and providing corresponding work conditions and work protections, (2) informing the seconded employee of the work requirements and remuneration, (3) paying overtime wages, performance bonus and providing welfare in relation to the job positions, (4) providing the seconded employee with requisite training for the job position, and (5) implementing normal remuneration adjustment schedule for the seconded employee in case of consecutive secondment.

In addition, employers for which the seconded employees work may not dispatch the seconded employees to work for others. An employer may not set up a labor secondment company to dispatch employees to itself or its subordinate entity.

### **Non-Full-Time Employment**

Non-full-time employment means employment that is paid on an hourly basis, and the same employee works for the same employer for no more than 4 hours per day in average and 24 hours per week in total.

A non-full-time employment contract can be concluded orally. The employer or the employee can rescind the non-full-time employment contract with a notice to the

other party at any time. The employer need not pay any compensation for the rescission or termination of the non-full-time employment contract.

## **CHAPTER 6: SUPERVISION AND EXAMINATION**

The State Labor Administrative Authority is in charge of the supervision and management of the nationwide implementation of the labor contract system under the Labor Contract Law. The labor administrative authority of the local People's Government of county level or above is responsible for the supervision and management of the implementation of the labor contract system under the Labor Contract Law within its administrative region.

The relevant administrative authorities of construction, health and work safety and etc of the local People's Government of county level or above shall supervise and administrate the implementation of the labor contract system by the employer under the Labor Contract Law within their respective purviews.

The labor union shall safeguard the lawful rights and interests of the employee pursuant to the law and supervise the performance of the employment contract and collective employment contract by the employer. If the employer breaches the law, regulation, employment contract or collective employment contract, the labor union shall provide its opinion or request the employer to rectify. Where the employee applies for arbitration or files a lawsuit against the employer, the labor union shall provide support to the employee pursuant to the law.

## **CHAPTER 7 AND CHAPTER 8: LIABILITIES AND SUPPLEMENTARY**

Where the rules or system formulated by the employer with direct relation to the employee's vital interests violates any provision of law or regulation, the labor administrative authority shall require the employer to rectify and give a warning to such employer. If the violation has caused damage to the employee, the employer shall have compensation responsibility for such damage.

Where the employee rescinds the employment contract in violation of the law or violates the provisions of confidentiality or non-competition stipulated in the employment contract, which causes damage to the employer, the employee shall have compensation responsibility. However, in accordance with Article 25 of the Labor Contract Law, the employer can not agree with

the employee on any penalty on the employee except for the cases of confidentiality, non-competition and special training expenses mentioned above. The employer and the employee can agreed upon a certain amount as penalty for the breach of the provisions of confidentiality, non-competition or service period.

Where the employment contract is deemed to be void pursuant to the law, which causes damage to a party, the other party at default shall have compensation responsibility.

Where an employer hires an employee who has not terminated or rescinded his/her employment contract with the existing employer, which causes damage to the existing employer, such new employer shall jointly undertake the compensation responsibility to the existing employer with the employee.

Where there is any of the circumstances stated below, the labor administrative authority shall require the employer to pay the remuneration, overtime wage or economic compensation to the employee within a stipulated period. If the remuneration is lower than the local minimum remuneration standard, the shortfall shall be paid. If the employer fails to fully pay within the specified time limit, the employer shall pay additional compensation at the rate of 50 percent to 100 percent of the amount payable:

- (1) The employer fails to fully and timely pay the remuneration to the employee pursuant to the provisions of the employment contract or the State rules;
- (2) The remuneration paid by the employer is lower than local minimum wage standard;
- (3) Overtime wage is not paid by the employer for employee's overtime work; or
- (4) The employer fails to pay compensation for rescission or termination of the employment contract pursuant to the provisions of the Labor Contract Law.

Where there is any of the following circumstances, relevant administrative punishment shall be imposed on the employer pursuant to the law. If the case constitutes a criminal offence, criminal liability shall be pursued in accordance with the law. If the employee suffers damage from this case, the employer shall have compensation liability:

- (1) The employer forces the employee to work by means of violence, threat or illegal restriction of personal freedom;
- (2) The employer instructs the employee to work against rules of safety operation or forces the employee to work in danger, which endangers the personal safety of the employee.
- (3) The employer exercises insult, corporal punishment, beating, illegal search or detention over the employee; or
- (4) The working condition is bad or the working environment is severely polluted, which causes serious damage to the physical or mental health of the employee.

The Labor Contract Law came into effect 1 January 2008, but an employment contract concluded and existing before the effectiveness of the Labor Contract Law shall be consecutively performed. The times of the consecutive conclusion of a fixed-term-employment contract, which entitles the employee to propose the conclusion of a non-fixed-term employment contract as mentioned above, shall be counted with effect from the first renewal of such fixed-term employment contract after the effectiveness of the Labor Contract Law.

## CONCLUSION

The Labor Contract Law was created with an inclination to emphasize more liabilities on the employer's side to rectify the situation of insufficient protection for the employee in the past. The Labor Contract Law will have a major impact on the operation of the employer. First of all, the operation cost relating to the human resources of an employer may increase in order to fully comply with the Labor Contract Law, for certain employers, such increase may be significant. Secondly, the flexibility to choose the term of an employment contract, to some extent, will be restricted. For instance, an employer will find it is more difficult to sign a short term employment contract with an employee under the Labor Contract Law, because if the same employment contract is renewed, the employee has the right to demand the conclusion of a non-fixed-term employment contract. Thirdly, more responsibilities will be imposed on the employer who breaches the employment contract or law. Of course, the provisions of non-competition and confidentiality of the Labor Contract Law are positive signals to the employer, which will improve the protection on the business secret and intellectual property of the employer.

With the effectiveness of the Labor Contract Law, the employer has to comply with the new law. It is advisable for employers, especially the foreign invested entities or its investors, to review their current employment documents and policies and revise them if necessary to make sure their compliance with the Labor Contract Law. For example, employers should review and revise their current employment contracts pursuant to the Labor Contract Law. In addition, a well drafted employment system and comprehensive work rules are also highly recommended for the employer. If an employer has no sufficient internal human resource support to deal with such affairs, it is time to enhance it or seek competent external advisors' help as soon as possible.

In addition, as a fundamental law governing the employment relationships, most provisions of the Labor Contract Law are very general. An implementing rule of the Labor Contract Law, which will be more practical, is still in the process of creation. The employers may need to further adjust or specify their employment policies and other legal documents upon the issuance of the implementing rule.

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