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# China Employment Law Update - August 2011

## **Abstract**

This report provides an overview of recent developments in laws and regulations relating to labor and employment law in China.

## **Keywords**

Baker & McKenzie, China, employment law, maternity leave, benefits

## **Comments**

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# China Employment Law Update

People's Republic of China

BAKER & MCKENZIE

August 2011

## New Rules on Maternity Leave Benefits May Increase Costs for Employers

Authorities in Shanghai and Qingdao have each promulgated new rules with regard to the pay during maternity leave, each of which took effect on July 1. These new rules are based on the Social Insurance Law, which stipulates that such compensation shall be calculated and paid on the basis of the average wages of all employees of the same employer in the previous calendar year.

The new rules in both cities provide that while a portion of the employee's compensation will be paid by the social insurance fund up to a capped amount, the employer must pay an additional amount to the employee to make up for the gap between the capped amount the fund will pay and the average wage of all employees at the company ("**Average Company Wage**"). However, existing national regulations and local regulations in both cities also state that female employees are entitled to their full salary during their maternity leave, which meant that previously, employers were responsible for making up the difference between what was paid by the fund and the individual's full salary. Now, even if the employee's individual salary is lower than the Average Company Wage (which is oftentimes the case for young female employees taking maternity leave), the company would be responsible for ensuring that the employee receives the Average Company Wage. Conversely, if the employee taking maternity leave is a highly paid employee, the new regulations appear to state that the company only needs to pay her up to the Average Company Wage rather than her own full salary, but this would conflict with existing national and local regulations. Based on inquiries made with the authorities in each city, the different local authorities currently seem to be handling this apparent conflict differently.

While these rules only apply in Shanghai and Qingdao, since they are based on the national Social Security Law, it is possible that the national or other local governments will promulgate similar rules.

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## Amended IIT Law: Change of Standard Deduction and Tax Rates

The Individual Income Tax Law (“**IIT Law**”) and the Implementing Rules to the IIT Law have been revised effective September 1, 2011.

The main changes to the revised IIT Law and the Implementing Rules are summarized below:

- The standard monthly deduction for Chinese individuals’ employment income is increased from RMB 2,000 to RMB 3,500.
- The standard monthly deduction for expatriates’ employment income remains unchanged at RMB 4,800.
- The progressive tax rates applicable to salaries and wages will change from the current nine brackets to seven brackets.
- The monthly IIT reporting deadline is extended to the 15th day after the end of a month from the current 7th day.

The revised IIT Law reflects a policy of mitigating the tax burden of “low and middle income individuals”. To a certain extent, high income individuals may be subject to a higher tax burden. It is evident that the China tax authorities are continuing to strengthen IIT administration and collection in relation to investment income. Further IIT reform is expected.

For more information on these amendments please see Baker & McKenzie’s China Tax Monthly update which can be accessed via [this link](#).

## New Developments on Hot Temperature Subsidy Requirements

In June, national government authorities and the All China Federation of Trade Unions issued a notice requesting authorities at all levels to inspect and supervise the protection of employees’ rights in hot weather, with particular focus on enforcement of the hot temperature subsidy (“**Subsidy**”) requirement. Under existing national and local regulations, employers are required to pay the Subsidy to employees who work outdoors or otherwise in a hot temperature workplace during summer.

On July 1, Shanghai issued new regulations under which employers must pay eligible employees a high temperature subsidy of RMB 200 per month from June to September each year regardless of actual temperatures during those months. In the past, eligible employees were entitled to the Subsidy at a rate of RMB 10 per day for each day of high temperature.

Guangdong Province issued draft measures on August 9, under which employers may be fined up to RMB 20,000 if they continue to fail to pay the Subsidy after the local labor bureau orders them to do so. However, these draft measures have not yet been finalized and passed.

## Company's Unilateral Termination Rescinded for Failure to Notify Union

In August 2011, a Court in Yancheng City, Jiangsu Province reportedly ruled a public transportation company's (the "**Company**") unilateral termination of a vehicle attendant (the "**Employee**") unlawful for failing to notify the labor union prior to the actual termination pursuant to Article 43 of the Employment Contract Law.

During an inspection, a Company officer discovered that the Employee had sold two invalidated tickets with a face value of 1 RMB each to passengers. Based upon internal Company rules (which were voted on and passed by the Company's employee representatives), the Company unilaterally terminated the Employee. The Court held that, although the Company's internal rules were binding, the termination was still unlawful because the Company failed to notify the union. Article 43 of the Employment Contract Law requires an employer to provide notice to the union prior to any unilateral termination of an employee. (The case report was not clear whether the Company had its own union or whether it was required to notify the upper level branch of the All China Federation of Trade Unions).

This case demonstrates that, although companies may have valid substantive reasons for terminating an employee in China, procedurally, they still must notify the labor union prior to terminating an employee. Otherwise, companies risk having their termination decision overturned in court.

## Court Adopts Broad Definition of Employees Exempt from Overtime

On July 25, 2011, the Shanghai Jing'an District Court reportedly rejected an employee's claim for overtime payment, based on his senior management status and the flexible working hours provision in his employment contract.

The employee's employment contract stated his position as Supply Chain Manager of a cosmetics company, and his monthly salary was RMB 25,000. The employment contract also provided that Mr. Jiang was subject to the flexible working hours system (and therefore not entitled to overtime pay), based on his senior

management status. The company had obtained approval from the local labor bureau for “senior management” to be subject to flexible working hours. In response to the employee’s claim that he was not a senior manager, the court ruled that the employee failed to provide sufficient evidence to prove that he was not a senior manager, and further commented that he should not be taken as a regular employee taking into account the amount of his monthly salary and his job level. The court also relied on the fact that the employment contract stated he was a senior manager.

The definition of “senior management”, for flexible working hours purposes, is not clear under national law and oftentimes approval certificates issued by the labor bureau will not detail all the different types of positions within the company that may be covered. A few local regulations (e.g., Shenzhen) provide that the definition should follow the narrow definition under the Company Law (e.g., the general manager, the deputy general manager and CFO), and many local labor bureau officials informally hold the same position. However, in this case, the court adopted a broader definition of senior management for flexible working hours purposes, based on the amount of the employee’s compensation, his job level, and the wording in his employment contract. Companies therefore, where possible, should ensure that employment contracts with personnel who may qualify for flexible working hours status are properly worded to ensure the employee is exempt from overtime.

## Court Rules Summary Dismissal Unlawful Despite Being Based on Company Rules

In July 2011, the First Intermediate People’s Court of Beijing Municipality ruled in favour of an employee who was dismissed by Carrefour, a supermarket chain, for alleged serious violation of the company’s rules and policies.

Mr. Li, a former employee of Carrefour, was found to have input incorrect financial information into the company’s accounting system in violation of the company’s working procedures, and also wrongfully gave access to the company’s database to unauthorized colleagues. He was summarily terminated without severance pay for serious violation of the company’s policies.

The court ruled that though Mr. Li committed misconduct, Carrefour failed to prove any serious economic loss or harm it suffered, and thus ruled the dismissal decision as unreasonable and therefore unlawful. As a result, the court ordered Carrefour to pay Mr. Li a penalty for the wrongful termination at an amount equal to RMB 69,540.

The case shows that even if a termination is based on the company's written policies, many courts will still scrutinize whether the termination and the company's policies whereupon the termination is based are reasonable. Companies should therefore ensure that termination grounds listed in their rules and policies are reasonable and assess the seriousness of an employee's misconduct before proceeding with a termination.

## Demotion of Employee with Poor Performance Ranking Held Illegal

In August 2011, the Jing'an District People's Court of Shanghai reportedly affirmed the ruling of a Shanghai labor arbitration commission in favour of an employee who was demoted and had his pay reduced after receiving the lowest performance ranking among all mid-level staff. The court ordered the employer, a property management company, to back pay RMB 8,000 to the employee, which represented eight months of underpaid salary after the employee was reassigned to another post.

In the reported case, the employer argued that it should be able to reassign the employee for poor performance based on the fact the employee had received the poorest ranking among employees at his level in various performance evaluations. The Court, however, found that the employer was unable to submit sufficient evidence to prove the employee's failure to fulfil job assignments and the performance evaluation scores the employee received showed that he had passed the performance evaluations; the only issue was that such scores were lower than the scores received by others. As a result, the Court held that the demotion and salary decrease were illegal. However, taking into account that the employee had reached the age for retirement, the Court did not order reinstatement but merely ordered a back payment of the underpaid salary through the employee's retirement age on May 1, 2011.

This reported court ruling shows the difficulties of demoting employees, especially with a salary decrease. Also, the court ruling indicated the importance for employers to carefully keep records of actual performance results in relation to assigned tasks if they plan to demote or terminate an employee for poor performance.

## Termination for Employee's Refusal to Get Second Medical Check-Up Held to be Unlawful

In July 2011, the Changning District People's Court in Shanghai ruled that the termination of an employee who refused to get a second opinion on her illness at a company approved hospital constituted wrongful termination.

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The employee had repeatedly tendered sick leave notices for five different and unrelated causes of illness following the company's relocation. To confirm the veracity of the alleged illness, the company requested that another staff member accompany the employee to have a second medical check-up at the company's designated hospital. The employee refused. The company then unilaterally terminated the employee on the grounds that the employee's refusal to have a second medical check-up rendered her sick leave unauthorized, and thus the employee's extended sick leave constituted unauthorized leave of absence which seriously violated the company's rules and policies.

The Changning District People's Court held that it was unreasonable for the employer to unilaterally require the employee to undergo a second medical check-up, since the employee had submitted her medical history, clinic invoices, and sick leave notices chopped by a legitimate hospital. There was no indication in the report whether the company's policies had specific provisions requiring the employees to go through a second medical check-up at the request of the company.

In practice, employees claiming sick leave oftentimes can get a doctor's note even when they are not truly sick, and in this way get protection from termination. Companies should therefore consider including language in their employee handbooks giving companies the right to demand a second opinion; while the enforceability of such provision is not clear under the law, it at least puts the company in a stronger position to make such demand than if the company has no written basis at all to assert such right.

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