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## China Employment Law Update - April 2014

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# China Employment Law Update - April 2014

## **Abstract**

[Excerpt] The government of the southern province of Guangdong publicly issued draft Collective Bargaining and Collective Contract Regulations, which, if passed into law, would grant employees a right to strike in certain circumstances.

According to the draft regulations, if no less than 1/3 of all employees or employee representative council members demand that a collective bargaining process be initiated, the company union or (if the company has no labor union) the upper level union should send a written demand to the management for collective bargaining. The management must respond to such demand within 20 days after receipt of the demand notice. If the management fails to respond or refuses the demand for collective bargaining without justification, and the employees go on strike, then the employer may not terminate the striking employees. This would put further pressure on companies to engage in good-faith collective bargaining with employees if and when such a demand is made by the company union or other employee representatives.

However, if the management agrees to collective bargaining, and during the collective bargaining process some employees strike or engage in other disruptive activities, e.g. blocking entrances or exits of the company's facility, then such employees can be terminated if their conduct is defined as serious violation of company rules in the company's legally adopted rules or policies.

## **Keywords**

China, employment, unions, organization, employee rights

## **Comments**

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# China Employment Law Update

People's Republic of China

BAKER & MCKENZIE

April 2014

## Draft Guangdong Regulations Grant Employees Right to Strike in Defined Circumstances

The government of the southern province of Guangdong publicly issued draft Collective Bargaining and Collective Contract Regulations, which, if passed into law, would grant employees a right to strike in certain circumstances.

According to the draft regulations, if no less than 1/3 of all employees or employee representative council members demand that a collective bargaining process be initiated, the company union or (if the company has no labor union) the upper level union should send a written demand to the management for collective bargaining. The management must respond to such demand within 20 days after receipt of the demand notice. If the management fails to respond or refuses the demand for collective bargaining without justification, and the employees go on strike, then the employer may not terminate the striking employees. This would put further pressure on companies to engage in good-faith collective bargaining with employees if and when such a demand is made by the company union or other employee representatives.

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In a related development, the Ministry of Human Resources and Social Security, the All-China Federation of Trade Unions, and the All-China Association of Enterprises recently issued a notice requiring their local counterparts to enhance efforts to initiate collective bargaining with companies. The goal set out in the above notice is that no less than 80% of all employers in China shall have established collective bargaining mechanisms and begun conducting collective bargaining with employees. This notice and the above Guangdong draft regulations indicate a trend that the Chinese government is trying to use collective bargaining as a tool

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to increase workers' wages and welfare benefits. Another purpose of the government's push for collective bargaining may be to use it as a tool to reduce the tension in labor relations, and thus reduce the number of strikes and other forms of labor unrest. According to China Labor Bulletin, a labor rights group, the number of strikes during the first quarter of 2014 increased by 31% as compared to the first quarter last year.

## Recent Local Developments in Enforcement of Labor Dispatch Rules

Following the Provisional Regulations on Labor Dispatch issued by Ministry of Human Resources and Social Security, which took effect on March 1, 2014 ("**Labor Dispatch Regulations**"), a number of cities and provinces have issued local measures to administer the use of labor dispatch. The Labor Dispatch Regulations require companies that exceed the maximum cap on the use of dispatched employees (10% of the total workforce) to reduce their use of dispatched workers to below the legal threshold within two years (i.e. by February 28, 2016), and that such companies file a "workforce adjustment plan" with the local labor authorities.

The Beijing labor authorities were the first to issue measures related to such workforce adjustment plans on March 10, 2014. They require companies that use labor dispatch employees in excess of the 10% cap to file a "workforce adjustment plan" with the labor authorities by August 31, 2014. The Beijing measures provide some guidance on what should be in the plan such as information on total workforce, number of direct hires, number of dispatched employees, percentage of dispatched employees, plans to reduce use of dispatched employees, etc. The measures require that the labor bureau issue a recordal receipt within 5 business days upon receipt of the companies' plans. This may implicitly provide the labor bureau a "quasi-approval" right with respect to the content of such plans. However, neither the Labor Dispatch Regulations nor the Beijing measures specify any penalties or other consequences for not submitting a workforce adjustment plan by the deadline, so it remains to be seen how strictly this will be enforced.

The Beijing measures likely are being reviewed by other cities / provinces. A handful of other cities / provinces have already issued their own measures related to submission of a "workforce adjustment plan" by a certain deadline, such as Hebei Province

(by August 31, 2014), Fujian Province (by August 31, 2014); Shanxi Province (by December 31, 2014); and Guangdong Province (by June 30, 2014). However, most of these local measures do not provide as much guidance or detail as the Beijing measures, and none stipulate any penalties for not meeting the stipulated deadlines.

In some locations (such as Guangdong and Hunan Provinces), the local notices require that labor authorities closely monitor the use of outsourcing arrangements and prevent “disguised” labor dispatch arrangements. Therefore, companies that plan to use outsourcing arrangements (i.e., arrangements for services rather than labor) should carefully review the business structure with their service vendors to ensure that such structure would not expose the company to legal risks.

## Draft Regulations on Employee Service Inventions May Dramatically Increase Compensation Costs for Employers

On April 1, 2014, the State Intellectual Property Office (“**SIPO**”) released the latest draft regulations on employee service inventions (“**Service Invention Regulations**”) pending approval by the State Council.

The draft Service Invention Regulations have kept many of the controversial provisions from an earlier draft issued in 2012. The most noteworthy one is that, under the Service Invention Regulations, even if an invention is not granted a patent but is treated as a technology secret or knowhow by the employer, the employee inventor(s) are still entitled to receive reward and remuneration by reference to the requirements for a normal invention patent. In contrast, the current PRC Patent Law and its implementing rules only require compensation for patented inventions.

Another significant set of provisions is the large increase in the compensation payable by employers. For instance, in the absence of an agreement or company policies, the minimum reward payable to the employee inventor(s) would be twice the average monthly salary of all the employees of the employer, in contrast to the RMB 3,000 under the current regulations. Likewise, the annual remuneration payable to the employee-inventor(s) would be increased from 2% of the operational profits to 5%. The percentage

of any license fees derived from the invention that are payable to the employee inventor(s) are also significantly increased.

On the other hand, the draft Service Invention Regulations seem to indicate that companies can pre-empt the default requirements on service invention compensation by reaching agreements with employees or implementing their own policies, provided that the agreements or policies do not deprive employees of their legitimate rights nor set unreasonable conditions on the employees' claim for and use of such rights. Only in the absence of an agreement or policies would the statutory default compensation rules apply.

In light of the potential increased compensation requirements, companies have an even greater impetus to reach agreements with employees or adopt company policies regarding employee inventor compensation, so as to have more control over compensation costs for service inventions.

## Termination Without Notice to Labor Union Ruled Lawful in Chongqing

In a recent case reported on April 10, 2014, The First Intermediate People's Court of Chongqing ruled that a company's unilateral termination of an employee without notice to a labor union was lawful. The People's Court ruled that the Employment Contract Law requirement to notify a company labor union of the reasons for a unilateral termination is inapplicable if a company has yet to establish a company labor union among its employees.

An employee in Chongqing abused and assaulted one of his colleagues during a dispute. According to the employer's company policy, the employer could unilaterally terminate the employee for this behavior. The employer terminated the employee under Article 39 of the Employment Contract Law for seriously violating company policy. However, the employer did not notify a labor union of the unilateral termination, because no company union had been established.

After being unilaterally terminated, the employee sued the employer for illegal termination. The employee claimed that the employer failed to provide advance notify to a labor union of the reasons for unilateral termination as required under Article 43 of the Employment Contract Law and a Supreme People's Court guiding opinion ("**SPC Opinion**"). Additionally, the employee argued that the SPC Opinion directs the People's Court to order

compensation for the employee if the employer fails to notify the labor union in advance of the unilateral termination and fails to make remedial notification to the labor union of the termination before the employee brings a suit, even if the unilateral termination satisfied all other legal requirements.

The Yubei District People's Court and the Chongqing First Intermediate Court both dismissed the employee's claim for compensation. The Chongqing First Intermediate Court ruled that an employer is not required to establish a labor union. Therefore, the employer is not required to notify a labor union in order to unilaterally terminate an employee if the employer has not established a labor union.

This case shows that the People's Courts in Chongqing do not require employer notification to a labor union to unilaterally terminate an employee if the employer has not established a labor union. However, courts in other cities might still require some form of labor union notification. For example, a court might require an employer to notify an upper level labor union, e.g. a district-level labor union, of the reasons for unilateral termination if the company has not established a company labor union.

## Employee Ordered by Court to Terminate Employment in Fulfilment of Post-termination Non-Compete Obligation

The Taizhou Intermediate People's Court reportedly affirmed the lower court ruling, ordering an employee under a post-termination non-compete obligation to terminate her current employment relationship (as it was with a competitor of her former employer) and pay liquidated damages in the amount of RMB 80,000.

In this case, the employee formerly worked at a commercial bank as a finance relationship manager. The bank signed a confidentiality and non-compete agreement due to her access to confidential information concerning enterprise loans. Under the non-compete agreement, the employee would be subject to a two-year post-termination non-compete restriction during which period she would be restricted from working at any other bank or similar organizations. The bank agreed to pay non-compete compensation, the annual amount of which equalled one third of the employee's total annual income in the last year of employment. In addition, the

non-compete agreement stipulated that in the event of a breach, the bank has the right to demand the employee to continue to perform the non-compete obligation by leaving her employment with any other bank or similar organizations. After the employee resigned, the bank started to pay her non-compete compensation. However, the employee soon joined another bank and refused the bank's request to perform the non-compete obligation.

This case reveals that at least some courts are willing to vigorously enforce non-compete restrictions if the clauses such as the definition of competitor company, the amount of non-compete compensation and the remedy that the company can seek, are well drafted. It is notable that the court ordered both liquidated damages and provided injunctive relief in the form of ordering the employee to terminate her current employment. In the past, courts oftentimes would only grant monetary relief in a non-compete case and take the position that they did not have the authority to order an employee to terminate her current employment. It still remains to be seen whether other courts will also be willing to order this type of injunctive relief, including preliminary injunctive relief, in non-compete cases.

## Beijing Court Rules HR Director Automatically Exempt from Overtime Pay Requirements

In a recently reported case, a Beijing court ruled that a company was not required to pay overtime compensation to its HR director.

The employee joined the company as HR director with a monthly salary of RMB 10,000. Before the Beijing court, the company admitted the employee did work overtime on weekends. However, the company argued as follows: (i) the employee's position as HR director made her a part of the company's senior management; (ii) senior management are automatically subject to the flexible working hours system ("**FWH System**") under local Beijing regulations; and (iii) therefore the employee was not entitled to overtime pay. The court supported the company's argument.

In most cities, an employer must receive approval from the local labor bureau to implement the FWH System for its employees (regardless of the level of the employees). However, Beijing rules explicitly provide that senior management are automatically treated as employees under the FWH System (i.e., the company is

not required to apply for approval to implement the FWH System for its senior management). “Senior management” is not clearly defined under the Beijing rules. In practice, officials in various Beijing district labor bureaus have expressed different opinions on what constitutes “senior management”; some of these officials have even interpreted “senior management” to include only the general manager of a company. However, this case indicates that some Beijing courts might deem an HR director with a relatively high salary to be “senior management”.

## Employer Ordered to Pay Statutory Severance for Asking Employee to Work from Home

In March 2014, the Suzhou Intermediate People’s Court recently upheld a sales employee’s statutory severance claim of RMB 25,830. In this case, the company issued a notice of change of work location to the employee, which required the employee to work from home, and to return all company property. The employee’s base salary was RMB 3,000, and his sales commission was determined based on his sales performance (the amount of which was agreed to be no less than RMB 250,000 per year). After receiving the notice, the employee terminated his employment contract and demanded statutory severance.

The judge pointed out that the company’s home-based arrangement rendered the employee unable to work as a sales employee. Even though his base salary remained unchanged, his total salary would be materially affected since his main income source was from sales commissions. Therefore, the court ruled that the company failed to provide labor protections or conditions in accordance with the employment contract, and thus ordered the payment of statutory severance.

As a strict legal matter, an amendment to an employment contract (especially change of any material terms of the contract, including the employee’s work location) requires the employee’s consent. However, in judicial practice, if the employee is fully paid, he/she is generally not able to claim for financial damages and/or statutory severance simply for being instructed not to come to the office. This case shows that the court probably would pay attention to the employee’s total salary structure, not just the base salary, when determining whether the employee is fully paid.

Should you wish to obtain further information or want to discuss any issues raised in this newsletter with us, please contact:

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## Procedural Defects in Leave Application Do Not Constitute Ground for Summary Dismissal

In a recently reported case, the court ruled in favor of an employee who took annual leave without obtaining the employer's approval and was then terminated by the company for job abandonment.

According to the report, on December 9, 2012, the employee submitted his leave application along with a copy of a doctor's note to the company. In the leave application form, the employee checked "Annual Leave" but not "Sick Leave," because as testified by the company's HR manager, the company normally allows its employees to take accrued but unused annual leave when they need to take time off due to sickness. On December 10, 2012, however, the employee's department manager rejected the leave application. The company then terminated the employee for three days' unexcused leave of absence from December 10 to 12, 2012, which according to the company, constituted a serious violation of the company's rules and policies.

The court ruled that because the employee has submitted the leave application and supporting documents for taking time off for sickness, the employee's leave should not be treated as job abandonment; rather, in accordance with the company's common practice, the company should treat the employee's leave application as one for sick leave rather than for actual "annual leave," and should approve such leave as it usually does. Further, the court ruled that the company's termination is wrongful as it invoked the statutory ground of "serious violation of company rules and policies," while the company failed to prove that the employee was made aware of such rules and policies. As such, the company was ordered to pay the employee wrongful termination compensation in the amount of approximately RMB 286,000.

This case shows that courts may take a company's common practice as its unwritten "rule" and apply such "rule" when ruling on cases. Also, companies should keep careful records of its employment policy adoption procedure, especially proof that all employees have received notice of the company's policies.

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