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# China Employment Law Update - December 2006

**Abstract**

An update in ongoing developments regarding labor relations and employment in China.

**Keywords**

China, labor law, employment, public policy, labor relations

**Comments****Required Publisher Statement**

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# China Employment Law Update

People's Republic of China

BAKER & MCKENZIE

December 2006

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## Employment Contract Law Postponed

Continuing controversy and extensive revisions are the likely reasons the Employment Contract Law (劳动合同法) was not included on the legislative calendar for the October meeting of the Standing Committee of the National People's Congress (NPC). The law has also not been announced for consideration during future sessions of the Standing Committee.

Expectations are that approval of the law may be delayed until a full session of the NPC convenes in March 2007.

The last draft of the law to be made publicly available was released in March 2006. Reports indicate that subsequent drafts have been revised to generally favor the interests of employers. For example, the role of labor unions has been reduced and the grounds for terminating employees have been expanded. The draft also carves out an exemption for senior managers. Thus, it may be possible to employ senior managers on an "at-will" basis.

Recent drafts of the law, however, still require employers to pay severance to employees in the event that fixed-term contracts are not renewed.

Significant changes are also expected regarding the permitted length of probation periods and the enforceability of training contracts.

The proposed law would be China's first national law specifically governing employment contracts.

## Goals for Labor Relations Announced

On October 13, the State Council announced that the legislative priorities in the 11th Five-Year Plan include amending the Labor Law (劳动法), and enacting the Employment Contract Law, Employment Promotion Law (促进就业法), Social Insurance Law (社会保险法) and Labor Dispute Settlement Law (劳动争议处理法). The Five-Year Plan covers the years 2006-2010.

The Five-Year Plan emphasizes the use of mediation to address a forecasted increase in the number of labor disputes. The plan also calls

for the creation of regional and industry mediation committees and the strengthening of enterprise mediation committees as well as an overall increase in the number and quality of labor arbitrators.

The Five-Year Plan also aims to expand the use of collective employment contracts covering employees from multiple companies on a geographic and industry-wide basis. These contracts will be negotiated under the “tripartite coordination mechanism”, which refers to the involvement of representatives from trade unions, labor bureaus, and employers.

## **Shanghai Issues Sexual Harassment Rules**

On September 30, the Standing Committee of the Shanghai People’s Congress issued proposed regulations regarding sexual harassment. The proposed regulations aim at implementing the Law on the Protection of the Rights and Interests of Women (妇女权益保障法), which was amended by the national government in 2005.

The 2005 amendment of the law represented the first effort in China to outlaw sexual harassment. The amendment, which targeted both employment and non-employment related sexual harassment, was faulted for being ineffectual due to its failure to define behaviors that constitute sexual harassment.

The proposed Shanghai regulations state that sexual harassment can occur through speech, words, images, electronic information and physical contact. The regulations, however, fail to provide a detailed definition or examples of proscribed behaviors.

The proposed regulations also require that employers not only investigate complaints from female employees, but also take steps to prevent sexual harassment. The regulations do not provide further details on what types of preventative measures may be required or what penalties may be imposed on employers who fail to comply. However, it is conceivable that female employees will be able to sue employers for damages if employers fail to take measures to guard against harassment in the workplace.

On October 1, similar local regulations came into effect in Hunan province.

## **High-income Individuals Required to File Annual Tax Returns**

Individuals earning more than RMB 120,000 (US\$15,000) a year will be required to file annual tax returns, the State Administration of Taxation announced on November 6. Annual returns for the 2006 tax year will be due by March 31, 2007.

The rules are intended to increase collection of individual income tax by requiring persons to declare their incomes from all sources.

The filing requirement applies to PRC nationals as well as foreign nationals who have resided in China for more than one year and are otherwise subject to PRC individual income tax. Foreign nationals have to declare only income that is taxable in China unless they have resided in China more than five continuous years, in which case they are subject to tax on worldwide income.

PRC nationals employed outside of China are subject to the annual reporting requirement and remain liable for tax on their worldwide income.

The new reporting rules do not affect the obligation of employers to withhold individual income tax on a monthly basis. The annual returns will not permit consolidation of income and calculation of income tax on an annual basis.

Fines of up to RMB 10,000 may be assessed for failure to file a return. Filing false returns may result in fines of up to RMB 50,000 in addition to penalties of up to five times the amount of any tax due.

## **Employees on Supervisory Boards Required for Some FIEs**

Foreign-invested enterprises (FIEs) established after January 1, 2006 may be required to include employees on company supervisory boards. The requirement is a result of a September 22, 2006 interpretation of the State Administration for Industry and Commerce confirming that FIEs are subject to a PRC Company Law requirement to establish a supervisory board.

Supervisory boards are intended to serve a watchdog function to oversee company management and boards of directors.

The Company Law requires that supervisory boards have at least three members, at least one-third of whom must be “democratically elected” by the employees of the company.

FIEs with only one investor may appoint a single supervisor in lieu of a supervisory board. In such cases, the single supervisor may be appointed by the investor without any requirement of employee representation.

## **Court Rules Issuance of Employee Handbooks Must Follow Required Procedures**

An Intermediate People’s Court in Nantong, Jiangsu ruled in September that an employer could not rely upon a provision in an employee handbook to deny an employee an annual bonus because the employer had not followed required procedures when issuing the handbook.

The case was brought against Meiya Power Company Ltd. by a Canadian national, who was employed as a senior manager. The employee resigned before the end of his 19-month contract, but demanded that Meiya pay him an annual bonus. His contract entitled him to an annual bonus, but provided that Meiya would determine the amount in accordance with his performance.

Meiya refused to pay him any annual bonus, arguing that the company's employee handbook required employees to be employed at the end of the calendar year in order to be eligible for a bonus.

The court ruled that the handbook requirement was unenforceable because the company had not adopted the handbook in accordance with "democratic procedure". Although the court did not define the required procedure, it is commonly understood to mean that an employer should obtain the consent of employees or employee representatives, or at least provide prior notification to employees along with the opportunity for them to comment.

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