

# Salans News

## Employment Law China

### December 2010



#### Social Security Law

At the end of October the long-awaited Social Insurance Law was promulgated, and is set to take effect on July 1, 2011. The law primarily aims to prevent the improper use of social security funds. The Social Insurance Law stipulates a general right for all citizens to access and enjoy five categories of insurance: pension, medical, work-related injury, unemployment and maternity insurance. It also allows employees to transfer their pension insurance accounts from one place of residence to another, and includes a basic pension coverage for rural residents.

The final provision of the law stipulates that foreigners working in China must also pay social security contributions. With China's economy and society becoming more open, this regulation is regarded as following international practice and providing equal treatment. According to the Ministry of Human Resources and Social Security, it intends to conclude social security agreements with more countries to regulate the insurance situation for expatriates. China currently has agreements with Korea and Germany. As currently many local funds are not prepared to receive payments from foreigners, it remains to be seen how they will implement these regulations and which insurance categories will be open to foreigners.

Employers are well advised to prepare for future payment obligations for foreign employees as this will certainly have a financial impact. The current contributions for all amount to approximately. 35 to 40 % for the employer and 10 to 15 % for the employee; the maximum contribution basis is calculated based on three times the respective local average salary (e.g., Beijing: RMB 12,111, Shanghai: RMB 10,698, Suzhou: RMB 10,065 Shenzhen: RMB 11,682).

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## Raising Retirement Age?

In September, the government reported its considerations on increasing the current retirement age ( 60 years old for men, 50 years old for women and 55 for females on management or technical positions).

Shortly thereafter, the Shanghai Bureau of Labour and Social Security issued regulations on raising the age threshold for drawing a pension (“Interim Regulations”). According to the Interim Regulations, upon reaching requirement age employees may choose – and agree with their employer - to postpone their pension to an older age (65 for male at the latest; 60 for female at the latest) subject to meeting the requirements for pension drawing and filing formalities.

However, the labour contract ends when the employee reaches the statutory retirement age. Companies and elder individuals may conclude a work contract to specify these rights and obligations as well as termination issues. The Interim Regulations require companies to comply with labour standards such as working time, labour protection, minimum salary, etc. Also, contributions to pension and work-related injury funds are required. It is therefore the employee who mainly benefits from this policy, as companies can always hire pensioners based on a service agreement. (Please refer to our newsletter of March 2010 for details of such “employment”.)

Although the Interim Regulations do not raise the retirement age, continuous contributions to pension after retirement remain possible; this could be an interim step before retirement age is finally raised.

## PE risks in Foreign Employment

In the last year, the trend to localization was strengthened by the tax authorities’ view on dispatched foreign employees which created a fear of establishing Permanent Establishments (“PE”) in China. The recently issued interpretations for the China-Singapore double taxation agreement (“DTA Interpretations”) by the PRC State Tax Bureau may provide guidance on foreign employment. The criteria stipulated in the DTA Interpretations also apply to other DTAs as long as the specific provisions are the same, which is generally the case for various DTAs in terms of PE issues involved in dispatching expatriates, including those with Germany, U.S. France, Spain, Korea, etc.

Under the DTA Interpretations, by dispatching employees, an overseas company may establish a PE in the PRC if the expatriate works for the

overseas company instead of its Chinese subsidiary. The expatriate will be considered as working for the Chinese subsidiary under any of the following conditions:

- the overseas company has the right to direct expatriats' work and bears relevant risks and liabilities;
- the overseas company decides on the headcount and qualification of the expatriates to be dispatched to the Chinese subsidiary;
- the overseas company bears costs of the expatriate's remuneration;
- the overseas company earns profits from its Chinese subsidiary resulting from the expatriates' activities in the subsidiary.

To minimize PE risk, all the above should be avoided if a foreign employee is employed under a dispatch module. Moreover, under the localization module for foreign employment, local contracts concluded with Chinese companies should also avoid any of the above, in particular, a reporting line directed to a superior seated in the overseas company. In addition to the PE risks, local contracts are also recommended for PRC Labour Contract Law and immigration reasons.

## Third Judicial Interpretation on Labour Disputes

In September 2010, the Supreme People's Court issued its third judicial interpretation concerning labour disputes - Interpretations on Several Issues of Applying Laws in Adjudication of Labour Dispute (No. 3) ("Interpretation"). This Interpretation mainly reaffirms proceeding issues related to labour litigation. Some of its main regulations concern the following issues:

### Overtime

Under the current regulations, employees are generally obliged to provide evidence for overtime claims. Now, the Judicial Interpretation has clarified that if an employee can prove that his/her employer holds evidence of the existence of overtime work but fails to provide such, the employer bears adverse consequences, meaning provide overtime payment.

### Agreement on Termination Related Issues

The Interpretation confirms that an agreement on termination related issues, (e.g., formalities, salary payment, overtime payment, severance payment, etc) is valid as long as it observes mandatory provisions is not concluded by means of fraud, coercion or exploitation of the other party's vulnerability, or is based on gross misunderstanding or unconscionability; only then can a party apply to a people's court to revoke the agreement.

### Claims related to Social Insurance

Not all disputes related to social insurance may be brought before a people's court. The Interpretation clarifies that if an employee suffers loss because he

may not enjoy social insurance benefits as the employer failed to fulfill relevant social insurance formalities and the social insurance handling agency cannot take remedial measures, the employee may claim for damages against the employer before a people's court. Other disputes related to social insurance, for example, delayed contributions should be settled by the social insurance management authority and are not admitted before a people's court.

### Additional Indemnification for Payment Failures

According to Article 85 of the PRC Labour Contract Law, the labour authorities may impose additional indemnification requirements on an employer in cases of delayed salary payment, failure to provide overtime payment or statutory severance payment. The additional indemnification ranges from 50% to 100% of the outstanding payment. As provided by the Interpretation, employees may claim the additional indemnification in front of a people's court.

### Important HR Laws and Regulations under Formulation

According to information from Shanghai Municipal Human Resource and Social Security Bureau, nine important HR related laws and regulations are under formulation at the national level. Companies need to prepare for the implementation of the following laws and regulations in the near future:

- The fourth judicial interpretation on labour disputes to stipulate substantial labour issues, e.g., how to understand two consecutive fixed-term contracts, base for calculating overtime payment;
- Regulations on Labour Dispatch to regulate democratic procedures for identifying temporary, auxiliary or substitute positions allowed for labour dispatch;
- Enterprise Salary Regulations to define "salary" as basis for severance payment, overtime payment, etc. and to regulate salary collective bargaining;
- Regulations on Work-related Injury to include non-motor vehicle accidents during commuting as work-related injuries;
- Regulations on Labour Protection of Female Employee to detail protection during the "three periods" (i.e., pregnancy, maternity and nursing period) and to prohibit employers' restrictions on marriage, maternity, etc.;
- Regulations on the Human Resource Market to regulate the HR service market and to specify the Employment Promotion Law.
- Regulations on Training and Verification of Vocational Skills to require employers to allocate a certain proportion of payroll to an education



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and training fund.

Note: The above draft contents are not final provisions and are for reference only.

## Focus on Hong Kong: Employment Ordinance 2010

Contributed by Darren FitzGerald and Roberta Chan, Salans Hong Kong

The Employment (Amendment) Ordinance 2010 has just come into effect. The main objective of the Ordinance is to create an offence relating to an employer's failure to pay any sum awarded by the Labour Tribunal or Minor Employment Claims Adjudication Board (collectively called "the Tribunal") containing any specified entitlement, such as wages, annual leave pay and end of year payment to further safeguard the interests of employees. Under the Ordinance, an employer who willfully and without reasonable excuse fails to pay the awarded sum within 14 days after it becomes due is liable to prosecution and, upon conviction, to a fine of \$350,000 and imprisonment for three years.

### Today's Q&A: Compensation for Untaken Annual Leave

Q: Must I compensate an employee at year's end for any untaken annual leave?

A: In general, if an employee cannot take his annual leave due to company operational needs, a company must compensate that employee at the rate of 3 times his daily salary for each day of untaken annual leave. In practice, most companies adopt a prior application-approval process for annual leave. As such it is driven by employees, companies usually lack supportive documents for proving their faultlessness. To change this passive situation, companies may consider notifying employees in writing before year end about how many days of annual leave entitlement are untaken and encourage them to use them before they are forfeited. Further, in an employment contract the sequence of taking and handling leave exceeding the statutory minimum entitlement should be made very clear.

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