

## CHINA'S NEW LABOR LAW

On January 1, 2008, there will be a massive change for all employers in China. On that day, China's new labor law goes into effect and those who have employees in China (especially those who "unofficially" have employees in China) absolutely must take various steps to get into compliance AND to avoid being sued.

Chinese lawyers are already salivating about suing foreign companies pursuant to this new law. Indeed, Chinese lawyers have indicated to the authors of this Commentary, that they have plaintiffs all lined up and ready to sue various foreign companies when those foreign companies fail to comply with the law.

The new labor law is going to apply to all employers, no matter how few employees (even one!) a foreign company might have. It requires all labor contracts be in writing and it imposes significant penalties on employers for failure to comply. (Article 10) Employees can claim double salary for months worked without a contract for up to 12 months' salary. (Article 82) This rule is absolutely going to be applied to "informal" employment relationships common to so many foreign businesses doing business in China. Thus, one can expect a whole slew of lawsuits to be filed on January 1, 2009, by employees seeking double damages for the 12 months they just completed without a contract.

The new law will also require that all employers maintain a written employee handbook setting out the basic rules and regulations of employment. (Article 4) Without an employee handbook, an employer will effectively be unable to discharge employees for cause, since "cause" must be determined with reference to the employee handbook. (Article 39) So if a foreign company with employees in China has not yet created an employee handbook for those employees, it should be done immediately.

The new law also greatly limits the use of term contracts and probationary periods, previously popular ways to skirt China's existing labor law regime. Under Chinese law, an employee can be discharged either at the expiration of a term contract or for cause. To avoid the need to terminate for cause, employers in China have typically engaged employees under a series of short-term contracts. This practice is no longer possible under the new labor law. The employer is permitted to enter into a maximum of two term-contracts with the employee. (Article 14)

If the employee continues on after the expiration of a second term-contract, the subsequent employment contract is deemed to be an "open-term contract." Under an open-term contract, the employee is employed until he or she chooses to terminate the contract or reaches retirement age. The employer can only terminate the employment contract by discharge of the employee for breach. This means that once the relationship has shifted to an open-term contract, the result for competent employees is effectively "employment for life." (Article 14)

The new law imposes severe restrictions on the use of probationary periods in the employment relationship. Probationary periods are permitted, but the length is limited based on the term of the employment contract, with an absolute maximum set at six

months. (Article 19) Furthermore, an employee can only be subject to a single probationary period by a single employer. (Article 19) Wages during the probationary period must also be no less than 80% of the contract wage. (Article 20)

The new law also clarifies requirements for employee non-compete agreements and a failure to abide by those renders the non-compete ineffective. (Articles 23 and 24) Only senior management and other employees with access to critical trade secrets can be required to enter into non-competition agreements. (Article 24) The agreement must be limited in duration to two years, must be limited in geographic scope to a reasonable area and the employer must pay compensation to the employee during the period that the non-competition restriction is in effect. (Article 24) In other words, employers must pay their employees some consideration for the non-compete the employer is requesting the employee to sign and must continue payment for the non-compete provision to remain effective.

Employers who fail to abide by the new law face administrative fines, awards of double wages and liability for actual damages. (*See* Articles 80-95) More importantly, virtually every violation of the law gives the employee the right to sue the employer for penalties and damages in the local employment arbitration bureau or in the local courts.

And unlike so many of China's laws that are laxly enforced, the private right of action on this one all but guarantees plenty of enforcement through litigation. The new law has been actively publicized and employees are well informed about their rights under the new law. Growing numbers of Chinese attorneys are taking a strong interest in representing employees under the new law in filing group claims against employers. It is this sort of employee "self help," rather than administrative sanction that is likely to be the greatest threat to employers under the new law.

As part of this power shift [from employer to employee], the new law allows employees to sue and seek damages from their employers. Most experts believe U.S. companies will be the prime targets of suits because of their deep pockets and the strained relationship that exists between the Chinese government and multinationals. This is a change from the past when employees were not allowed to file claims against companies.

Smart employers will, at minimum, initiate signed contracts with all of their employees and draft an employee manual setting out the basis for termination with cause.