

# China TIPs

泰乐信律师事务所

## Also in this edition:

### Page 3

**Anti-Monopoly Law: concentration declaration criteria**

**Advanced recovery of investment in CJVs**

**New rules on foreign representative offices?**

**Equity pledge registration**

**Taylor Wessing expands in Shanghai**

## Labor Contract Law Implementing Regulations

By Roland Falder / Ralph Koppitz

In addition to the *Labour Contract Law of the Peoples Republic of China* (LCL) which took effect on January 1, 2008, on September 18, 2008 the long awaited *Implementing Regulations* have been issued and took effect on the same date.

### Written Contracts

One of the main intentions of the Chinese legislature was to ensure the compliance of employers with the formal requirement to have written employment contracts. In addition to the stipulations of the LCL, Articles 5 – 7 of the Implementing Regulations now describe a detailed process, how employers can deal with the situation especially if the employee is refusing to sign an employment contract.

According to Article 5 an employer must notify his employee in writing and ask him to immediately sign an employment contract. During the first month after the start of the employment relationship the employer may, if the employee does not follow his instruction, terminate the employment relationship by written notice and is in such case not obliged to pay any severance or other compensation. According to Article 6 of the Implementing Regulations, the employer must – however – pay a severance if he misses the one month period and no written employment contract is signed between the first month of employment and the end of the first year of employment. Due to this regulation it seems inevitable for employers in such situation to issue the written notification mentioned in Article 5 well before the end of the first month of employment, since any delay would otherwise lead to the obligation to pay severance. The Implementing Regulations do not address the case of an employee refusing to sign a written contract with an employment relationship already lasting for more than one year.

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The failure to conclude a written contract within the first year of employment leads - according to the LCL - to the employees' claim for a double salary payment. The Implementing Regulations now clarify that such obligation to pay twice the monthly wage does end on the last day of the first year of employment (a question that was left open by Article 82 of the LCL). They failed to clearly confirm whether after the one year period, due to the then possibly applying fiction of a contract of unlimited duration (Article 14 last para. LCL), the obligation to pay twice the monthly wage would continue based on Article 82 para. 2 LCL.

### Unlimited Term Contracts

Another clarification concerns Article 11 of the Implementing Regulations which clearly says that an unlimited term contract must be concluded when the conditions of Article 14 para. 2 LCL are given and the employee requests the conclusion of an unlimited term contract. Before the Implementing Regulations were issued it was unclear whether the simple request of the employee in such situation is sufficient or whether the employer must have expressed his wish to continue the employment relationship as well.

The wording of Article 11 ("the employer shall conclude a contract of unlimited duration") might be interpreted as the employer's unconditional obligation to enter into a contract, i.e. the employer not having a choice whether or not to conclude the contract. On the other hand, it might also be understood as emphasizing only the type of contract, namely one of unlimited duration to be entered in the cases mentioned in Article 14 para. 2 LCL. In case the former interpretation applies, it would e.g. mean:

- Right of the employee to ask for

an unlimited contract, once he/she has worked for the employer consecutively for more than 10 years (making e.g. any future expiry of the then valid contract irrelevant, once the 10 year anniversary has passed)

- Right of the employee to ask for an unlimited contract after expiry of two fixed-term contracts (leaving the employer only one exit option when renewing the first fixed-term contract by deciding not to renew at that time, but without similar option at the expiry of the second fixed-term contract)

In practice, employers should for the time being assume that the stricter interpretation set out above applies in favor of the employee.

### Termination

The Implementing Regulations further contain welcome clarifications of termination rules. First of all, Article 13 of the Implementing Regulations clearly states that an employer and an employee may not stipulate circumstances in which the employment contract shall end other than those specified in Article 44 LCL. Articles 18 and 19 of the Implementing Regulations contain comprehensive lists of termination reasons for both parties.

Article 21 does – other than Article 44 (2) LCL - state that an employment contract ends when the employee reaches the legal retirement age (i.e. does not repeat the stricter precondition of "commencing to draw basic pension").

Finally and probably most important for company practice, Article 19 (11) to (14) mention (operational) reasons when an employer may terminate an employment contract (upon observance of the notice period). The described termination reasons which are similar to the ones set out in Article 41 LCL for mass lay-offs, seem to confirm the

understanding that termination based on these reasons is permitted even if the thresholds for mass lay-offs are not met (i.e. no reduction by 20 people or more, or by 10% or more of the total staff occurs).

According to these provisions, an employer may terminate the employment e.g. if he experiences serious difficulties in its production and/or business operations or if the enterprise switches production, introduces a major technological innovation or revises its business matters and, after amendment of the employment contracts, still needs to reduce its work force. Therefore it can be said that Chinese employment law now clearly recognises the regular termination of an employment relationship for operational reasons as it is known in most Western countries.

### Conclusion

The Implementing Regulations for the LCL do contain a number of welcome clarifications, however, other questions were unfortunately left open and still need to be dealt with. Among those questions are e.g. the status of (Chinese) employees with foreign representative offices, as well as the permitted scope of post-contractual non-compete obligations.

## Anti-Monopoly Law: concentration declaration criteria

On August 3, 2008, the State Council promulgated the *Provisions on Standard of Declaration of Concentration of Business Operators* (Provisions), to implement the *PRC Anti-monopoly Law* effective as of August 1, 2008.

The Provisions define three types of concentration and the respective thresholds. The Ministry of Commerce is in charge of the declarations. Any potential concentration possibly causing exclusion or restriction of competition shall also be subject to declaration.

## Advanced recovery of investment in CJVs

On August 6, 2008, the Ministry of Finance circulated *Notice Cai Qi [2008] No. 159* to regulate the advanced recovery of investment by a foreign party of a cooperative joint venture enterprise (CJV). The Notice clarifies that the "other methods" for an advanced recovery of investment under Article 3 of the *Measures on Approval on Advance Recovery of Investment by Foreign Parties of a CJV* (2005) includes distribution of profits.

No advanced recovery by the foreign party is allowed before any losses of the CJV have been made up. The foreign party is subject to a joint and several liability regarding the CJV's debts.

## New rules on foreign representative offices?

On August 29, 2008, the State Council issued the *Draft of the Administrative Regulations on Registration of Representative Offices (RO) of Foreign Enterprises* (Draft)

for soliciting public comments to revise the current *Administrative Measures on Registration of RO of Foreign Enterprises* (1983 Measures).

Compared with the 1983 Measures, the permitted activities of a RO are addressed in a more detailed way. The Draft contains more detailed rules on the closing-down of and changes to the registration of a RO. The appointment of chief representatives and representatives are subject to qualification requirements similar to those applicable to directors under the Chinese Company Law. Most notably, the Draft contains the obligation to formally open a representative office at each location in China where permanent liaison activities shall be carried out. If enacted, this could impose a substantial burden on investors, especially also in case of a later exit. As an alternative, investors may consider to establish a small-scale limited liability company (e.g. a foreign invested commercial enterprise), which could then set-up liaison offices in other cities. Liaison offices in general do not require any approval or registration at the moment.

## Equity pledge registration

On September 5, 2008, the State Administration for Industry and Commerce promulgated the *Measures on the Registration of Pledged Equity with the Authorities of Industry and Commerce* followed by *Sample Documents for Registration of Pledged Equity*. The Measures are designed to regulate the registration of equity pledges according to the Property Law.

### Questions or comments?

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## Tips & Dates

*Dr. Sven-Michael Werner and Dr. Martin Rothermel – **Legal and Liability Issues with Chinese Suppliers** organized by Management Circle*

*9 and 10 February 2009 - Munich*

## Taylor Wessing expands in Shanghai

European law firm Taylor Wessing has completed the third expansion of its Shanghai Office, existing since 1996. Enlarged conference room facilities and additional space for new work places for both legal and support staff have been created.

This expansion follows the opening of the Beijing Taylor Wessing Office in 2008. The firm's China Group operates from its offices in Munich, Frankfurt, Hamburg, London, Paris, Shanghai (headed by Ralph Koppitz) and Beijing (headed by Christoph Hezel).

M.-Florian Ranft, heading the firm's international China Group commented: "*With the Shanghai expansion, we have further improved the service capabilities for our European and Chinese clients. We are looking forward to the hiring of new staff supporting the ongoing growth of our China practice, in particular in the areas of mergers & acquisitions, and investment restructuring.*"

### Disclaimer

The contents of this newsletter are general information on the respective subject matter only and neither is a complete description nor substitutes any specific advice.

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