



## THE NEW PRC SUPREME PEOPLE'S COURT INTERPRETATION ON EMPLOYMENT ISSUES IN CHINA

The PRC Supreme People's Court issued the Interpretation on Several Issues concerning the Application of Laws in Labor Dispute Case (IV) ("the Fourth Interpretation") which took effect from February 2013. The Fourth Interpretation clarifies several employment law issues including the enforceability of non-competition covenants, the validity of oral amendments to an employment contract, the calculation of service years transferred from one entity to another and the employment of foreign nationals. Apart from the Fourth Interpretation, the new Exit-Entry Administration Law of China ("Administration Law") which came into effect on 1 July 2013, also provides guidelines on and sets out penalties in relation to unlawful employment.

### EMPLOYMENT OF FOREIGN NATIONALS

In China, a foreign employee working in China must obtain a valid work permit. Occasionally, a foreign employee (including Hong Kong, Macau and Taiwan residents) may sign an employment contract with a Chinese company without obtaining a valid work permit. Such employment is considered to be unlawful employment. Further, under Article 14 of the Fourth Interpretation, an employment contract with a foreign employee (including residents of Hong Kong, Macau and Taiwan) is enforceable only if the foreign employee has obtained the required work visa.

The Administration Law provides these specific examples what constitutes unlawful employment, namely:

- working without a valid working permit and working visa;
- working beyond the scope of the working permit; and
- visa students who violate the work-study regulations by working beyond the stipulated scope.

For cases of unlawful employment, the following penalties may be imposed, either alone or together:

On the foreign employees

- Fines ranging from RMB 5,000-20,000;
- Arrest and detention for 5-15 days;
- Repatriation and prohibition from entering into China for 1-5 years after the date of repatriation.

On the domestic employers

- Fines of RMB 10,000 for each illegal employee (subject a cap of RMB 100,000);
- Confiscation of any income which is derived from the unlawful employment.

### NON-COMPETITION COVENANTS

In China, non-competition covenants are only enforceable if the employer provides compensation to the employee during the non-competition period. Article 6 of the Fourth Interpretation stipulates that if the employment contract is silent as to the amount of compensation, the employee is entitled to 30% of the average monthly salary of the employee for the 12 months preceding the termination of employment. If the employee's salary is lower than the minimum wage, the local minimum monthly salary will be used to calculate compensation.

In addition, the Fourth Interpretation allows an employer to terminate the non-competition provision earlier by paying three months' compensation to its employee. If the employer fails to pay the non-competition compensation for three months, an employee can discharge the non-competition covenants.

### VALIDITY OF VERBAL AMENDMENT TO THE EMPLOYMENT CONTRACT

According to the PRC Labor Contract Law, amendments to the employment contract are enforceable only if they are made in writing. However, the Fourth Interpretation provides an exception to this general rule. Article 11 of the Fourth Interpretation stipulates that oral amendments to the employment contract are enforceable if the parties have performed the amendment for more than one month.



## CALCULATION OF SERVICE YEARS FOR TRANSFERRED EMPLOYEES

A common scenario is where an employer transfers or assigns an employee to another entity (i.e. transfer within the group or merger and acquisition). The law was not clear whether the years of service prior to the assignment should be included when calculating the severance payment of employee.

As a general rule, when an employer unilaterally terminates a labor contract, the employer is liable to pay severance payment to the employee based on the employee's year of service. Usually, the employee is entitled to one month's salary for each year of service with the employer.

The Fourth Interpretation clarifies this uncertainty by stating that where an employee is assigned to work with a new employer for reasons not attributable to the employee, the service years with the previous employer should be taken into consideration when calculating the severance payment and the new employer is responsible for paying the severance payment for the employees' years of service with their former employer. Pursuant to Article 5 of the Fourth Interpretation, the reasons not attributable to the employee include the following:-

- The employee still works in the same location and same position, but the employer has been legally changed into a new one.
- The employer transfers the employee to a new employer by delegation or appointment.
- The transfer of employee is a result of a merger, split or any other change of organization of the employer.
- The employer and its affiliated enterprises arranged to take turns to enter into labor contract with the employee.
- Other reasonable circumstances.

## KEY TAKEAWAYS

1. An employer now has an option to shorten the non-competition period by giving a three-month notice to the employee.
2. An employer should note that any oral amendment to the employment contract will be enforceable if it has been performed for more than one month. It is thus recommended that employers keep documentary evidence related to performance of the oral amendment (such as attendance reports, bank statements which show the transfer of salary, and salary receipts) and to put any oral amendments down in writing as soon as they are made.
3. For transfer of employees within the group or merger and acquisition transactions, the new employer is liable to pay the severance payment for service years with former employer to the employee.
4. Employers of foreign employees without work permits should take steps to obtain a proper work permit in China as soon as possible. The processing time is generally five working days. Although the employee may work prior to the issuance of the work permit, the employee will not be protected by PRC labour laws.

Employers should further ensure that the scope of their foreign employees' work remains within the scope of their respective work visa.