Proposed Amendments to the PRC Employment Contract Law - Impact on Labour Dispatch Companies (Part 1)

Headline

November 2012: Anticipated changes to PRC Employment Contract Law this month will affect labour dispatch companies, if approved. Changes are likely to be retroactive and will, therefore, impact all existing, as well as new, labour dispatch companies.

This is the first in our 2-part series addressing the changes to the PRC’s laws regarding labour dispatch companies. In this issue we consider the national-level legal changes to the Employment Contract Law and how this impacts labour dispatch companies. In part 2, we consider the regulation changes at regional level regarding labour dispatch in Chongqing, Shanghai, Tianjin, Jilin and Guangdong, as well as the practical issues that have been left unsolved by the draft amendment.

In Brief

**IMPACT ON EMPLOYERS IF THE DRAFT AMENDMENT BECOMES EFFECTIVE**

- The cost of labour dispatch employment will increase;
- The legal risks associated with labour dispatch employment will increase significantly;
- The scope of labour dispatch employment arrangements adopted by companies will be strictly limited.

**THE 6 KEY CHANGES**

- A labour dispatch company must be licensed with the relevant labour authority and registered with the local Administration of Industry and Commerce;
- The minimum registered capital required to establish a labour dispatch company will increase from RMB500,000 to RMB1 million and the company will be required to establish a labour dispatch management system;
- The principal of “equal pay for equal work” will apply, and be specifically stated to apply within the employment agreement. Where there is no comparable co-employee, the remuneration of a dispatched employee will be decided with reference to the same or a similar position within the locality where the employee is based;
- The new legislation will apply to temporary, auxiliary and replaceable positions, as now specifically defined;
- More stringent punishment will be available for non-compliance with the law and regulations regarding labour dispatch. This may include confiscation of illegal income and significant fines;
- The draft amendment to the Employment Contract Law will have retroactive impact and will, therefore, apply to labour dispatch companies existing before the date on which the legislation comes into effect.

**ADVICE FOR COMPANIES**

- Stay abreast of changes to labour dispatch requirements at both the national and regional level;
- Understand the basic status of your company regarding the current employment arrangements and the situation of employees dispatched (e.g., positions, percentages and the extent of reliance, etc.); and evaluate the potential risks due to the implementation of relevant laws and regulations;
- Develop a feasible adjustment programme for the company’s current employment structure (i.e., reduce the use of labour dispatch and change the status of dispatched employees...
to direct-hire employees, where possible). Furthermore, review and revise relevant legal documents, such as labour dispatch service agreements and engagement contracts, to minimize the potential legal risks.

**In Detail**

**CHANGES TO THE EMPLOYMENT CONTRACT LAW**

In the 27th Session of the Standing Committee of the Eleventh National People’s Congress (NPC), held on 26 June 2012, the Draft Amendment to the *PRC Employment Contract Law* (ECL) was deliberated. The Draft Amendment was published on the NPC website and public opinion was invited between 6 July and 5 August 2012. A remarkable 550,000 opinions were received.

According to a senior official of the Legal Work Commission of the NPC, the Draft Amendment is very likely to be promulgated and implemented before the end of this year.

The Draft Amendment is likely to focus on the four provisions of “Labour Dispatch” under Section 2 of Chapter 5 of the ECL, and will not be relevant to any other provision.

The main revisions proposed by the Draft Amendment are:

a. strictly to limit the scope of the job positions in labour dispatch arrangements;

b. to raise the capital threshold for the establishment of labour dispatch companies;

c. to maintain the right of employees dispatched to “equal pay for equal work”; and

d. to impose stringent punishments for related illegal conduct.

For the purposes of this paper, “labour dispatch” is where an employee is made available to an enterprise through a labour service intermediary (e.g., FESCO, CIIC). As such the employer and the “end user” are different entities.

**IMPACT OF THE DRAFT AMENDMENT ON COMPANIES USING LABOUR DISPATCH**

The cost of using labour dispatch employment will increase.

The increased standards for establishing a labour dispatch company and setup of the administrative license system in the Draft Amendment will lead to a gradual decrease in small and medium labour dispatch companies and to a gradually increased number of large labour dispatch companies. While the market is dominated by large labour dispatch companies, work entities will be restricted in negotiating key contents of the Labour Dispatch Agreement, such as the dispatch service fee and assumption of liabilities, which will definitely increase the cost of using labour dispatch.

In addition, the expression of the entitlement of dispatched employees to “equal pay for equal work” in the Draft Amendment does not seem semantically to differ significantly from the position under the ECL. However, in light of the response of various professionals to the Draft Amendment and some of the existing Local Regulations (e.g., Chongqing and Tianjin), in judicial practice, “equal pay for equal work” is likely to at least be considered to mean that “dispatched employees should be included in the unified remuneration system and wage system of the work entity, enjoy the same welfare as the employees directly entering into labour contract with the work entity, and subject to the same wage distribution and performance appraisal methods”.

The legal risks of companies using labour dispatch will increase significantly.

The Draft Amendment sets out specific provisions regarding the scope of the labour dispatch employment arrangements. If a company employs personnel by labour dispatch in violation of the provisions, then that labour dispatch relationship is likely to be deemed invalid by law.

The Draft Amendment defines more clearly and specifically the employer’s legal liability for breaching the law and increases the punishment, thereby increasing the risk for labour dispatch.
employment arrangements for the company. In some localities such as Chongqing, according to its local regulations, this risk may have become a reality.

In addition, the strict rules provided in the Draft Amendment regarding the establishment of labour dispatch companies and legal liability for breaching the law will also increase the legal risk of the work entity due to labour dispatch company’s breach of law as a result of the former now bearing joint and several liability with the latter.

The scope of the labour dispatch employment arrangement adopted by a company will be strictly restricted.

The Draft Amendment and certain published local regulations (such as those of Chongqing, Jilin and Guangdong) have set out specific provisions regarding “temporary, auxiliary, or, replaceable positions” in labour dispatch employment. Although its definition and detailed rules for operation are pending further clarification in judicial practice, there is no doubt that the scope of the labour dispatch employment arrangement for small companies will be significantly reduced.

SIX MAIN REVISIONS PROPOSED BY THE DRAFT AMENDMENT

A Labour Dispatch Company must be Licensed by the Labour Authority.

The Draft Amendment prescribes, “A labour dispatch company shall obtain the administrative approval from the competent labour authority; upon approval, it shall go through the corresponding formality of registration with its local Administration of Industry and Commerce.”

This provision aims to reinforce the supervision of the government over labour dispatch companies, and impel them to operate lawfully. However, the Draft Amendment is silent on the level of administrative licensing. According to previous custom provided in relevant laws, licensing is generally done by the competent labour authority at least county level.

The Proposed Minimum Required Amount of Registered Capital to Establish a Labour Dispatch Company will be Increased from RMB500,000 to RMB1 Million.

Furthermore, the Draft Amendment also explicitly requires a labour dispatch company to establish a legitimate labour dispatch management system. This provision aims to raise the capital threshold for labour dispatch companies, and ensure the ability of any labour dispatch company to undertake its external legal responsibilities.

**Equal Pay for Equal Work.**

“Equal pay for equal work” is an important principle provided in the ECL. Article 63 of the ECL currently stipulates that dispatched employees have the same right of “equal pay for equal work” as other employees; and where no similar or comparable position exists, the remuneration of dispatched employees will be decided with reference to the same or a similar position in the locality where the work unit is based.

The Draft Amendment goes further to add that the labour contracts entered into:

i. between the labour dispatch company and the dispatched employee; and

ii. the dispatch company and the work entity itself,

must both specify that the remuneration of dispatched employees shall comply with the principle of “equal pay for equal work”.

**Strict Limitations Imposed on the Scope of the Job Position of a Dispatched Employee.**

Article 66 of the ECL provides that labour dispatch shall “generally” apply to temporary, auxiliary, or replaceable positions (“Three Conditions”). Nevertheless, the ECL and its relevant rules and regulations have not provided any specific definition of the Three Conditions. The Draft Amendment changes the word “generally” in Article 66 to “only”, and further defines the Three Conditions, as follows:

- “temporary positions” refer to those with a term of no longer than 6 months;
- “auxiliary positions” refer to those that serve the main or core business of the company; and
- “replaceable positions” refer to those that can be performed by dispatched employees in place of permanent employees during the period when such employees are out of work for study, vacation or other reasons.
More Stringent Punishments Imposed on Illegal Conduct Relating to Labour Dispatch.

The Draft Amendment prescribes that where a company operates a labour dispatch business without a license, its business shall be banned by the competent labour authority, the illegal income shall be confiscated, and a fine shall be imposed of not less than one times but not more than five times the illegal income, or a fine of up to RMB50,000 if there is no illegal gain.

It further provides that where any labour dispatch company or work entity breaches the law, it shall be fined at a rate of not less than RMB5,000 but not more than RMB10,000 per person dispatched (the existing rate is not less than RMB1,000 but not more than RMB5,000 per person).

For the labour dispatch company, its granted administrative license shall be revoked by the competent labour authority; and in case of any loss caused to any dispatched employee, the labour dispatch company and the work entity involved shall bear joint and several liability for compensation.

This provision aims to enhance the punishment imposed on the illegal conduct of labour dispatch companies and work entities, by increasing the punishment imposed on the non-licensed operation of labour dispatch business, and raising the amount of fine imposed.

The Draft Amendment will take Retroactive Effect with Significant Impact for Labour Dispatch and Connected Businesses.

The Draft Amendment explicitly stipulates that where a work entity is using dispatched employees when the Draft Amendment officially comes into force, the labour dispatch company involved and connected work entity shall make necessary changes in accordance with the Draft Amendment.

Any labour dispatch company established before the implementation of the Draft Amendment, must apply for and obtain a license or approval from the competent labour authority and go through the registration of change with the local Administration of Industry and Commerce.

Specific measures shall be stipulated by the State Council separately.

The employment arrangements in cases of labour dispatch, and the operations of such businesses, will face significant adjustment in the near future as a result of this amendment.

ADVICE FOR COMPANIES

Based on the above legal amendments, there is a definite trend, both at national and local levels, in favour of increased restriction and standardization of employment arrangements for labour dispatch companies.

In order to anticipate and deal with this trend, the following may be considered by companies using, or considering using, labour dispatch:

- Stay abreast of changes to labour dispatch requirements at both the national and regional level.
- Understand the basic status of your company regarding the current employment arrangements and the situation of employees dispatched (e.g., positions, percentages and the extent of reliance, etc.); and evaluate the potential risks due to the implementation of relevant laws and regulations.
- Develop a feasible adjustment programme for the company’s current employment structure (i.e., reduce the use of labour dispatch and change the status of dispatched employees to direct-hire employees, where possible). Furthermore, review and revise relevant legal documents, such as labour dispatch service agreements and engagement contracts, to minimize the potential legal risks.
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