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Rule of Law in China: Chinese Law and Business

Labour Law: Trends and Practices in China

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Executive Summary

- China has enacted a number of laws and regulations to govern labour relations and protect workers' rights. On the face of it, these laws are fairly well written, and reflect internationally recognized workers' rights.
- Nevertheless, labour disputes, workplace safety violations, and labour unrest have increased dramatically in recent years.
- The Ministry of Law and Social Security, and its provincial branch offices, have always been understaffed, and unable to fully supervise and enforce China's workplace standards.
- Trade unions, too, have never supervised the workplace effectively. Historically, trade unions have been a marginalized power base of the Chinese Communist Party (CCP). They were instructed to play a supporting role in the workplace, without interfering in the country's development objectives.
- Beginning in 2005, a new policy was adopted in response to tensions created by growth-fuelled workplace issues. The messages to the trade unions were: get involved to control labour unrest; become self-sufficient, and generate stronger sources of revenue (since the government is tired of paying for the unions); and do a better job of conveying the Chinese Communist Party's vision and values (important for national unity and stability).
- Purportedly, the message was to increase union activity in foreign-invested enterprises. No equivalent message was directed at domestic industry. At the same time, there was a noticeable increase in economic nationalism, reflected in a number of government policies and regulations seeking to repeal foreign investment in the name of 'national economic security'.
- The emboldened trade unions sponsored the draft Labour Contract Law, which included a provision making clear that all work rules must be approved by the unions.
- The government received almost 200,000 pages of written comments, including feedback and suggestions from domestic and international businesses, and employer organizations.
- Additional to objecting to the provision requiring union approval of work rules, foreign and domestic business communities also raised questions about the draft's treatment of contract employees; the right of employers to terminate fixed-term labour contracts; statutory severance pay upon expiration of labour contracts; mandated compensation for non-competition provisions; the treatment of probationary periods; and other matters.
- Changes to the draft law were substantial. A key change in the second draft, which was much more balanced than the first draft, was to delete the requirement that work rules must be approved by trade unions; and to simply allow the unions the right to be consulted in the development of such rules.

Labour Law: Trends and Practices in China

The forces of change are working more critically and more explosively in China than anywhere else on the entire continent. The peace of Asia and our own future security depend on our understanding how powerful these forces are, what creates them, and what holds them back.

White, T. H. and Jacoby, A. (1946) *Thunder Out of China*. New York: W. Sloane Associates.

Over 60 years after these words were written, we are once again witnessing and participating in the forces of change at work in China. The People's Republic of China (PRC) has gone through a period of staggering economic growth, unprecedented in world history, averaging nine per cent over the past two decades. China has experienced record trade volumes of over US\$1.15 trillion and foreign direct investment of over US\$70 billion in 2006, a significant increase over the investment of US\$2 billion in 1986.

In parallel with such phenomenal economic growth, there is focus on development in the coastal areas and major cities; uncontrolled internal migration of workers; strain on environmental resources; increased labour-related deaths and injuries, especially at state-owned enterprises, construction sites, and mining operations; and increased labour unrest, triggered by unpaid worker wages, primarily with respect to wages owed to migrant construction site labourers.

The Ministry of Law (MOL) and Social Security, and its provincial branch offices, have always been understaffed, and unable to fully supervise and enforce China's workplace standards. Trade unions, too, have never supervised the workplace effectively. Historically, trade unions have been a marginalized power base of the Chinese Communist Party (CCP), instructed to play a supporting role in the workplace without interfering in the country's development objectives. Most manufacturing facilities that were unionized, both domestic and foreign-owned, had a manageable relationship with their trade unions; namely, they paid their fees to the unions, and the

unions ensured a content labour force. China has never allowed true independent trade unions, as recognized by the tripartite system of the International Labour Organization. Foreign companies operating in China have learned to live with the system, and most foreign companies have workplace conditions that far exceed their local counterparts.

At some point during 2005, and through 2006, in response to tensions created by growth-fuelled workplace issues, an interesting message began to descend from China's leadership about the new role of trade unions in the country. The messages to the trade unions were: get involved in controlling labour unrest; become self-sufficient, and generate stronger sources of revenue (since the government is tired of paying for the unions); and do a better job at conveying the Chinese Communist Party's vision and values (important for national unity and stability).

Purportedly, the message was to increase union activity in foreign-invested enterprises. No equivalent message was directed at domestic industry. At the same time, there was a noticeable increase in economic nationalism, reflected in a number of government policies and regulations seeking to repeal foreign investment in the name of 'national economic security'.

Why is the drive for unionization directed at foreign companies? Why now? Is there a broader agenda? Is there a more sinister agenda? Why are the trade unions driving labour legislative agenda? And why is the US Congress seeking to get into the fray?

China's Labour Laws and Standards

To put the questions in context, it is important to understand Chinese labour laws and regulations, which, on the face of it, are fairly well written, and reflect internationally recognized workers' rights. As is the case with many other laws in China (including intellectual property and environmental standards), the real issues are the lack of resources and inter-agency tools to implement and enforce existing laws.

The PRC has adopted laws specifically addressing general employment issues for local Chinese citizens employed by both domestic and foreign-invested enterprises (FIEs), and foreigners employed by FIEs in China. The National People's Congress (NPC) enacted a comprehensive national Labour Law in 1994 applying to all enterprises, including FIEs, state-owned enterprises and private enterprises.

The Labour Law sets out fundamental workers' rights for all employees in China, including the following rights: equal employment opportunity; choice of job; compensation for labour; rest periods, vacations and holidays; workplace safety and healthy working conditions; vocational training; social insurance and benefits; and the right to resolve labour disputes.

The Labour Law stipulates that all employers are required to execute labour contracts with their employees to establish terms and conditions of the employment relationship. In addition to and separate from an individual labour contract, the employees of an enterprise may negotiate a collective bargaining agreement with an FIE. The Labour Law protects the rights of employees to join or organize trade unions. A collective bargaining agreement sets the minimum conditions for all employees, with respect to compensation, working conditions, hours and wages, vacation and rest periods, and benefits.

The Labour Law provides that an employer may not discriminate on the basis of nationality, race, sex or religious belief. In addition, it provides that an employer is prohibited from discriminating against female workers; unless the type of work is 'unsuitable for woman as stipulated by the state'.

The written policy of the government is to encourage the employment of disabled persons, minority nationalities and military personnel retiring from active service.

Chinese law provides that employees are entitled to, and employers are required to provide, social insurance and welfare benefits, even if the employee prefers to waive such benefits. The Labour Law provides for a national social insurance system that includes the following social insurance and welfare benefits: retirement and pension benefits; worker compensation for job-related injuries and diseases; medical care and disability benefits for injuries or diseases that are not employment related; unemployment benefits; pregnancy and maternity benefits; and death benefits for survivors. The benefits provided under the PRC system are required to be consistent with the level of national economic development.

The Labour Law prohibits the employment of persons under the age of 16 years. Under-aged workers, between the ages of 16 and 18 years, are prohibited from working in underground mining operations and pits, with poisonous or harmful substances; or to engage in physically intense labour. An employer is required to arrange, at its own expense, for regular medical examinations of under-age workers. The law further mandates maternity leave of a minimum of 90 days; and some local jurisdictions permit a greater leave entitlement. Nurses, who are also mothers, are not allowed to work overtime or night shifts, or to engage in strenuous physical labour for a period of up to one year after their child is born.

Employers are required to establish a programme of workplace health and safety, and to take specific measures to guard against workplace accidents. Such a programme requires that employees be provided with the necessary protective equipment such as goggles, work clothes, head covering and any other items needed for their protection as workers. Employers are also required to train employees in health and safety issues; and to discipline errant employees that fail to follow company rules and labour regulations. For workers in dangerous

occupations or exposed to hazardous substances, the employer is required to provide regular medical examinations at company expense. A worker has the right to refuse to engage in any task that is considered unsafe, and the right to seek relief from the labour authorities in situations where there are uncorrected problems that may jeopardize employees.

The laws in China provide for a five day, forty hour working week, although the employer may extend the hours of work after consultation with a trade union and employee, on the condition that overtime pay is provided, and the work does not exceed thirty-six hours per month. In certain professions and emergency situations, the law stipulates that overtime work may be required of employees.

FIEs are required to pay their employees the 'average wage standard' of employees in the 'same industry in the local area'. The law also requires that the average wage standard of a FIE increases progressively, in line with the economic development of the enterprise. A decision concerning wages is made by the FIE's board of directors, which must take into consideration the enterprise's productivity rate, economic results, the consumer price index and wage guidelines for the region.

The MOL and the local labour administrative departments are responsible for supervising compliance with the Labour Law and applicable regulations. Labour officials have the full right to enter the premises of an employer; inspect the work premises; and demand access to documentation and other tangible items, such as the safety equipment provided to employees, to determine compliance. Trade unions also have contractual and regulatory rights to oversee the activities of employers.

If an employer violates the Labour Law or applicable regulations, including violations of child labour standards, standards for women, and wage and hours violations, the MOL, or its local labour department, may issue a notice of violation; or order compensation for the injured employee, or a monetary penalty against the employer. For violations of workplace health and safety

standards, or other serious violations, labour officials may suspend operations of the enterprise, or, in egregious cases, take steps to cancel the company's business license.

For serious infractions involving false imprisonment, improper search or seizure, battery, conduct considered insulting or physical violence, the public security bureau (i.e., the Chinese police) is empowered to initiate a criminal investigation and prosecution of the responsible management personnel. In such situations, the public security bureau also has the right to detain the management personnel for up to fifteen days pending an investigation.

The parties to a labour dispute are required to resolve the dispute in stages. First, the parties, including the enterprise and the employee, are required to engage in consultation. If the parties are unable to resolve the matter informally, they are required to apply to the labour dispute mediation committee of the enterprise for voluntary conciliation.

Under the Labour Dispute Rules, mediation of a dispute is strongly encouraged. If such efforts fail, the parties may apply to the local labour dispute arbitration commission to initiate an arbitration proceeding. If one party disagrees with the tribunal's arbitration award, the disputing party may file a claim in the people's court.

Both foreign and domestic employers in China should be held accountable to the same workplace standards. The laws should also be enforced in a uniform and objective manner, and without regard for whether an operation is foreign or domestically owned. While new laws and regulations balancing the interests of employers and employees are always helpful, the current laws on the books are not being fully enforced, due to the lack of agency resources. To improve workplace conditions, China needs to bolster the ranks of those labour bureaus with jurisdiction over workers' rights.

The emerging role of China's trade unions: Party politics or workers' rights?

The message from the leadership to empower trade unions in ways unseen in the past are rooted more in politics than in a recognition of workers' rights. An opinion issued by the Work Committee of the Chinese Communist Party highlights this 'new' role, and emphasizes the importance of politics in the drive for unionization:

The party organizations at all levels and the relevant functional departments shall unify ideas and have a clear understanding of the arduousness and complexity of the work involved in setting up trade unions, and fully understand that the trade unions should not only concern themselves with promoting the establishment of trade unions, but also to be actively involved in the consolidation of the class base and ruling base of the Chinese Communist Party (CCP), and the overall situation of the development and opening up of the bonded zone and the building of a harmonious society. We shall enhance the awareness of politics and overall situation, and take powerful measures to implement the requirements of the Central Government and the provincial committee of the CCP, so as to promote the CCP and the government to jointly administer the organization and establishment of trade unions, and to give powerful support, and the trade unions shall try their best to confront difficulties and to solve them to obtain actual effect.¹

Throughout 2006, many foreign companies began receiving notice to unionize, even if their workers were not interested: twenty-five employees must vote to form a union. Some foreign companies have ignored the notices; whilst others have stalled and engaged in lengthy negotiations with the unions to figure out their true intentions and alleviate

suspicions; others still have worked out arrangements that usually result in paying unions fees of two per cent of wages of all workers. Other government agencies, including those agencies responsible for insurance of investment approvals, business licenses and land-related grants have also supported the union drive. They have instructed foreign companies that they would not receive approval to operate or expand their operations, unless they caved in to union demands.

If unions were to genuinely operate either more independently, and/or like a workers' club, most employers would find this acceptable. But the use of company facilities and resources to espouse the virtues of Party politics is something that both foreign employers, and, most likely, local Chinese employees themselves, would find unpalatable. Foreign companies find this trend troubling. They would, if possible, resist the use of the workplace as a conduit for Party politics.

Trade union legislative agenda: Circling the wagons around the foreign workplace

The emboldened trade unions took further action at the end of 2005 to sponsor the draft Labour Contract Law, which included, *inter alia*, a provision making clear that all work rules must be approved by the unions.

The draft Labour Contract Law was hurriedly sent to the National People's Congress (NPC), and passed through its 'first reading' (laws are required to go through three readings in order to be adopted). In a lesson on transparency, when the NPC received the draft law, given the obvious one-sided nature of the draft law sponsored by the trade unions, they sent it back for public comment and review.

In early 2006, after a thirty-day notice period, the government received almost 200,000 pages of written comments, including feedback and suggestions from domestic and international businesses and employer organizations.

1. 'Opinions on Lawfully Promoting the Work for Setting up Trade Unions in Foreign-funded Enterprises, Documents of the Communist Party of China Work Committee' in Zhangjiagang, J. (2006) *Bonded Zone No. 4 of Zhang Bao Dang Fa*.

Additional to objecting to the provision requiring union approval of work rules, both foreign and domestic business communities also raised questions about the draft's treatment of contract employees; the right of employers to terminate fixed-term labour contracts; statutory severance pay upon expiration of labour contracts; mandated compensation for non-competition provisions; treatment of probationary periods; and other matters.

After conducting an internal review, in December 2006, the government released the second draft of the Labour Contract Law, with substantial changes. A key change in the second draft, which was much more balanced than the first draft, was to delete the requirement that work rules must be approved by trade unions; and to simply allow the unions the right to be consulted in the development of such rules.

The second draft also provides helpful clarification over a number of labour contract issues, such as non-competition clauses, probationary periods, non-fixed term contracts and standards applicable to labour contractors. The second draft, likely to be adopted mid-2007, takes into consideration input from foreign and domestic business communities; and reverses some of the restrictive language advocated by Chinese trade unions.

While new laws and regulations that clarify workplace standards in a balanced manner are always welcome, the current laws on the books are not being fully enforced, given the lack of agency resources. To improve workplace conditions, China needs to bolster the ranks of labour bureaus with jurisdiction over labour standards.

US Congress in the fray: Do they really understand what is happening?

In October 2006, US Congress injected itself into the Labour Contract Law debate. In a letter to the US administration, it demanded that the US government rebuke the foreign business community in China, which participated in the law-drafting process. This was on the basis that Congress felt that US business interests were erroneously meddling with the development of workers' rights in China.²

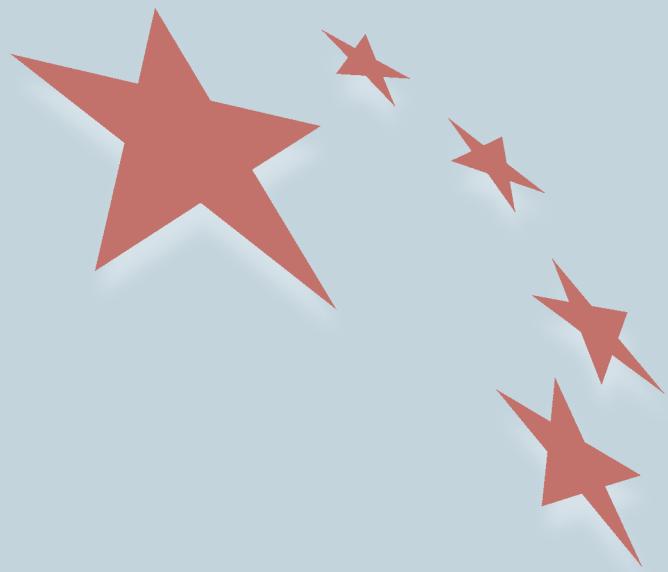
But little did Congress know that the US business community, the Chinese domestic business community, and the public were invited by the Chinese government to participate in the public dialogue and review process in developing the draft Labour Contract Law. Neither did Congress know that the US business community was focused on eliminating the key provision that would allow Chinese trade unions the unfettered right to approve all work rules; which would have taken away an employer's right to manage its business.

Congress might have thought twice about taking such a hard-line view of the lobbying efforts of the American business community in China, had they been aware that most US companies with operations in China have workplace standards that far exceed local norms. Most US companies are models for labour and environmental standards in China. Most operate using codes of conduct and best practices that reflect practices in the US.

Most foreign observers on the ground in China would agree that the drive for unionization directed at foreign companies has nothing to do with workers' rights, at least not yet. Trade union resources would be better utilized if they focused on correcting the problems in state-run companies. But trade unions have shown little interest in targeting state-owned enterprises given that – in contrast to the foreign facilities offering higher wages – state-owned facilities are not a good source of revenue for union dues. Thus the more lucrative choice is to target foreign companies.

How far will the drive for unionization and trade union legislative agenda go? What are its intended and unintended impacts? Will stronger trade unions be good for workers? Or will they just be used to fulfill the Party's agenda? The answers to these questions are left for observation.

2. Congress letter to the White House, 31 October 2006. The source of Congress allegations were based upon an incorrect *New York Times* article, which mischaracterized the role of the AmCham community, with respect to the drafting process of the Labour Contract Law.



The Foundation

The mission of the Foundation is to study, reflect on and promote an understanding of the role law plays in society. This is achieved by identifying and analysing issues of contemporary interest and importance. In doing so, it draws on the work of scholars and researchers, and aims to make its work easily accessible to practitioners and professionals, whether in government, business or the law.

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The main objective of the programme is to study the ways in which Chinese law and legal institutions encounter and interact with the social environment, including economic and political factors, at local, regional, national, and international levels.

The Foundation's perspective in pursuing this objective is that of entrepreneurs considering investment in China, the lawyers advising them, executives of an international institution or non-governmental authority, or senior public officials of another country. The combination of this objective and our particular perspective constitutes a unique approach to the study of the role of law and its relationship to other aspects of society in China.

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