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together

Doing Business in China:  
Key Employment and Corporate Considerations

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# Topics

- U.S.-initiated business activities in China
- Considerations in forming a China operating entity
- Hiring of local staff in China
- Employee termination scenarios
- Acquisition-related employee transfer issues

# U.S.-Initiated Business Activities in China

# Hypothetical #1

- Your U.S.-based company has no legal presence in China, but it is interested in engaging in business activities there.
  - Can it directly hire PRC employees?
  - What are its options in providing on-the-ground services?

# Exploratory Trips

- Send U.S. employees on exploratory trips
- What type of visa is required?
  - “F” visa
- Scope of activities
  - Business meetings
  - Market research
  - Scientific, technological, and/or cultural exchanges

# Exploratory Trips

- “F” visa
  - Single, double, or multiple entry
  - Duration of stay is 30 days
  - 90 days in a rolling 12-month period
    - *Payroll & all remuneration remains outside China*
  - Requires invitation letter from host organization

# Secondment of Employee

- Considerations for sending U.S. employees on secondment
- Immigration considerations
  - Need to locate host organization in China to sponsor U.S. employees
  - What type of visa is required?
    - *Work & residence permit*
    - *Documentation to support application*

# Secondment of Employee

- Employment considerations
  - What type of documentation?
    - *Secondment agreement between U.S. employer & employee*
    - *Services agreement between U.S. employer & host organization*
  - What is governing law?
    - *U.S. or China?*



# Agency Employee

- Locate local agency companies to employ PRC individuals & assign them to work for your company
  - PRC labor laws apply
  - Special deposit or fee charged by consulting companies
  - Due diligence on consulting companies to ensure such services are within their business scope

# Hiring of Individual Consultants

- Engage PRC individual as consultant/contractor
- No specific regulations concerning “independent contractor” concept
- Law may presume employment relationship between individuals & entities

# Considerations in Forming a China Operating Entity

## Hypothetical #2

- Your company decides that it wants a legal presence in China.
  - What are its corporate entity options?
    - *Representative Office*
    - *WFOE/JV (“wholly foreign-owned enterprise”/“equity or cooperative joint venture”)*
    - *Branch Office*

# Representative Office

- Representative Office
  - Scope of permitted activities: ancillary & promotional
  - “Legal” risk: not a separate legal entity
  - Major setup considerations:
    - *Lease signing*
    - *Employee compensation & tax*
    - *Provision of various credential documents*

# Foreign Invested Enterprise

- WFOE/JV
  - Scope of permitted activities: enumerated in business license
  - “Legal” risk: liabilities of a shareholder
  - Major setup considerations:
    - *Capital investment – trapped cash issue*
    - *Tax-efficient structuring under tightened rules*
    - *JV agreement terms*

# Branch Office

- Branch Office
  - Not a legal entity but required to be set up if business (e.g., contract signing, sales, hiring, tax) is conducted in another city
  - Scope of permitted activities: same as main corporate entity (e.g., WFOE/JV)
  - “Legal” risk: main corporate entity (e.g., WFOE/JV) is liable for Branch Office’s liabilities
  - Major setup considerations:
    - *Comply with local requirements*
    - *Local employment/benefit-related regulations*
  - Liaison Office – not to conduct “business”

# Hiring of Local Staff in China



## Hypothetical #3

- Your company decides to establish a Representative Office in Beijing & hire several marketing employees.
  - What is the hiring process?

# Indirect Hiring

- Must hire PRC employees through a “service corporation”
  - What is a service corporation?
  - Foreign Enterprise Service Corporation (FESCO)
  - China International Intellectech Corporation (CIIC)
- What types of services are provided?
  - Conducting reference checks
  - Registering with local tax authority & labor bureau
  - Arranging contributions to social insurance funds

# Service Corporation

- Advantages
  - Service corporations handle employment-related matters (e.g., hiring & termination formalities) to ensure compliance
  - Payroll-related tasks (e.g., payroll, tax withholding, social security contributions) can be outsourced to service corporations
- Disadvantages
  - Costs associated with using a third-party agent
  - Employment relationship is “tri-party” so service corporation’s “view” must always be considered

# Hiring Documents

- Template documents
  - Labor services contract between service corporation & Representative Office
  - Labor contract between service corporation & PRC employee
- Representative Office may enter into supplemental employment contract with PRC employee

# Supplemental Employment Contract

- Recommended provisions
  - Probationary period
  - Fixed term of employment
  - Company benefits & allowances
  - Confidential information
  - Intellectual property
  - Restrictive covenants
  - Notice & severance (if different from template labor contract)
  - Sick-day benefits
  - Detailed job/target descriptions

## Hypothetical #4

- What if your company decides to establish a WFOE (or Branch Office) in Beijing?
  - What is the hiring process?

# Direct Hiring

- Direct hiring of PRC employees
- Advantages
  - No need to use service corporation: cost savings & direct dealing with employees
  - Employment-related matters can be taken care of in-house
- Disadvantages
  - HR staff may not be as experienced as service corporation in dealing with employee issues, so outside legal counsel's assistance may be needed

# Indirect Hiring

- Certain types of employees can be hired through service corporation, i.e., temporary workers
- Indirectly hired employees have the same rights as directly hired employees
- Legal risks: service corporation shifts liability of determining eligibility of temporary workers to WFOE/Branch Office
- Benefit: simplifies HR functions



# Hiring Documents

- Mandatory written contract terms
  - Name, domicile, & legal representative of company
  - Name, domicile, & ID card number of PRC employee
  - Term of contract
  - Job description & place of work
  - Leave policy
  - Remuneration
  - Social insurance
  - Labor protection, working conditions, & protection against occupational hazards

# Additional Contract Provisions

- Recommend other provisions be added to contract
  - Probationary period
  - Training & reimbursement arrangement
  - Confidential information
  - Intellectual property
  - Restrictive covenants
  - Notice & severance

# General Contract Requirements

- Either Chinese or bilingual, but Chinese prevails in case of dispute
- Signed contract within one month from commencement date
- Penalty for noncompliance
  - If not signed after one month & before one year of employment, must pay double salary from second month until contract is signed
  - If not signed after one year of employment, must pay double salary for 11 months, & it is deemed indefinite-term contract

# Employee Termination Scenarios

## Hypothetical #5

- Your WFOE (or Branch Office) has a PRC employee who is not performing up to company standards & expectations. The manager wants to terminate the employment relationship.
  - What are the issues?
  - Does it make a difference if the employee is in the probationary period?

# No At-Will Employment

- Fixed-term employment
  - Allowed two consecutive term contracts
- Indefinite-term employment
  - Indefinite term if renewed for second time
- Can only terminate prior to expiration of fixed term or during indefinite term for specific statutory reason

# Statutory Termination Reasons

- Examples
  - Employee fails to satisfy job requirements during probationary period
  - Employee is in serious violation of employer rules & policies
  - Employment contract was entered into by employee's deception
  - Employee is not qualified for position & continues to fail to satisfy job requirements after training or reassignment
  - Employer has change of business direction, major technological improvement, or adjustment to mode of operations
  - Employer & employee mutually agree to termination

# Documentation for Possible Termination

- Job description
  - Detailed & verifiable
  - Anticipating performance-related actions (e.g., demotion/termination, although very difficult)
- Documentation of unsatisfactory performance
  - Record of warnings & low performance ratings



# Procedural Requirements

- Training
  - No legal standard
  - Outside training program, internal training program, one-on-one meetings with manager
- Adjustment/reassignment
  - Adjust/change employee's position
  - Reassign employee to lower-level position

# Termination Options

- Unilateral termination
  - Written notice & statutory severance pay
- Mutual agreement to terminate
  - Company severance pay (in addition to statutory severance pay)
  - Execute termination agreement
- Continued employment if fixed-term contract
  - Low base salary
  - Expiration of fixed term

# Termination Agreement

- Either Chinese or bilingual, but Chinese prevails in case of dispute
- Recommended provisions
  - Specific mutual agreement
  - Itemized statutory & company payments
  - Confirmation of full settlement of all claims (release/waiver may not be valid)
  - Nondisparagement
  - Confidentiality
  - Return of company materials & property
  - Restrictive covenants

# Acquisition-Related Employee Transfer Issues

## Hypothetical #6

- Your China subsidiary would like to sell a division (including the assets thereof) to a business partner. However, only a portion of the employees will be transferred to the buyer.
  - How do you “transfer” the employees?
  - What are your options regarding those employees who will not be transferred?

# Change of Employment Relationship

- An employee's contractual relationship is with her/his current employer, so any changes to such relationship either:
  - require employee consent
    - *Art. 35 of the Labor Contract Law – labor contract may be amended with mutual consents*
  - or should be sanctioned by law
    - *Art. 40(3) of the Labor Contract Law*
    - *Explanation from the Ministry of Labor Concerning the Various Regulations of the Labor Law*

# Transferred Employees

- Employee agrees to be transferred to buyer
  - Procedures
    - *Employee & current employer reach mutual agreement to terminate labor contract*
    - *Buyer hires transferred employee*
  - Severance payment
    - *either current employer pays, or*
    - *buyer assumes seniority*

# Nontransferred Employees

- Employee refuses to join buyer or receives no offer from buyer
  - If division assets are also sold:
    - *Employer & employee discuss contract amendment re: whether employee can continue working for employer under different terms*
    - *If changes cannot be agreed to:*
      - Employer can terminate labor contract with 30-day notice or compensation in lieu thereof
      - Compensation should be made according to “standard” severance pay formula
  - If assets are not sold:
    - *Labor contract cannot be terminated*



# Our Team



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