

CHINA'S LABOR LAW EVOLUTION: TOWARDS A NEW FRONTIER

*Monique Garcia**

I.	INTRODUCTION	236
II.	THE ERA BEFORE THE LCL—A WEAK BODY OF LABOR AND EMPLOYMENT LAWS	237
III.	THE LCL WAS ADOPTED AMID A LABOR CONTROVERSY—THE TIDE SHIFTS	238
IV.	THE PURPOSE BEHIND THE LCL—HARMONIOUS EMPLOYMENT RELATIONSHIPS	238
V.	THE ADOPTION OF THE LCL—THE INTERNAL AND EXTERNAL PRESSURES	239
VI.	THE LCL'S MAIN PROVISIONS WHICH INCREASE LABOR COSTS FOR AMERICAN FIES	241
	A. <i>The LCL's Central Tenet—the Obligation to Conclude Written Labor Contracts</i>	242
	B. <i>Cap on Fixed-Term Contracts—Less Flexibility For FIEs</i>	243
	C. <i>Non-Fixed Term Employment Contracts—More Rigid than the American Counterpart</i>	243
	D. <i>Probationary Periods—Stricter than Ever</i>	244
	E. <i>Employees' Rights to Terminate Contracts and Receive Severance Pay</i>	244
	F. <i>Increased Involvement of Labor Unions</i>	246
VII.	THE LCL'S IMPACT ON AMERICAN FIES—THE RISING COST OF DOING BUSINESS	247
	A. <i>Vague Laws Confuse FIEs</i>	247
	B. <i>The LCL Increases FIEs' Labor Costs</i>	248
	C. <i>Litigation Increases—No Escape for FIEs</i>	250
	D. <i>Arbitration and Litigation Courts Favor Workers</i>	251
	E. <i>Some Companies Prefer To Shut-Down</i>	252
VIII.	LABOR DISPATCH AGENCIES AS LOOPHOLES	252
IX.	CONCLUSION	254

* J.D. Candidate, May, 2010, Nova Southeastern University, Shepard Broad Law Center; B.A., McGill University (Montreal, Canada), Political Science Honors Program; LL.B., Université de Montréal (Montreal, Canada), Quebec Civil Law. She served as a legal intern for the International Criminal Defense Attorney's Association and for the Honorable Judge Peter M. Weinstein, Circuit Civil Judge of the 17th Judicial Circuit of Florida. The author wishes to thank her parents, Graciela Sanchez-Garcia and Percy Garcia Vargas for their guidance and her husband, Jan Gora, for his unending support.

I. INTRODUCTION

The People's Republic of China (P.R.C.) is moving towards becoming the biggest economy in the world. The P.R.C., like India, is on the fast track to usurping Germany, Japan and the United States in this regard. A huge export of artificially low-priced Chinese-made products is one of the primary reasons behind this growth. Currency manipulation, government subsidies, and repression of workers' rights—cumulatively help to create artificially low prices.¹ The P.R.C.'s ability to offer cheap labor is mainly due to lax labor laws, routine violations of workers' rights, the non-uniform implementation of these labor laws, and the loopholes that exist in them. The unfair competitive advantage the P.R.C. enjoys in the international market translates into trade deficits with other countries, like the one with the United States, which now stands at more than 123 billion U.S. dollars.²

The Labor Contract Law (LCL)—which became effective on January 1, 2008³—significantly increases workers' rights and consequently, the cost for their labor services. The price for Chinese-made products that were traditionally produced at very inexpensive rates, will translate into higher costs for the producers including U.S. foreign investment enterprises (FIEs). The U.S. administration has yet to officially support the P.R.C.'s LCL. The U.S. administration should strongly support the LCL, not in spite of the fact that it will increase labor costs for U.S. FIEs in the P.R.C., but because it will necessarily increase production costs. By supporting the P.R.C. in their efforts to decrease labor abuses and exploitation of workers by domestic and foreign businesses, the United States will provide the international strength and global support needed to advance workers' rights. In addition to promoting the LCL for traditional reasons, the United States should officially support the LCL because many U.S. FIEs in the P.R.C. will look towards the United States for guidance. If the United States strongly supports the LCL, then U.S. FIEs will be more likely to abide by it. Consequently, production costs will increase, thereby making it less likely that the United States will continue to import the massive amounts of Chinese-made products it currently does.

1. Brett Gibson, Legislative Representative, AFL-CIO Indus. Union Council, Implications of US-China-Pacific Trade and Investment Trends, Address to the US Int'l Trade Comm'n on US-China Trade, available at <http://www.aflcio.org/issues/jobseconomy/manufacturing/upload/GibsonChina20070308.pdf> (last visited Sept. 29, 2009).

2. United States Census Bureau, *Trade in Goods (Imports, Exports and Trade Balance) with China*, FOREIGN TRADE STATISTICS, available at <http://www.census.gov/foreign-trade/balance/c5700.html#2009> (last visited Sept. 29, 2009).

3. Lao dong he tong fa, Labor Contract Law (P.R.C.) (promulgated by the Standing Comm. Nat'l People's Cong., Jun. 29, 2007, effective Jan. 1, 2008), 2008 China Law Lexis 2288.

This note will explain why the LCL is a welcome addition to the existing body of labor law in the P.R.C., and it will further explain the circumstances surrounding the adoption of the LCL including internal and external pressures. This note will introduce the LCL, its purpose, and the main provisions that will increase labor costs for American FIEs; the LCL's impact on American FIEs, including increases in labor costs and litigation; the problems concerning its implementation and the bias in the courts; the loopholes that exist in the LCL that help FIEs, and provide a new justification for the U.S. administration to support the LCL.

II. THE ERA BEFORE THE LCL—A WEAK BODY OF LABOR AND EMPLOYMENT LAWS

Before the implementation of the LCL, there was no cohesive body of laws regulating labor and employment law⁴, including those found in the P.R.C. Constitution. The first wave of modern labor law reform—attempting to cure the deficiencies—appeared in 1994 with the passage of the Labor Law, a response to large-scale protests denouncing workers' exploitation.⁵ The 1994 Labor Law made significant strides towards protecting workers from employer exploitation but did not fully succeed. There were two main reasons why the 1994 Labor Law only minimally decreased employee exploitation. First, the local, as opposed to the national, governments were the primary source of implementation of these laws, and therefore these laws varied from district to district.⁶ Secondly, the 1994 Labor Law was perceived by employers and enforcers as a voluntary and non-binding measure which led some employers to routinely violate its provisions.⁷ Therefore, while the 1994 Labor Law seemingly protected workers from exploitation by, for example, stipulating that laborers could not work for more than eight hours a day,⁸ there was a lack of adequate enforcement.⁹ Some reports revealed that workers—in the

4. Jeffrey A. Blount & Lixin Chen, *Working with China's New Labor Contract Law*, in *DOING BUSINESS IN CHINA 2008, PRACTICING LAW INSTITUTE COURSE HANDBOOK* 129, 131 (2008), available at 1681 PLI/Corp 129 (Westlaw) (last visited Oct. 20, 2009).

5. See Feng Xu, *Labor Law Developments in China: The Emergence Of Temporary Staffing Agencies In China*, 30 *COMP. LAB. L. & POL'Y J.* 431, 448 (2009) [hereinafter Xu].

6. Blount & Chen, *supra* note 4, at 131.

7. See *id.*

8. Lao dong he tong fa, Labor Law (P.R.C.) (promulgated by the Standing Comm. Nat'l People's Cong., Sept. 5, 1994, effective Jan. 1, 1995) (P.R.C.), 1995 China Law LEXIS 764.

9. Winston Zhao, Owen D. Nee Jr., & Jones Day, *Ensuring Compliance with China's New Labor Laws*, in *DOING BUSINESS IN CHINA 2008, PRACTICING LAW INSTITUTE CORPORATE LAW AND*

southern manufacturing district of China—were forced to work twelve-hour days, six days a week and eight hours on Sundays; there were frequent delayed payment of wages and employees needed permission to resign.¹⁰ The weak enforcement has led labor-rights' activists and international critics to accuse the P.R.C.'s authorities of willful blindness to employee exploitation.¹¹ In essence, the 1994 Labor Law was viewed as a non-binding voluntary proposal by domestic and foreign investment enterprises and because there were no enforcement mechanisms in place the provisions were neither respected nor enforced.

III. THE LCL WAS ADOPTED AMID A LABOR CONTROVERSY— THE TIDE SHIFTS

Massive labor protests prompted the adoption of the LCL on July 7, 2007.¹² The labor protests were in reaction to the Chinese press reports revealing that some workers “were kept like slaves in brickworks,” which subsequently became a “national matter.”¹³ In the Shanxi and Henan provinces, police freed nearly 600 workers held as slave laborers, many of them children.¹⁴ Partly because of the widespread reaction to this horrifying story, the LCL was quickly adopted on June 29, 2007 to become effective on January 1, 2008.¹⁵

IV. THE PURPOSE BEHIND THE LCL—HARMONIOUS EMPLOYMENT RELATIONSHIPS

The stated purpose of the LCL is to institute and further a harmonious relationship between employers and employees.¹⁶ The President and Supreme Leader of the P.R.C., Hu Jintao, stated that the goal of the “Harmonic Society” is akin to the “Long March” from the civil war; however, he declared that “this journey would be just as challenging with

PRACTICE COURSE HANDBOOK 149, 155 (2008), available at 1681 PLI/Corp 149 (Westlaw) [hereinafter Zhao, Nee Jr., & Day] (last visited Oct. 20, 2009).

10. Blount & Chen, *supra* note 4, at 131–32.

11. *Id.* at 132.

12. Xu, *supra* note 5, at 448–49.

13. Wolfgang Daubler & Qian Wang, *The New Chinese Employment Law*, 30 COMP. LAB. L. & POL'Y J. 395, 404 (2009) [hereinafter Daubler & Wang].

14. Joseph Kahn & David Barboza, *As Unrest Rises, China Broadens Workers' Rights*, N.Y. TIMES, Jun. 30, 2007, at A1, available at ProQuest 1297271211 [hereinafter Kahn & Barboza] (last visited Oct. 20, 2009).

15. Labor Contract Law; Zhao, Nee Jr., & Day, *supra* note 9, at 158.

16. Labor Contract Law art. 1.

hazards and risks”.¹⁷ In essence, the law was formulated to improve labor relations by specifying workers’ rights and the duties of parties to labor contracts. In so doing, the legal reform would protect the legitimate interests of workers and thus create stable and harmonious employment relationships.¹⁸

V. THE ADOPTION OF THE LCL—THE INTERNAL AND EXTERNAL PRESSURES

“Both the National People’s Congress (NPC) and its Standing Committee (NPC SC) have the authority . . .” pursuant to the P.R.C. Constitution to pass laws.¹⁹ The NPC has about 3000 delegates and meets approximately once a year to pass “basic laws” regarding criminal, civil, and other matters.²⁰ On the other hand, the NPC SC, with a membership of 150 delegates, meets throughout the year when the NPC is not in session, to enact “ordinary laws” which are not specifically delegated to the NPC.²¹ Despite the seemingly overlapping nature of their rights and duties to pass laws, a trend has emerged that delineates the perimeter for passing laws. Basic laws, which are exclusive to the NPC, include criminal law and procedure, property law, and economic and contract law.²² Ordinary laws, including labor and employment law, are traditionally passed by the NPC SC.²³

From nearly its inception, the NPC SC controlled the drafting process of the new LCL and held open debates amongst themselves.²⁴ There was a caucus that believed that there should be an explicit bias in favor of the traditionally exploited employee. On a more cogent side of the spectrum was a group of delegates that believed that an explicit bias would scare FIEs into neighboring countries, like Vietnam, for cheap labor. Those members favoring an explicit bias in favor of employees reasoned that workers were the weaker party who adhered to a standard labor contract written by the economically stronger employer.²⁵ Therefore, employee advocates in the

17. Daubler & Wang, *supra* note 13, at 408.

18. Labor Contract Law art. 1.

19. Hilary K. Josephs, *Measuring Progress Under China’s Labor Law: Goals, Processes, Outcomes*, 30 COMP. LAB. L. & POL’Y. J. 373, 377 (2009) [hereinafter Josephs].

20. *Id.*

21. *Id.*

22. *Id.* at 378.

23. *Id.*

24. Josephs, *supra* note 19, at 381.

25. *Id.*

NPC SC favored a provision, which was not incorporated, that any ambiguity in the LCL would be construed in favor of the employee.²⁶ Meanwhile, those favoring neutrality disfavored a provision, which was incorporated, that required severance pay for employees whose fixed-term contracts had lapsed.²⁷ Overall, the LCL is riddled with this tension between neutrality and an overt bias in favor of employees.

In addition to the internal debates, there were external pressures from different interest groups opposing the LCL. The government allowed public comments to be made on the first draft of the LCL and received more than 190,000 responses.²⁸ Among the communications, there were strong oppositions by various FIEs, complaints from workers concerning unpaid overtime wages, delayed payment of wages, non-payment of social insurance premiums, and concerns by labor dispatch agencies (LDAs), also known as personnel staffing agencies, that provide temporary workforce to companies.²⁹

However, the strongest and most organized opposition came from foreign businesses operating in the P.R.C. Because the LCL's central tenet requires companies to conclude written contracts with their employees³⁰—a provision likely to increase labor costs because of the lack of workforce flexibility³¹—many American corporations strongly lobbied against this new law through their Chambers of Commerce or local trade associations.³² For example, the American Chamber of Commerce in China (AmCham) vigorously lobbied against the LCL stating that it would increase labor costs and would make products less competitive.³³ In addition, some large U.S. multinational corporations waged a strong lobbying campaign against the LCL.³⁴ Some even threatened to move their businesses to Vietnam.³⁵ At least one commentator believes that the negative press these organizations

26. *Id.*

27. *Id.* at 382.

28. Blount & Chen, *supra* note 4, at 131; AsiaLaw.com, Preview of China's Draft Labour Law, <http://www.asialaw.com/Article/1971109/Preview-of-Chinas-Draft-Labour-Contract-Law.html?Print=true&Single=true> (last visited Sept. 29, 2009).

29. Josephs, *supra* note 19, at 385.

30. Labor Contract Law art. 10.

31. *See infra* § VII.

32. Joe W. (Chip) Pitts III, *Corporate Social Responsibility: Current Status and Future Evolution*, 6 RUTGERS J.L. & PUB. POL'Y 334, 400–01 (2009).

33. Xu, *supra* note 5, at 454–55.

34. David Barboza, China Drafts Law to Empower Unions and End Labor Abuse, N.Y. TIMES, Oct. 13, 2006, at A1.

35. Xu, *supra* note 5, at 455.

received in the West—essentially labeling them “anti-union”—were unfounded; since many FIEs brought their labor practices into the P.R.C., Chinese workers were essentially treated the same as workers in the United States.³⁶ In essence, most American FIEs argue that the LCL established standards too high for a country historically known for its cheap labor market.³⁷ Despite AmCham’s lobbying campaign against the LCL and some American FIEs threatening to move their businesses to Vietnam, some high profile FIEs distanced themselves from the negative reactions to the LCL. Particularly, Nike revoked its support for the U.S. Chamber of Commerce in Shanghai.³⁸

The temporary staffing industry lobbied against two articles of the LCL, which were eventually taken out. The first of these two articles required the LDA to deposit 5000 yuan³⁹ for every one of its employees in a government-designated bank account; the second article required a dispatched employee who worked for the same corporate client for more than one year to terminate the contract with the LDA and sign a labor contract with the corporate client, if the company intended to keep the employee.⁴⁰ The final version of the LCL obliges LDAs to sign a labor contract for at least two years with employees and pay the local minimum wage to employees for whom the LDAs have not found employment with an employer.⁴¹

VI. THE LCL’S MAIN PROVISIONS WHICH INCREASE LABOR COSTS FOR AMERICAN FIEs

Notwithstanding the provisions concerning labor unions, the articles of the LCL that most impact the rising cost of labor for FIEs include the obligation to conclude written contracts with all full-time employees, the non-fixed term employment relationship, the various situations in which employees are entitled to severance pay, and the regulations regarding the labor dispatch industry.

36. Zhao, Nee Jr., & Day, *supra* note 9, at 159.

37. Xu, *supra* note 5, at 455.

38. *Id.*

39. Equivalent to approximately 732 US dollars, exchange rate from yuans to dollars as of September 18, 2009. Google Unit Conversion, www.google.com/UnitConversion (last visited Oct. 5, 2009).

40. Xu, *supra* note 5, at 455.

41. Labor Contract Law art. 58 para. 2.

A. The LCL's Central Tenet—the Obligation to Conclude Written Labor Contracts

There are three types of employment contracts stipulated in the LCL: fixed-term, non-fixed term, and project-specific contracts.⁴² Regardless of the type, an employer must conclude a written contract with all of its employees and has a one month grace period—starting from the date the employee started working—in which to comply.⁴³ This is the foundation and the heart and soul of the LCL. If the employer fails to abide by the requirement to sign an employment contract—for more than one month but less than a year—then he/she must pay double the employee's salary for every month the employee was working without a contract and still sign a written labor contract.⁴⁴ If the employer abstains from signing a labor contract with the employee for one year or more, then the employment relationship automatically becomes one based on a non-fixed term labor contract—which will later be explained to have its own serious repercussions.⁴⁵ The employment contract must identify the employer and employee, contain basic contact information of both parties, specify the employment period, job description, place of work, working hours, breaks and leave, remuneration, social insurance benefits, labor protection, working conditions, protections against occupational hazards, and other requisite terms.⁴⁶ In addition, the employer and employee may negotiate—while still respecting the law—additional clauses in the employment contract such as probationary periods, training, confidentiality, supplementary insurance, and other benefits.⁴⁷ The LCL creates a floor of minimum standards for employees while leaving the parties to the labor contract the opportunity to negotiate better terms. The requirement to have a written labor contract for every employee creates an obligation previously unknown or unpracticed by most employers, thus reducing workforce flexibility for the employer and hence increasing labor costs.

42. *Id.* art. 12.

43. *Id.* art. 10.

44. Shi shi gui li zai zhong hua ren min gong he guo, Implementing Regulations of the People's Republic of China on Labor Contract Law art. 6 (promulgated by the State Council, Sept. 18, 2008, effective Sept. 18, 2008), 2008 China Law Lexis 204; *see also* Labor Contract Law art. 82 para. 2.

45. Implementing Regulations of the People's Republic of China on Labor Contract Law art. 7.

46. Labor Contract Law art. 17.

47. *Id.* art. 17 para. 2.

B. Cap on Fixed-Term Contracts—Less Flexibility For FIEs

In the past, employers would entertain a flexible workforce by executing multiple and consecutive fixed-term employment contracts without any consequences.⁴⁸ For example, an employer would conclude a two year employment contract, followed by a one year contract, and then another two year contract, thus maintaining flexibility over the workforce.⁴⁹ Currently, the LCL permits an employer to conclude no more than two consecutive fixed-term employment contracts with an employee; after the second fixed-term employment contract—and if the employer and employee intend to continue the employment relationship—the employee will automatically have a non-fixed term employment contract.⁵⁰ In addition, the employee will be entitled to a non-fixed term employment contract if he has worked consecutively for the employer for ten years or more.⁵¹ In both situations, the employee may waive his rights to a fixed-term contract, if he/she so chooses.⁵² However, if the employee chooses to enforce his/her rights pursuant to the law and demand a non-fixed term employment contract—but the employer does not comply—then the employer will be sanctioned and be required to pay double the salary of the employee starting from the day the non-fixed term contract was supposed to begin.⁵³ These provisions create new and costly obligations for employers.

C. Non-Fixed Term Employment Contracts—More Rigid than the American Counterpart

A corporation's greatest fear concerns the provisions concerning non-fixed term contracts.⁵⁴ A non-fixed term employment contract is unlike its American counterpart—which is typically known as at-will employment.⁵⁵ In the United States, an employer may unilaterally terminate an employment at-will relationship without serious repercussions, for good cause, bad cause or no cause at all. However, in China, a non fixed-term employment contract may only be terminated for good cause and with

48. Zhao, Nee Jr., & Day, *supra* note 9, at 162–63.

49. *Id.*

50. Labor Contract Law art. 14 para. 2 (3).

51. *Id.* art. 14 para. 2 (1).

52. *Id.* art. 14 para. 2.

53. *Id.* art. 82 para. 2.

54. Xu, *supra* note 5, at 456.

55. Jian Hang, *Understanding China's Newly Adopted Labor Contract Law*, in *DOING BUSINESS IN CHINA 2008, PRACTICING LAW INSTITUTE CORPORATE LAW AND PRACTICE COURSE HANDBOOK 105, 109 (2008)*, available at 1681 PLI/Corp 105 (Westlaw) (last visited Oct. 20, 2009).

severance pay, creating serious obligations for the employer. In that sense, the main difference between a non fixed-term employment contract and a fixed-term employment contract is that the latter expires automatically, while both warrant severance pay.⁵⁶ Consequently, this increases labor costs for American FIEs who would rather maintain a flexible workforce.

D. Probationary Periods—Stricter than Ever

Prior to the passage of the LCL, probationary periods were highly discretionary, and employers used it as a tool for exploitation. Employers controlled the length of the probationary period, terminated without cause, and paid less than the amount to be paid after the probation period or even less than the local minimum wage.⁵⁷ Now, the LCL calculates the probationary period based on the term of the employment contract. For a contract duration of less than three months or for a specified completion of work, the probation periods are prohibited; for a contract with a three month duration or more but less than a year, the probationary period is one month; for a contract duration of one year or more but less than 3 years, the probationary period is a maximum of two months; if the contract duration is for three years or more or constitutes an open-ended contract, then the probationary period cannot exceed six months.⁵⁸ Likewise, the LCL provides that an employee on probation must not be paid less than eighty percent of the salary agreed upon in the employment contract post probationary period, or not lower than eighty percent of the lowest salary for the same job with the same employer—but in neither circumstance can the probation period wage be less than the local minimum wage.⁵⁹

E. Employees' Rights to Terminate Contracts and Receive Severance Pay

The situations in which employees are entitled to severance pay pursuant to the LCL are more extensive than ever before, hence significantly increasing labor costs.⁶⁰ There are many enumerated instances where an employee may unilaterally terminate the employment contract and receive severance pay. For example, if the employer's rules and policies

56. Blount & Chen, *supra* note 4, at 133.

57. *Id.* at 134.

58. Labor Contract Law art. 19.

59. Labor Contract Law art. 20; Implementing Regulations of the People's Republic of China on Labor Contract Law art. 15.

60. Meg Utterback, *Utterback on Chinas Labor Contract Law*, LEXISNEXIS EXPERT COMMENTARIES, Jan. 14, 2008, at 4–6, available at 2008 Emerging Issues 1778 (Lexis) (last visited Oct. 20, 2009).

violate the law thereby harming the employee or his interests, then the employee may sever employment ties and receive severance pay.⁶¹ This would be cause for concern to any domestic or foreign investment enterprise which have not updated their employment manuals outlining the company's policies which may otherwise violate the law.

In addition, an employee is not required to provide notice prior to terminating the employment contract and is still entitled to severance pay for a slew of statutory reasons concerning employees' workplace safety. More precisely, the employee will be entitled to severance pay—and not be required to provide notice of termination of the employment contract—when the employer fails to provide safety measures,⁶² fails to pay wages on time and in full,⁶³ or fails to contribute to social insurance premiums for employees as required by law.⁶⁴ Furthermore, the employer must also pay severance if the employer compels the employee to work or conclude a contract using coercion, violence, threats, or unlawful restriction of personal freedom,⁶⁵ or when the employer instructs the employee to perform dangerous tasks, thus putting the employee's safety at risk.⁶⁶ In all these circumstances, the employer's costs substantially increase because the LCL creates new and extensive obligations to pay severance. However, when an employee deceives the employer or moonlights, the employer may terminate the employment relationship for cause.⁶⁷

Severance pay is calculated based on the number of years the employee has continuously worked for the employer: one month's salary is to be paid for every year of service or portion thereof, if the employee worked for at least six months, while working less than six months will be rewarded with half a month's salary.⁶⁸ In turn, salary is defined as the employee's average monthly wages over a twelve month period immediately preceding the termination of his employment contract.⁶⁹ However, to lessen the burden on employers, severance pay is calculated from the LCL's effective date, January 1, 2008, and not from when the employee started working—which may have been many years before

61. Labor Contract Law art. 38 (4).

62. *Id.* art. 38 (1).

63. *Id.* art. 38 (2).

64. *Id.* art. 38 (3).

65. *Id.* art. 38 para. 2.

66. Labor Contract Law art. 38 par. 2.

67. Blount & Chen, *supra* note 4, at 138.

68. Labor Contract Law art. 47.

69. *Id.* art. 47 para. 3.

2008.⁷⁰ In addition, if the employee earned three times as much as the average employee in the district, then the severance pay will be “three times . . . the average monthly wages of employees’ . . .” as determined by the local government.⁷¹ Notwithstanding the provisions capping the amount of severance to be paid per employee, the fact that there are many more situations requiring the payment of severance creates a substantial increase of labor costs for employers, including American FIEs.

F. Increased Involvement of Labor Unions

The LCL presupposes that labor unions are established in all domestic and foreign investment enterprises; as such, it grants labor unions’ increased involvement which in turn increases labor costs significantly. In addition, the LCL may be interpreted as strongly encouraging foreign and domestic enterprises to establish labor unions by acknowledging—in the language of the LCL—that labor unions already exist in the workplace.⁷² In fact, the Communist Party and the All-China Federation of Trade Unions (ACFTU) have quotas to establish union presence in ninety percent of all private corporations, including FIEs.⁷³

An employer must give prior notice to the labor union when unilaterally terminating an employment contract, even when an employee is not a member of the union.⁷⁴ The labor union may even channel the interests of the employee and demand reinstatement.⁷⁵ The LCL further requires that the employer consider the opinions of the labor union and inform the union of its final decision.⁷⁶ For example, if the employer terminates an employment contract in violation of the law, then the employee is entitled to reinstatement,⁷⁷ and the labor union can rally for the worker’s rights in this regard. If reinstatement is impossible—because the worker has been replaced—then the employer must pay the employee double the amount of severance pay owed as a penalty.⁷⁸ In general,

70. *Id.* art. 97 para. 3.

71. *Id.* art. 47 para. 2.

72. Lesli Ligorner & Monica Lynn Debiak, *Navigating the New Employment Contract Law*, CHINA LAW & PRACTICE, § 2, Jul., 2007, available at ProQuest 10126724 (last visited Oct. 20, 2009).

73. *Employment Law Prompts Foreign Companies to Clean House*, CHINA LAW & PRACTICE, § 57, Jul., 2007, available at ProQuest 1319071201 (last visited Oct. 20, 2009).

74. Labor Contract Law art. 43.

75. *Id.*

76. *Id.*

77. Labor Contract Law art. 48.

78. *Id.*

arbitrators and courts have utilized the payment of double severance pay as a penalty, but in some cases they have ordered reinstatement.⁷⁹ The obligation to pay double the salary as payment for failure to lawfully terminate an employment contract is indeed a hefty fine for employers who previously took the lax labor laws for granted.

Lastly, clauses in an employment contract that exploit workers and/or infringe on their statutory rights will render the contract invalid.⁸⁰ For instance, securing consent of an employee through threats or duress,⁸¹ a contract containing terms contrary to the provisions of the LCL,⁸² a written waiver of the employee's statutory rights—are all examples of invalid contracts.⁸³ Hence, any deviation in the employment contract to the obligations set forth in the LCL will be considered, in part or in whole, invalid. This creates a heavy burden on employers who seek to maintain a flexible workforce.

VII. THE LCL'S IMPACT ON AMERICAN FIEs—THE RISING COST OF DOING BUSINESS

While some experts believe that the LCL replaces and abridges the 1994 Labor Law, others think that it simply elaborates and builds upon existing rights.⁸⁴ However, most observers agree that employees' rights are extensively increased by this new development in Chinese labor law.⁸⁵

A. Vague Laws Confuse FIEs

The LCL is vague in many respects. For example, although the purpose of the LCL is to foster harmonious employment relationships, the result may be quite the opposite whereby adhering to the LCL's obligations creates animosity and distrust. The P.R.C.'s central government recognized that the lack of governmental interpretation prevented the complete and uniform implementation of the LCL. For direction, the government must issue guiding opinions since court interpretations in the P.R.C.'s civil law society do not adhere to *stare decisis*.⁸⁶ The central government has been

79. Blount & Chen, *supra* note 4, at 142.

80. Labor Contract Law art. 26.

81. *Id.* art. 26 (1).

82. *Id.* art. 26 (3).

83. *Id.* art. 26 (2).

84. See Josephs, *supra* note 19, at 379.

85. See *id.* at 383–84.

86. Lauren Carasik, "Think Glocal, Act Glocal": *The Praxis of Social Justice Lawyering in the Global Era*, 15 CLINICAL L. REV. 55, 117 (2008).

late with issuing guiding opinions and hence some local governments have issued their own clarifications of the LCL, thereby contributing to the non-uniform implementation of the law. For example, the Guangdong province issued its own guiding principles before the central government released its own. The key clarification in the Guangdong guiding principles is that the objective of the legislation—a harmonious employment relationship—must correspond with the social *effect* of the law by analyzing the ultimate outcome by applying the LCL and not merely applying it in a social vacuum.⁸⁷ Therefore, many FIEs are confused about how the LCL's obligations work in practice. Although there have been a few Chinese legal commentaries on the ambiguities, in which gaps and loopholes are present, such legal commentaries that would help interpret its meaning have no legal force and effect on the LCL's interpretation, because only the government has that authority to the exclusion of courts and commentators.⁸⁸

B. The LCL Increases FIEs' Labor Costs

Since the P.R.C. opened its doors to foreign investors in the late 1970s, there has been a growing number of FIEs establishing manufacturing plants. There are currently more than 570,000 FIEs in the P.R.C., and they employ more than twenty-eight million Chinese workers—mainly in the coastal cities.⁸⁹ In 2008, there was 2.9 billion U.S. dollars in American non-financial foreign direct investment (FDI) in China.⁹⁰ These investments constitute American businesses that have invested in projects and not just monetary resources into China that mainly employ Chinese workers.

U.S. officials predicted on May 7, 2009 that 2009 would continue to be a challenging year for U.S. companies based in China as opposed to those

87. Joanna Law, *Labour Law: State Council Delays, as Guangdong Makes it Better*, CHINA LAW & PRACTICE, Sept., 2008, available at ProQuest 1572464961 (last visited Oct. 20, 2009); *Guangdong Province, Guiding Opinion on Several Issues Concerning the Application of the Law (Law on the Mediation and Arbitration of Employment Disputes) and the (Employment Contract Law)*, CHINA LAW & PRACTICE, Sept., 2008, available at ProQuest 1572464631 (last visited Oct. 20, 2009).

88. Daubler & Wang, *supra* note 13, at 405–06. The lack of Chinese legal commentary is due to the Chinese culture's repression of individual observations; such observations would constitute an undesirable self-aggrandizement of the individual.

89. Zhao, Nee Jr., & Day, *supra* note 9, at 159; see Samuel Estreicher, Michael J. Gray, & Winston Zhao, *Preparing for China's New Employment Contract Law*, METROPOLITAN CORPORATE COUNSEL, Nov., 2007, at 33, available at <http://www.metrocorp counsel.com/current.php?artType=view&artMonth=November&artYear=2007&EntryNo=7428> (last visited Sept. 25, 2009).

90. The US-China Business Council, *Foreign Direct Investment in China*, http://www.uschina.org/statistics/fdi_cumulative.html (last visited Oct. 5, 2009).

based in the United States.⁹¹ Due to the various LCL requirements that increase labor costs and decrease workforce flexibility,⁹² it is estimated that some labor-intensive businesses will have to raise their selling prices or move to neighboring countries that offer a cheaper labor force. For example, Olympus Corp.⁹³ and Yue Yuen Industrial Ltd.⁹⁴ are among companies shifting some production to Vietnam to cut costs.⁹⁵ There are some commentators who believe that many FIEs do not commit serious labor violations in the P.R.C., and therefore it is unlikely that they will alter their practices or policies at least at the onset.⁹⁶ However, most American FIEs operating in China believe that the LCL will negatively affect their businesses—mainly based on the obligation to conclude and enforce written labor contracts with all personnel, thus limiting their workplace flexibility.⁹⁷

Manufacturers, especially in labor intensive industries, will continue to experience rising costs and witness their products become less competitive in the global market with the adoption of the LCL. The improved working conditions will enable Chinese workers to be treated more equitably thus helping to close the gap of disparate treatment with workers from developed countries. In addition, the corollary cost increases will, over time, further narrow the trade imbalance as the price of Chinese-made goods become less competitive. Furthermore, since the P.R.C. constitutes such a large portion of the world's manufacturing capacity, the improved working conditions will make an impact on neighboring countries towards labor law reform. If more and more developing countries take the step towards labor law reform, like the P.R.C. to create harmonious employment relationships, which inevitably increases the wealth of workers, companies will have a more global consumer base willing and able to purchase goods and services. The

91. *U.S. Official Predicts Difficult U.S.-China Trade Relations in 2009*, INSIDE US TRADE, May 15, 2009, available at 2009 WLNR 9293476 (last visited Oct. 20, 2009).

92. Such as the obligation to conclude written labor contracts and the many instances where severance pay is due. *See supra* notes 33, 48, 50–53.

93. The world's fourth largest digital camera producer. *Labor Contract Law Enhances Workers' Rights*, CHINA DAILY, Jan. 1, 2008, at A1, available at http://www.chinadaily.net/bizchina/2008-01/01/content_6362688.htm (last visited Oct. 20, 2009) [hereinafter *Labor Contract Law Enhances Workers' Rights*].

94. *Id.* The biggest maker of brand name shoes. Yue Yuen Industrial (Holdings) Ltd., Corporate Profile, http://www.yueyuen.com/about_corporateProfile.htm (last visited Oct. 2, 2009).

95. *Labor Contract Law Enhances Workers' Rights*, *supra* note 93.

96. Zhao, Nee Jr., & Day, *supra* note 9, at 160.

97. GLOBAL LABOR STRATEGIES, WHY CHINA MATTERS: LABOR RIGHTS IN THE ERA OF GLOBALIZATION 43 (2008), http://laborstrategies.blogs.com/global_labor_strategies/files/why_china_matters_gls_report.pdf (last visited Sept. 30, 2009); Kahn & Barboza, *supra* note 14.

increased consumer base could only help American companies looking for new markets in which to sell their products.

Perhaps the most direct and immediate consequence of FIEs remaining in China is the need to update their employment manuals and revise employment contracts, and policies to ensure compliance with the LCL. They have had to employ law firms and experts to undertake this project at costly rates. Many FIEs have indeed revised or are updating their employment manuals, policies and contracts to comply with the LCL while other FIEs have taken a wait and see approach.⁹⁸ The wait and see approach may be a wise tactic for those circumstances that require further clarifications from the government.

C. Litigation Increases—No Escape for FIEs

The LCL has caused a sharp increase in litigation. This is mainly because the LCL was so well publicized that Chinese workers all over the country were made aware of their new and increased rights and because it is now free to file a claim.⁹⁹ Chinese lawyers were reported to have a multitude of employees ready to sue FIEs when the LCL was passed. Most experts agree that the prime targets for suits are U.S. companies because of their deep pockets.¹⁰⁰ To put a figure to the fact, 60,000 applications were set for arbitration at the end of 2008 in the Guangdong province—known as China's manufacturing hub—which is more than double the amount in the previous two years combined.¹⁰¹

Prior to the adoption of the LCL, an employee would be charged the equivalent of seventy three U.S. dollars to file a labor arbitration case; now, it is free of charge. The lack of a monetary barrier to sue has provided employees with an outlet in which to try their luck with an arbiter, whether their grievance is large or small and even if they were at fault.¹⁰² Some employees not entitled to full-time employee benefits, i.e. part-time employees or those hired on a consulting basis, have used the arbitration system as a means of threatening employers into providing full benefits

98. Blount & Chen, *supra* note 4, at 144; Brandon Kirk, *Putting China's Labor Contract Law into Practice*, CHINA LAW & PRACTICE, Mar., 2008.

99. Steven M. Dickinson & Daniel P. Harris, *Dickinson and Harris on China's New Labor Law*, LEXISNEXIS EXPERT COMMENTARIES, Dec. 6, 2007, at 2, available at 2008 Emerging Issues 1369 (Lexis) (last visited Oct. 20, 2009).

100. *Id.* at 1, 3.

101. Joanna Law, *Employers, Prepare for Tribunal Trouble*, CHINA LAW & PRACTICE, Feb., 2009, at 1, available at ProQuest 1663842791 [hereinafter Law] (last visited Oct. 20, 2009).

102. *Id.*

because of employers' fear of litigation.¹⁰³ Meanwhile, other employees simply do not understand the new LCL, thinking they have the right to sue based on minor and major issues alike, and some readily sue, thus further burdening companies with undue litigation.¹⁰⁴

Furthermore, a significant upsurge in litigation has presented the Chinese government with a huge problem, a lack of resources with which to enforce the law through arbitration and the courts.¹⁰⁵ These bureaucratic agencies have only minimally changed their staffing requirements and funding over the last decade. Consequently, the arbitration committee and court personnel are overworked. For example, in Guangzhou's central Haizhu district, the arbitration committee only has three members who work six days a week and hold evening sessions three times a week.¹⁰⁶

D. Arbitration and Litigation Courts Favor Workers

According to some reports, the arbitration tribunals in mainland China are biased in favor of employees suing their employers.¹⁰⁷ Because arbitration tribunals are sympathetic towards employees—who are traditionally seen as the weaker party—they will sometimes overlook a contract violation by the employee.¹⁰⁸ In addition, sometimes tribunals assume that companies can bear the financial losses more readily than employees.¹⁰⁹ Therefore, more often than not, employees win in arbitration or in court based on prejudice in their favor, thus creating huge burdens on companies. On average, plaintiff-employees “won in more than ninety five percent of the concluded cases, obtaining compensation for work-related injury, recovering unpaid wages, getting job reinstatement, or obtained other benefits such as labour insurance payouts.”¹¹⁰ In total, employees obtained equivalent to 1.5 million U.S. dollars in compensation and other benefits.¹¹¹ In addition, the burden of evidence lies with the employer,¹¹²

103. *Id.*

104. *Id.* at 2.

105. Geoffrey Crothall, *Workers' Rights in China*, WALL ST. J., May 1, 2008, at 15, available at <http://online.wsj.com/article/SB120958396010557153.html> (last visited Sept. 29, 2009).

106. *Id.*

107. *Law, supra* note 101, at 2.

108. *Id.*

109. *Id.*

110. China Labour Bulletin, *An Introduction to CLB's Labour Rights Litigation Work*, <http://www.china-labour.org.hk/en/node/100020> (last visited Oct. 2, 2009).

111. *Id.* Exchanged from 10.3 million yuans to dollars as of September 18, 2009. Google Unit Conversion, www.google.com/UnitConversion (last visited Oct. 5, 2009).

thus making it easier for employees to bring a suit. Most often, the employers' best evidence constitutes written records of how and when the employee violated company policy.¹¹³ However, even this will create problems, if the FIEs have not invested time in updating company policy and manuals to adhere to the new LCL. Furthermore, even when the evidence favors employers, they are advised to settle before reaching labor arbitration because of increasing costs associated with counsel, litigation, and general diversion of time.¹¹⁴

E. Some Companies Prefer To Shut-Down

At least some factories are choosing to discontinue operations to avoid paying workers' claims for unpaid wages and severance pay.¹¹⁵ Guangzhou city even issued an emergency circular reinforcing the provisions of the LCL for lawful mass lay-offs; it was reiterating that employers cannot engage in mass lay-offs to circumvent the LCL's requirements.¹¹⁶

VIII. LABOR DISPATCH AGENCIES AS LOOPHOLES

Whether called temporary staffing agencies, talent dispatch agencies, or human resource outsourcing, LDAs are intermediaries between the employers and employees providing a workforce. LDAs form a triangular employment relationship, whereby the employer—as client—pays an LDA for providing an employee, who in turn pays a salary to the employee. This triangular employment relationship provides employers with an intermediary which gives needed flexibility without breaking the law.¹¹⁷

In the weeks preceding the adoption of the LCL, reports surfaced that some companies were trying to conduct a “reverse-labor dispatch.” Employers would sever ties with their existing employees, have LDAs bid to be the designated LDA, have the employees sign an employment contract with the designated LDA, and be dispatched to their usual workplace.¹¹⁸ It

112. Law, *supra* note 101, at 3.

113. *Id.*

114. *Id.*

115. James Pomfret, *Chinese Workers Find Rights Imperiled in Crisis*, N.Y. TIMES, Feb. 9, 2009, <http://www.nytimes.com/2009/01/29/business/worldbusiness/29iht-labor.1.19774934.html> (last visited Oct. 2, 2009).

116. Guangzhou City, *Urgent Circular on Strengthening the Administration of Mass Layoffs by Employers*, CHINA LAW & PRACTICE, § 21, Feb., 2008, available at ProQuest 1506108311 (last visited Oct. 20, 2009).

117. Xu, *supra* note 5, at 431.

118. *Id.* at 457 (citing to Chinese article by Xue Song 2008).

is estimated that approximately twenty five million people in the P.R.C. work as “dispatched employees,” especially in the construction industry.¹¹⁹

LDAs are a preferred mode of obtaining a flexible, hence cheaper, workforce because it “. . . reduce[s] key costs, including pay-roll taxes; move their contributions to workers’ social security benefits from their wage bills to a tax-deductible cost; pay labor-dispatch workers lower wages than contract workers for the same job; and reduce the transaction costs and risks involved in employing workers such as hiring and firing.”¹²⁰

Furthermore, because labor dispatch workers work harder to keep their jobs, their presence alongside contract workers puts pressure on their contract worker colleagues to work harder as well.¹²¹ However, LDA supporters believe that it helps unemployed workers find at least temporary work.¹²² Although LDAs play a key role in helping unemployed workers find a source of income¹²³—albeit most often a temporary one—LDAs are viewed as a corporate mechanism to curtail the LCL’s obligation to conclude a labor contract with employees.¹²⁴

Not surprisingly, LDAs’ main clients include FIEs¹²⁵ who consider using LDAs as a means to provide needed flexibility without the need to conclude employment contracts. LDAs’ promise of lower transaction costs in the labor market—thus redirecting time and resources to strategic goals—is the main selling point that captures companies’ attention and business.¹²⁶

The LCL for the first time in Chinese legal history regulates LDAs.¹²⁷ Rather than ban LDAs altogether, the LCL’s purpose is to legalize and regulate them. Article 57 describes a required system of licensing and registration, whereby each LDA must have a minimum capital of 500,000

119. Josephs, *supra* note 19, at 380.

120. Xu, *supra* note 5, at 452.

121. *Id.*

122. *Id.* at 434–435; see also People’s Daily, Growing Number of Laid-Off Workers Turn to Employment Agencies, http://english.peopledaily.com.cn/200209/13/eng20020913_103161.shtml (last visited Oct. 26, 2009).

123. Some also believe that dispatch agencies play the role of trusted mediator between employers and employees whereby employees have a fair chance at finding employment in a society known for its nepotism. It is also the P.R.C.’s active employment policy to encourage the unemployed to seek seasonal, part-time and temporary work for which labor dispatch agencies play a key role. Xu, *supra* note 5, at 434.

124. See *id.* at 434.

125. It is also fair to note that other main clients of labor dispatch agencies include state-monopoly industries such as power, tobacco, telecommunications and banks. Xu, *supra* note 5, at 452.

126. *Id.* at 434.

127. Labor Contract Law § 2.

yuan.¹²⁸ LDAs must sign at least a two year contract with all of their employees.¹²⁹ They must pay monthly remunerations to the employed workers, i.e. those who have been staffed at a company, and a minimum wage salary to the unemployed workers, i.e. those who have not been staffed, in accordance with the local minimum wage laws.¹³⁰ The LCL also requires LDAs to keep records of contracts signed with clients, positions of dispatched workers, the number of dispatched workers, the term of dispatch, the amount and payment of remunerations and social security premiums, and the liability for breach of the agreement.¹³¹

In addition to the minimal regulations concerning LDAs in the LCL, some of the relative provisions are vague and not interpreted. The most prominent example of an ambiguity is the provision limiting LDAs to “temporary, ancillary, or substitute positions.”¹³² The vagueness of what amount of time constitutes temporary work allows domestic industries and FIEs a wide loophole to fully utilize LDAs as a source of a flexible workforce with no obligation of signing a contract.¹³³

IX. CONCLUSION

The large trade imbalance with the P.R.C. has been characterized as a growing area of concern for the stable growth of the U.S. economy. The expansion of workers’ rights necessarily translates into increased costs of production for American FIEs operating in China. American FIEs recognized this fact and for that reason they waged a strong lobbying campaign against the LCL before it even got passed by the Chinese government. Although the U.S. administration will elicit protest from AmCham and the American FIEs in the P.R.C. by supporting the LCL, the broader benefits to the nation outweigh the short-term political pain and limited gain for those American FIEs. If American FIEs abide by the LCL—thereby increasing their labor costs—the artificially low-priced Chinese-made products will be less competitive in the international market thereby helping to decrease the U.S.-China trade deficit. Many other variables contribute to this outcome. For instance, if American FIEs simply relocate to a neighboring country which offers cheap labor with few legal

128. Equivalent to approximately 70,000 US dollars; exchange rate from yuans to dollars as of September 18, 2009. Google Unit Conversion, www.google.com/UnitConversion (last visited Oct. 5, 2009); see Labor Contract Law art. 57.

129. Labor Contract Law art. 58 para. 2.

130. *Id.* art. 58.

131. *Id.* art. 59.

132. *Id.* art. 66.

133. See Xu, *supra* note 5, at 457.

restrictions and poor enforcement mechanisms, then a corresponding trade imbalance with this new neighboring country would result. On the other hand, neighboring countries may take the P.R.C.'s lead and institute labor law reforms to create harmonious employment relationships that increase the cost of labor thereby no longer being a source for cheap labor. However, notwithstanding other possible variables, targeting the cost of labor used to manufacture traditionally artificially low-priced products in one of the world's strongest emerging economies should make a serious dent in the trade imbalance that further cripples the U.S. economy.