

Dispatched Workers to 'Fry Squid'

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On December 28, 2012, half a year after it released a draft for public consultation, the Standing Committee of the PRC National People's Congress enacted amendments to the PRC Labor Contract Law. The amendments to the PRC Labor Contract Law ("LCL Amendments") will come into effect on July 1, 2013.

Before the PRC Labor Contract Law came into effect in 2008, labor outsourcing (i.e., where staff are sourced through employment agencies instead of being employed directly) was predominantly used to staff representative offices of foreign companies and as a stop-gap measure for other employers while they looked for permanent, full-time employees. Labor outsourcing (also referred to in China as "labor dispatch") is recognized as a legitimate labor arrangement under PRC Law. Employers only began to use labor outsourcing arrangements more widely when they found they could use them to sidestep the additional costs and long-term employment obligations of directly hired staff imposed under the PRC Labor Contract Law ("LCL").

Over the past four years, many employers in a range of sectors have come to rely heavily on labor outsourcing on an unprecedented scale. By the PRC government's estimates, there are now at least 27 million outsourced workers in China, many of them working in large state-owned enterprises and public institutions.

The authorities have grown concerned about abuses of employee rights which, in some instances, have resulted in workplace health and safety issues. A more widespread problem is that outsourced workers are not receiving pay or social security benefits commensurate with their work or with directly-hired staff within the same organization. As outsourced workers, most of them will also not be entitled to most of the long-service benefits of directly-hired staff. The LCL Amendments were promulgated to curtail this widespread use of labor outsourcing and force employers to employ the bulk of their work force directly.

The LCL Amendments essentially restates labor outsourcing arrangements by imposing new restrictions on labor outsourcing arrangements and on labor outsourcing agencies. We summarize these new restrictions as follows:

1. Restrictions on Use of Labor Outsourcing Arrangements. Effective from July 1, 2013, employers can only use outsourced workers to fill temporary, ancillary or substitute positions. As defined by the LCL Amendments:

- a "temporary" position is one which lasts no longer than six months.
- an "ancillary" position is one that is meant to provide a supporting role to the employer's core business functions.
- a "substitute" position is one which provides temporary replacement cover for another employee who is away on vacation or on study leave, etc.

The drafters of the LCL Amendments included these definitions to close loopholes left in the Labor Contract Law which implied there might be other legitimate categories of outsourced workers. As a further restriction, the LCL Amendments stipulates that under new rules – which have yet to be released – employers will be strictly limited in the proportion of outsourced workers they may hire.

2. Equal Pay for Equal Work. The LCL Amendments reiterates the principle of "equal pay for equal work" which was articulated in the Labor Contract Law. After the LCL Amendments come into force, all compensation (including basic salary, bonuses, subsidies and allowances, etc.) received by outsourced workers must be on par with directly-hired employees in equivalent positions.

3. Stricter Requirements for Labor Outsourcing Agencies. Starting from July 1, 2013, all labor outsourcing agencies must have a minimum registered capital of not less than RMB 2 million (up from RMB 500,000), must operate from fixed office locations and must be managed responsibly. All companies established after July 1, 2013, to provide these services will need to meet local labor bureau requirements before they can be licensed. Existing agencies that are already licensed have until July 1, 2014 to meet local labor bureau requirements before renewing

their business registration. Any business that fails to meet local labor bureau requirements will be prohibited from providing labor outsourcing services.

4. More Severe Penalties. The drafters of the LCL Amendments have given it teeth. After the effective date, local labor bureaus will have the power to order employers to rectify any non-compliance with the new hiring provisions. Failure to comply could result in fines ranging from RMB 5,000 to RMB 10,000 per worker. Labor outsourcing agencies operating without the proper license will be liable to receive a fine of between one and five times the amount of any income they receive while operating without a license, or can be fined up to RMB 50,000 even if they have received no labor outsourcing income.

Representative Offices

None of the labor outsourcing restrictions will apply to representative offices. Representative offices are not independent legal entities and are therefore required to rely on labor outsourcing to meet all of their local staffing needs. This will not change.

Grandfathering of Existing Contracts

All existing labor outsourcing contracts executed before December 28, 2012 can continue until they expire, which will give employers time to put their staffing arrangements in order.

Impact on Employers

It remains to be seen whether the already-stretched labor bureaus across China will have the resources to effectively enforce the LCL Amendments, particularly the new agency licensing requirements. However, given the recent controversy surrounding labor outsourcing, it seems likely that the authorities will make a concerted effort to crack down on employers that fail to rein in their use of labor outsourcing.

Employers that use outsourced workers – with the exception of representative offices – should begin reviewing their current staffing arrangements now and make plans to replace any outsourced positions with directly-hired staff once the existing labor outsourcing contracts expire. The LCL Amendments will prompt some companies in China to restructure in an effort to save costs, by shedding positions in non-core areas (e.g., administration, HR, marketing, etc.) and then outsourcing from third party providers. For employers that choose to continue relying on outsourced workers, it will be necessary to review and update compensation arrangements for those workers to ensure that the re-stated “equal pay” requirements are complied with.

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