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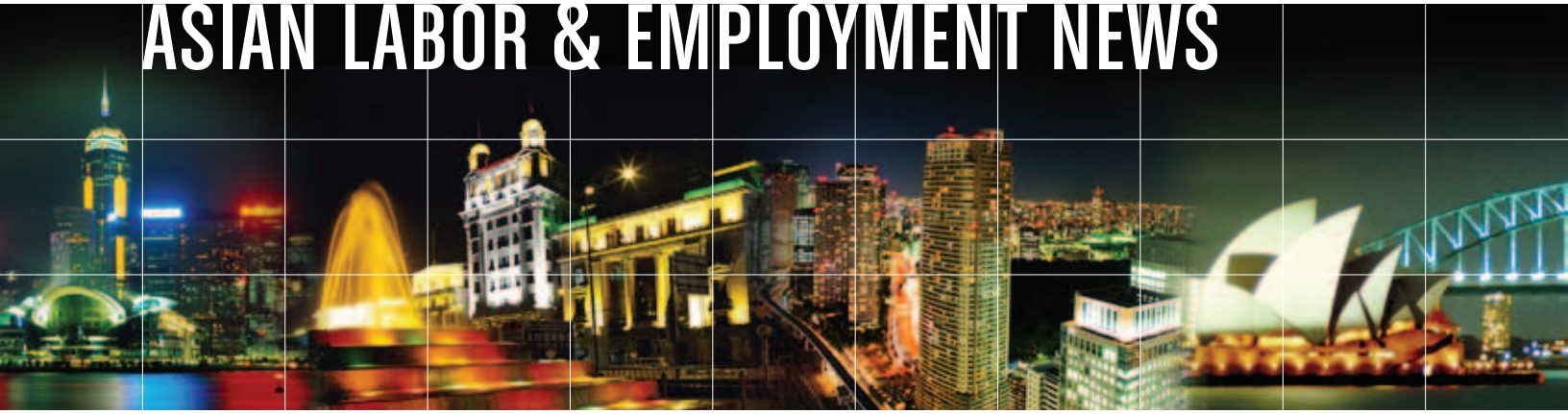

A NEW LABOR ERA: HIGHER COSTS AND GREATER PRESSURES

A series of labor conflicts erupted in China in 2010. Various foreign-invested factories concentrated in China's coastal areas experienced a string of labor-related protests and strikes. These publicized conflicts may signal the end of an era of low-cost labor and the beginning of a more challenging labor environment for foreign-invested enterprises (FIEs) and other employers in China.

RECENT UNREST

The most high-profile labor incident last year involved a number of suicides at Foxconn International Holdings, a Taiwan contract manufacturer for foreign consumer electronics companies. Though the precise cause of the suicides at Foxconn's factory in Shenzhen, Guangdong, remains unclear, some advocacy groups and media outlets have pointed to the factory's unfavorable working conditions and, above all, low wages. In response to public criticism and local government pressure, Foxconn raised basic monthly salaries for its production workers from ¥900 ($137) to ¥2,000 ($305). The Shenzhen municipal government subsequently increased the city's minimum monthly wages to ¥1,100 ($168), an average increase of 15.8 percent. In April 2011, Shenzhen raised its minimum wage again to ¥1,320 ($201). In late June 2010, Foxconn declared it would outsource the management of its worker dormitories and relocate some facilities to Taiwan and China's inland regions, where monthly minimum wages can be as low as ¥600 ($91) to ¥800 ($122). In March 2011, the company further announced that it would move 200,000 jobs to inland provinces with lower costs.

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In addition to the Foxconn developments, a string of strikes broke out in May 2010 at several other factories in Guangdong and China's coastal regions. The most publicized strikes occurred at Honda Motor Co. factories in several Guangdong cities. In late May, Honda workers in Foshan walked out, demanding higher wages and better working conditions. Honda responded with a 24 percent general pay increase. The Foshan strike then triggered work stoppages at several other facilities in Guangdong: a Honda lock systems supplier, one of Honda's gearshift suppliers, and Honda's affiliate Nihon Plast Co., Ltd. Because of repercussions from the labor unrest, Honda's sales in China fell 2.7 percent in June, lagging behind China's overall auto industry sales, which increased 23.5 percent from a year earlier.

SOURCES OF LABOR UNREST

Though not widely reported by the Chinese media, observers believe that strikes in China extend beyond the well-publicized incidents at Foxconn and Honda. Several factors suggest that labor unrest may become an increasingly significant aspect of the Chinese manufacturing industry.

Tight labor market

The tight labor market in China's coastal regions is a critical element of the recent labor unrest. China's labor shortages first appeared in Guangdong in 2003 and have since appeared in other major industrial regions, including the Yangzi River Delta around Shanghai. The shortages are in part because of the PRC government's one-child policy and the household registration (*hukou*) system, which discourages the rural population from moving to the cities.

High cost of living

The high cost of living in China's coastal regions is also fueling demands for higher wages. In 2007 and 2008, China's consumer price index rose by 4.8 percent and 5.9 percent, respectively—well exceeding the official annual targets. Though cost of living in cities such as Shenzhen rose significantly in the last decade, some profitable companies have not increased wages to reflect higher prices, spurring worker dissatisfaction.

Several companies involved in the May 2010 strikes were paying the minimum wages required by local law. The wage complaints may have reflected the fact that Japanese- and Taiwan-owned factories often paid lower wages than comparably sized German-owned facilities and other FIEs, sometimes in the same area.

Greater "rights-consciousness" of workers

The new generation of Chinese blue-collar workers, born during the 1980s and 1990s, are more sensitive to social issues and workplace rights than their parents. Previous generations might have taken any city job available, even for low salaries. But young workers today seek jobs that not only pay well enough to secure a better life for their families, but also provide career development, treat employees with respect, and help them gain a foothold in the cities. Furthermore, despite state oversight, Internet access has helped workers learn quickly about strikes, wages, and working conditions at other companies.

GOVERNMENT INTEREST IN LABOR MARKET REGULATION

In the early decades of the reform era, the PRC government primarily focused on economic growth—starting with coastal regions, which rose ahead of rural areas. Since 2003, however, the government has begun to shift its focus to include social harmony, political stability, and better income distribution. The new minimum wage law issued in 2004 and the much-touted 2007 Labor Contract Law, which enhances statutory rights for employees and imposes greater obligations on employers, reflect this shift in focus. The government's tolerance of sustained, extensive media coverage of the suicides and strikes at several FIEs may also reflect this new thinking. It remains unclear, however, whether the new approach will extend to wholly and partially state-owned enterprises.

The PRC government is also formulating more labor contract regulations to protect worker rights. In September 2010, the PRC Supreme People's Court issued Interpretations on Several Issues Concerning the Application of Laws in Labor Dispute Trials (III)—the first set of judicial guidance since the 2007 Labor Contract Law and Labor Dispute Mediation Law. The interpretations contain 18 articles, which focus on procedural issues in court trials, and include important provisions that

- Accept disputes that arise from restructuring the enterprise;

- Place the burden of proof on employees to show they worked overtime but penalize employers that refuse to produce the same evidence; and
- Generally recognize employment agreements as valid and binding, provided that they do not violate mandatory provisions of laws or regulations or involve fraud, coercion, or exploitation.

China is drafting new national regulations on wages with the aim of guaranteeing wage payments and salary increases. The proposed regulations would, among other things, clarify that

- Local legally required minimum wages do not include overtime payment or social security fees;
- Salary security funds must be set up to prevent late salary payments; and
- Cost of living increases should be factored in when determining wages.

In February 2011, the PRC National People's Congress revised the Criminal Law to make it illegal for companies to intentionally withhold employee wages if

- The company has the means to pay the wages;
- The company willfully withholds payment by refusing to pay or by transferring assets to escape the obligation to pay; and
- The situation or its effects are "serious."

These regulations and revisions may increase labor costs for some companies, but much depends on how the PRC government implements and enforces the rules.

GOVERNMENT INTEREST IN PROMOTING ACFTU

The PRC government has long desired to install the All-China Federation of Trade Unions (ACFTU), the official state union system, in the FIE sector. ACFTU functions largely as an arm of, or "transmission belt" for, the state by supporting government policies and promoting workplace stability. In many regions, the local government selects ACFTU representatives. In addition, nearly all ACFTU officials and personnel are members of the Chinese Communist Party.

ACFTU has been relatively inactive in the FIE sector so far. At the end of 2006, only 18 percent of FIEs in China had entered into collective wage contracts (such contracts presumably reflect some ACFTU presence in the company). According to media reports, more than 10 million of the 13 million small and medium-sized enterprises in China did not have collective wage bargaining systems as of June 2010.

The government has taken several measures in recent years to boost ACFTU's presence in FIEs.

- In 2008, the PRC Ministry of Human Resources and Social Security issued a "Rainbow Plan," for the stated purpose of encouraging the establishment of collective bargaining systems in companies in eastern and central China by the end of 2010 and expanding the system to all of China by 2012. In May 2010, ACFTU and two other central-government agencies issued a notice regarding implementation of the Rainbow Plan, which aimed for all companies to be covered by collective wage bargaining agreements by the end of 2012, including 60 percent coverage by the end of 2010 and 80 percent coverage by the end of 2011.
- ACFTU and Shenzhen's local government in early 2010 jointly announced that they would push for collective agreements in 120 Fortune 500 companies that have operations in Shenzhen.
- The Shanghai government in early 2010 issued new regulations on collective labor contracts, setting out procedural and substantive requirements for such agreements.

The government initiatives are bearing some fruit. For example, KFC Corp. and Pizza Hut, Inc.—both owned by YUM! Brands, Inc.—in June 2010 signed collective wage contracts with their employees in Shenyang, Liaoning. The contracts marked the company's first collective agreement with employees in China.

Because many workers reportedly distrust ACFTU, it is unclear whether ACFTU initiatives or the recent publicized labor unrest will lead to greater ACFTU penetration of FIEs. Many of the FIEs in which large-scale strikes took place in 2010 did not have unions; even where unions were present, they were bypassed by the protestors. For example, although Foxconn had unions at group company levels, the unions did not function at the plant level. Moreover, even in companies that had local factory union representatives (such as in Honda's

Foshan facility), the striking workers sought a new election of union representatives as one of their strike demands.

IMPLICATIONS FOR FIES

FIEs operating in China will face a more challenging labor environment and increasing costs. Given the recent labor unrest, companies may need to consider boosting employee compensation and benefits and improving work hours and supervisor-employee relationships. Though methods for achieving these goals vary, companies should consider paying fair wages based on commonly accepted practices and developing better communications systems with employees.

Periodic review of labor regulation compliance

FIEs in China should periodically review their employment policies and practices to ensure full compliance with all applicable labor rules and regulations. Companies operating in China should expect expanded state regulation and promotion of the collective wage-bargaining system, particularly in FIEs. Foreign companies should also extend their compliance review to their supply chains, because labor compliance problems in upstream or downstream companies may negatively affect the FIE's costs and operations. Furthermore, most labor disputes filed in China's mediation and arbitration councils involve failure to issue an employment contract, though required by the PRC Labor Contract Law, and failure to pay promised wages, which is now deemed a crime under the revised Criminal law. Carefully reviewing contract manufacturers' payroll practices can reduce these causes of disputes.

Consider proactive posture on wages and unions

FIEs should consider whether they wish to take a proactive posture on wages and relations with ACFTU. These steps may have drawbacks if they are not carefully executed, however. For example, increasing wages to keep pace with inflation is one way of eliminating an oft-mentioned cause of worker discontent, but it may also stoke demands for ever-increasing pay levels. Likewise, entering into a relationship with ACFTU, possibly with local-government help, may stem labor protests but may also invite an arm of the state onto the shop floor.

FIEs should at least consider whether they wish to maintain wage parity with other comparably sized foreign manufacturers in the region to avoid being singled out by workers and the local government. Employers may also wish to consider wage parity between FIEs operating in the same industry and region as an overarching policy.

Consider moving westward

When pressed by increasing labor costs in coastal cities and provinces—including traditional manufacturing bases such as the Pearl River Delta and the Yangzi River Delta regions—FIEs in labor-intensive industries may wish to consider relocating their operations to inland provinces, especially to traditionally less-developed central and western regions. Minimum wages in China vary widely by region. Under the recent Western Development Strategy issued by the central government, companies—including FIEs—in central and western regions may enjoy benefits that are no longer available in the coastal regions, such as reduced income taxes and low land prices and labor costs.

CHALLENGING ROAD AHEAD

This is a challenging time for China's manufacturing sector and for FIEs that own, operate, or source from facilities in China. Close review of existing practices and strategic planning to avoid future problems can help companies navigate the difficult waters. Whether the labor disputes will rise in number and importance depends on several factors, including how migrant workers are treated by their employers and the courts, whether wages sufficiently keep up with inflation, whether manufacturing remains a low-labor cost sector, and the overall economy in China.

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DEVELOPMENTS IN MINIMUM-WAGE STANDARDS IN CHINA

Thirteen Chinese provinces and cities have adjusted their minimum-wage standards in the first quarter of 2011, with an average increase of 20.6 percent. Most of these adjustments took effect in April or May, raising minimum wages to more than ¥1,000 (US$154) per month in around 10 provinces and cities, mainly in eastern China. These new laws are part of a general pattern of increased minimum wages across

the country over the past year. Labor shortages, a spate of strikes, and surging inflation have contributed to the trend in rising wages.

Chinese minimum-wage standards are separated into monthly minimum wages for full-time employees and hourly minimum wages for part-time employees. Wage standards, determined by provincial governments (*i.e.*, municipalities, provinces, and autonomous regions) must be adjusted at least biennially.

Local governments base wages on a variety of factors, including, among others, the cost of living, average wages in the area, the consumer price index, economic development levels, and employment conditions in the area. Under these conditions, minimum-wage standards vary widely among regions. For instance, the minimum wages are as high as ¥1,310 (US$202) per month and ¥10.7 (US$1.65) per hour in Zhejiang Province, but as low as ¥500 (US$77) per month and ¥4.7 (US$0.73) per hour in Jiangxi Province. This explains, in part, why some companies are relocating facilities to China's inland regions, where minimum wages can be considerably lower than those found near the coasts.

Within a region there is also variance, as provincial governments set different standards for the areas within their jurisdictions, with particular emphasis on a locality's level of economic development relative to its neighboring areas and the government's development policy goals for the area. For example, officials have established three minimum-wage levels within the Ningxia Hui Autonomous Region.

There are also differences in the components that make up the minimum wage that can complicate comparisons of rates throughout China. For instance, Shenzhen and Shanghai are among the cities with the highest minimum-wage rates in the country. Officially, Shenzhen's rate of ¥1,320 (US$204) is higher than Shanghai's, which is ¥1,280 (US$198). In Shanghai, however, employee contributions to the housing fund are excluded from the minimum wage, whereas in Shenzhen such contributions are included, which in practice results in a higher minimum wage in Shanghai than Shenzhen when this is taken into account.

This example and the others above underscore the importance of understanding differences not only in the stated minimum-wage rates themselves, but also in the components of those rates that determine whether they are met, as well as the factors influencing the changes in rates within and among regions and provinces and at the local level. These increases followed the announcement in February 2011 that the National People's Congress revised the PRC's Criminal Law to make it a crime for a company intentionally to withhold employee wages if: (1) the company has the means to pay the wages; (2) it willfully withholds payment by either refusing to pay or transferring assets to escape the obligation to pay; and (3) the situation or its effects are "serious." Whether this law will have an effect on how the PRC government implements and enforces the rules remains to be seen.

INDEPENDENT CONTRACTORS IN JAPAN MAY STILL RETAIN THE COLLECTIVE BARGAINING RIGHTS THEY HAD WHEN THEY WERE EMPLOYEES

In Japanese labor law, problems regarding the definition of "workers" arise mainly in two contexts. The first context is the definition of "workers" in the Labor Standard Act and the Labor Contract Act. In such case, "workers" means employees who work for employers. The second context is the definition of "workers" in the Labor Union Act ("LUA"), where ostensibly independent contractors may have certain rights alongside traditional employees. If individuals are considered to be "workers" under the LUA, they can organize a labor union and exercise collective bargaining for the purpose of concluding collective agreements regulating relations between the employers and workers. Japanese law defines the term "workers" under the LUA to include not only employees who have entered into labor contracts with employers but also other workers who should be protected by being given the right to exercise collective bargaining. The question then is whether independent contractors performing work that they previously had performed as employees may still be considered "workers" with collective bargaining rights under the LUA. In its ruling of April 12, 2011, the

Japanese Supreme Court held that customer engineers ("CEs") who were engaged in the repair of housing equipment under outsourcing contracts with INAX Maintenance Corporation ("INAX") are "workers" under the LUA. In the case in question, the Supreme Court adopted the framework previously established in practice, which considers five factors when deciding whether labor suppliers in question are "workers" who should be accorded the right to engage in collective bargaining:

(i) Whether labor suppliers are included in the organization of the company as indispensable labor to perform its business and for the purpose of ensuring such labor on a permanent basis;
(ii) Whether terms and conditions of work are decided unilaterally by the company;
(iii) The extent to which compensation for such work is similar to wages or salaries;
(iv) Whether labor suppliers can freely accept or reject offers from the company; and
(v) Whether work is performed under instruction, supervision, and restrictions regarding time and place provided by the company.

In the case before it, the Supreme Court made the following determinations:

(i) INAX relied on the CEs as a means of providing needed services on a permanent basis;
(ii) INAX decided terms and conditions of contracts with the CEs unilaterally;
(iii) INAX compensated the CEs by adding an amount corresponding to overtime work payments to the invoice to INAX's customers;
(iv) The CEs basically had to accept assignments from INAX as a matter of practice between the CEs and INAX based on the common understanding as such; and
(v) INAX specified how the CEs would perform their services and generally supervised their work.

This Supreme Court decision suggests that even if a company converts its workforce into ostensible independent contractors, the contractors may still be able to exercise their collective bargaining rights.

SECONDMENTS AND TRANSFERS: COMPLYING WITH ANNUAL AND LONG SERVICE LEAVE REQUIREMENTS IN AUSTRALIA

Cross-border assignments are becoming increasingly popular with multijurisdictional employers, in order to attract employees, "up-skill" their workforces, and fill labor or skill shortages. Such assignments may be carried out by way of a transfer of employment, whereby the employee's original employment contract is terminated and a new agreement is formed with a related entity in the foreign jurisdiction. Alternatively, the employer may "second" or "loan" its employee to a host company, with the original employment contract remaining in place but subject to the terms of a secondment agreement between the employer and the employee and a separate agreement between the employer and the host company.

Employers that transfer or second their employees to foreign jurisdictions will need to consider a number of issues, including migration and taxation requirements as well as local employment and discrimination laws. A key issue for employers is to ensure that their employees receive the benefits to which they are entitled by law, both at home and abroad, without incurring additional tax and other expenses. This article will focus on the entitlements to annual leave and long service leave that are due to employees who are transferred or seconded to work in Australia.

An employer that seconds or transfers an employee to Australia will be required to provide that employee with his or her minimum entitlements to annual leave under the Fair Work Act 2009 (Cth) ("FWA"). The employee will progressively accrue a pro rata amount of four weeks' annual leave per year for the period of time worked in Australia. The employer should ensure that any contractual entitlement the employee may have to annual leave is coordinated with or expressly set off against the employee's statutory entitlements under the FWA. It is also important that the relevant contractual arrangements clarify that the employee is entitled only to the public holidays that are declared in the Australian state in which the employee is working, not those to which he or she would be entitled in his or her home country.

In contrast, although an employee's long service leave entitlements will vary within each Australian state or territory, employees who can be characterized as "temporary" or "expat" workers generally do not accrue long service leave for the period in which they are working in Australia. Instead, an employer will need to consider whether the employee's service while in Australia will count towards any similar long service entitlements under the law of the employee's originating jurisdiction.

OFFICE INFORMATION

SHANGHAI

Jones Day's first location in Mainland China, the Shanghai Office opened in 1999 and has long been one of the preeminent foreign law firms in Shanghai. The team includes a mix of Western-trained lawyers who have practiced in Greater China for most of their careers and China-trained lawyers with significant experience in Chinese and Western legal environments. As a group, Jones Day's Shanghai lawyers are fluent in English, Mandarin, French, Shanghainese, and a number of other Chinese dialects.

BEIJING

Jones Day's Beijing Office opened in 2003 and has since expanded to become one of the largest foreign law firms in Beijing. Team members (the vast majority of whom are Chinese nationals) include legal professionals who are qualified in the jurisdictions of Hong Kong, the U.S., the U.K., Canada, Singapore, and New Zealand.

HONG KONG

Jones Day's Hong Kong Office opened in 1986, and in 1996 it became the first branch of a U.S. law firm permitted to practice Hong Kong law. The office comprises 35 lawyers admitted to practice in jurisdictions covering Hong Kong, the U.S., the U.K., Australia, Singapore, and Canada. Clients include multinational and local corporations, financial institutions, and government organizations.

TAIPEI

Jones Day's Taipei Office opened in 1990 to serve the legal needs of international and Taiwanese clients. Lawyers in the Taipei Office are fully qualified to practice both Taiwanese and U.S. law. Most attorneys are multilingual and are experienced in both Taiwanese and foreign transactions. The Taipei Office regularly advises clients on a wide range of Taiwanese legal issues, as well as on U.S. and other international legal matters.

TOKYO

Since 1989, the Tokyo Office has offered comprehensive and cost-effective counsel. In 2002, the Tokyo Office of Jones Day entered into a joint-venture arrangement (*Tokutei-kyodo Jigyo*) with Showa Law Office. The two firms fully integrated their operations in 2005. The Tokyo Office serves as the local window to the resources of the Jones Day worldwide network, giving our clients access to a broad range of legal experience in the various markets in which they operate.

SINGAPORE

Jones Day's Singapore Office opened in 2001, but our lawyers have been advising clients in Southeast Asia for more than 20 years. These lawyers represent a diverse list of clients, with particular focus on corporate/M&A, financing, and dispute resolution work throughout the Asia-Pacific region. Lawyers in the Singapore Office are fluent in English, Mandarin, Cantonese, Hakka, Bahasa Malaysia, Bahasa Indonesia, Thai, Hindi, French, and Arabic.

SYDNEY

The Firm's Sydney Office opened in 1998. It has a core team dedicated to the provision of high-quality transactional and advisory support across Australian, Asian, U.S., and European jurisdictions. Consistent with the Firm's commitment to providing high-quality client service, the Sydney Office delivers technically accurate, creative, and efficient legal services that help further our clients' business objectives.

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