

Treatment for Foreign Investment Enterprise In China

In recent years, especially after China entering into the WTO, with its steady development, growing transparency and improvements in administration of justice of its legal system, China has become more and more attractive to foreign investors. However, we know that there are still many issues which foreign investors concern, such as the three issues we will discuss today: namely (1) intellectual property right ("IPR") protection; (2) labor system; (3) taxation; and (4) remittance of profit out of China.

Intellectual Property Right Protection

Generally speaking, FDI projects always involve IPR issues, such as trademark licensing, assignment of patent, and the like. Some investors complain about the "rampant" piracy in China, and there has been reported that China "is still infamous for IPR infringement". On the other side, it is common that many foreign investors are not aware of that there are appropriate measures they could take to protect their technologies/products/trademarks in China. For example, the fact that the foreign investors license their Chinese subsidiaries to use their trademark without registering it in China may allow their Chinese subsidiaries to reproduce their patented products without applying for a Chinese patent..

What I want to say here is that having promulgated its first IPR protection law, the *Trademark Law* in 1983 and having amended its main IPR protection laws and regulations so as to comply with its obligations being a WTO member, China has already developed a comparatively comprehensive IPR protection system. Therefore, **a well designed IPR planning will help the foreign investors protect themselves from IPR infringement.** And I believe such system will continue to be improved

over time.

1. Overview of the IPR Protection System in China

China's IPR protection system consists of a mixture of statutes and regulations at both the national level and the local provincial level, including the *Patent law*, the *Trademark Law*, the *Copyright Law* and their *Implementation Regulations*, the *Anti-Unfair-Competition Law* and other relevant regulations. Accordingly, the IPRs which can be protected and enforceable include patents, copyrights, trademarks, trade secrets, and etc. China also provides a special protection for the computer software and the integrated circuit layout design.

As a member of the WTO, China is obliged to implement the principles of the *Agreement on Trade Related Aspects of Intellectual Property Rights* ("TRIPs Agreement") in its national laws. Therefore, from the end of 2000 to the end of 2002, China has made many amendments to its IPR laws and regulations

In addition to the national laws and regulations, China has acceded to several international conventions concerning IPR protection, including:

- the *Paris Convention for the Protection of Industrial Property* (the "*Paris Convention*");
- the *Patent Cooperation Treaty*
- the *Madrid Agreement for the International Registration of Trademarks* (the "*Madrid Agreement*");
- the *Berne Convention for the Protection and Literary and Artistic Works* ("*Berne Convention*");
- the *World Copyright Treaty*; and
- the *Treaty on Intellectual Property in Respect of Integrated Circuits* (the "*Washington Treaty*").

These conventions and treaties also require IPR protection in China.

2. IPR Protection Strategy: Pre-Investment Phase

Prior to the investment, some measures can be taken to minimize the risk of IPR infringement.

- (1) Check your investment plan and find out what kinds of intellectual properties will be involved in the project. It means that you shall get a clear picture of whether any of your trademark, patent, software, and/or trade secret will be used in China, so that protection strategies may be devised for the subject properties specifically.
- (2) Check the current IPR involved in the subject intellectual properties. Because of the territorialism of the IPRs, most IPRs can only be protected in those countries in which they are registered. Therefore, before you decide to introduce any IPR to China, it is advisable to make sure whether it is protected or can still be protected in China.

Let's take patent as an example. If a patent has already been protected in any foreign country, the patented technology is most likely to be considered as publicly available in China, and thus not patentable in China, unless a patent application had been filed within the priority period as provided in the *Paris Convention*. In other words, if you introduce a foreign patented technology to China but have not filed a patent application in China within the priority period, anybody can lawfully use it.

- (3) Check the subject intellectual property and make sure in what manner it will be involved in the FDI projects: whether it will be injected as an investment, or just

be licensed to Foreign Investment Enterprises (“FIE(s)”), or be invested in any other way. The investment manner will determine the IPR protection strategy too.

Again, take patent as an example. If you want to license a Chinese patent to a Chinese company, you shall execute a licensing agreement with the Chinese company and make detailed provisions in the agreement concerning the obligation of the licensee in respect of IPR protection. However, if you make the patent as the injected investment to a FIE, the patent shall be assigned to the FIE and then become the property of the FIE. That's to say, you, as the original patent owner, will no longer hold the patent and will not be in the position to protect the patent in China.

(4) Make a well-balanced strategy to establish a sufficient IPR portfolio to prevent your products and technologies from being replicated or copied. Generally speaking, the following measures shall be taken into account:

- Apply for IPR in China, such as applying for a Chinese patent; registering your trademark in China; registering your copyright, software and layout design (if any) in China, and etc.

The time for different kinds of IPR applications are different. For example, as for software, it will take you only one month to go through the registration formalities; but it will take you about one year to register your trademark in China. It means that, you should register your trademark in China before you initiate the FDI project. (I will make a brief introduction of the IPR application in the following Section 3)

- Draft complete provisions concerning IPR protection in the joint venture contract or other related contracts to clarify the obligations of the Chinese

party or the FIE in that regard.

3. IPR Application in China

(1) Patent

As we have mentioned above, a foreign patented technology will most likely not to be patentable in China. Therefore, our suggestion here is that, **in the case that any patentable technology is proposed to be brought into China, please file a patent application in China first; or if you have already filed a patent application in other countries, please submit your application in China within the priority period.**

According to the current *Patent Law* and its *Implementing Regulation*, foreign individuals/entities may avail themselves of the patent application procedures and apply for Chinese patents. But as for the foreign applicants having no habitual residence or business office in China, a locally qualified firm has to be retained for filing a patent in China.

China implements a "first-to-file" rule in patent application. That means, if there are two or more applicants for patent for the same technology, the patent will be granted to the applicant who first files the application. Nevertheless, since China is a signatory State to the *Paris Convention* and the *Patent Cooperation Treaty*, therefore, the following priorities are available in China:

- an applicant who applies for patent in a member of the *Paris Convention*, such as Chile, may enjoy a 12-month priority period: if he files an patent application for the same invention in China within one year from the date on which he first filed patent application in the member recognizing the patent, and claims the priority, the filing date in that member will be treated as the

filing date in China.

- an applicant can also file an international patent application in any member of the *Patent Cooperation Treaty*, designating China, and enter into China within 32 months from the priority date.

In addition, we also provide the following suggestions for your reference:

- **Make use of utility model patent or design patent** There are three kinds of patents in China: an invention patent, a utility model patent or a design patent. It will normally takes three to five years to obtain an invention patent, but a utility model patent or design patent can be easily obtained within a relatively short period of time (about one or two years). So, a utility model patent or a design patent is more appropriate for small improvements or changes of your product or technology.
- **Never unduly rely on trade secrets protection** Since reverse-engineering is generally allowed in China, you cannot stop others from obtaining technical information from your products in the market unless patent, copyright or other IPR subsists therein.
- **Preserve evidence of early use** Sometimes, your local competitors or even co-operative partners may file utility model patent or a design patent inspired by your products in the market. Your evidence of early use of the technology or product can be used for invalidating your competitor's patent or at least provide an effective defense against a charge of patent infringement.

(2) Trademark

According to the *Trademark Law*, only the Chinese registered trademarks are protected in China. Use of an unregistered trademark in China generally will not give rise to any trademark right, unless the trademark is "well-known".

Please note that, to claim for a "well-known trademark" status is a kind of remedial measures in case of failure to register the trademark in advance while encountering infringement. However, this is not recommended, because to apply for the "well-know trademark" status, the trademark owner is required to submit large amount of evidences and materials to the Trademark Office for its verification and examination and the Trademark Office can make the decision at its sole discretion.

China also implements a First-to-file rule in trademark application. The Trademark Office will preliminarily approve the application and publish the mark for a three-month opposition period. When the opposition period expires without an opposition, the mark will mature for registration. Normally, the whole application procedure will last for about twelve months. If an opposition is filed, the application will be pending until the result of the opposition comes out.

Since China is a signatory State of the *Paris Convention*, foreign trademark owners are entitled to rely on the priority period of six months from the date of filing in their home jurisdiction under the *Paris Convention*.

(3) Copyright

According to the *Copyright Law*, the foreigner's works will be protected as follows:

- Foreign copyrighted works will be protected automatically in China

according to the treaty between China and the country to which the author belongs, or according to the international convention to which both China and the country which the author belongs to are parties;

- The works of foreigners, which are first published in China, will obtain copyright in China automatically;
- If there is no treaty concerning copyright between the country of the foreign author and China, or international convention to which both China and the country which the author belongs to are parties, the work of the aforesaid foreign author may obtain copyright protection when it is published first in a signatory State to an international convention concerning copyright, to which China is also a signatory State.

Although the copyrightable subject matter will be under the copyright protection as soon as it is created, it is strongly recommended to register your copyright works with the Copyright Protection Center of China, because the Registration Certification may be used as prima facie evidence of the copyright before the Chinese courts and arbitration tribunals.

(4) Software

In China, computer software is primarily protected under the *Copyright Law*. Nevertheless, since software is much different from the other works, China promulgated a series of regulations to detail the protection and enforcement of copyright protection for computer software, including the *Regulations on the Protection of Computer Software* (the "*Software Regulations*"), the *Rules of Computer Software Copyright Registration*, the *Rules of Software Products Administration*, and other relevant regulations.

If you plan to license a Chinese company to **use** your software, the software copyright registration is recommended, because the Registration Certification may be used as prima facie evidence for the copyright.

If you intend to license a Chinese company to reproduce and sell your software in China, in addition to the copyright registration, the following registrations are necessary:

- **Software Copyright License Agreement Registration and Authorization**

According to relevant regulations, any Chinese entities which proposes to distribute or reproduce foreign-originated software shall register and authorize the copyright license agreement with the local Copyright Bureau. For foreign-originated software reproduced or sold in China without registration, the copyright administration authorities are entitled to sequester such software for copyright infringement and the producer will be punished severely.

- **Software Product Registration** According to the *Rules of Software Product Administration*, any software product which will be produced and sold in China, including software incorporated into devices or equipment, shall go through such registration.

The aforesaid two registrations are the legal obligations of the Chinese licensee's, instead of yours. However, since they are mandatory obligations, to ensure the smooth operation of your investment project and also to ensure the possibility of remittance of profit, you'd better push your licensee to go through the formalities.

(5) Integrated Circuit Layout Design

According to the *Regulation of Mask Works Protection*, the mask works are

subject to registration protection: the owner of the mask works shall register it with the SIPO (the State Intellectual Property Office of PRC). In absence of such registration, the mask works will not be protected in China. In addition, if the registration application is not filed within two years from the date when the mask work was first commercially exploited in any country other than China, the mask work will not be protected in China.

Protection covers not only the layout design itself, but also the integrated circuits incorporating the layout design and any articles incorporating such integrated circuits.

4. **IPR Protection Strategy: Facing the Infringement**

A well-balanced strategy at the pre-investment phase will help you obtain IPR protection in China, which will serve the basis for you to go against the probable infringement.

To prevent infringements in a timely and effective manner and to protect the legitimate rights and interests of the IPR holders, China implements a "double-track system": **judicial remedies** and **administrative punishment**.

(1) Judicial Remedies

Upon infringement, IPR owners may seek judicial remedies via lawsuits. China has attached importance to the IP protection. Most IP-related cases in the first instance are subject to the jurisdiction of Chinese intermediate courts (at the metropolitan city level) whereas common civil/commercial cases in the first instance are normally subject to the jurisdiction of the district court (at the local city, county and township level).

On the other hand, the IPR protection consciousness of the Chinese people has enhanced over the past several years, which can be proved by the increasing number of the IP-related lawsuits in China. According to the statistics of the Supreme Court of the People's Republic of China, during the five years from 1998 to 2003, there were more than 40,000 IPR-related cases filed with Chinese Courts of various levels, representing an average annual increase of 4% approximately. During the first eleven months in 2003, there were 5750 cases, 24.57% increase of that of the corresponding period in 2002.

Both injunctive remedies and damage compensation are available in the judicial proceedings. Damages can be calculated based on the IPR owner's losses arising from the infringement or the profit gained by the infringer from the infringement. If there is no basis for the calculation, statutory damages from RMB 5,000 to 500,000 can be awarded.

Before initiating a legal action concerning patents, trademarks, copyrights, and/or layout design, the IPR owner may request the court to issue an order to stop the infringement in order to avoid irreparable damages to the legitimate interest of the IPR owner. A deposit has to be provided for the pre-trial injunction.

(2) Administrative Punishment

In addition to the judicial remedies, competent government authorities, such as the Administration for Industry and Commerce (AIC), the Bureau of Copyright Administrative Authorities (BCAA), and the Intellectual Property Office (IPO), are also entitled to impose administrative punishment upon infringers.

The following chart shows the competent authorities governing the IPRs and their competence regarding their administrative punishment. For example, upon discovery of a trademark infringement, the trademark owner can apply to the AIC

(Administration of Industry and Commerce) for an order to confiscate and destroy the infringer's pirated items so as to prohibit the infringer from further infringement, to destroy the equipments used for making the pirated marks or items and even to impose a fine upon the infringer.

Agencies	IPRs	Powers	Effectiveness
AIC	Trademark	<ul style="list-style-type: none"> -- order to stop infringement -- confiscate and destroy pirated goods -- destroy tools used for making the pirated marks or goods -- impose a fine 	High
	Trade Secrets	<ul style="list-style-type: none"> -- order to stop infringement -- impose a fine 	
	Unique name, Package & decoration	<ul style="list-style-type: none"> -- order to stop infringement -- confiscate unlawful income -- impose a fine -- revoke business license 	
IPO	Patent	-- order to stop infringement	Low
	Layout design	<ul style="list-style-type: none"> -- order to stop infringement -- confiscate and destroy the pirated goods 	
BCAA	Copyright	-- order to stop infringement	Medium

Agencies	IPRs	Powers	Effectiveness
	Software	-- confiscate unlawful income -- confiscate and destroy infringing reproductions -- impose a fine -- confiscate materials, tools and equipment mainly used for making infringing reproductions	

In Contrast to the judicial proceedings, administrative measures are more economical and efficient in stopping the infringement. But the administrative procedures do not provide the IPR owner with remedy for financial loss.

Taxation

1. General rules

Foreign investment enterprises shall pay income tax on both their income derived from sources inside the People's Republic of China and their income derived from sources outside the People's Republic of China.

The Enterprise Income Tax payable by foreign investment enterprises and the Enterprise Income Tax payable by foreign enterprises on the income of their establishments or the sites set up in the PRC to for production or business operations shall be calculated on the amount of taxable income of the enterprises, at the rate of 30 per cent. Local income tax shall be calculated on the amount of taxable income, at the rate of three per cent.

2. Preferential tax treatment

- (1) Foreign investment enterprises established in Special Economic Zones, and foreign enterprises that set up establishments or sites in Special Economic Zones to engage in production or business operations and production-oriented foreign investment enterprises in Economic and Technical Development Zones shall be assessed Enterprise Income Tax at the reduction rate of 15 per cent.
- (2) Manufacture-oriented foreign investment enterprises established in Coastal Open Economic Zones or the old urban districts in the cities where Special Economic Zones or Economic and Technical Development Zones are located shall be assessed Enterprise Income Tax at the reduction rate of 24 per cent.
- (3) Foreign investment enterprises established in Coastal Open Economic Zones, the old urban districts in the cities where Special Economic Zones or Economic and Technical Development Zones are located or in other areas designated by the State Council that are engaged in energy, communication, port, pier or other projects encouraged by the state may be assessed Enterprise Income Tax at the reduced rate of 15 per cent. Specific provisions for such reduced assessment shall be formulated by the State Council.
- (4) Manufacture-oriented foreign investment enterprises with terms of operation of 10 years or more enjoy exemptions from Enterprise Income Tax in the first and second years and 50 per cent reductions of Enterprise Income Tax in the third to fifth years, commencing with the first profit-making tax year. Where such enterprises involve projects for the exploitation of resources such as oil, natural gas, rare metals or precious metals, the State Council shall formulate separate provisions. Where the actual period of operation of a foreign-investment enterprises is less than 10 years, the enterprise must repay the amount of Enterprise Income Tax that was reduced or exempted.

- (5) The Enterprise Income Tax reduction and exemption provisions promulgated by the State Council before the implementation of this Law for energy, communications, port and pier projects and other important production-oriented projects that are longer in duration than those provided for in the above paragraph, as well as the tax reduction and exemption provisions for important projects that are not production-oriented, shall continue to be effective after the implementation of this Law.
- (6) Foreign-Investment Enterprises engaged in agriculture, forestry or animal husbandry, and foreign investment enterprises that are established in economically underdeveloped, remote areas, may, after the expiration of the period for exemption and reduction of tax stipulated in the preceding two paragraphs and upon approval by the department of the State Council in charge of taxation of an application filed by the enterprise, continue to enjoy a 15 per cent to 30 per cent reduction in their Enterprise Income Tax in the subsequent 10 years.
- (7) If the foreign investor in a foreign investment enterprise directly reinvests in such enterprise with the profits it receives from the enterprise, thereby increasing its registered capital, or uses the share in profits as capital investment for the establishment of another foreign investment enterprise, and the term of operation of the enterprise invested in is not less than five years, the investor shall, upon approval of an application by the tax authorities, obtain a refund of 40 per cent of the income tax already paid on the reinvested amount. Where other preferential provisions have been stipulated [on this matter] by the State Council, the matter shall be handled in accordance with the State Council provisions. Where the investor withdraws the reinvested amount within five years, it shall pay back the refunded tax.

Remittance of Profit

Under the Chinese legal system, there is little restriction on foreign investors to remit their profits out of China, but the required formalities and the taxation preferential treatment concerning the remittance are different from one investment manner to another.

1. Investment Manner I: Establishing a Foreign Investment Enterprise ("FIE")

(1) Remittance of Profit

According to the relevant Chinese laws and regulations, foreign investors (both the individual-investors and the company-investors) are permitted to remit their dividend and may be **exempted from income tax**, provided that the registered capital of the foreign invested enterprise has been fully contributed in due time. (Only the investors of the FIEs in which the foreign investments consist of more than 25% of the total investment can enjoy tax exemption treatment.)

To remit the dividend, the FIE shall submit the following documents to the designated bank: (1) the Tax-paid certificate and taxation declaration form of the FIE; (2) the FIE's Audit Report of the current year issued by a CPA; (3) the resolution of board of directors concerning the distribution of profits; (4) Foreign Exchange Registration Certificate of the FIE; (5) the Capital Assessment Report issued by a CPA; (6) Other documents required by the Administration of Foreign Exchange.

One thing worth mentioning here is the proportion of profit distribution. According to the relevant Chinese laws and regulations, there are three kinds of

FIEs: Wholly Foreign Owned Enterprise (the "WFOE"), Equity Joint Venture (the "EJV"), and Contractual Joint Venture (the "CJV"). With regard to the WFOE, since all the investors are foreigners, there is no special provision on the profit distribution. As for the EJV and the CJV, the provisions concerning the EJV are much stricter than that for the CJV: if the FIE is an EJV, the profit distributable shall be distributed **according to the proportion of each participant's investment**; and if the FIE is a CJV, the parties are allowed to distribute the profit in the form of profit distribution, products distribution or any other distribution form as agreed by the parties, and if it is provided in the joint venture contract that the CJV's fixed assets will be transferred to the Chinese partners for no consideration when the operation term of the CJV expires, the foreign investors are also allowed to, in addition to the distribution in accordance with the investment and/or cooperative means rendered, increase its share in the distribution in the joint venture contract.

(2) Remittance of Income from Transferring the Share in a FIE

Foreign investors are also permitted to transfer their share in the FIEs, wholly or partly, to other investors or third parties. Under such circumstance, if its income from the share transfer exceeds the amount of its investment, **the investor shall pay withholding income tax (for company-investors) or individual income tax (for individual investors) in respect of the amount exceeding the amount of investment at the rate of 20%.**

(3) Remittance of the Dividend of the FIE's liquidation

In case the FIE somehow enters into the liquidation procedure, the foreign investors are also permitted to remit the dividend of the liquidation property.

2. Investment Manner II: Holding Shares of a Chinese Company

(1) Remittance of Dividends

For the foreign investors who do not establish a FIE in China but own B-shares or overseas shares of a Chinese listed company, the income from dividends (bonuses) gained by the foreign investors will **be exempted from enterprise income tax (for company-investors) and individual income tax (for individual-investors)**.

(2) Remittance of the Income from Transferring the Share

In case a foreign investor transfers the B-shares and overseas stocks of a Chinese domestic enterprises, which are not held by its offices and/or sites set up within China, or an individual foreign investor transfers his B-shares and overseas stocks of China's domestic enterprises, **the net profit so earned is exempted from income tax**.

Labor System

I will introduce the labor system of PRC from respects of employment and recruitment, employment contract, working hours, rest days and holidays, wages, social security:

1. Employments and Recruitment

(1) The employment of employees by foreign investment enterprises

(A) A foreign-investment enterprise shall comply with the provisions of Chinese

law when deciding, **at its sole discretion**, the number of employees to be recruited, the method and timing of the recruitment, and the terms of employment.

(B) It may recruit employees locally **through employment agencies** designated by the local labor administration department or, with the approval of the local labor administration department, **recruit directly** either from local area or from other areas.

(C) It shall not recruit employees who have not terminated their employment contracts with their former employers, or who are minors under 16 years old.

(2) The employment of foreigners in China

An employer may not employ foreigners unless and until it has applied for and secured a “Permit to Employ Foreign Nationals in the PRC”.¹ To obtain a license to employ a foreign national, the employer shall complete an “Application to Employ Foreigners in China” and submit it together with the following documents:

(A) the curriculum vitae of the foreigner to be employed;

(B) a letter of intent concerning the employment (original);

(B) a report stating the reasons for the employment of a foreigner;

(C) certificates evidencing the foreigner’s qualifications for the position for which he or she is to be employed;

¹ Such regulations do not apply to foreigners belonging to foreign embassies or consulates or the representative offices of the United Nations and other international organizations in China who have diplomatic privileges and immunities.

(D) a health certificate for the foreigner to be employed; and

(E) other documents stipulated in laws and regulations.

The employment license may then be used to apply for a work permit and residence permit for the foreign employee.

Additionally, the individual economic organization and private citizens are prohibited from employing foreigners. However, since the regulations of labor law of PRC don't apply to the family nurse, a foreigner may be retained by an individual economic organization or private citizens as a family nurse.

(3) If foreigners working in China have signed employment contracts with foreign legal entities located outside of China and their remuneration is also paid from abroad, do they still need to secure a work permit?

If they have worked in China for *three months* or more, and be deemed to be employed in China (with the exception of foreign engineers, technicians and professionals working under technology transfer contracts), such foreigners shall complete the procedures for securing and *employment visa*, *work permit* and *residency permit* with the relevant certificate-issuing authority of the labor administration department.

(4) May foreigners use their employee identification cards in lieu of passports or other travel documents as a form of identification?

An employee identification cards may serve as an evidence only for their entering or exiting from the work premises, or when they undertake the production or other business operations of the enterprise. Such cards may not be used by

foreign employees in lieu of passports, residency certificates or travel documents.

2. Employment Contract

(1) The governing law for the employment contract of FIEs

The labor law applies to all enterprises within the territory of China that have reached employment relationships with their employees, pursuant to which labor services are provided by the employee for consideration. Accordingly, the applicable scope of the labor law covers FIEs, as it is applicable throughout China (except for any Special Administrative Regions established by the central government, such as Hong Kong), employment contracts concluded by FIEs may only be governed by the Labor Law of PRC and not by any foreign law.

(2) Different terms of employment contract

According to the labor law, there are three types of employment contract, namely, those with a fixed term, non-fixed term and with a specific term for completion of a certain task.

A fixed term employment contract is an employment contract with specific commencement and expiry dates. For example, if an employment contract is stipulate to come into effect on 1 January 1995 and to terminate on 31 December 1997, its term is three years and it would be considered a fixed term employment contract.

A non-fixed term employment contract is an employment contract that does not stipulate an expiry date. Generally, where an employee has been working for 10 years and above consecutively with the same employer and both parties agree to renew the labor contract, a non-fixed term employment contract shall be

concluded if the employee proposes so.

An employment contract with a term of “until completion of a specific job” is a contract under which the employee is obliged to complete a certain task or project and the conditions for the commencement and termination of the contract are stipulated. The starting date and the completion date of such a job or project are the corresponding dates of the employment contract. As such, this type of contract is actually a form of fixed term employment contract, with the commencement and termination dates not specified directly.

A distinction should be drawn between an employment contract for the completion of a specific job and *a sub-contracting agreement*. The latter constitutes an economic contract, pursuant to which the contractor and the enterprise do not establish an employment relationship.

(3) Early termination of employment contract

Under the Labor law, the employer may terminate an employment contract before its expiry in the following four situations:

- (A) reaching an agreement by the parties through negotiation;
- (B) the employer may terminate the employment contract in any of the following situations *without further legal liability to the employee*:
 - (a) the employee’s job performance during the probationary period does not conform to the requirements of his positions. It should be noted that, after the probationary period has expired, the employer cannot cite the employee’s failure to perform to the requirements of the position as the reason for terminating the employment contract;

(b) the employee seriously violates the disciplinary rules or guidelines of the employer. The employer's disciplinary rules or guidelines mentioned in item b must comply with the law. If an employer's disciplinary rules or guidelines are in violation of the relevant laws or administrative regulations, they cannot be relied upon to terminate the employment contract;

(c) the employee commits a serious dereliction of duty, is guilty of gross negligence, or engages in conduct which causes the employer to suffer severe losses. If the employee's conduct has not resulted in severe losses to the employer, it may only impose disciplinary sanctions upon the employee and not terminated the employment contract; or

(d) the employee has been charged with a crime.

(C) an employer may terminate the employment contract by servicing 30 days' prior written notice to the employee in any one of the following circumstances:

(a) where the employee, after undergoing a period of medical treatment and recuperation for an illness or a non-work-related injury, remains unable to return to the original position, and is also unfit for reassignment by the employer;

(b) where the employee is unable to fulfill the duties of his or her position and, despite undergoing further training or a transfer of his or her position, remains unable to do so; and

(c) where force majeure sets in, thereby rendering performance in part or in whole of the original contract impossible and, following consultation, the parties cannot agree upon the necessary modifications to be made to the employment

contract.

- (D) the employer may reduce its workforce in situations where it is undergoing reorganization in order to cope with temporary insolvency or due to business hardship.

In such cases, a reduction in workforce is actually a form of early termination of the employment contract. Termination in this case generally involves a relatively large number of employees and the reasons for termination, namely economic hardship, are very clear. In this type of situation, the employer must, 30 days before termination, explain the situation to the trade union or all of the employees, solicit employee opinions and submit a report to the labor administrative department.

(4) Under what circumstances is the employer prohibited from terminating the employment contract?

The employer is prohibited from terminating the employment contract if any one of the following circumstances arises:

- (A) an employee has a work-related illness or is confirmed to be partially or totally disabled due to a work-related injury;
- (B) a sick or injured employee is in the midst of a medical treatment and recuperation period;
- (C) a female employee is in the midst of her pre-natal, birth or nursing period; and
- (D) other circumstances in which termination of the employment contract is prohibited under relevant laws or administrative regulations.

(5) Under what circumstances may an employee prematurely terminate his or her employment contract?

An employee may terminate his or her employment contract prior to the expiry of its term under the following circumstances:

(A) during the probationary period stipulated as in the employment contract; or

(B) where the employer has committed any of the following violations of the employee's rights:

(C) uses violence, threats or an illegal restriction of personal freedom to force the employee to work; or

(D) fails to pay remuneration to the employee or abide by the terms of employment in accordance with the employment contract.

Except as stipulated above, where an employee intends to terminate the employment contract before its expiry, he or she must give the employer 30 days' prior written notice. The employer may deny an employee's request for early termination of the contract if the employee has not given the required 30 day's written notice. Where an employee illegally terminates an employment contract, thereby causing economic losses to the former employer, the employee shall be liable for compensation in accordance with the law and the employment contract.

3. Working Hours, Rest Days and Holidays

(1) Standard working hours

“Standard working hours” refers to the working hours system implemented by employers under normal conditions, as stipulated by the laws and regulations and is classified into daily and weekly working hours. “Standard daily working hours”, also called a working day, are the working hours arranged by an employer for each 24-hour period, from morning to evening. “Standard weekly working hours”, also called a working week, are the working hours arranged by an employer for each seven-day week. According to the standards for working hours currently implemented by the State, a working day consists of eight hours and a working week consists of 40 hours over a five-day week.

(2) Non-fixed working hours system

A “non-fixed working hours system” is a system whereby working hours are not calculated according to a fixed-length working day. It is a system adopted by those enterprises which cannot assess standard working hours because of special production or which require employees to work on ad hoc base. Employees for whom a non-fixed working hours system is adopted and who engage in production and work outside the standard working hours will not be regarded as working overtime shifts or hours. Accordingly, the wages for overtime shifts and hours will not apply to them.

An enterprise may implement a system of non-fixed working hours for any of the following employees:

- (A) senior managerial personnel, field personnel, sales personnel, some shift employees and other employees of an enterprise whose standard working hours cannot be assessed owing to the nature of their work;
- (B) personnel engaged in long-distance transport of an enterprise, taxi drivers,

some railroad, port and warehouse personnel engaged in loading and unloading of cargo and other employees who are required to work on ad hoc base owing to the special nature of their work; or

(C) other employees for whom the system of non-fixed working hours is suitable owing to the special circumstances of production, special working requirements or the scope of their duties.

(3) The Comprehensive calculation of working hours system

“Comprehensive calculation of working hours ” is another system whereby working hours are not calculated on a fixed basis. It is a system which allows the comprehensive calculation of working hours on a weekly, monthly, quarterly, annual or other basis for some employees who, because of the special nature of the work involved, are required to be engaged in work of a continuous nature or whose work is restricted by natural or seasonal conditions. However, the average daily working hours and average weekly working hours should basically be the same as the legally prescribed standard working hours.

An enterprise may implement the system of comprehensive calculation of working hours for any of the following employees:

(A) employees in the transportation, railroad, postal and telecommunications, maritime freight, aviation, fishing and other industries where, because of the special nature of the work involved, operations must be continuously performed;

(B) some employees in the geological and resource exploration, construction, salt production, sugar refining, tourist and other industries which are subject to seasonal or natural restrictions; or

(C)other employees for whom the system of comprehensive calculation of working hours is suitable.

4. Wages

(1) **Minimum wage standard**

Minimum wage refers to the minimum labor remuneration payable by an employer in law for normal labor provided by an employee during higher statutory working time or labor work provided by an employee during either statutory working time or working time that is agreed in a legally-signed labor contract, according to provisions in the legally-signed labor contract. The labor is deemed to have provided normal laour work when he or she is legally on paid annual leave, family visit leave, marriage leave, funeral leave, birth delivery leave, conception-surgery leave or other vacation period regulated by the state or when the employee participates in social activities in accordance with the law during statutory working time.

For an example, the hourly minimum wage of Beijing municipality is from *Rmb* 2.78 to *Rmb* 2.96 and the monthly minimum wage is from *Rmb* 465 to *Rmb* 495. And please note that this standard may be amended by local labor authorities from time to time.

(2) **How are wages of the senior management personnel of a Chinese party to a Sino-foreign joint venture determined?**

In view of the system of income distribution in the PRC, the system of nominal and actual wages may be implemented for senior management personnel of the

Chinese party of a Sino-foreign joint venture.

If no senior management personnel of the foreign part are involved with the management of a Sino-foreign joint venture or if their wages are not paid by the joint venture, then the system of actual wages is to be implemented for the senior management personnel of the Chinese party. However, the senior management personnel of the Chinese party must be paid according to the dual system of nominal and actual wages.

Senior management of personnel of the Chinese party refers to the managing director or deputy managing director, general manager or deputy general manager, financial controller and the principal management personnel who participates in the day-to-day operations.

Actual wages are the real wages paid by the joint venture to senior management personnel of the Chinese party. These wages must be determined by the investment department of the Chinese party in accordance with such economic factors as the enterprise's scale of operation and production, productivity, the return rate of the capital, the depreciation and appreciation rates of State assets, actual profits as well as the average income of the employees of the joint venture.

The difference between the nominal and actual wages must be paid as contributions to the supplementary social security, welfare and funds of the Chinese employees of the joint venture, the use of which shall be supervised by the joint venture's trade union.

5. Social Security

(1) the regulations have been put in place by the Chinese Government for FIE's

participation in employees' social insurance.

FIEs and the employees of the Chinese party² must participate in the social insurance system for pensions, unemployment, medical treatment, work-related injuries and maternity care in accordance with the relevant Chinese laws and administrative regulations. An enterprise and its employees must make their prompt and full social insurance contributions to the relevant social insurance organizations in accordance with the standards stipulated by the local government.

FIEs must, within 30 days of registering their business, complete the social insurance registration procedure by presenting their business licenses and other documents to the relevant social insurance organization. And when its ceasing operations, it must by law pay in full all social insurance fees stipulated by the State. Failure to comply with the same will result in the State Administration for Industry and Commerce and the State Administration for Taxation refusing to carry out the procedures to cease operations of the enterprise and to revoke its registration.

² Presently, the regulations of social security of PRC don't apply to the foreigners except for Korean and German which country has a convention with China.