Power Struggles – The Rise of Labor Unrest in China

Employee protests and labor unrest are on the rise in China in all senses—overall occurrences, frequency, geographical spread, number of employees involved, and media coverage. Such unrest can take a variety of forms, including strikes, lock-outs, production slow-downs, legal actions, and media campaigns. The Hong Kong-based China Labour Bulletin reported that there were more than 1,170 strikes in China between June 2011 and the end of 2013. Foreign companies in particular are increasingly faced with a diverse range of such situations and a workforce that is more willing and determined to collectively assert their labor rights.

Causes

Labor unrest is arising regularly in a number of different circumstances, especially in connection with workforce reductions, business closures or relocations, and in the context of company acquisitions. Even in situations where employers have a legal right to take the proposed action and are willing to comply with the relevant minimum legal obligations for severance or other requirements, employees are pushing and negotiating to be paid higher amounts. Or in some cases, to be paid severance or given benefits to which, strictly and legally, they have no entitlement.

In other cases, employees are using these circumstances to bring to light actual or alleged non-compliance with legal obligations, such as payment of the correct amounts to statutory social insurance and welfare funds, or failure to pay overtime or agreed bonuses. While employees are free to complain about such issues or bring legal claims at any time, employees seem to be more assertive in this regard when able to do this collectively and against the background of a change or transaction that may require their cooperation. There is also increasingly sophisticated knowledge and use of the media to convey employee messages.

Labor unrest, in whatever form, can complicate, delay, and potentially even scupper a potential “transaction.” Foreign companies should note that, while each circumstance is different, it is normally a mistake to assume that it will be sufficient to simply follow the minimum requirements prescribed by law in order to achieve a specific objective. Companies need to consider employee issues strategically in advance, have a strategy to avoid any unrest, and have a plan for dealing with it if it does occur. Communications can be vital to the process.

Forms of Unrest and Legal Basis

The unrest in China has taken the form of store or factory closures or lock-outs, go-slow, employee marches, and arriving at work to clock in and then clock out without any activity in between. Unrest is sometimes planned to coincide with key sales or production periods to maximize the pressure on an employer. In some cases, management or owners have been locked-in to the company premises to negotiate with employees, as in media reports regarding U.S. businessman Chip Starnes. The police will normally observe, but will not take action, saying that such events are a civil dispute to be resolved by the parties. The police are more likely to intervene in situations involving domestic companies or institutions (e.g., the hospital in Guangdong where striking staff were arrested for being on the roof, creating a threat to safety and security).

PRC law is silent on whether employees have an express right to strike—there is no automatic right to terminate employment due to organization of or involvement in a strike or other labor unrest. There is always a delicate balance between keeping the population happy and maintaining social stability.
Mass Lay-Off

The global financial crisis, economic downturn, and rising costs have forced many foreign companies, even in China, to consider restructurings, cost reductions, downsizings, and partial closures in order to remain viable and profitable.

Under PRC law, there is a right for employers to reduce their staff if experiencing financial losses, major technological changes, or other similar situations. There must be a minimum of 20 employees (or 10% of total headcount) involved. However, the employer must conduct a consultation with all employees (or with the company’s labor union or staff representatives) and file a report with the labor bureau. While no outright approval is required from the union or the labor bureau, they may ask the company to reconsider items and the proposed package. This is where the threat of unrest becomes very tangible.

In practice, many companies try to negotiate a mutual termination with affected employees by offering a higher level of severance in return for the employee signing a separation agreement and a smooth exit. This eliminates the need for filing a report with the labor bureau. The authorities often prefer this approach so that they do not find themselves caught between representing employee interests on the one hand and following the letter of the law (i.e., statutory severance) on the other.

The Role of Labor Unions

Labor unions are a complicated area in China. Companies may have a labor union within the company (with elected and appointed employee representatives), but large companies may have different unions and representatives in separate branches and sites within the company. This can make negotiations complex if dealing with different groups. In the past, union representatives have often been viewed as malleable and “in the pocket” of employers, but recent large-scale unrest indicates that such representatives are now more aggressive, organized, and savvy in acting for employee interests, especially if their own positions are affected by a proposed downsizing or transaction.

In addition, there is the All China Federation of Trade Unions (“ACFTU”), the single official union, which has regional and local branches throughout China. The ACFTU has a conflicted position that not only aims to represent employee rights, but to also maintain harmonious labor relations and uphold social stability. For this reason, it can be an effective strategy for employers to approach the ACFTU themselves to assist in handling disputes and unrest and to intercede with the company unions.

Acquisitions

A number of high-profile cases of labor unrest arising from acquisitions have been reported in the media in the last two years.

For an asset deal, there is no mechanism for employees to automatically transfer with the assets. Accordingly, buyers and sellers need to coordinate closely and communicate with employees to be transferred. The seller will not have an automatic right to terminate any employees who are not required or choose not to transfer to the buyer. Employees have the right to be paid severance by the seller or have their period of service with the seller recognized by the buyer. Increasingly, employees are seeking to have severance paid and negotiating a package that is above the statutory calculation (broadly one month’s salary per year of service, but with a cap on the salary amount that can be used for this purpose, which in Shanghai is currently RMB 15,108). And if a higher level of severance is offered to transferring employees, any remaining employees may seek to negotiate the same deal in case the seller seeks to lay them off after the sale. This appeared to be the situation in a recent sale in southern China. If the buyer needs existing employees to transfer in order to operate the assets, this obviously gives employees a good hand to negotiate.

For a share deal, legally there is no change to employment, other than the change of ownership of the employer. Employees remain on their existing contracts and on the same terms and conditions. In particular, there is no right for employees to receive any severance as a result of the transaction. It is increasingly common, however, for employees to seek to obtain assurances or payments, regardless of whether they have any legal entitlement.
In some cases, there is uncertainty or nervousness regarding the new owner. Chinese employees often feel nervous if the sale will result in a foreign company transferring ownership to a Chinese buyer, or to a buyer from a country with which they are not familiar (as was reported in relation to a proposed merger by an Indian corporation). Employees fear that their rights will not be respected, and they will seek assurances as to whether there will be lay-offs down the line and whether a level of severance will apply in such a scenario. In some cases, pressure is put on the seller to provide severance before the transaction proceeds, or on the buyer to guarantee salary levels or to pay a bonus or increase benefits. Employees are aware that labor unrest can put pressure on a proposed deal and that a buyer may potentially treat unrest as a material adverse change and walk away.

Employee nervousness in these situations is increased in locations or industry sectors where it would be hard for employees to find equivalent positions if they are laid off. This is particularly true of middle-aged and unskilled workers. This is another reason why there is also focus on whether a seller has paid the correct social insurance contributions (including pension) and overtime amounts to employees prior to selling. In other situations, unrest seemingly driven by workers may in fact be led by management. A takeover by a competitor may result in management cuts due to duplication of roles, even if the jobs of sales or factory employees are in fact safe. While there may be understandable concerns or legitimate grievances behind labor unrest in relation to proposed transactions, there can also be a strong element of opportunism, fuelled by media reports (often with limited detail on the exact scenario or legal basis) of pay-outs or concessions in other situations.

**Strategies for Avoiding or Mitigating Unrest**

**Compliance** – Employers should check that their existing policies and practices comply with relevant laws, especially in relation to mandatory payments and benefits. In addition, they should be familiar with what documentation is in place and whether a consultation process has been conducted for the implementation of policies—without this, it will be even more difficult to effect terminations if employees are involved in or inciting unrest.

**Law and Practice** – Foreign companies should not assume that it is sufficient to comply with the bare minimum required by law. In practice, foreign companies are often held to a higher standard, regardless of whether this is legally required. It may be expedient to consider some form of assurance or incentive to employees in order to achieve a specific objective as smoothly as possible.

**Preparation and Strategy** – Employers should prepare, as fully as possible, for any lay-offs, transactions, or other scenarios in which employee unrest could arise. This means considering all the implications and coming up with a plan ahead of time, before employees get wind of any changes. It may also involve arranging for private security to be on-hand and keeping the company’s PR team informed to manage media aspects. Above all, confidentiality and timing are vital and information should be distributed on a “need to know” basis. For example, while union representatives have the right to be consulted on and involved in matters involving the welfare of employees, it normally does not make sense to alert them to a possible sale or lay-off until there is certainty and a strategy. Employers should identify how many different unions there may be within the company and ensure a coordinated and consistent approach to dealing with employee representatives.

**Communication** – Clear and timely communication with employees is critical. Many instances of unrest have come about because employees were not given clear details about a given situation. This can lead to nervousness and panic. This should not prevent employers from being firm in their messaging. Communication should be verbal and written, as appropriate. Employers should also engage local authorities where possible. Communications should not only stress that the company is complying with applicable laws, but should also seek to show that the company has taken a considered and reasonable approach to any changes and how these will affect employees.

As always, when doing business in China it is essential to plan ahead and have a strategy!
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