



**PRC Employment/Retail Newsletter**  
*23 January 2008*

**Product Safety Developments**

In spite of recent class action lawsuits against large US toy retailers resulting in widespread recalls, China's efforts to strike a balance between product safety and cost efficiency continue to be hampered by large international companies indirectly forcing them to reduce costs. Such pressure increases the tendency to compromise product quality, including a reluctance to upgrade old equipment, cutting corners and employing young and untrained workers. Given the negative impact that the toy recalls have had, on 11 September 2007, the US Consumer Product Safety Commission (CPSC) and China's General Administration of Quality Supervision, Inspection and Quarantine (GAQSIQ), held the 2nd Biennial Sino-US Consumer Product Safety Summit (**Summit**) in Washington DC.

**Key Developments from the Summit**

- **Reporting Requirements:** The CPSC has imposed stringent reporting requirements on manufacturers, distributors and retailers. If a product has breached a US consumer product safety rule, the CPSC must be notified of such breach within 24 hours.
- **Certification Requirements:** Section 14 of the 1972 US Consumer Product Safety Act (CPSA), provides that all toys fulfilling certain criteria require a certificate evidencing the product's compliance with the appropriate standards, in order to be exported to the US. According to the Certification and Accreditation Administration of the PRC, as of 1 January 2008, toys that contain bamboo, paper, plastic or metal, are powered by electricity, equipped with ejection functions, designed for riding or intended for children under the age of 14 fall within the ambit of the CPSA.
- **Increased Penalties:** In a bid to increase the CPSA's deterrence of potential violators, the CPSC Reform Act (12 September 2007) has significantly increased the maximum administrative penalty from US\$8,000 to US\$250,000 and the maximum penalty for a related series of violations from US\$1.8 million to US\$100 million.

**Commentary**

- The plans brought about by the Summit, collectively named "The Toy Working Group Plan", are scheduled for a review within 1 year. In view of the fact that the CPSC does not have the jurisdiction to test products before they enter the US market, US toy retailers are proposing that an independent third-party testing body test the toys before they are exported to the US. The qualification criteria of such a testing body are likely to be determined during the aforementioned review.

- In the event that any defects in Chinese products are discovered, in order to ensure that solid foundations for an amicable indemnity process are laid, US retailers are advised to furnish to the Chinese manufacturers, fully compliant safety standard product designs for all products (and secure proper valid evidence of such delivery and acceptance).

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### **Initial Impact of the New Employment Contract Law on Retail Operations in China**

On 1 January 2008, the new PRC Employment Contract Law (ECL) became effective, giving rise to a wave of HR-related changes to companies in labor-intensive industries. Based on our experience, some of the hardest hit are large retailers with chains spanning across China, which have found themselves in a crisis situation.

#### **Major Changes**

As a result of the ECL, retailers are now faced with the cumbersome task of conducting an overhaul of all individual employment contracts, particularly:

- signing comprehensive written contracts with existing and new employees, covering major areas such as job descriptions, working conditions, workplace location, occupational hazards, work safety, remuneration;
- determining the length of fixed term employment contracts in order to delay the onset of indefinite term contracts by employees; and
- redefining part-time employment arrangements, a common employment arrangement adopted by retailers, and which must not exceed an average of 4 hours per day and no more than 24 hours per week (failure to adhere to these limitations will result in such part-time employees being entitled to the same salary benefits as regular employees).

#### **Legal Liabilities**

Employers are also exposed to the risk of administrative or criminal liabilities in certain circumstances, of which the most relevant to retailers include the following:

- Where employment contracts are not distributed or if employees receive contracts lacking mandatory clauses, the company must rectify the situation immediately and pay compensation for damages where applicable.
- Unlike manufacturers, the employees of which tend to be concentrated in one or very few locations, retailers with a nationwide presence must deal with numerous local labor bureaus with regard to local policies, and this may significantly delay the entire process.
- If the company illegally withholds its employees' resident ID cards and other employment-related documents, it must return such materials to the employee immediately and pay a fine in accordance with the relevant laws and regulations.

- If the company requires unnecessary financial guarantees from employees, it must return the subject of such guarantee to the employee and pay a fine of no less than RMB 500 and not more than RMB 2,000 per employee. The company will also be liable to pay compensation for damages where applicable.

If an employment contract is unlawfully terminated, the employee has the right to request for the continued performance of the contract, in which event the employer must comply. If the contract can no longer be performed or if no request for continued performance is made by the employee, then the employer must pay compensation. The ECL provides that such compensation shall be twice the amount of the corresponding severance pay.

### **Commentary**

- In addition to compensation and other legal costs, the intangible costs of harming the employees' confidence in the company and their morale in general, both of which tend to be difficult or impossible to regain, are legitimate concerns. As such, based on our experience, a key factor in managing ongoing or preventing future disputes is to open up direct communication lines with employees to ensure mutual understanding and avoid an unnecessary escalation of the dispute.
- In view of the new provisions on indefinite term contracts, companies should refrain where possible from offering short fixed-term contracts (say, 1 year), which would hasten the onset of such an indefinite term contract. In order to give the company sufficient time to assess the employee, the term of the first fixed term contract must be carefully considered in view of the employee's background and qualifications
- Despite the government's granting of a 30-day 'grace period' for the signing of written contracts with existing employees, the risk of unforeseen disputes which may delay the process is high. Therefore, it is imperative that basic compliance issues such as the contents of the contract are addressed from the outset; otherwise the company may be exposed to penalties as of 31 January 2008, if such contracts are not signed in time.

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We trust that you find this newsletter useful. If you have any questions on this subject or any other areas of retail law, please contact:

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Full English translation of any aforementioned PRC legislation as well as other rules and regulations are available for purchase upon request.

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