Will Companies Fire Expats to Avoid Expensive Social Welfare Payments?

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Getting a handle on budgets for China businesses in 2012 is proving to be a headache this year, as so much is hanging in the balance. In emerging markets such as China, it is difficult enough already to cater for the inevitable bumps along the road, preparing for the forthcoming year is as difficult as I ever remember it.

There remain the rumbling uncertainties of the Global Financial Crisis, with China seemingly out of the woods, yet still reliant on overseas markets for export sales. Other trends revolve around the uncertainty of the widening spread of China's social welfare system. The changes affect two groups of people as expatriates in China and their employers must now start to pay mandatory social welfare to China.

> *Come Chinese New Year, we expect to see a drop in the numbers of expatriate faces.*

While the additional costs of employing expatriates are now well-known and can be planned for, the removal of caps on social welfare payments in China is another potential issue concerning social welfare, and there is no clear direction concerning how this will pan out. This affects all employees in China, both local and expatriate. Currently, in most cities, contributions to the social welfare fund that need to be made by employers are capped at a percentage of average local salary. These caps typically differ from city to city, but have the effect of maintaining a ceiling on the maximum amount employers have to contribute for any single employee to generally around RMB 4,000 per month. This means that regardless of how much an employee earns, the social welfare contributions will not impose a large burden on the employer.

However, Dalian has recently announced that it has (at least temporarily) removed its cap, and that social welfare payments payable by employers would now be a standard 31.3 percent of any individual employee's monthly salary. The more the employee earns, the more welfare is paid by the employer (although the cap still remains in place for the employee). A difficult planning point for 2012 then is the question over whether this will be rolled out on a national basis or not. There are already rumors that certain key Chinese cities are planning to introduce a cap-free social welfare security system. If that happens, operating costs for businesses employing higher-paid Chinese and expatriate personnel will see their mandatory welfare contributions shoot up.

This is a huge potential issue, and will massively increase operating costs in China. It remains at present only a possibility, however it does not require any new legislation to enact as the decision on whether to do so or not lies at a local government level. Some governments may feel their corporate businesses can sustain such an increase; by definition these would be cities where investment has no choice other than to remain extant, with any move out of the question. Other local governments may wish to retain the advantage of keeping a cap on welfare payments in order to attract investment. The possibility that the central government puts pressure from above on certain cities to remove the cap cannot be dismissed.

Until there is any official policy – and there may not be – the risk is difficult to determine. However, for 2012 budgeting issues and assuming the worst position, I would recommend working out the potential cost factor and including it as a cost factor in first tier city locations in China. If it's not implemented, you have cash on hand, and if it is, you've covered for the potential costs.

Expatriates in China

The social welfare demands now expected from expatriate employees and their employers will almost certainly result in a decline of expatriates working in the country. Official statistics put the number at some 660,000, of which 250,000 are registered for tax. Non-essential expatriates will be relocated, simply have their contracts terminated, or asked to work in China while on business or tourist visas to keep them off the welfare and tax payroll. The latter also means many will not legally be compliant. Localization of many roles previously held by expatriates will occur. Come Chinese New Year, we expect to see a drop in the numbers of expatriate faces.

Expatriate options

If being passed over in China for 2012, what can the expatriate do? Most we suspect will find it hard to gain new employment in China, at least legally. The bad news is that back home in Europe or North America the economy isn't doing so great either. The good news is Australia is booming, as are other parts of Asia. As one door closes, another opens.

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