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Mastering Employment in China: Essential Insights for Global Employers

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Agenda

- **Key Considerations in Employment Contracts in China**
- **Mandatory Benefits for Employees in China**
- **Calculating Employment Costs in China**
- **Managing Employee Individual Income Tax: Employer Obligations and Strategies**
- **Hiring Employees Without a Local Presence: PEO in China**
- **Special Focus: Hiring Tendencies in the Greater Bay Area**

i. EMPLOYMENT CONTRACT

The Trident of Hiring



Handle with extra care

What do I need to check in an employment contract?

Q: Is it necessary to have an employment contract?

A: Labor Law of the People's Republic of China (Amended in 2018)

Article 16 A labor contract is an agreement made between a worker and an employer to establish work relationships and define the rights and obligations of both parties.

A labor contract shall be concluded for establishment of work relationships.

What do I need to check in an employment contract?

Labor Law of the People's Republic of China (Amended in 2018) Article 19 A labor contract shall be concluded in writing and shall include the following clauses:

- (1) term of the labor contract;
- (2) work tasks;
- (3) labor protection and labor conditions;
- (4) labor remuneration;
- (5) labor discipline;
- (6) conditions for termination of labor contract; and
- (7) liability for breach of labor contract.

Apart from the essential clauses as stipulated in the preceding paragraph, the parties to the labor contract may **agree upon other contents through consultation.**



Checklist for startup

- Name of the company, address, name of the legal representative or a key person-in-charge of the employer;
- Name of the employee together with a valid address and identification number;
- The term of the labor contract;
- Description of the job and the location where it is to be implemented;
- Working hours, rest periods, and off days;
- Salary details;
- Statement that the employer will contribute social insurance for the employee; and
- Labor protection, labor conditions and protection from occupational hazards.

ii. SOCIAL WELFARE

What are the mandatory benefits in China?

What about foreign employees?

Category	Employer rates	Employee rates	Description
✓ Pension insurance	14%-16%	Around 8%	Designed to provide necessary financial support to individuals after their retirement
✓ Unemployment insurance	0.5%-1%	Around 0.5%	Designed to provide financial support to individuals who involuntarily lost their job within certain period
✓ Medical insurance	5%-12%	Around 2%	In the event of illness/non-occupational injury, an employee can have part of the treatment cost covered by medical insurance
✓ Work-related injury insurance	0.5%-2%	/	Designed to cover the cost of treatment should an occupational injury or occupational disease occur
✓ Maternity insurance	0.5%-1%		Designed to cover part of the female employee's medical expense of childbirth and their salary during the maternity leave
? Housing fund	5%-12%	5%-12%	Designed to ensure that workers save to purchase housing

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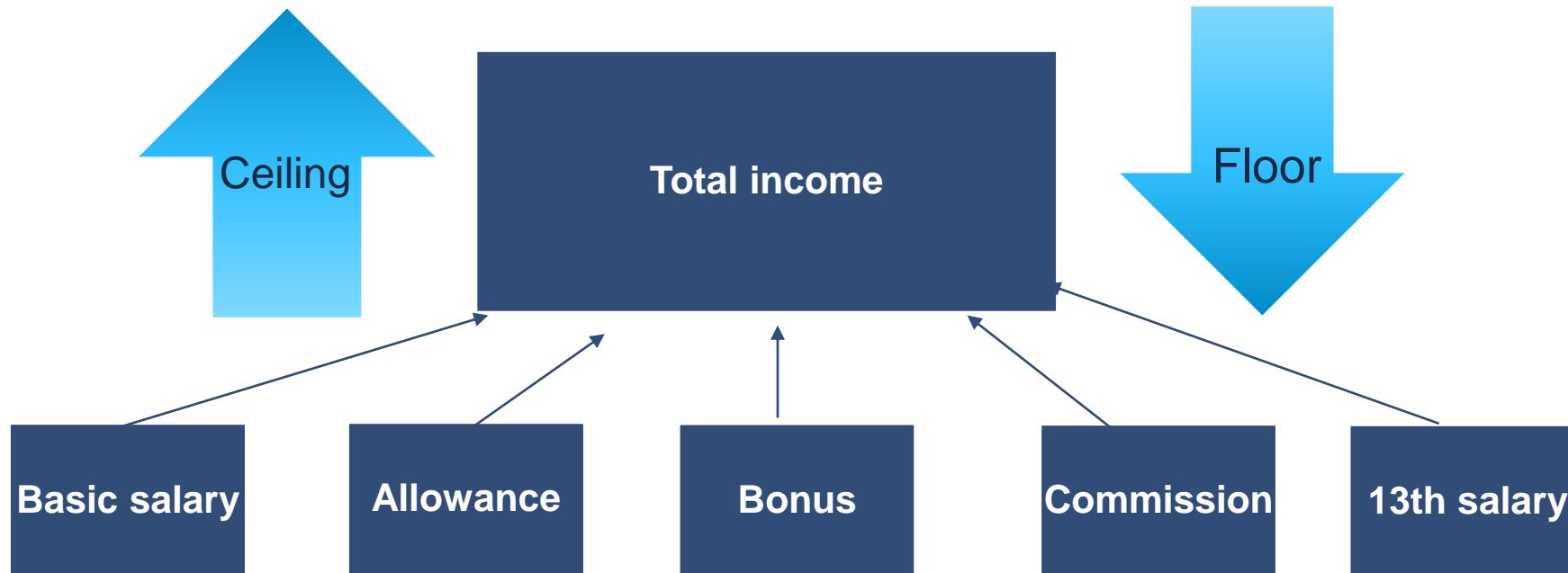
**Do I have to
provide
social
welfare to
my
employees?**

- **Employment termination (Labor Contract Law of the People's Republic of China article 38)**
- **Work injury (Regulations on Work-related Injury Insurance article 62)**
- **Unemployment subsidy (Unemployment Insurance Regulations)**

Article 97 Foreigners employed in China shall participate in social security with reference to the provisions of this Law.
● (Social Security Law of the People's Republic of China)

How to calculate the contribution base for the social welfare?

Social security contribution base = Previous year's total income / 12



How to calculate employment cost ?

- **Employment cost = Gross salary+ Employer portion social welfare**
- E.g. Employee's gross salary is RMB 10,000 per month, SZ company's housing fund is at 10%

Employer portion social welfare:

- Pension $14\% * 10000 = 1400$
- Unemployment $0.30\% * 2360 = 7.08$ (base fixed for all employee)
- Injury $1.40\% * 10000 = 14$
- Maternity $0.50\% * 10000 = 50$
- Medical $6.20\% * 10000 = 620$
- Housing fund $10\% * 10000 = 1000$

Employee portion social welfare

- Pension $8\% * 10000 = 800$
- Unemployment $0.30\% * 2360 = 7.08$
- Medical $2\% * 10000 = 200$
- Housing fund $10\% * 10000 = 1000$

Employment cost= $10000 + 1400 + 7.08 + 14 + 50 + 620 + 1000 = 13091.08$

What are the mandatory benefits in China?

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Social Insurance in China

Overview of the social security system

China's social security system is made up of five different kinds of insurance, plus one mandatory housing fund, as follows:

China Social Security System

In This Section

- Overview of the social security system
- Employers' social insurance obligations
- Social insurance foreign employees' contributions
- FAQ: HR in China – Navigating the Country's Social Security Scheme

iii. INDIVIDUAL INCOME TAX

Individual Income Tax (IIT)-Taxable income

Under the IIT Law, the following income of an individual shall be subject to IIT:

1. Income from wages and salaries; **Yearly Computation Withhold On Monthly Basis**
2. Income from remuneration for independent services (20 percent of the income is regarded as deductible expenses);
3. Income from author's remuneration (20 percent of the income is regarded as deductible expenses, and a further 30 percent discount is available when computing the taxable income);
4. Income from royalties (20 percent of the income is regarded as deductible expenses);
5. Income from business operation;
6. Income from interest, dividends and bonuses;
7. Income from lease of property;
8. Income from transfer of property; and
9. Contingent income.

Individual Income Tax (IIT)

Resident tax payer

183 days

Non-resident tax payer



Individual Income Tax (IIT)-Tax Rate

(progressive tax rate)

IIT Withholding Rates Table for Resident Individuals

Level	Taxable income amount subject to cumulative withholding (RMB)	Withholding rate	Quick deduction (RMB)
1	≤36,000	3%	0
2	36,000 - 144,000	10%	2,520
3	144,000 - 300,000	20%	16,920
4	300,000 - 420,000	25%	31,920
5	420,000 - 660,000	30%	52,920
6	660,000 - 960,000	35%	85,920
7	>960,000	45%	181,920

Individual Income Tax (IIT)-Tax Rate (Monthly tax rate)

IIT Rates Table for Non-resident Individuals		
Taxable income amount (RMB)	IIT rate	Quick deduction (RMB)
≤3,000	3%	0
3,000 - 12,000	10%	210
12,000 - 25,000	20%	1,410
25,000 - 35,000	25%	2,660
35,000 - 55,000	30%	4,410
55,000 - 80,000	35%	7,160
>80,000	45%	15,160

How to decrease my total IIT legally?

1. Check for tax exempt income
2. Use all the standard deductions (5000 per month)
3. Check for special deductions
4. Utilize tax-exempt fringe benefits for foreigners
5. Finish Annual Tax Reconciliation (ATR)
6. Utilize preferential tax policy (GBA subsidy)

Special additional deductions

Nursing expenses for children under 3 years old

Children's education expenses

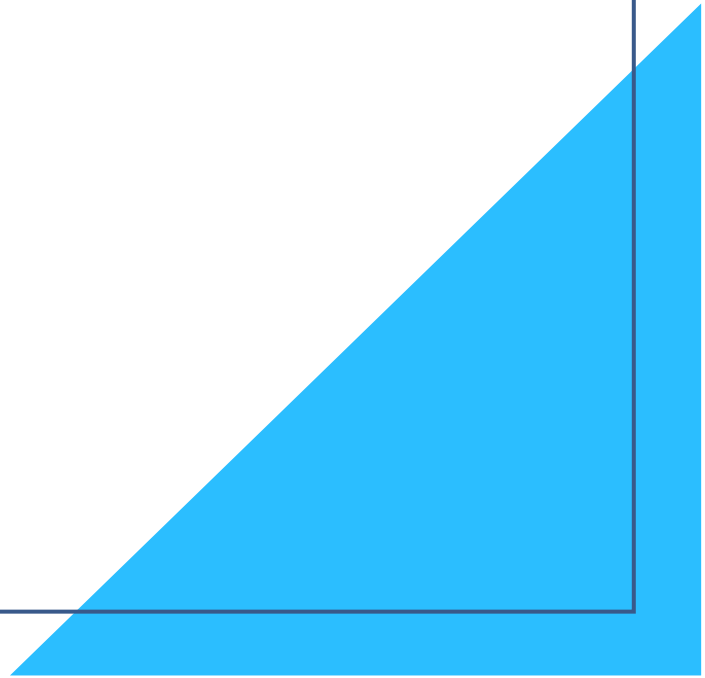
Continuing education expenses

Healthcare costs for serious illness

Housing loan interest

Expense for supporting the elderly

Housing rent



Tax-exempt fringe benefits for foreigners

**Housing
expense**

Meal fee

**Laundry
fee**

**Education
expense
for children**

**Language
training
expense**

**Relocation
expense**

**Business
travel
expense**

**Home visit
expense**

iv.CONCLUSIONS

**Core
takeaway-
Consistency**

Employment contract hiring
entity

Salary payee

IIT submission entity

Social welfare contribution
entity

v. Hiring Employees Without a Local Presence: PEO in China



The Most Popular Legal Entity Structures in China

Strategy must lead structure.

The FIEs Foreign Invested Enterprises

Representative Offices (ROs)

Foreign Investors

A liaison office - cannot engage in profit-generating activities

Wholly Foreign Owned Enterprises (WFOEs)

Foreign Investors	100%
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100% ownership and management control.

Joint Ventures (JVs)

Foreign Investors	Chinese Investors
-------------------	-------------------

Restricted industry category
To leverage a local partner's existing hard assets or soft resources

Non-Entity Options



1) Independent/Individual Contractors

- To be fully aware of PE applicability. Once an enterprise triggers PE status in China, it becomes subject to a lot of taxes, including the staff will be subject to IIT.



Pros	Cons
<ul style="list-style-type: none">• Little to no entrance cost• Little to no maintenance cost• Little to no exit cost	<ul style="list-style-type: none">• Not in full compliance with Chinese Labor Law• Employee(s) will not have access / have limited access to Chinese Social Insurance system• Employee(s) will be required to self file taxes (w/ tax rates being different from those applicable to salaries)• Creates potential corporate tax issue for overseas company (i.e., Permanent Establishment Risk*)• Individual limited to receiving USD 50,000 per year in overseas payment

↪ **Suggestion: any such relationship entered should be as short-term as possible.**

2) Local Distributor / Partner

➤ Choosing a Distributor is a KEY:

A credit and background check is a must-have

- Check/ask do they have good networks and contacts?
- Regular communication - by meeting the distributor in their own market and observing their knowledge and presence in the market.

Pros

- Potentially low entry cost
- Potentially low maintenance cost
- Potentially low exit cost
- No employee liabilities
- Immediate access to a supply chain and distributors and consumers

Cons

- Lack of control (technology, intellectual property, brand, sales processes, compliance)
- Lack of transparency and accounting for sales and profits and pricing
- Only a contractual relationship requiring enforcement

BORDER CLOSED

3) Professional Employer Organization (PEO) or Global Staffing Solutions (GSS)

➤ When do companies or individuals use PEO?

- Overseas Expansion
- Headcount freeze/tight budget
- Restructuring/Consolidation

**Having an expert HR team
without the expense
that comes with having a team on staff.**



Cons

- Potential legal grey area for PEO
- Lack of control (technology, intellectual property, brand, sales processes, compliance)
- Lack of transparency and accounting for sales and profits and pricing

Pros

- Low entry requirements
- Potentially low maintenance cost
- Potentially low exit cost
- Employee(s) would have access to Chinese Social Insurance system
- Administrative duties: onboarding, payroll, and people management

An important note: the company still directs the employees in their day-to-day tasks.

What is PEO and how does it work?

- Offshore recruitment before setting up an entity
- Employing staff at local labor costs
- Outsourced employee management
- Hiring foreign employees legally and in compliance
- Getting legal support on labor contract issues



PEO in China



Real Case

Company A is well-known training company that is considering expansion to China.

Established overseas, its knowledge of Chinese market is limited. Company A is hesitant.

Decision

- Decides SZ has the main point of entry;
- objective is to place some feet on the ground to build relationships with potential customers;
- rather than do the substantial investment of incorporating a company, Company A opts for a more cautious solution and chooses **PEO**

After 8 months:

- market is stable;
- profitability is certain in the coming year;

Therefore...

- Company A decides to incorporate a subsidiary in Shenzhen.

Strategy

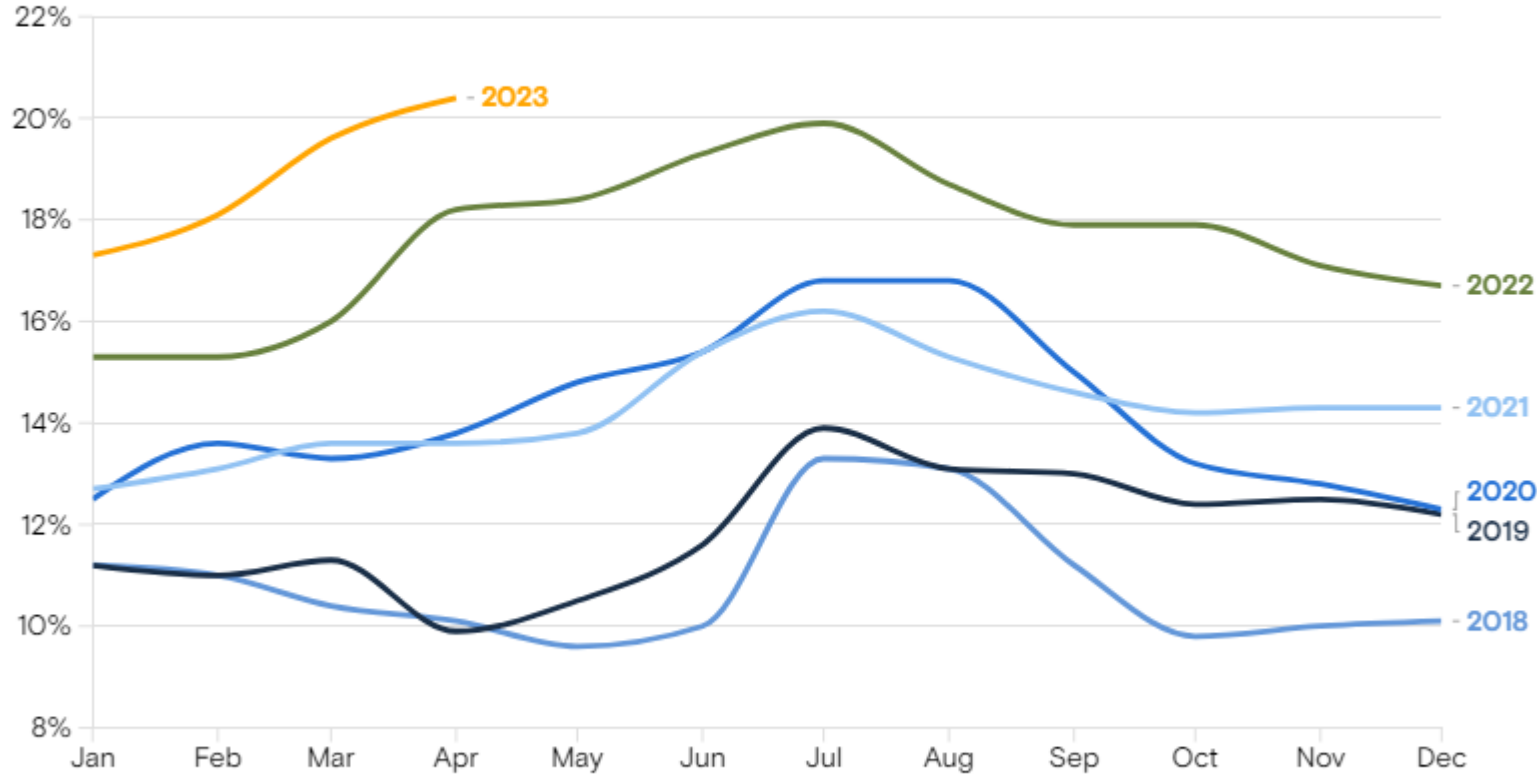
- Mitigation of risks;
- Saving resources;
- “test” the market.



vi. Special Focus: Hiring Tendencies in the Greater Bay Area

China's youth unemployment is climbing despite economic recovery

China urban unemployment rate (age 16-24)



Source: NBS, Goldman Sachs Research

Goldman Sachs

Main Reasons:

- **Less work experience**
- **service industries hire younger staff and were affected during the pandemic**
- **No skill match**

Note:

20,4% is double what it was in 2019 (10%)

Strong supply of graduates this summer can increase the rate by 3%

Hiring Trends in China in a post Covid Economy

Tendencies:

1. Strong Demand for Digitally Competent Staff
2. Increasing need to hire Cybersecurity Professionals
3. Freelancing and flexible work arrangements
4. Some companies willing to accept Remote work.

Recurring and new problems:

5. Working /Residence Permits are increasingly more bureaucratic
6. Rules/Timings for these permits vary from city to city
7. Lack of logic.
8. Some foreign degrees not being recognized by Chinese authorities
9. Foreigner's exodus continues and even foreign companies increasingly hire less foreigners (**10%** of inquired by EU chamber hire zero)

“56 percent of businesses reported being unable to recruit and hire the necessary international talent” - British Chamber, Position Paper 2023



Top Recruitment Strategies in China in the Post-COVID Era

offline and virtual
job fairs

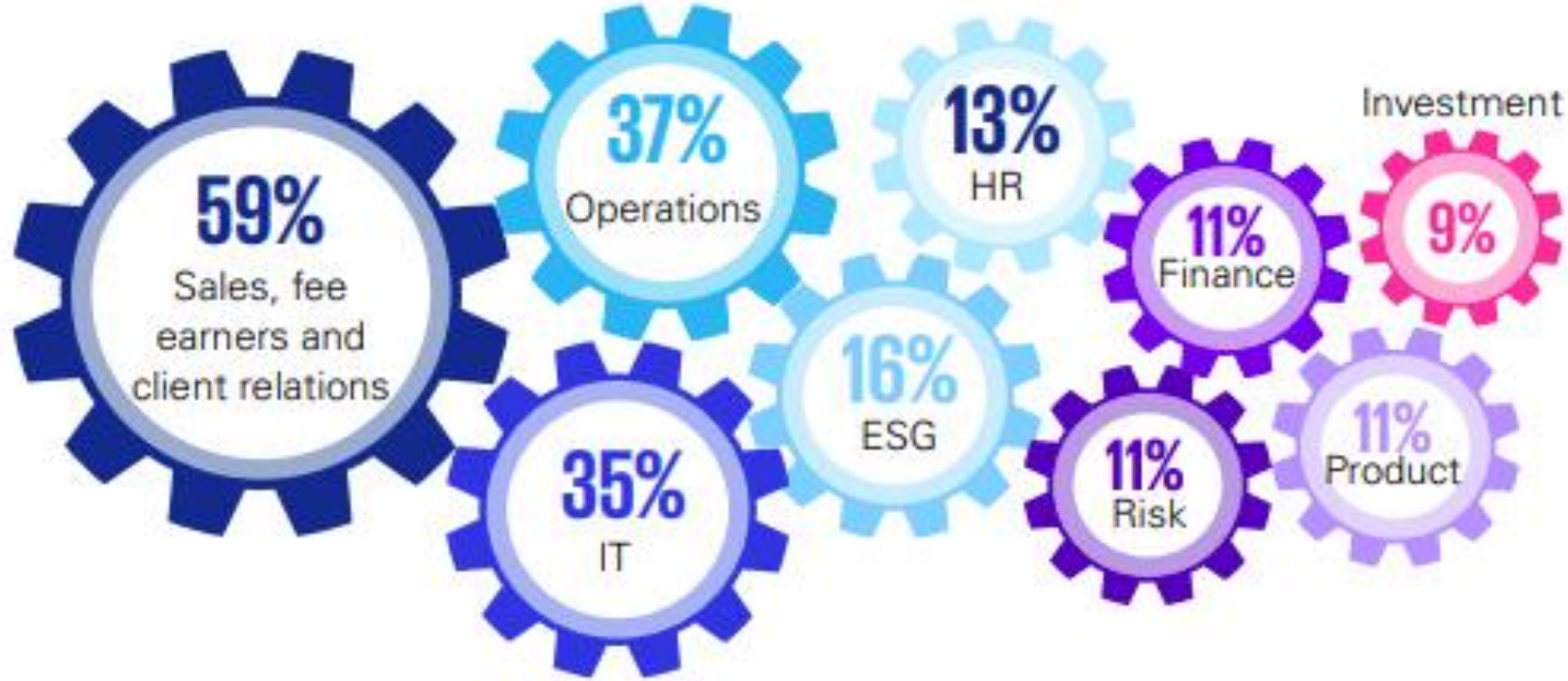
Skills-based hiring

Upskilling and
reskilling programs

Referral programs

Collaborative hiring

Figure 3 Areas in which headcount increases are focusing on



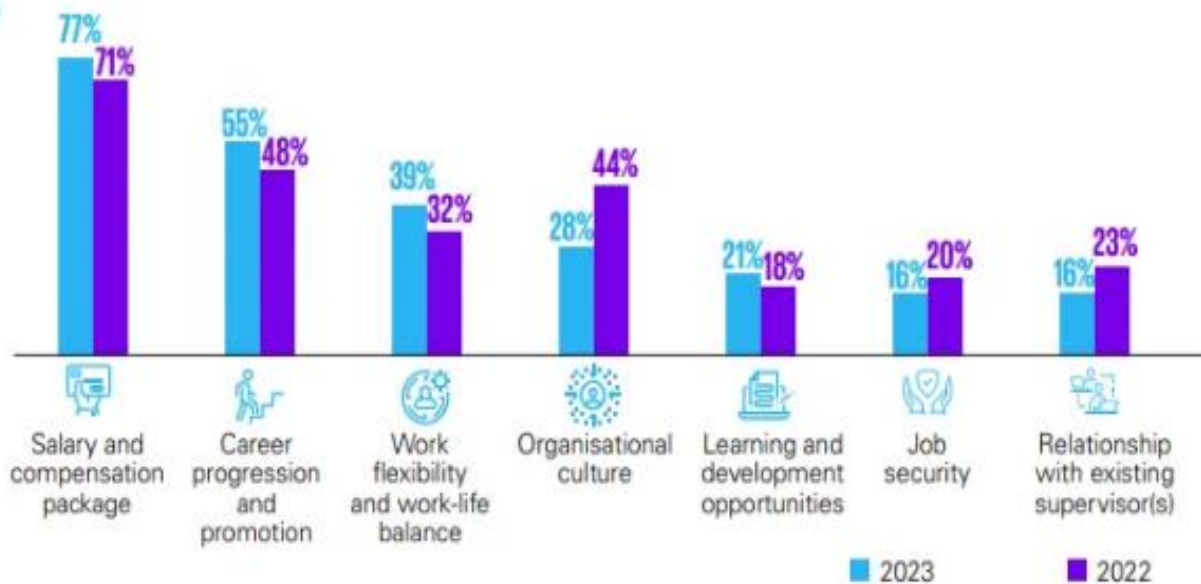
Base: C-level and HR respondents in Hong Kong SAR who are expecting an increased headcount at their organisation in 2023

Respondents were invited to choose more than one answer

Source: KPMG survey analysis

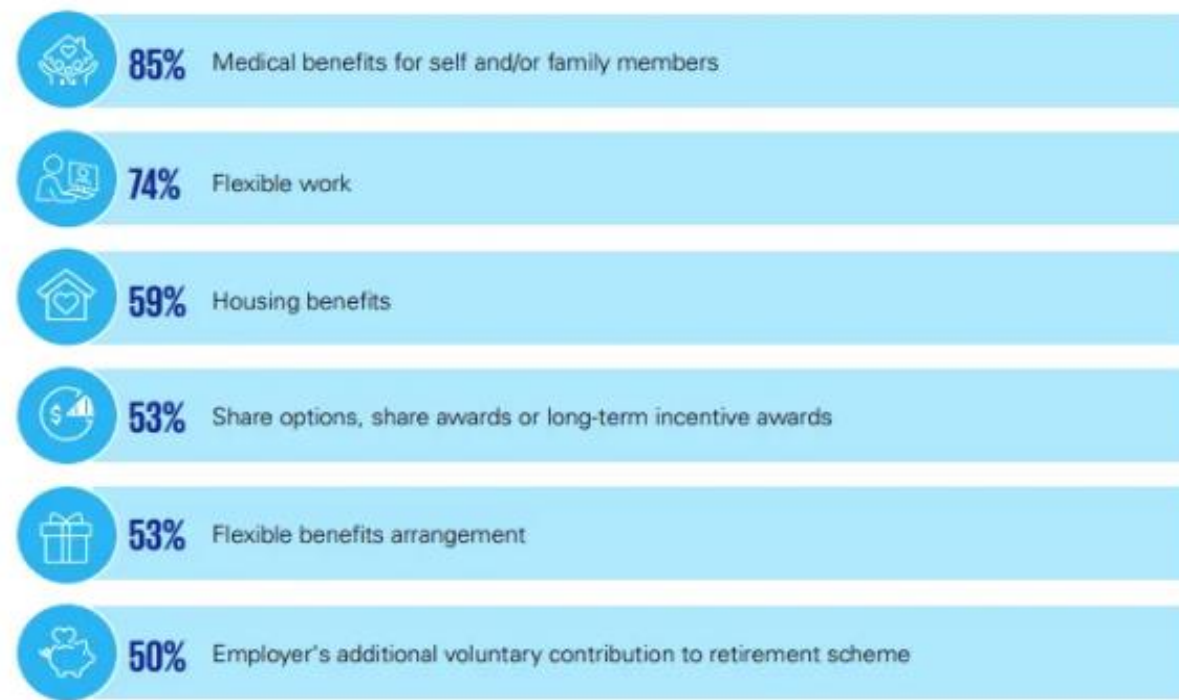
'ESG': Environmental, social and governance

Drivers for Seeking a new Job in 2023



Base: All respondents in Hong Kong SAR
 Respondents were invited to choose more than one answer
 Source: KPMG survey analysis

Most Desired Benefits



Reference Materials

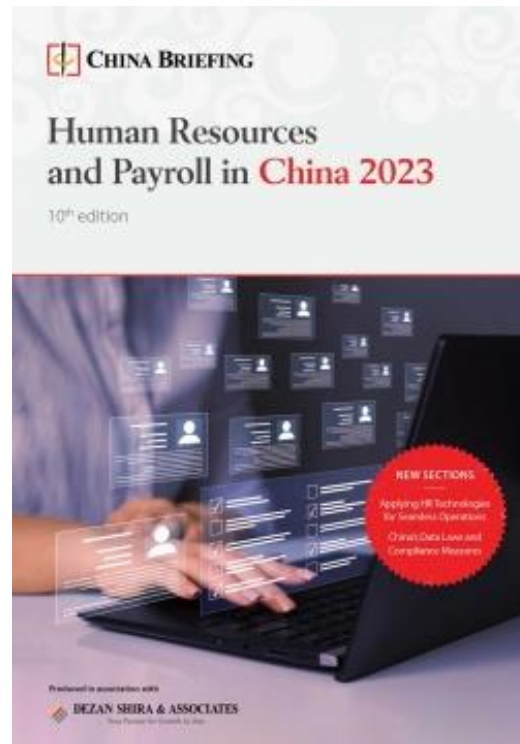
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