

Labour Dispatch Versus Outsourcing

In China, businesses requiring additional manpower for their activities without wishing to hire new employees often use either the labour dispatch system or the labour outsourcing system.

In the case of a labour dispatch agreement: an employee from a temporary employment agency is dispatched for a shorter or longer period of time to a host company to perform specific tasks. The dispatched employee is subject to the management of the host company employing them.

On revision of the *PRC Labour contract law* in 2013, the Chinese government reinforced supervision of the labour dispatch regime. Additionally, a strict framework for the labour dispatch regime was set up with the publication of the *Provisional regulations on the labour dispatch regime* in 2014.

As a result, only companies that hold a professional licence for labour dispatch services issued by the administrative authority for labour are authorised to offer this kind of service.

The number of dispatched employees must not exceed 10% of the total number of staff at the host company. Moreover, it may hire dispatched employees for the following posts:

- (a) Temporary positions of a maximum duration of 6 months;
- (b) Ancillary positions, i.e. to support the main activities; or
- (c) Replacement positions, e.g. in the event of the temporary absence of the usual holder of the position.

The system of outsourcing of labour has not, however, been the object of dedicated and explicit regulations nor has it been defined. It is generally presented as a system whereby a company entrusts one or more parties with its ancillary activities - such as human resources management, IT support, one or more parts of the manufacturing process (for manufacturing firms) etc. - to another firm with specialised expertise or know-how. Such firm will therefore dedicate its teams to the contractually-agreed activities in consideration for payment for services. The firm benefiting from the service shall not have a direct legal relationship with the outsourced workers who shall remain subordinate to the service contractor.

Case study:

Company A (a manufacturing company) and company B (a manpower contractor) entered into a labour dispatch agreement in 2010 for the dispatch of employees of Company B to Company A.

Mr Fan joined Company B in 2008. He was dispatched by Company B to Company A to hold a technical position from 2010 onwards.

In 2014, the labour dispatch agreement between Company A and Company B was terminated and replaced by a labour outsourcing service agreement providing that Company B would provide services to Company A. The annual amount of the services provided amounted to RMB 650,000, to which were added monthly management costs of between RMB 200 and 300 per employee providing services to Company A.

On 20 November 2015, Company A returned part of the outsourced workforce to Company B, which included Mr Fan. Company B dismissed Mr Fan on the same day on the grounds of a material change to the objective conditions prevailing at the time his employment agreement was entered into (*Article 40 of the PRC Labour Contract Law*).

Following his dismissal, Mr Fan instigated proceedings against Company A and Company B before the Chinese labour arbitration court and subsequently before the civil courts to seek confirmation of the unlawfulness of his dismissal and obtain economic compensation.

Decision of the judge

In a dispatch relationship, in accordance with Article 9 of the PRC Labour Contract Law, the company dispatching the employee (i.e. the employer) and the company hosting the dispatched employee are jointly and severally liable for any compensation which may be due to the dispatched employee. In the labour outsourcing system, on the other hand, only the employer is liable for economic compensation due to their employees.

Consequently, once the judge had confirmed the unlawfulness of Mr Fan's dismissal, the outstanding key point was to determine whether or not Company A should be held jointly and severally liable with Company B for the economic compensation due to Mr Fan. In order to do this, it was necessary for the judge to decide on the classification of the contractual relationship between Companies A and B.

For this purpose, the judge highlighted the two main differences between the employee dispatch regime and the labour outsourcing regime:

- Difference in the object of the contract and the invoicing of services: The main object of a labour outsourcing agreement is the performance of a specific task / mission. The services provided are invoiced on the basis of the amount of work required for the realisation of this task / mission. In the context of a dispatch, the services provided are calculated on the basis of the number of dispatched persons and their remuneration (including wages, social charges, housing funds, overtime, allowances etc.) independently of the effective task performed by the dispatched persons.
- Difference in terms of link of subordination: Outsourced employees remain subordinated to the labour outsourcing company and therefore report to that company. Under the dispatch regime, however, dispatched persons are subordinated to the host company and therefore report to the employees / managers of the host company.

It is interesting to note that in their analysis, the judge did not take into account the title of the contract itself but rather its content, that is to say:

- The calculation of the services provided directly connected with the number of employees affected rather than with the content of the service; and
- The very clear link of subordination of Mr Fan with Company A.

In conclusion, the judge held that although Company A and Company B had signed a contract entitled "labour outsourcing agreement" in force since 2014, the parties had continued to perform the previous dispatch agreement, and that therefore Company A was indeed jointly and severally liable for the economic compensation due to Mr Fan.

Recommendations from DS Avocats

As demonstrated by this case study, in order to be discharged from the obligations and restrictions applicable to labour dispatch systems and the liabilities inherent to this system, it is not sufficient to change only the title of a labour dispatch contract to that of labour outsourcing agreement but it is necessary to fundamentally change the structure and content of the agreement.

In a general manner, a labour outsourcing agreement containing the following provisions would run the risk of reclassification by the courts as a labour dispatch agreement:

- The host company is in charge of the management, control and supervision of the workers, notably with respect to their diligence, the allocation of posts, bonuses and sanctions, returning to the employer etc.;
- The provision of services is calculated on the basis of the number of persons and/or their employment cost (wages, social charges, accommodation costs, overtime etc.);
- The wages are paid directly by the host company.

Businesses generally tend to use the labour outsourcing system as they hope to thereby mitigate their risks as an employer. However, as opposed to temporary employment agencies which are subject to specific licence requirements and are generally trustworthy businesses, companies offering outsourcing services are often small businesses, that have sometimes been formed to provide this kind of service for only one client, and which do not always satisfy their legal obligations as an employer. It is not unusual to find that these firms do not sign employment agreements with their employees, do not pay social charges or contribute on bases that are lower than they actually are etc. Now, in the event of reclassification into a dispatch relationship, the host company would be jointly and severally liable and potentially be liable to compensate for all the omissions of the labour outsourcing firm.

In any event, without going as far as to advise against the adoption of a labour outsourcing regime, we strongly recommend that:

1. Businesses that have adopted a dispatch regime should verify due compliance with the conditions for dispatch (nature of the post, percentage of dispatched persons within the business), and, of course, ensure that the selected temporary employment agency selected does indeed have the legal qualifications required for this activity.
2. Businesses that have adopted / shall adopt the labour outsourcing regime should:
 - Select a reliable outsourcing company;
 - Ensure that the adopted regime does not run the risk of reclassification into a system of dispatch of employees;
 - Instruct legal counsel to review the labour outsourcing agreement;
 - Ensure that the outsourcing company is compliant with all its obligations as an employer;

- Ensure that its external employees are fully aware that they are the employees of an outsourcing company. It would be advisable for this purpose to, for instance, make them to wear uniforms that are different from those of employees of the host company, and for them not to enjoy the benefits awarded to employees of the host company;
- Ensure that the outsourcing company supervises and manages the outsourced employees on a daily basis.

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