



People's Republic of China adopts Social Security System

Law Firms with a Presence In China and Certain Foreigners Must Make Social Security Contributions Starting October 15, 2011

The China Social Security Law (“The Law”), which took effect on July 1, 2011, introduced a national framework aiming to standardize and strengthen the social insurance scheme administered by local governments for Chinese and foreign individuals, as well as their employers in China.

On September 6, 2011, the Ministry of Human Resources and Social Security (“MHRSS”) issued the final *Provisional Measures for Foreigners Working in China regarding Participation in the Social Insurance Scheme* (“The Provisional Measures”) which will take effect on October 15, 2011.

The key provisions of The Provisional Measures that affect U.S. law firms with a presence in China are summarized as follows:

- Foreigners hired directly by Chinese companies, or assigned by foreign (non-Chinese) employers to work at their Chinese subsidiaries, branch offices or representative offices and who have legally obtained work permits, resident permits or permanent resident permits in China are required to make Chinese social security contributions (which includes pension, medical insurance, work-related injury insurance, unemployment insurance and maternity insurance) effective October 15, 2011.
- Chinese employers or China host companies are likewise required to contribute the employer's portion of the social security contributions, as well.
- Foreigners participating in the new social security scheme will receive social security cards and can enjoy benefits similar to local Chinese residents. For example, the number of years of pension contributions by foreigners can be aggregated if the person returns to work in China after a previous employment in China. Foreigners are also entitled to receive a monthly pension payout after retirement if certain criteria (i.e. minimum contribution years) are satisfied, or the cumulative balance of the individual social security account can be withdrawn upon written application for termination by the foreigner.

-
- Foreigners from countries which have entered into Totalization Agreements with China may be exempt from making Chinese social security contributions in accordance with the coverage of the relevant agreement. However, to date China has only entered into Totalization Agreements with Germany (for pension and unemployment) and South Korea (for pension).
 - The Provisional Measures require the local labour bureau (which is the agency that issues work permits to foreigners) and the local social security bureau to establish timely and regular communications to monitor the compliant status of social security contributions of foreigners. Noncompliance in making required social security contributions will be subject to a penalty under the social security regulations.

Challenges in local rules

The Provisional Measures provide general guidance for foreigners participating in the Chinese social security scheme. The details of implementation -- such as contribution rates and base, administrative procedures, etc. are highly dependent upon local rules issued by local governments and their enforcement, which may vary greatly from city to city. Some local social security bureaus are still drafting their updated local rules.

Given that Article 97 of The Law indicates that foreigners should participate in the Chinese social security scheme from July 1, 2011 while the effective date of The Provisional Measures is October 15, 2011, it remains to be seen whether or not backlog social security contributions for the period from July 1 to October 14, 2011 must be made. This may eventually depend on local social security bureau's interpretation of The Law and The Provisional Measures. For example, a local social security bureau in southern China has taken the view that foreigners should make contribution from July 1, 2011.

Financial impacts to employees and employers

Table 1 (at the end of this memo) is an illustration of the costs associated with making social security contributions for the foreign employees and their employers based on current contribution rates and the bases in Shanghai, Beijing and Guangzhou.

Since the great majority of foreigners are paid a monthly salary that exceeds the local salary ceilings, the additional employer's and employee's combined social security contribution cost would be around RMB5,600 per month for each foreign employee.

What benefits could foreigners enjoy?

While it is indicated that foreigners participating in the Chinese social security scheme should be entitled to benefits similar to those enjoyed by local Chinese, The Provisional Measures do not elaborate on how foreigners could apply for benefits other than a pension.

As a reference, qualified participants in Shanghai who retired in year 2010 could receive around RMB2,000 per month as their retirement pension payout (about \$313 USD). Although the amount will be increased on a yearly basis taking into consideration inflation, practically speaking this is not much of a benefit to foreigners. In addition, except for a pension, the benefits for making contributions to unemployment insurance, maternity insurance, work-related injury and medical insurance are not clear at this time. For example, local Chinese are not allowed to claim unemployment insurance under The Law if they have immigrated to another foreign country. Since foreigners who become unemployed would usually leave China once their work permit is cancelled, they would similarly not be eligible to claim the unemployment insurance in this circumstance.

Protection under totalization agreement

While China has only entered into Totalization Agreements with Germany and South Korea, a number of countries have started discussions with China on entering into Totalization Agreement since the draft Provisional Measures was released. It is expected that more Totalization Agreements will be concluded (plus Germany and South Korea may expand the categories of social security insurance under their Totalization Agreements with China) to relieve foreign individuals' Chinese social security obligation in the future. However, it is still unknown how local social security bureaus will enforce the exemption that is typically available under a Totalization Agreement. For example, a local social security bureau has indicated that both the employers and employees should first make the social security contributions, but any refund will be limited to the employees' contributions only.

Impacts on residents of Taiwan, Hong Kong and Macau ("THKM")

The draft Provisional Measures indicated that THKM residents should make social security contributions as set forth in The Provisional Measures to follow. However, this clause was removed from The Provisional Measures issued on September 6, 2011. Thus, the question exist whether THKM residents are "exempted" from making such contributions under The Provisional Measures or the local authority may continue to rely on the Labour and Social Security Bureau Order [2005] No. 26 which requires participation of THKM residents in the Chinese social security scheme if they are employed by a Chinese company in China. It is also possible that a separate guideline covering THKM residents may be issued by some local authorities down the line.

Law firms with offices in Hong Kong and/or Taiwan, in addition to those with a presence in China, must decide whether to participate in the program, or to take the chance and delay participation until some definitive clarification is issued.

Any time bar for enforcing backlog contributions?

While it is not specified under The Law, the Implementation Rules for The Law and The Provisional Measures whether there is a time limit in which the relevant local authorities could require employers and the employees to make backlog contributions, it is stated in The Provisional Measures that in the case of non-registration and non-contribution, reference should be made to State Council Order [2004] No. 423 ("Circular 423"). According to Circular 423, there is a time bar of two years beyond which no further investigation may be conducted and no penalty would be imposed. However, it is uncertain that this interpretation will be accepted by the local social security bureaus and be in line with their updated local rules.

The bottom line- effect on US Law Firms

Law firms and their foreign attorneys working in China should ensure that they will be compliant with the latest local social security rules and practices to avoid non-compliance penalties.

PricewaterhouseCoopers' team of professionals is ready to assist its law firm clients in providing services and advice with respect to complying with the new social security requirements. Please contact Stanley Kolodziejczak at (646) 471-3160, Gregg Sincoff at (646) 471-1335 or Nancy Regan at (646) 471-6104 in New York; and Rex Chan at +86 (10) 6533 2022, and Michael Ho at +86 (10) 6533 2783 in China.

Table 1

	Shanghai		Beijing		Guangzhou	
Social insurance items	Employee's portion	Employer's portion	Employee's portion	Employer's portion	Employee's portion	Employer's portion
Pension	8%	22%	8%	20%	8%	12%
Medical	2%	12%	2%+3	10%	2%	8%
Unemployment	1%	1.7%	0.20%	1%	1%	2%
Maternity	0%	0.80%	0%	0.80%	0%	0.85%
Work-related injury	0%	0.50%	0%	0.3% - 1%	0%	0.5%-1.5%
Total	11%	37%	10.2% + Rmb 3	32.1% - 32.8%	11%	23.35% - 24.35%
Ceiling for 2011 monthly salary base for contribution (Rmb)		11,688		12,603		13,623
Maximum monthly contribution (Rmb)	1,286	4,325	1,289	4,046 – 4,134	1,499	3,181 - 3,317

General Disclaimer:

This document is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.

Solicitation.

© September 2011. PricewaterhouseCoopers. All rights reserved.

In this document, "PwC" refers to PricewaterhouseCoopers LLP, which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity. This document is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.