Novel Coronavirus (COVID-19) Presents New Legal Challenges in China

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The outbreak of novel coronavirus (COVID-19) has affected many businesses in China. Since the start of the outbreak in December 2019 through this date, more than 80,000 cases including more than 3,000 deaths have been confirmed in Mainland China.

To combat the epidemic, central and local governments have announced a variety of regulations and administrative measures, including holiday extensions, quarantines, temporary business shutdowns, city lockdowns and travel bans. Many companies have suffered substantial disruptions to their operations and face novel legal challenges arising from the epidemic, including the performance of commercial contracts, employment-related matters, occupational health and safety, and protection of personal information. We will discuss in this client alert some of these new legal challenges encountered by businesses in China.

I. Contract Performance and Force Majeure

The outbreak of novel coronavirus has affected many companies' ability to perform commercial contracts. One of the key issues is whether the epidemic constitutes a "force majeure event" whereby the "force majeure" clause in commercial contracts can be invoked to suspend the performance and/or release the affected party from potential liability.

"Force majeure" is a legal doctrine widely recognized in the world. The doctrine is also recognized and supported under Chinese law and juridical practice.

China's *Contract Law* (as amended) provides in Article 117 that a party which is unable to perform a contract due to force majeure is exempted from liability in part or in whole based on the impact of the force majeure event, except as otherwise provided by law. The Contract Law defines "force majeure" as "any objective circumstance which is unforeseeable, unavoidable and

insurmountable". The *General Principles of Civil Law* in Article 107 and the *General Provisions of Civil Law* in Article 180 have similar provisions.

The Supreme People's Court (SPC)'s *Judicial Interpretations on Several Issues Concerning Application of Contract Law (II)* (2009) further provides that if a significant change in circumstances has occurred after the formation of a contract that is not a commercial risk, could not have been foreseen or controlled by relevant parties at the time of entry into the contract, and renders the continual performance of the contract unfair to the affected parties or impossible for the parties to realize the purpose of the contract, the people's court when reviewing a petition shall determine whether the contract should be amended or terminated based on the principle of fairness taking into consideration the actual circumstances.

In litigation practice, Chinese courts have focused on the following considerations in determining whether an event constitutes a force majeure event and its impact on contract performance:

(i) Whether an event that impacts the performance is unforeseeable, unavoidable and beyond the parties' control. Normal commercial risks may not be treated as force majeure events.

For example, the SPC in a 2016 case[1] ruled that the failure to obtain government approval of a project involved in the case does not constitute a force majeure event because the government under law had the right to exercise discretion in determining whether to approve a project of this type and the parties could have foreseen the risks of disapproval when the contract was executed, which should constitute an inherent business risk, rather than a force majeure.

In another case,[2] the SPC ruled in 2019 that the promulgation of implementing rules after the contract in dispute was executed did not constitute a force majeure event because the implementing rules were to implement an existing law that pre-dated the contract and the parties should have anticipated promulgation of the implementing rules at the time when the contract was executed.

(ii) In determining whether an event constitutes a force majeure event, the courts will also look at the timing when such event occurs. In order to constitute a force majeure event, an event must occur after a contract has been entered into but before the contract is fully performed.

If an event occurs after a contract is fully performed, the occurrence of such event should not constitute a basis for unwinding the contract. The SPC ruled in

[1] (2016) Zuigaofaminzhong No. 90

[2] (2019) Zuigaofaminzhong No. 960

a case in 2018[3] that the fact that a mining company, the target of an acquisition, was subsequently ordered by government to wind down its business should not constitute a force majeure event or become the reason to unwind the acquisition because the acquisition had already closed and the parties had fully performed their obligations under the acquisition agreement by the time of government order.

(iii) Whether the occurrence and/or continuance of a force majeure event constitutes a changed circumstance in or otherwise frustrates the performance of a contract. An affected party may invoke a force majeure event and petition for non-performance of its obligations in part or in whole only if the performance of the contract is frustrated by a force majeure event.

(iv) The courts will review the impact of the force majeure event on the performance of a commercial contract in order to determine appropriate remedies. For example, if the performance is partially affected by a force majeure event, the courts in practice are unlikely to terminate the entire contract, but rather may grant partial release of performance obligations or suspension of performance pending the conclusion of a force majeure event.

Under common law, force majeure is usually not implied in the contract and the parties need to expressly include a force majeure clause in the contract as an excuse for non-performance or partial performance.

In China, while the Contract Law provides that the parties need to have a force majeure clause in the commercial contract to petition for exemption from performance, the SPC judicial interpretations, the General Principles of Civil Law and the General Provisions of Civil Law nevertheless allow the parties to be exempted from performance based on the doctrine of "changed circumstances" where the affected party needs to prove an event affecting performance was unforeseeable, unavoidable and beyond its control.

This suggests that the force majeure doctrine is somewhat implied under Chinese law and judicial practice. However, in practice, the absence of an express force majeure clause may subject the affected party to a higher burden of proof.

In an effort to stabilize its economy, the Chinese government has been supporting companies affected by the epidemic (including multinationals' China subsidiaries) to take precautionary measures to mitigate or reduce risk exposure. The Legislative Affairs Commission of the Standing Committee of the National People's Congress stated in an interview on February 10, 2020 that if the measures taken by the Chinese government in relation to the prevention and control of the epidemic affect the parties' ability to perform contracts, such measures should be regarded as force

[3] (2018) Zuigaofaminzhong No. 387

majeure events because they are unforeseeable, unavoidable and insurmountable.[4] The China Council for the Promotion of International Trade ("CCPIT), a quasi-governmental organization responsible for the promotion of foreign trade, has reportedly issued more than 3,000 "force majeure" certificates to Chinese companies to certify the occurrence of the epidemic and relevant government policies and their impact on businesses operations. Many other leading chambers of commerce and industry associations, such as the China Chamber of Commerce for Import and Export of Machinery and Electronic Products ("CCCME"), a national trade association for machinery and electronic products import and export, have been issuing similar certificates.

These force majeure certificates are likely to be recognized and accepted by Chinese courts in legal proceedings in China. However, these certificates alone will not satisfy the entire burden of proof on the affected party. The certificates only certify factual matters relating to the occurrence and/or continuance of a force majeure event (e.g., factories are ordered to shut down pursuant to government policies to combat epidemic) and the affected parties still need to present evidence to prove whether and to what extent its ability to perform is impacted by the epidemic and government policies.

For example, during the outbreak of the Severe Acute Respiratory Syndrome ("SARS") in 2003, while the Chinese courts generally determined that the circumstances relating to SARS constitute a force majeure event, decisions on whether a party claiming the force majeure event can be released from its performance obligations were still made on a case-by-case basis, depending on the actual circumstances and impact of SARS on the party's ability to perform.

If the venue for dispute resolution or the governing law of a commercial contract is outside China, the legal force of these force majeure certificates is less clear and will depend on governing law and judicial practice in the jurisdiction or arbitration institution where disputes under the contract are to be resolved.

In any event, the outbreak of COVID-19 in China presents significant challenges to contract performance in China. Businesses affected by the epidemic should carefully review their commercial contracts and the force majeure clauses contained therein when deciding whether and how to invoke these clauses. Moreover, businesses must also pay attention to the notice requirements, the obligations to take necessary actions to mitigate the negative impact, and good faith consultation mechanisms required under a force majeure clause.

For contracts lacking express force majeure clauses, companies seeking release from performance obligations will need to rely on the "changed circumstances" doctrine and prepare sufficient evidence to prove that the epidemic results in changed circumstances in its ability to perform a contract.

[4] http://www.npc.gov.cn/npc/c30834/202002/b9a56ce780f44c3b9f6da28a4373d6c3.shtml

II. Employment and Occupational Health and Safety

To prevent the spread of the novel coronavirus, the State Council extended the Chinese New Year holiday to February 2, 2020 and many provincial and municipal governments (such as Beijing and Shanghai) further extended the non-work periods to February 9, 2020 during which companies remained closed. Furthermore, to comply with government quarantines, lockdowns and travel restrictions, many companies adopted flexible work arrangements for their employees, including work from home, staggered work time, and shift rotation after they resumed operations.

These all present unique challenges to companies with respect to management of employment-related matters. We summarize below some of the key questions raised by businesses and our responses to these questions.

- *Can businesses terminate or lay off employees due to the novel coronavirus?*

In a nutshell, employees who receive confirmed or presumptive COVID-19 diagnoses and receive medical treatment may not be terminated during the medical treatment period. The *Labor Contract Law* provides that an employer may not terminate an employee who is ill or suffers non-work-related injury during his prescribed medical treatment period.

In addition, the Ministry of Human Resources and Social Security ("MOHRSS") in a notice on January 24, 2020 ("MOHRSS (2020) No. 5 Notice")[5] further provided that companies may not terminate employment contracts with any employee who is infected by the COVID-19 virus or suspected to be so infected, any employee in close contact with such a person or any other employee who is not able to work as a result of the government's quarantine measures or other emergency measures, during relevant medical treatment, observation, quarantine or isolation periods. Employment contracts that are about to expire during such periods will need to be extended accordingly.

For other employees, the outbreak or continuance of the coronavirus does not automatically constitute a legal basis for companies to terminate the employment unilaterally. Companies should carefully review causes for termination permissible under law.

Under the *Labor Contract Law*, companies may unilaterally terminate employees (for reasons not attributable to employees) only under the following circumstances: (i) if there is a "significant change in circumstances", *i.e.*, if the circumstances under which an employment contract is concluded have significantly changed which renders the continued performance of the employment contract impossible and the parties fail to reach an agreement to amend the contract; (ii) if a

[5] MOHRSS Notice on Properly Handling Relevant Employment Matters during the Period for Prevention and Control Novel Coronavirus Epidemic.

company encounters serious difficulties in its business operations; or (iii) if a company changes its products or business operations or encounters a significant change in economic situation.

Based on the above, companies may not terminate or lay off employees simply because of the coronavirus; companies instead need to prove that the coronavirus causes serious difficulties in business operations or otherwise constitutes a significant change in circumstances which renders the continued performance of the employment contract impossible.

Note that in order to terminate or lay off employees, the companies need to demonstrate that the impact of the coronavirus on the business is of such severity that the employment contract must be terminated. If the impact does not reach the level of severity to warrant termination, companies may not terminate and instead need to discuss amendment of the employment contracts in good faith with affected employees.

Based on the MOHRSS (2020) No. 5 Notice, companies that suffer serious difficulties in business operations due to the epidemic are encouraged to consult with employees on measures to mitigate difficulties in production and operations for purposes of maintaining work force stability and reducing the scale of layoffs.

- *How are employees to be compensated during the extended holiday?*

The State Council extended the Chinese New Year holiday to February 2, 2020, two days[6] longer than the normal week-long official Chinese New Year holiday. Note that this two-day extension does not constitute an official national public holiday under law. *The Regulations on Public Holidays for National Annual Festivals and Memorial Days* (2014) (the "National Holiday Regulations") specifically provide that the Chinese New Year holiday is three days and the total number of days of official national holidays in China is eleven per year.

As such, the extended Chinese New Year holiday is not an official national public holiday, rather a special holiday announced by the government to combat the spread of coronavirus. The same applies to the non-work periods as announced by many local governments (*e.g.*, the Beijing and Shanghai municipal governments postponed the resumption of work until February 9, 2020).

Under the rules, companies are generally required to pay normal salary to employees who become confirmed or presumptive COVID-19 cases or are otherwise subject to mandatory isolation or quarantine policies and unable to work during relevant medical treatment, isolation or quarantine periods.

For other employees, MOHRSS (2020) No. 5 Notice provides that in case a company suffers difficulties in business operations as a result of the COVID-19 virus, the company may negotiate

[6] We excluded a weekend day which is not an official national holiday.

with the employee to reach an agreement regarding salary adjustment, adjustment of work or rest days, or reduction in work hours, for the purposes of maintaining job security and reducing the scale of layoffs.

Moreover, if a company shuts down its business operations for a period within one salary payment cycle (normally one month) pursuant to government rules to combat COVID-19, employees are still entitled to normal salary. This means that at least for the first month of the shutdown, companies should still expect to pay normal salary to their employees. Companies can discuss with employees to reduce work hours and compensation.

If the shutdown extends beyond one salary payment cycle, compensation for employees may be adjusted in accordance with the contract and relevant rules and regulations. For example, some localities announced that minimum municipal employee salary shall be paid for shutdowns extending beyond the first salary payment cycle.

In calculating daily salary, the standard of 21.75 paydays each month remains unaffected by the holiday extension. Under the *Labor Law* and relevant regulations, the number of paydays each month is calculated pursuant to the following formula: (365 days – 104 days (weekends))/12 months = 21.75 days. Legal national holidays are excluded from the calculation.

Employees asked to work during the extended holiday will be entitled to an overtime pay equal to 200% of their normal pay. Since the extended holidays are not official national holidays under the *Regulations on National Holidays*, employees are in general not entitled to 300% overtime pay. However, 300% overtime pay applies if employees are asked to work during the initial period of the Chinese New Year holiday.

- *How are employees to be compensated during the period of alternative work arrangements?*

To comply with government policies on lockdown, restrictions on transportation, blockade of residential community, self-quarantine at home and other requirements, many companies have adopted alternative work arrangements, including work-from-home, staggered work time, work-on-shift, and others.

While the companies have certain flexibility in making work time adjustments for employees, if such adjustments are expected to reduce employee compensation, companies will be required to consult with employees in good faith.

Generally speaking, unless a company can prove that its business is seriously affected by the epidemic or employees accept reduced compensation, companies remain obligated to pay normal salary to employees who work under alternative work arrangements.

- *What measures should companies take to ensure a safe and healthy workplace after the resumption of work?*

Companies in China are obligated to maintain a safe and healthy workplace for their employees under the *Labor Law, Work Safety Law* and other laws and regulations.

Articles 52 to 55 of the Labor Law provide, among other things, that the employing entity must establish a comprehensive system for occupational safety and health, strictly implement the rules and standards of the State on occupational safety and health, educate employees on occupational safety and health, prevent accidents in the process of work, and reduce occupational hazards. The employing entity must also provide employee with occupational safety and health conditions conforming to the provisions of the State and necessary articles of labor protection.

The Work Safety Law also provides a legal framework for employers and government agencies to maintain a safe workplace with emphasis on production entities. Some key provisions include: employees have the right to stop work if the work conditions are not safe and employers may not reduce pay or terminate employees in such event; employers must provide employees with proper safety equipment suitable to the nature of their work; and employees may not be fired or retaliated against for criticizing or reporting their employer for work safety concerns.

These laws place obligations on employers with respect to provision of a safe and healthy working environment.

In anticipation of the resumption of work by companies and to continue to prevent and control the spread of the coronavirus, government agencies in various localities in China have promulgated guidelines setting out detailed workplace health and sanitation requirements.

For example, some cities have imposed specific limits on the percentage of total number employees who can return to work, mandatory space and distance requirements for employee desks and workstations, and other measures to reduce the density in workplaces.

Companies must comply with these rules and policies. In addition, it is advisable for companies to take additional precautions to ensure the health, safety and welfare of their employees.

Such precautions may include establishing a management-level task force to determine important measures with respect to prevention and control of the epidemic and occupational safety, providing masks, tissues and hand-sanitizer for use by employees, educating or conducting trainings to employees on the status of the epidemic, government requirements and self-protection measures, cleaning common office areas and facilities on a regular basis, and limiting unnecessary domestic or international travel.

Companies should also ensure that employees with potential coronavirus symptoms do not come into work and remain quarantined until the symptoms disappear. Moreover, it is important to note that companies in general have an obligation to report suspected cases to the local government. Under *the Law on Prevention and Treatment of Infectious Diseases* (2013) (the "Infectious Disease Prevention law"), any work unit or individual who discovers a person having infectious diseases or is suspected to have an infectious disease must promptly report the case to the relevant disease prevention and control authority or medical institution.

In any event, as more and more companies resume work, companies should develop a set of comprehensive office and workplace policies to prevent and control the epidemic and to ensure that employees have a safe and healthy workplace.

III. Resumption of Work and Collection, Use and Protection of Employee Personal Information

As a precautionary measure, government agencies in many localities have required that companies provide employee health and travel information as a condition for resumption of work. The information to be provided may include employees' individually identifiable information, travel history, health status and medical records. Sometimes such information requests also extend to family members of employees.

While companies under the *Labor Contract Law* may collect employee information relating to the performance of employment contracts, information such as health status, medical records and travel information of employees and their family members will likely exceed the scope of information what the companies can collect under normal circumstances. As such, companies should use caution when collecting and using such information.

One law on which companies can cite in collecting such information is the *Infectious Disease Prevention Law* which mandates as a general matter that all entities and persons are obliged to cooperate with the State to prevent and control an infectious disease by timely and accurately reporting relevant information. However, the *Infectious Disease Prevention Law* also prohibits data controllers from leaking sensitive personal information to other parties.

In 2017, China promulgated the *Cybersecurity Law* and relevant data privacy regulations which substantially tightened control with respect to the protection of personal information. "Personal Information" is defined under the *Cybersecurity Law* as "personal information recorded in electronic or other form, which can be used, independently or in combination with other information, to identify a natural person's identity including, without limitation, name, date of birth, ID number, biometric information, address and telephone number."

The mandatory national standard *State Information Security Technology: Personal Information Security Specifications (2018) (GB/T 35273-2017)* further defines "sensitive personal information",

a subset of personal information, as "personal information whose breach, theft, falsification or illegal use may endanger the safety or property of a person or damage the reputation or physical or mental health of a person". "Sensitive personal information" includes, without limitation, personal ID card number, bio-identification information, telecommunication records, property and asset information, creditworthiness information, travel and accommodation information, health and medical information and trading information of a person and information of anyone under 14 years.

As such, employees' travel and health information is clearly "sensitive personal information" which is subject to more stringent protection requirements under law.

Companies when collecting travel and health information from employees need to seek express consent from employees and such consent needs to be made on a voluntary and informed basis. Companies should also tell employees the uses of such information, *i.e.*, for purposes of prevention and control of the coronavirus, including submission of relevant data to government if requested.

During the information collection process, companies need to ensure that the information to be collected is limited to only such information relevant to the prevention and control of COVID-19 and unrelated employee personal information may not be collected.

As privacy data controllers, companies are required to formulate data privacy rules and confidentiality protocols to ensure that the data collected will not be leaked through unauthorized disclosures. Note that under both the *Cybersecurity Law* and the *Infectious Disease Prevention Law*, companies are prohibited from disclosing sensitive personal information of confirmed or presumptive cases to any third party absent express consent of the underlying patients.

Companies should also limit the number of internal personnel who gain access to employees' sensitive personal data and personnel handing such data shall be authorized to use the data only to the extent necessary for the intended purpose. Unauthorized photocopying, downloading or modification of the privacy data should be prohibited.

Companies are also required to adopt technical security measures to ensure that sensitive personal information is stored in a secure manner. In this connection, given the sensitivity of employees' travel and health information, it is recommended that foreign companies doing business in China store, maintain and process such data locally in China. In case of need to transmit relevant data to a company's overseas head office, the company should do a self-assessment on the potential impact of such cross-border transmission, seek employee consent, sign written agreements and take other compliance actions as required under the *Cybersecurity Law*.

Some local governments, in addition to requesting employee health and travel information, have also asked companies which intend to resume work to make certain written safety undertakings. While many such written undertakings focuses on compliance with government

regulations, some undertakings seem to include statements which impose unnecessary and excessive obligations on companies. For example, some local governments have asked companies to undertake that all employee information submitted by the companies are true or be subject to liability, or pledge that employees have not or will not be infected by COVID-19. Companies should push back on these requests to the extent possible to avoid excessive liability on matters that are beyond companies' own control.

IV. Matters Relating to Donations

Since the outbreak of the epidemic, many companies, including foreign companies doing business in China, have made donations to the Chinese government, charitable organizations, non-governmental organizations or local hospitals and communities to help combat the epidemic and save lives. The government has also promulgated rules to encourage voluntary donations, including policies on pre-tax deductibility. For example, based on a report released by the American Chamber of Commerce in China ("AmCham China")[7], as of February 26, 2020, AmCham China's member companies, to respond to unprecedented challenges presented the global outbreak of the novel coronavirus, have made donations to support Wuhan, Hubei, and other areas in need, totaling more than RMB 517 million ($74 million) .

However, foreign companies doing businesses in China should be aware of requirements relevant to soliciting, raising and making donations in China to be in compliance.

A foreign entity may not seek donations from individuals and entities in China unless special approvals are obtained under the *Charity Law* and relevant regulations. As such, if donations are expected to be solicited in China, foreign companies should let their China entities take the lead in this connection.

When soliciting donations in China, multinationals' China entities should limit such efforts to their employees and local partners in China and should avoid taking any actions that may be viewed as a public solicitation. Public solicitation of donations requires a special government approved permit. A company may solicit donations from its employees and corporate partners but may not solicit donations from the general public. Accordingly, any announcement to employees soliciting donations must be limited to employees and may not be extended to employees' family members or friends.

Donations must be made voluntarily. A company may encourage its employees to make donations on a voluntary basis, but may not impose donating obligations on employees, such as deducting the donation from employee payrolls without the employee's express consent.

[7] https://www.amchamchina.org/news/amcham-china-members-contributing-to-coronavirus-outbreak

Furthermore, companies need to ensure that the organizations receiving donations from the company have the necessary qualification to receive donations under the *Charity Law* or have partnered with organizations that have such qualification. Regardless of whether the donations are made through government or non-government channels, the organizations to which a company makes donations must have the necessary qualifications under law. For donations to be made to overseas non-governmental organizations ("NGOs") in China, companies are also advised to do background review to ensure that the overseas NGOs are legally established and validly exist in accordance with the Chinese *Overseas Non-Government Organization Law* (the "Overseas NGO Law") and have the necessary permit to receive donations.

Foreign companies when making donations may also want to consider and weigh the pros and cons of making donations through government channels vs. non-government channels. While NGOs are often found to be more professional and efficient compared to official government channels (such as local governments, the Red Cross Society of China, and the China Charity Federation), donations through NGOs may or may not be fully recognized by government.

This does not mean that making donations to licensed NGOs is illegal, but rather that such donations may or may not be fully recognized or appreciated by government because the donations are not made through government channels. So far, we have seen foreign companies making donations through both channels. Companies with larger China operations, closer government relations or seeking official recognition may consider making donations (or a part of the donations) through government or government designated organizations.

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