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COVID-19 Client Alert Series: COVID-19 Guidance on Civil Cases in China from the Supreme People's Court

By the Paul Hastings Greater China Practice

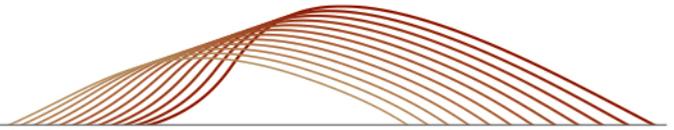
On April 20, 2020, the Supreme People's Court of the People's Republic of China ("PRC") published guidelines concerning COVID-19 (最高人民法院关于依法妥善审理涉新冠肺炎疫情民事案件若干问题的指导意见) and provided answers to certain frequently asked questions (the "Circular"). As the adverse impact of the various governmental and private actions intended to slow down the spread of COVID-19 continues across various industries, there is an increased focus on whether the impact of such actions can excuse any of their contractual obligations. The Circular provides guidance on the application of force majeure doctrine under PRC law as well as resolution of contractual disputes and labor disputes related to the COVID-19 pandemic.

Force Majeure

Generally, the force majeure doctrine excuses a party to a contract from performance of contractual obligations as a result of events which occur beyond such party's reasonable control. Unlike in many common law jurisdictions where the general rule of strict enforcement of contracts may lead to very limited relief in the absence of a specific force majeure clause under a contract, the force majeure doctrine is adopted under the PRC law as a statutory relief, which protects the grieved party in the absence of a specific force majeure clause in a contract. That said, the Circular emphasizes that, in light of the COVID-19 pandemic, the courts should remain cautious with the force majeure doctrine and that, notwithstanding the impacts of COVID-19, the parties to a transaction should comply with their respective contractual obligations to the fullest extent possible. The Circular requires the party that seeks to invoke the force majeure doctrine to bear the burden of proof for its inability to perform the relevant contractual obligations directly due to the COVID-19 pandemic, and to take all reasonable steps to mitigate losses or risks before receiving the benefit of the force majeure doctrine. This is consistent with the existing force majeure jurisprudence in China before the COVID-19 pandemic.

Contractual Disputes

The Circular provides that, where the impacts of COVID-19 renders the continuous performance of contractual obligations to be apparently unfair to one party, a court may determine whether, and to what extent, such affected party is entitled to modify the contractual terms, including adjustments to the transaction price, form of performance and performance schedule on a case-by-case basis. This is consistent with the existing "change of circumstances" principle (formerly known as the principle of fairness) jurisprudence in China before the COVID-19 pandemic. However, the Circular goes on to say that only in the circumstance where the fundamental purpose of a contract can no longer be achieved in the context of COVID-19, may a court consider the



termination of a contract. The requirement of a “fundamental purpose of a contract” makes this a high bar to reach.

The Circular also specifies certain factors to be taken into account by a court when determining whether a party is entitled to modify the contractual terms, including the disparate influence of the pandemic on different regions, industries, and types of cases as well as the mitigation effects of subsidies, tax incentives and debt forgiveness.

Labor Dispute

The Circular stipulates that unless there is a separate cause for termination, employers are not allowed to terminate labor contracts with certain types of employees, including suspected or confirmed COVID-19 patients or even employees who have only mild symptoms or are infected but asymptomatic. The protection extends to employees who are quarantined or simply come from areas with higher epidemiological risk such as Wuhan.

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The Circular signals the Supreme People’s Court’s efforts to eliminate the adverse impact of the COVID-19 pandemic on the economy and social stability. Nevertheless, we expect to see attempts to re-negotiate contractual terms under those commercial transactions that were entered into prior to January 2020 but have not yet been consummated. Since the Circular is newly issued and only provides high-level guidelines, its impacts on commercial transactions have not been tested, and its impacts will be highly dependent upon specific facts and circumstances of each transaction on a case-by-case basis.

It should be noted that party autonomy, to the extent not contradictory to the law, prevails over statutes. Therefore, contractual provisions should be drafted with these potential effects in mind, and going forward, we expect to see more heavily negotiated force majeure clauses.

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