

Implications of the Novel Coronavirus for Businesses in China

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What legal risks arise from the outbreak and how can you prevent or mitigate them?

The [World Health Organisation](#) declared the outbreak of the novel coronavirus (virus causing covid-19) a public health emergency on January 30. With the global response to the outbreak thus far, there are numerous potential and actual legal risks that arise from it, ranging from supply chain risks to employment law questions. Whether you are a business in China or are dealing with Chinese businesses from abroad, this outbreak may pose a significant threat to the integrity of your business. Understanding the legal risks will be a vital step to preparing your business in the coming months.

Situation in China

So far the vast majority of confirmed cases have been in China. Covid-19 has already claimed more lives than [SARS](#). The Chinese government implemented a number of measures in order to prevent the further spread of the coronavirus throughout its provinces and cities. These measures as well as the situation businesses are faced with vary greatly depending on the area.

The global community has also started to implement preventive measures. Most of [these measures](#) have been related to international travel to and from China with flights being cancelled and entry restrictions being applied to travellers coming from infection-stricken areas. With the progression of this outbreak, these measures are prone to change and governments may well ramp up their efforts to further contain this outbreak.

Employer Obligations

Employer Duty of Care

Employers have a general duty of care towards their employees. This includes preventing and mitigating any health risks employees may face in the course of their work as well as providing them with a safe working environment. If an employer fails this duty of care, he may face liability for any damages incurred by the employee.

Employee safety and health should be a business' first priority. In order to ensure the safety of their employees in connection with the outbreak, employers may consider taking a number of measures commensurate to the individual infection risk level. Currently appropriate measures may include:

- Issuing company-wide policies designed to prevent the spread of infection, including spreading awareness on best hygiene practices among employees
- Limiting business travel, especially to highly affected areas
- Ensuring sick employees stay at home, possibly including employees with sick family members
- Providing sanitary products, such as hand sanitiser, facemasks, and work-station cleaning products
- Allowing employees to work remotely, if their positions allow for that
- Increasing health monitoring of employees to ensure early discovery and reaction to possible outbreaks

Depending on the region a business operates in, they may find more extreme measures appropriate:

- Asking employees to work from home
- Forced leave of absences
- Suspension of business operations, especially in compliance with governmental prevention measures

It is important to remember that prevention measures employers take may infringe on the rights of their employees - especially their right to work and privacy. In this case there must be careful consideration of the employees' rights, the infection risk level and any possibilities in order to reduce the burden on employee rights.

Isolation & Medical Observation

Employees who are under medical observation or isolation orders and are therefore unable to perform their work are considered to be on sick leave and shall be afforded full pay for this period, as well as being protected from termination pursuant to the Labor Contract Law. Employees, who are able to work from home during this period are obligated to do so and shall also receive full pay.

Home Office, Forced Leave and Other Measures

Officially, local authorities had extended the Lunar New Year holidays with most provinces expecting employees to return to work by February 20 at the latest. In the meantime more than [90 percent of state-owned enterprises resumed operations](#). However, travel restrictions are still hindering many workers from returning to the factories after the holiday, limiting the capacity at which business operations can be maintained. Additionally, only around a third of small and medium-sized enterprises have been able to resume work.

In the past few weeks, the outbreak in China has been slowing down. Nevertheless, depending on the nature of their employees' work, businesses may still want to ask them to work from home. Most of the services sector will find itself easily able to implement this measure, though it will prove more difficult for businesses operating in production or other areas requiring on-site work.

Depending on how this outbreak continues to unfold, businesses not able to ask employees to work remotely may find themselves confronted with suspending operations. For example, if a factory with migrant workers living in close quarters in factory dorms is confronted with a case of covid-19, its best course of action may be shutting down business operations for at least 14 days. Additionally, the high risk of transmission throughout factory dorms will pose a serious threat to the health of the factory's employee base.

Chinese Business

Impact on Business

With around half of China's population currently subject to various restrictions, a major question for businesses is the integrity and stability of their business flow. There is a high probability that China will continue to expand the area governed by restrictions until the coronavirus has been contained sufficiently. Additionally, over the coming months businesses will be faced with navigating numerous governmental measures implemented with the intention of containing the virus responsible for covid-19.

Foreign travel advisories and foreign entry restrictions for people who have a Chinese travel history have a far-reaching adverse impact for businesses all throughout the mainland. In individual cases, it disrupts the flow of international business by preventing or complicating the fulfilment of certain contracts. In the broader scope, however, it also hinders future Chinese participation in international business.

The uncertainty surrounding the current outbreak and its further development, particularly also regarding future measures Chinese authorities may implement, will undoubtedly be a factor in foreign business decisions. Large corporations give much thought to diversification of their supply chain as a risk mitigation measure. However, even [multinationals are currently finding themselves too highly reliant on Chinese partners](#) and will likely start considering alternatives.

Additionally, Chinese businesses will not be able to participate in international conventions in the foreseeable future. Until the outbreak is contained and life returns to normal, these travel restrictions will make it extremely difficult for Chinese companies to present themselves at conventions. Furthermore, a large number of [trade shows in Asia](#) have already been postponed or cancelled. Restrictions will also impact Chinese participation in international conferences, affecting how well Chinese businesses (and academics) are able to keep up with the current state of technology and science.

Risk to Business

Businesses should prepare for various eventualities in the coming months. The first step requires taking a close look at their businesses and identifying risks that could cause further disruptions. All businesses will need to prepare, and businesses operating in fields with strict deadlines, such as construction companies, will find themselves most at-risk. Examples of current and future risks may include:

- Governmental travel restrictions, even within China
- Governmental lockdown measures affecting businesses and their business partners
- Foreign import / export restrictions affecting purchase agreements
- Purchasers backing out of agreements
- Certain employees not being able to return to work for extended periods

Depending on the case in question, businesses may find that simple preparation goes a long way, such as identifying alternative suppliers outside of the immediate area of risk or opening lines of communication regarding the outbreak with clients. It is also vital for businesses to not drop the ball - navigating the current situation is a continuous and evolving process with a multitude of different factors that may adversely affect their business continuity.

Communication with Business Partners

In extraordinary situations such as these, the most promising way to navigate any problems may be via open communication with all stakeholders. Approaching problems together with partners early and head-on may allow businesses to identify practical solutions that would otherwise not be available or obvious. The dialogue with business partners should also include what prevention measures have been taken or should still be taken in order to ensure the safety of all employees who are still working in at-risk areas during this time.

Legal Remedies

In case the efforts described above fail, the fundamental question for businesses will be, whether they, their suppliers or their clients are still required to fulfil their contractual obligations under these new circumstances, or if they may be liable for damages due to breach of contract.

Businesses will need to analyse their at-risk contractual relationships and determine whether they or their contractual partners have access to any legal remedies.

1. Force Majeure Clause

The most obvious legal remedy in this case may be *force majeure*. *Force majeure* clauses allow the suspension or even discharge of mutual contractual obligations based on the occurrence of a so-called *force majeure* event, a disruptive event over which the affected party has no control and was not reasonably able to prepare for. Whether or not a party is able to successfully invoke *force majeure* will depend highly on the individual clause's wording, as well as the governing law's understanding of *force majeure*.

Vital questions will be whether this outbreak constitutes a *force majeure* event and if the type of disruption is covered, if the invoking party could have reasonably prepared for the event, and what rights the parties receive from the clause.

To exemplify difficulties businesses will face when establishing *force majeure*, consider a European supplier tasked with installing equipment at a production site in China. However, due to governmental travel warnings regarding China, the supplier decides they cannot justify the risk to their employees and therefore refuses to perform the installation. Is the foreign government's travel warning sufficient for invoking *force majeure*, despite the specific region not being highly affected by the coronavirus?

Chinese authorities have started issuing *force majeure* certificates. These certificates may be required by individual clauses, however, the issuance of such a certificate is usually not binding in the courts. There have also already been reports of cases where large corporations [rejected their business partners' invocation of force majeure](#). When courts have to decide whether or not this outbreak constitutes a *force majeure* event, such certificates will nevertheless play an important role to establish the extraordinary nature of the outbreak. However, they will only be one of a multitude of factors. Whether or not *force majeure* can be invoked does not only depend on the event itself, but maybe more importantly on the event's actual impact on the invoking party. That is to say, the outbreak cannot be generally regarded as *force majeure* in all cases. Instead, the impact of the local epidemic on the performance of each contract in different projects must be considered comprehensively, combined with relevant supporting materials, such as the suspension notice issued by the local government and the certificate of failure of relevant personnel to resume work in time, in order to determine whether the outbreak of the coronavirus is enough to cause the failure of performance of the contract or the failure to achieve the basic purpose of the contract.

According to the existing relevant provisions and the guidance issued by the judicial organ, if a business is able to perform a contract during the outbreak, it is encouraged to continue to perform the contract and the party's claim to terminate the contract will generally not be supported. In case of failure to perform the contract due to the outbreak of the novel coronavirus, the affected business may invoke the legal provisions of *force majeure* and terminate the contract, exempt part of the contractual liability or postpone the performance of the contract. Businesses will need to keep the following points in mind when invoking *force majeure*:

- Businesses are obligated to notify the other party as soon as possible, as they may need to take remedial measures in order to mitigate the impact as far as possible.
- Relevant *force majeure* certificates should be provided in time, and the facts of the impact of the epidemic must be documented and notarized to the extent possible in order to prove that the epidemic constitutes a *force majeure* event in the local area.
- Payment obligations are not subject to *force majeure* exemptions.

2. Alternative Legal Remedies

If a contract does not include a *force majeure* clause covering the individual case, the governing law will be decisive in regards to legal remedies, either providing its own form of *force majeure*, as both China's Contract Law and General Principles of The Civil Law do, or possible alternatives. Parties may find that they are able to invoke legal institutions such as unforeseen changes (*clausula rebus sic stantibus*) or the similar doctrine of *frustration* in English law. These general legal instruments may afford parties the same or similar rights to *force majeure* clauses.

According to Chinese law, a party to a contract may request the modification or termination of a contract based on the principle of fairness if the objective circumstances surrounding a contract have changed significantly. These changes must have not been foreseeable at the time the parties concluded the contract. Additionally, the changes cannot have been caused by *force majeure* and do not constitute commercial risks. The continuing performance of the contract must either be obviously unfair to the party requesting modification or termination of the contract or would not realize the contract's original purpose. In such a case, the people's court would decide on the request based on the principle of fairness and the actual situation prevalent in the case.

Although the combination of the severity of the outbreak in the region, the magnitude of governmental control measures and the actual impact of the outbreak on the performance of the contract will not meet the condition that the original purpose of the contract cannot be fulfilled anymore, it may still result in the continuing performance of the contract being obviously unfair for a party. In this case, businesses may consider applying the principle of changed circumstances according to Chinese law and amending the contract while distributing the resulting loss according to the principle of fairness.

Additionally, businesses not affected by the outbreak may need to keep an eye out for parties who intend to abuse *force majeure* clauses in order to maliciously shirk their contractual obligations or debts. The key is to examine whether or not the opposing party has legally and reasonably invoked the *force majeure* clause. Vital points will be whether the outbreak's impact has reached the threshold at which the contract cannot be performed anymore, the other party has fulfilled their notification obligations and provided sufficient evidence of the event in time and whether the other party may have already delayed the performance of the contract before the *force majeure* event occurred.

3. Damages Due to Breach of Contract

In case a party in breach of contract does not have access to any legal remedy, this may become a question of damages and liability. Businesses should remember that depending on the situation, they may have duties to mitigate damages as far as is reasonably possible, for example by making an effort to find suitable alternative purchasers for perishable goods.

Businesses may have insurance that covers business liabilities. In case a business finds itself liable for damages, it will have to determine whether this specific case is covered by its specific insurance policy.

Broader Consequences

Even if businesses are able to invoke *force majeure* and successfully avoid liability vis-à-vis their business partners, they will still find themselves faced with losses due to the disruption period with wages, rent and other expenses accruing, and opportunity costs in the form of future contracts being lost. In order to lessen the burden on businesses due to the epidemic, the Chinese government, as well as [international banks](#), have been issuing [fast-approval, low cost loans](#), and [promising tax cuts](#) and [other aid](#). Although these measures will not be able to curb the damage this outbreak has dealt, they will certainly lessen the burden on businesses.

In order to cope with the economic blow this epidemic deals to them, strongly affected businesses may have to consider reducing their workforce. In this case, they will be faced with employment law questions regarding termination negotiations and labor unions, economic dismissal and suspension of payrolls.

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