



How companies manage the legal compliance risk during lockdown

Shaohe Law Firm | April 28, 2022 | Shanghai

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Human Resource Issues

Major protective requirements from the governments

Full payment of salaries to employees under quarantine measures

- If the employee is proved to be a Covid-19 patient, a suspected patient, or a person in close contact with a patient, or is subject to governmental isolation measures or other emergency measures, the company must pay him/her normal salary during the medical treatment period, medical observation period, or relevant periods of isolation measures or other emergency measures.
- The scope of salary

Major protective requirements from the governments

Negotiation for reduction of salary or working hours

- Collective consultation **OR** agreement with each employee
- Exception: production and operation are suspended
 - Within the first payment circle -- full payment
 - From the second payment circle -- according to local rules

Examples: Shanghai, Beijing and Suzhou

Major protective requirements from the governments

Restriction on termination due to epidemic

➤ Termination under 40 and 41 of ECL is limited

If the employee is proved to be a Covid-19 patient, a suspected patient, or a person in close contact with a patient, or is subject to governmental isolation measures or other emergency measures which makes him/her unable to provide working, a company cannot terminate him/her in accordance with Articles 40 and 41 of the ECL.

➤ Contract extension

Where the employee's employment contract expires during above periods, his/her contract shall be extended until the expiration of the employee's medical period, the expiration of the medical observation period, the expiration of the isolation period or the end of the emergency measures taken by the government.

Labor related Q&A

Q

How to pay salaries for employees during the lockdown?

A

- **Fixed salary:** full payment
- **Non-fixed salary :** detailed requirements of Beijing
 - Component parts of non-fixed salary: allowance, performance bonus or commission, etc.
 - Employees working at home: full payment
 - Employees not providing work: non payment

Labor related Q&A

Q If an employee contracts COVID-19 while at work, is that a work-related injury?

A According to the opinion from the Ministry of Human Resources and Social Security, except for the infection cases with regard to medical personnel and relevant personnel who engage in Covid-19 prevention and treatment activities, other infection cases e.g. a lawyer got infected by his/her colleague in the office, could not be identified as work-related injury.

But it remains open to doubt whether the identification of work-related injury with respect to Covid-19 infection cases will be conducted in such a “one size fits all” manner. According to rules under Regulations on Work-Related Injury Insurance, if an employee, due to illness, died suddenly during working hours and while on the job, or died within 48 hours despite emergency rescue efforts, the situation should be deemed as work-related injury (death). As the regulation makes no difference between various diseases, we find at least under such circumstance – i.e. the employee infected with Covid-19 died within 48 hours despite rescue efforts – the rules and regulations regarding the work-related injury should apply.

Labor related Q&A

Q

Could a company arrange employees to take leaves during lockdown period?

A

- Ministry of Human Resources and Social Security: to negotiate with employees.
- Beijing: Yes.
- Personal opinion: Yes.

Labor related Q&A

Q

Could a company change the payment of employees' salaries during lockdown?

A

Whether the company stops the production/operation

➤ Yes

- Within the first payment circle —— full payment
- From the second payment circle —— according to local rules

Examples: Shanghai, Beijing and Suzhou

➤ No: negotiation with employees

Labor related Q&A

Q If we suffer operating difficulties due to the epidemic, can we lay off our employees?

A During the lockdown period, No.

Afterwards, companies are allowed to lay off employees under fulfillment of conditions and procedures listed under the ECL. For example, if a company intends to lay off 20 employees or more, or lay off more than 10% of all the employees, it needs to notify the trade union or all the employees with the decision 30 days in advance and collect their opinion/feedback, and file the layoff plan to the competent labor administrative authority in accordance with Article 41 of the ECL.

Labor related Q&A

Q

Could a company postpone probationary period during lockdown period?

A

If the employee is unable to provide normal work during the probationary period due to the epidemic, such period may be extended by the agreement between the employee and the company, but the extension shall not exceed the period during which the employee is unable to provide normal work.

Labor related Q&A

Open questions for discussion:

➤ Employee information protection:

Whether employee's consent is necessary to collect the contact information (e.g., address, phone number) of the employee or his/her relatives for anti-epidemic supplies ?

➤ Termination for cause:

Whether a company could terminate an employee who is under administrative detention for spreading epidemic information ?

Measures to be taken by companies

- ❑ Arrangement of leaves
 - Statutory annual leave
 - Company leave
 - Alternative leave for OT
- ❑ Reduction of allowances
- ❑ Special working hours system
- ❑ Termination

Force Majeure and Covid-19

Understanding of Force Majeure

- “***Force majeure***” translates to “superior forces”.
- An exception to the principle under the law of contract “*agreements must be observed*”.
- *Force majeure* is based on the idea that **possibility is the limit of obligation**, and no one is expected to perform the impossible.
- It provides an **excuse** to a party for **nonperformance** or **deficient performance** when a **particular type of event occurs**.
- There is no internationally uniform definition of the term force majeure.



Force Majeure in the contract

Where is the applicable definition of Force Majeure?

➤ Force Majeure Clause under the binding contracts

Should either of the Parties be prevented from performing its obligations under the Agreement as a result of an event of force majeure, such as earthquake, flood, fire, war, government prohibitions or other unforeseen events, and their occurrence and consequences are unforeseeable and unavoidable ("Force Majeure"), that Party's obligations under the Agreement affected by such event shall be suspended for the period of delay caused by such event. The prevented Party shall notify the other Party by email, telefax or, if need be, other reliable means without any delay, and within fifteen (15) days thereafter provide detailed information of the events and a valid document of evidence issued by the relevant public notary organization explaining the reason of its inability to perform all or part of the Agreement. The Parties shall, through consultations, decide whether to terminate the Agreement or to exempt part of the obligations for a certain period or indefinitely until the event of Force Majeure has ended.

➤ Governing law

- Common law system (e.g. USA, England, Australia, Singapore): relying on the binding contract;
- Civil law system (e.g. Switzerland, German, France, China): beside the contract, statutory law provides for stipulations on force majeure.

Force Majeure under Chinese Law

Article 180 PRC Civil Code

Force majeure refers to any objective event, that is **unforeseeable**, **unavoidable** and **insurmountable**.

Unforeseeable

- ***At the time of the conclusion of the contract, the event could not be reasonably anticipated or expected.***

Unavoidable

- Overwhelming **external** events, which are **out of human control**.

Insurmountable

- Obligor **cannot overcome** the impact of the triggering event.
- Obligor must make its **best efforts** to overcome the impact of the event.

Does COVID-19 pandemic constitute Force Majeure?

- **Q&A of Shanghai High People's Court regarding the Contract Dispute amid the Pandemic dated 10 April 2022:**
COVID-19 pandemic and controlling measures to prevent pandemic are generally recognized as Force Majeure under PRC Contract Law. The people's court should consider the relevant factors and decide the causality between the pandemic or controlling measures and the failure of performance.
- **Whether COVID-19 constitutes Force Majeure in a specific contract relationship depends on several factors:**
 - the obligations of the parties;
 - The type of contract and industries ;
 - Signing date of the contract;
 - The impact of controlling measures on different areas;
 - The duration;
 - ...

Conclusion:

- **There must be a causal link between the force majeure event and the obligor's failure to perform.**
- **Force majeure is highly fact sensitive and can only be applied on a case-by-case basis.**

Consequences of Force Majeure (1/2)

Article 180 Civil Code of PRC

Liabilities shall be exempted in part or in whole in light of the effects of the Force Majeure event, except as otherwise provided by law.

➤ **Postponement of delivery**

If the production ceases / employees stay at home due to the controlling measures / the premise is expropriated for accommodating patients, etc., which makes the supplier unable to deliver as agreed.

➤ **Postponement of payment**

The tenant closes the store due to the controlling measures and has no revenue during the lockdown. Given the cash flow situation, it is unable for the tenant to pay the rental.

Consequences of Force Majeure (2/2)

➤ Termination of contract?

Decisive: Contractual purpose can still be achieved.

Case study (Case No.: (2020)沪0105民初10184号)

In 2011, Yufeng and Anhui entered into a lease agreement under which it was agreed that Yufeng leased the premise for operating a restaurant; The contract term was from December 2011 till December 2021. In January 2020, the restaurant was required to be closed because of the outbreak of COVID-19.

Despite that the government encouraged the companies to recover the business since February 2020, Yufeng argued that the employees can not go back to work due to the travel restrictions, there were no clients and business, Yufeng suffered great losses. Thereafter Yufeng delivered a termination notice to Anhui.

Decision

The court submits that as a restaurant operator, Yufeng's operation can be affected by the pandemic, but it does not necessarily result in failure to achieve the purpose of the contract. When Yufeng delivered the termination notice to Anhui, it was still possessing and using the premise. Therefore, the request of termination can not be supported.

Our suggestions

- ❑ Notify your contract partners of the circumstances. The government notice can be attached to the letters as supporting evidence;

Question: what if the recipient does not accept the notice regarding Force Majeure?

- ❑ Collect evidence on the occurrence of the Force Majeure event, provide certificates of the Force Majeure event. Notary public or China Council for the Promotional of International Trade (CCPIT) issues Force Majeure certificates.

Question: issue of fact vs. issue of law?

- ❑ Take necessary measures to mitigate the losses.
- ❑ Evaluate possible consequences of the Force Majeure event and figure out what is intended, e.g. change of delivery dates, termination of contract, etc.
- ❑ Discuss and negotiate with your contract partner on how to proceed.

Rental waiver and reduction

Supporting policy for rental waiver and reduction

- Given the lasting impact of pandemic since 2020, both national and local government has released supporting policy for rental waiver and reduction. The state-owned enterprises as landlord are required to waive the rental under certain conditions.
- Pre-requisitions:
 - a) The applicant should be small and micro-sized enterprises (“**SME**”) or self-employed businesses; and
 - b) The applicant should be the tenant who actually uses the premise (sub-lessor excluded).

Supporting policy for rental waiver and reduction

- Classification for SME in different industry sectors (*Statistics on the classification of small, medium and large micro enterprises released by National Bureau of Statistics in 2017*)

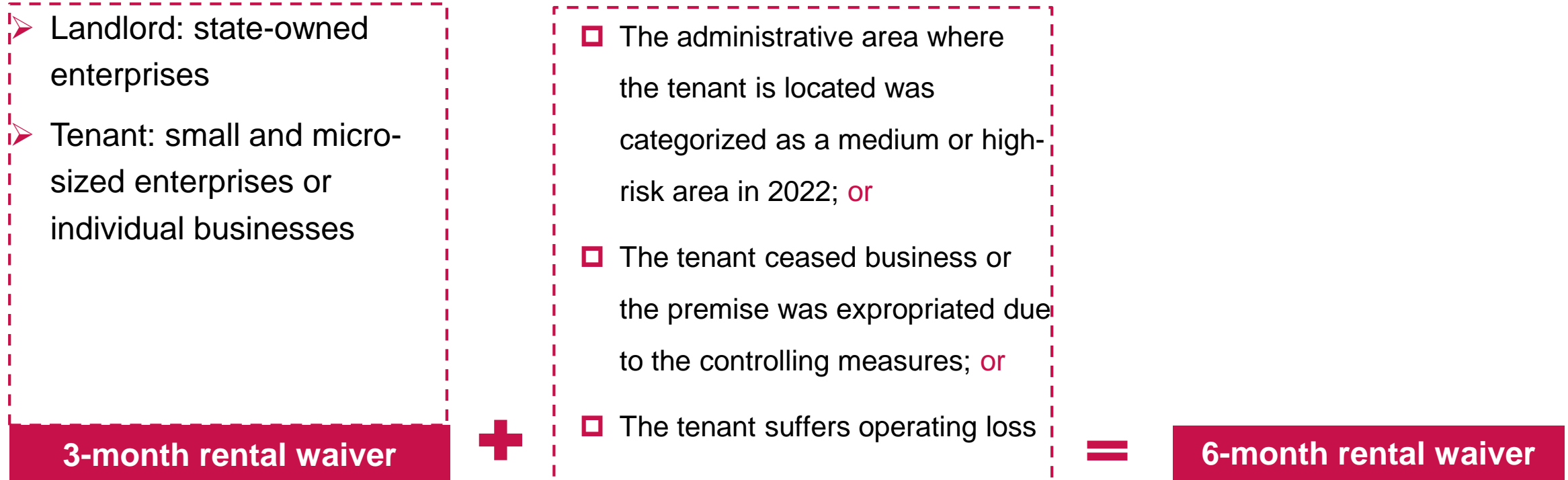
Industry sector	Small Enterprise	Micro Enterprise
Industrial	$20 \leq X < 300$	$X < 20$
	$3 \leq Y < 20$	$Y < 3$
Wholesale	$5 \leq X < 20$	$X < 5$
	$10 \leq Y < 50$	$X < 10$
Software and information technology	$10 \leq X < 100$	$X < 10$
	$0.5 \leq Y < 10$	$Y < 0.5$
...		

X - Employee

Y - Operating revenue, in millions CNY

- There is no difference between small and micro-sized enterprise in terms of the supporting policy.

Supporting policy in Shanghai



Non-state enterprises as landlord

- If the landlord is not a state-owned enterprise, the legislation also **encourages** the landlord to offer reduction of rental for the tenants. The government may reduce or waive the property tax and land use tax for these landlords if there exists difficulty for the tax payment.
- Q&A of Shanghai High People's Court regarding the Contract Dispute amid the Pandemic dated 10 April 2022: **if the tenant has no revenue or the revenue significantly shrinks**, it would be obviously unfair for the tenant to continue the payment of rental as agreed, the people's court may alter the contractual terms and support the claims of tenant to reduce the rental for a certain period.

Suggestions:

1. Check the lease agreement.
2. Send a request letter, discuss and negotiate with the landlord.
3. Cooperate with other tenants.

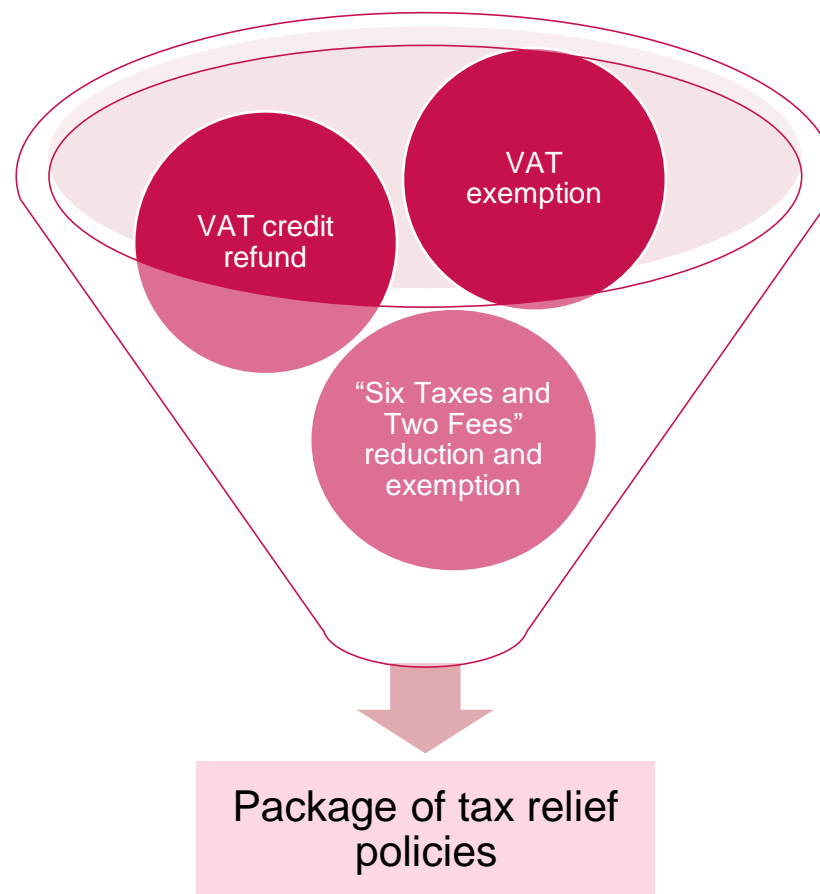
Tax Reliefs & Tax Compliance Measures

Tax Reliefs

Report on the Work of the Government 2022

- ❑ *Implementation of a new package of tax-and-fee policies to support enterprises.*
- ❑ *Continue to take temporary steps and institutional measures and apply policies for both tax reductions and refunds.*

**By Premier Li Keqiang
March 2022**



Covid-19 Related Tax Policies VS Tax Reliefs

Covid-19 Related Tax Policies (Abolished)

- Full deduction of new equipment purchase cost without depreciation for enterprises producing key suppliers.

(MOF & SAT Announcement [2020] No.8 , valid until March 31, 2021)

- Monthly refund of the incremental VAT credits for enterprises producing key suppliers.

(MOF & SAT Announcement [2020] No.8 , valid until March 31, 2021)

- Revenues obtained by taxpayers from transporting key supplies; and from providing public transportation services, lifestyle services and courier services delivering life necessities can exempt from VAT.

(MOF and SAT Announcement [2020] No.8 of, valid until March 31, 2021)

- In Hubei, from March 1 2020 to May 31 2021, VAT of small-scale taxpayers can be exempted from VAT; from April 1 2021, the VAT rate of small-scale taxpayers was reduced from 3% to 1%.
- From March 1, 2020, the VAT rate of small-scale taxpayers in China (except for Hubei province) was reduced from 3% to 1% .

(MOF&SAT Announcement [2020] No.13, valid until March 31, 2022)

- Loss carryover extension for enterprises in difficult industries (including transportation, catering, accommodation and tourism): 5 years to 8 years

(MOF & SAT Announcement [2020] No.8 , valid until March 31, 2021)

2022 Tax Reliefs

- Possible full deduction for micro, small and medium-sized enterprises for the equipment purchased from 1 January 2022 to 31 December 2022 for corporate income tax purpose.

(Cai Shui [2018] No. 54 ; MOF&SAT Announcement [2022] No. 12)

- Eligible for refund of incremental VAT credits if being small and micro enterprises or manufacturing and other five key industries.

(SAT Announcement [2022]No. 4; MOF&SAT Announcement [2022]No. 14)

- Can exempt from VAT from April 1 until 31 December 2022 if being small-scale taxpayer.

(MOF&SAT Announcement [2022]No. 15; SAT Circular [2022]No. 6)

- This provision is no longer in force, while the provision for a maximum loss recovery period of 8 years remains in force for losses incurred in 2020 in difficult industries.

**V
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Tax Reliefs

**Highlights of
this year's tax
reliefs**

01

Continuous Reduction on CIT payment

02

Temporary Exemption on VAT payment

03

Expanded VAT Credits Refund



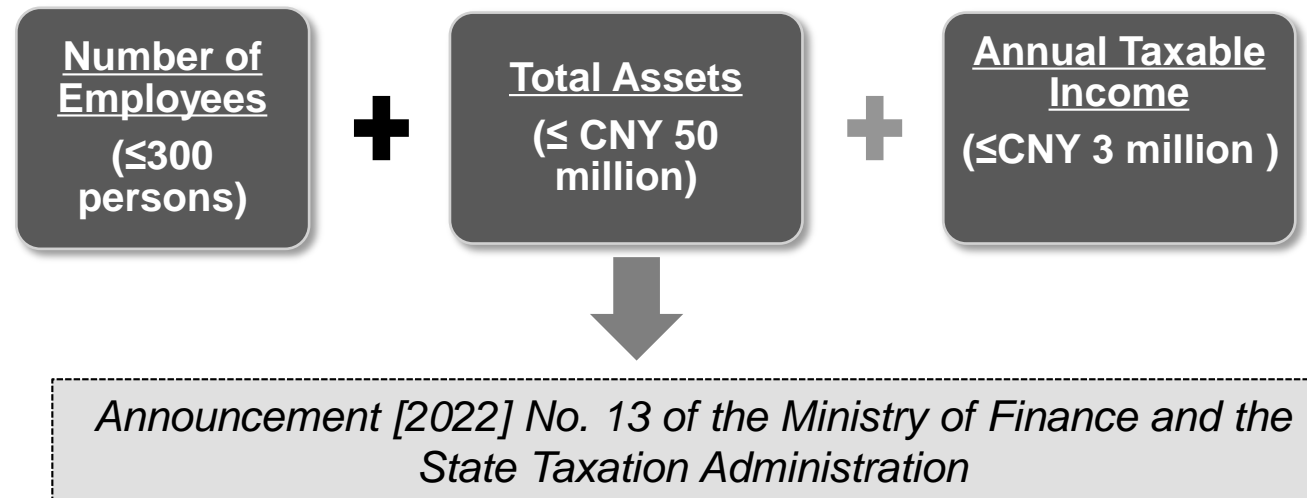
Tax Reliefs

➤ Continuous Reduction on CIT payment

For small and micro-profit enterprises (SMEs):

- where their annual taxable income is up to CNY 1 million (inclusive), they are applicable to the effective CIT rate of **2.5%** ($=12.5\%*20\%$) from January 1, 2021 to December 31, 2022;
- where their annual taxable income exceeds CNY 1 million but does not exceed CNY 3 million(inclusive), the amount in excess of CNY 1 million are subject to an effective CIT rate of **5%** ($=25\%*20\%$) from January 1, 2022 to December 31, 2024.

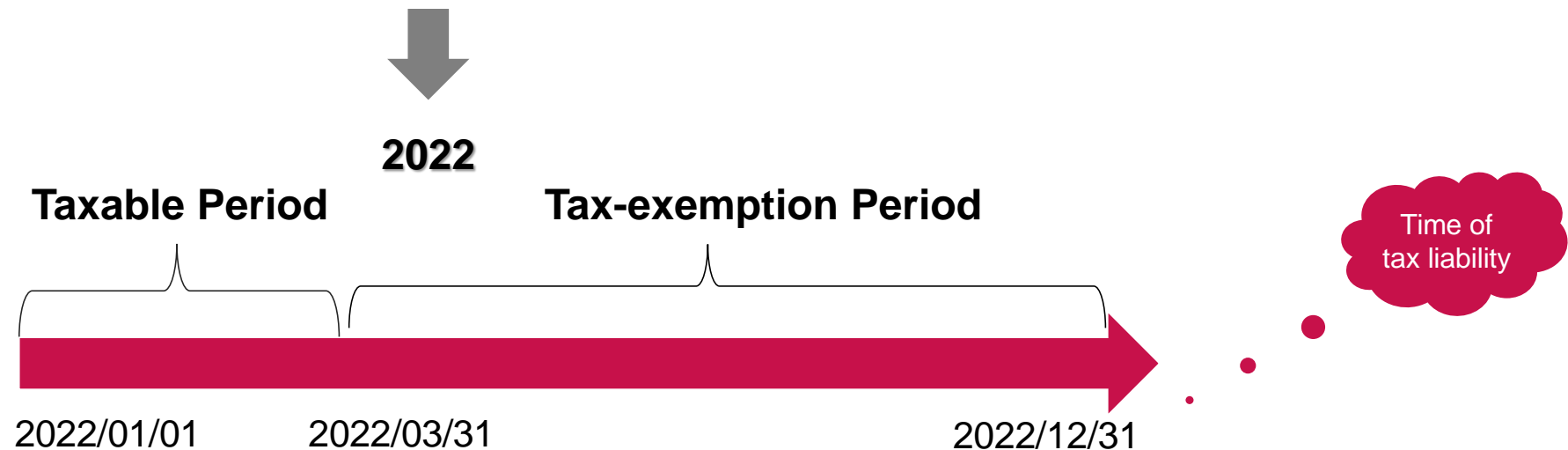
The following three criteria should be met simultaneously so as to be considered as a SME



Tax Reliefs

➤ Temporary Exemption on VAT payment

- Applicable only to small-scale taxpayers, regardless they are enterprises or self-employed individuals (个体工商户);
- Temporary valid for the period from April to December 2022;
- Not applicable to general VAT taxpayers;
- No threshold amount (eg. CNY 4.5million/quarter) anymore for VAT exemption.

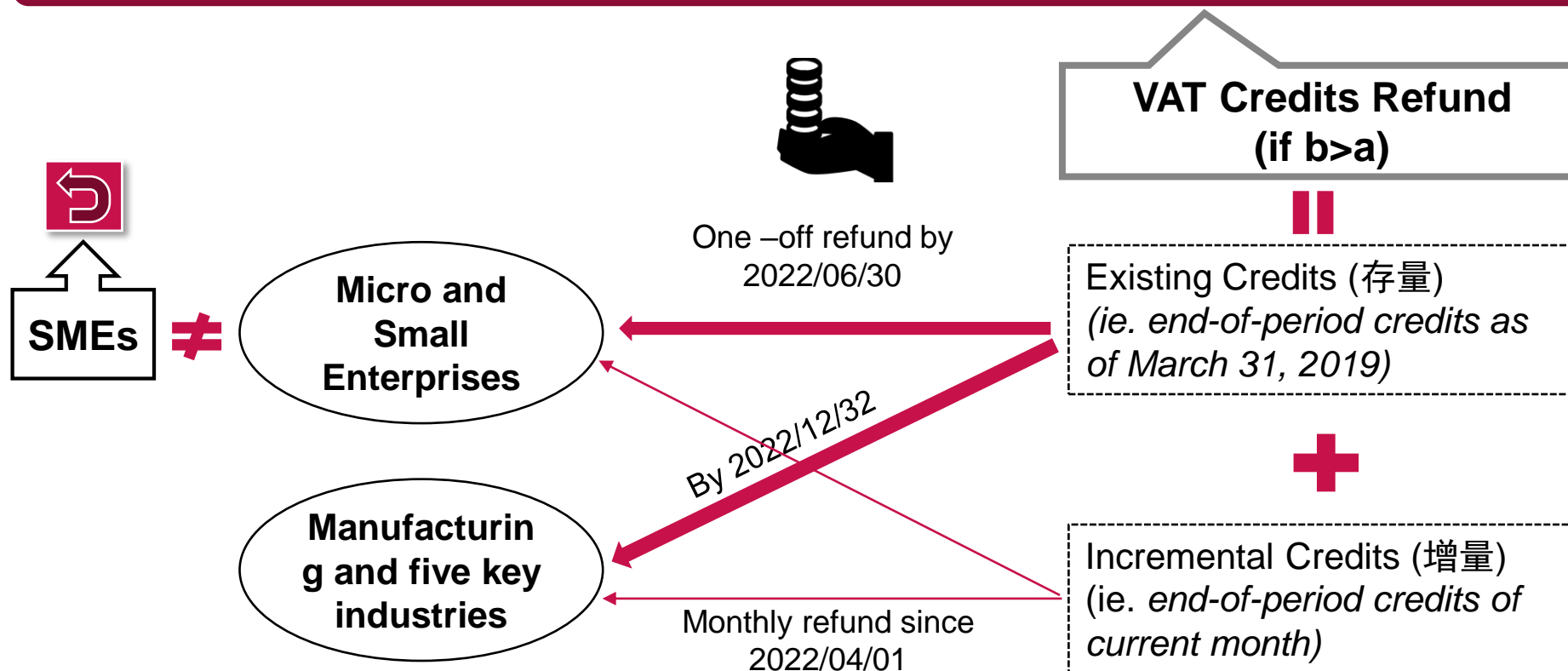


Tax Reliefs

➤ Expanded VAT Credits Refund

VAT credit mechanism

VAT payable amount = a (Output VAT amount) — b (Input VAT amount)



Tax Compliance Measures



Tax filing

- The tax filing deadline in April and May has been extended to **May 31, 2022.**
- Application for further extension of tax filing deadline is feasible.

Tax payment

- Postponing tax payment is permitted upon approval, for a maximum postponing period of no more than 3 months with no late payment fee.
- Subject to an application prior to the deadline of tax payment and a series of documents shall be provided for review.

Tax consequence for late tax filing

- Taxpayers who file late returns or submit relevant information late due to the pandemic can be exempted from administrative penalties and the relevant records are not included in the tax credit evaluation.

Any local financial support in Shanghai



Shanghai's 21 Policy Measures to Combat the Pandemic and to Support Businesses

《上海市全力抗疫情助企业促发展的若干政策措施》

✓ **Potential exemption of real property taxes**

Enterprises whose real estate was expropriated by the government and have difficulties in paying the real estate tax and urban land use tax can *apply for exemption of the real estate tax and urban land use tax*.

✓ **Subsidy policy for the exhibition industry**

Provide subsidies support for enterprises in difficulty affected by the epidemic or for foreign economic and technological exhibitions to be held in 2022.

Our Observations

- Since 2020, a series of tax policies have been introduced to support the prevention and control of the pandemic and to promote the recovery and development of the economy.
- To date, no tax policies have been introduced specifically in response to the current pandemic. But some of the current tax relief policies have been developed in the background of the gradual normalization of the pandemic.
- There is currently no social security relief available. Presumably, the government will introduce some similar social security relief policies to help businesses in Shanghai and the surrounding areas, as it did two years ago.



Q&A

Your Contact



QIN Anqi | 秦安琪

Senior Associate

qin.anqi@shaohe-lawfirm.com



ZHONG Yuan | 钟椽

Senior Associate

zhong.yuan@shaohe-lawfirm.com



ZHU Qin | 朱琴

Senior Associate, Tax Consultant

zhu.qin@shaohe-lawfirm.com

Thank You!