TianTong Dispute Resolution Review

天同律师事务所
TIANTONG LAW FIRM

About Tiantong

TianTong Law Firm was founded in 2002. As one of the leading Chinese law firms, it is solely dedicated to complex civil and commercial dispute resolution. Headquartered in Beijing, Tiantong has approximately 150 people nationwide, many of whom had served as senior judges for years at different levels of Chinese courts, including the Supreme People's Court and high courts of China. In the recent years, it has established 6 branch offices in Shenzhen, Nanjing, Chongqing, Shenyang, Xi'an and Zhengzhou, where the 6 circuit courts and 2 international commercial courts under the auspice of the Supreme People's Court are seated.

In the past decade, Tiantong has been keeping one of the highest winning rates among all Chinese law firms before the Supreme People's Court and various high courts of China. Over 30 cases won by Tiantong have been publicized as landmark guiding cases for national trial work on some of the most authoritative law journals in China.

Tiantong advises on all types of commercial disputes, including but not limited to litigation, arbitration, contentious bankruptcy and enforcement proceedings with its most impressive achievements in banking and finance, construction and engineering, corporate and M&A disputes etc. Its clients range from foreign governments such as the US Department of Justice, multinational corporations such as RBS to large Chinese companies such as Bank of China, China Construction Bank, Agriculture Bank of China, Sinopec, Sinochem, China Datang Corporation and Ping An Insurance etc.

In addition to its traditional advantages in litigation before Chinese courts, Tiantong has extensive experience in representing clients before domestic and international commercial arbitration proceedings. Tiantong lawyers previously worked for leading arbitration institutions as case manager (e.g. the Permanent Court of Arbitration in Hague, Netherland and Hong Kong International Arbitration Centre in Hong Kong) or clerked with the Justice of the UN International Court of Justice in Hague, Netherland. Some of them once worked at leading international law firms on international arbitration matters conducted before CIETAC, HKIAC, SIAC, ICC, SCC and LCIA, where the seats of arbitration include Beijing, Shanghai, Hong Kong, Singapore, Stockholm and London.

Tiantong is also specialized in advising clients for recognition and enforcement of foreign arbitral awards and judgments before Chinese courts, and is capable of effectively working together with leading international law firms and local counsel overseas to handle multi-jurisdiction disputes.

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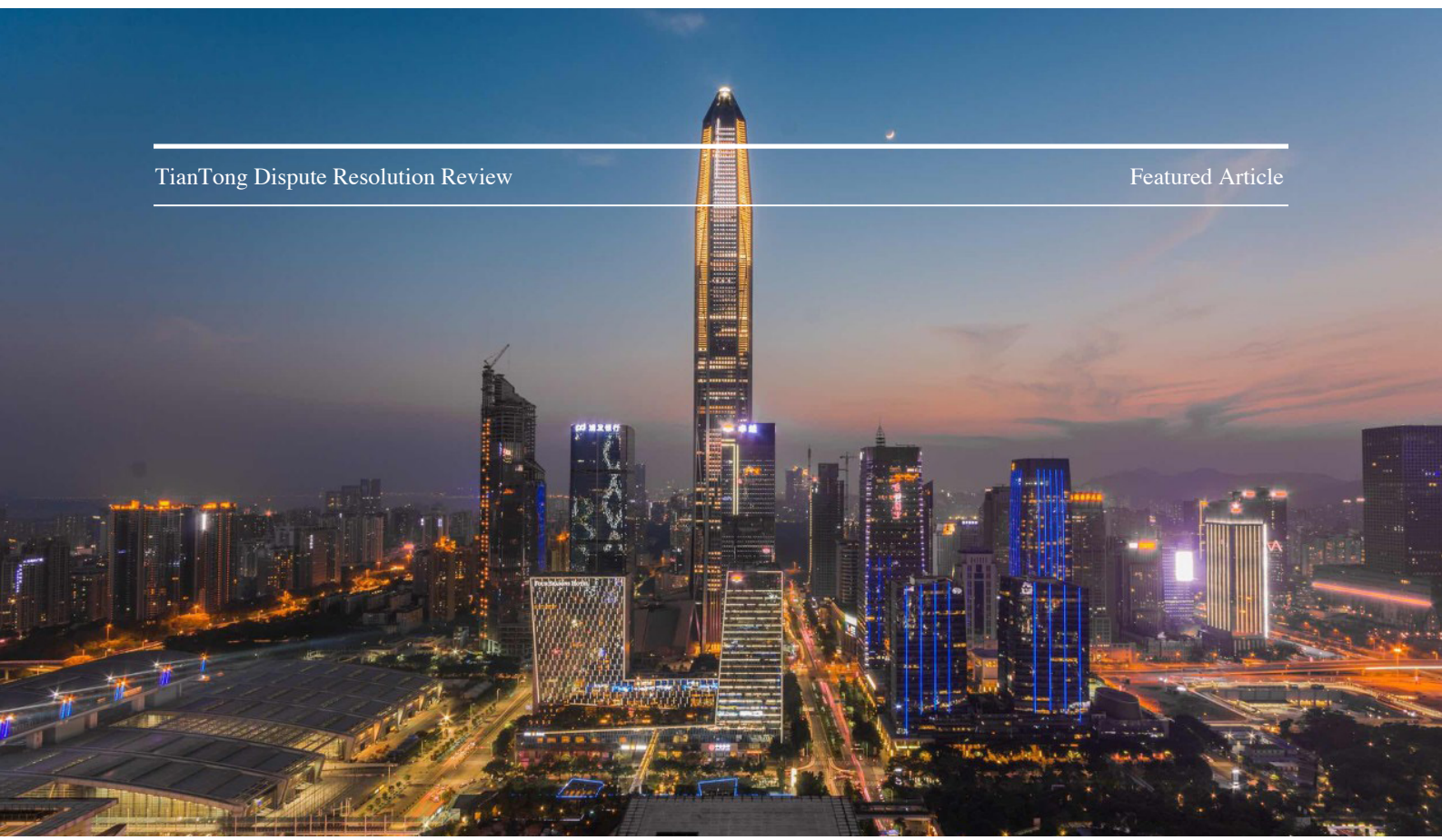


Featured Article

The COVID-19 Pandemic: Force Majeure and "Change in Circumstances" under Chinese Law

1. INTRODUCTION

In the early 2020, the COVID-19 pandemic evolves into a global shock and brings about government prevention and control measures in People's Republic of China ("**China**") such as lock-downs, travel restrictions and quarantines. Many companies in China may not be able to duly perform contracts due to the COVID-19 pandemic. Questions arise as to whether the affected parties can be excused from performance and what grounds under Chinese law the affected parties may explore to be excused from performance under current circumstances.

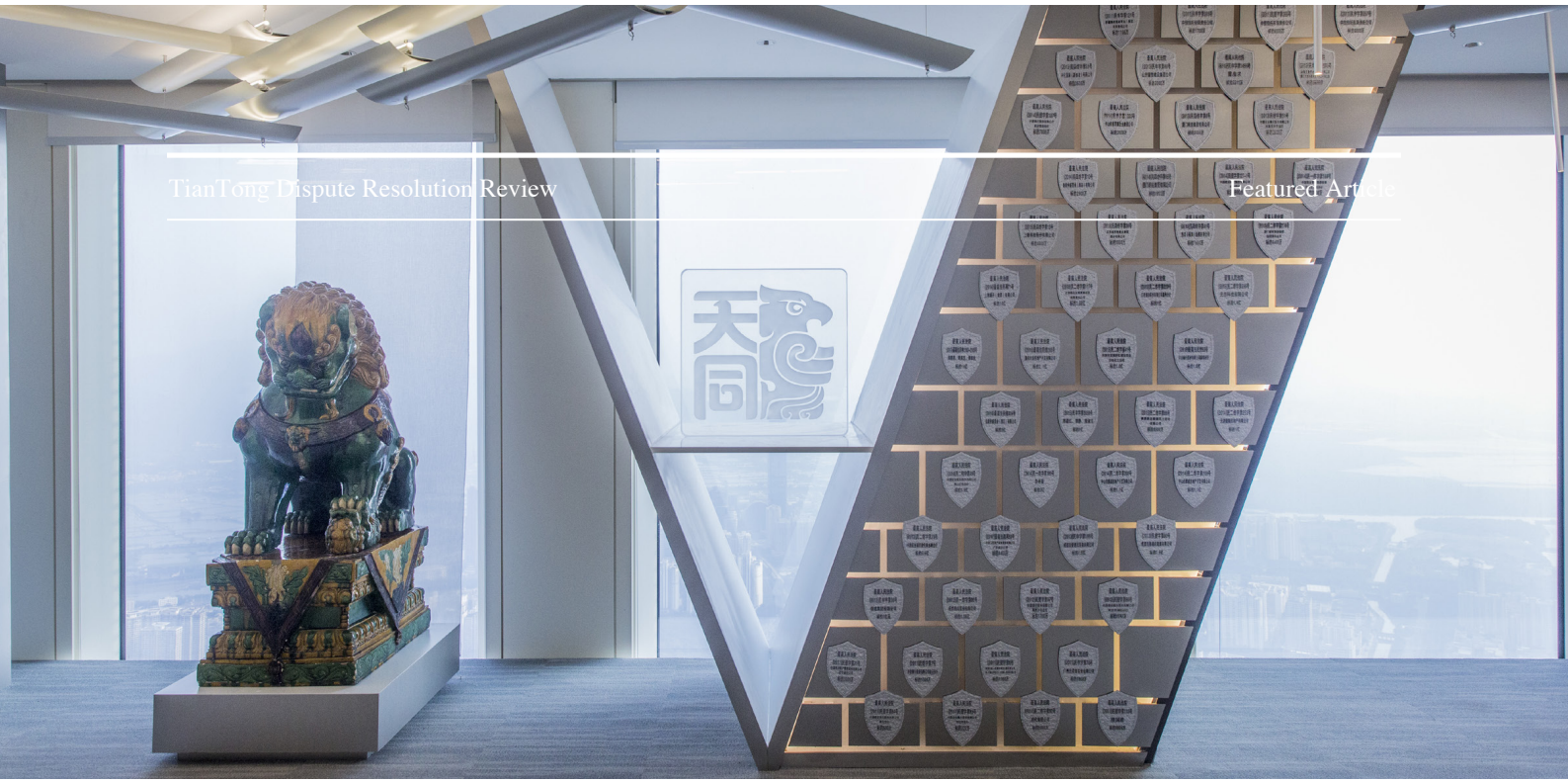
The COVID-19 pandemic and its subsequent impacts do not automatically exempt parties from liabilities for what otherwise would be a breach of contract. Under Chinese law, *force majeure* refers to "objective circumstances which are unforeseeable, unavoidable and insurmountable". If the parties have incorporated a *force majeure* clause in the contract, the affected party may first invoke the contract clause to see whether the current situation triggers a *force majeure* event. If the parties fail to incorporate a *force majeure* clause or the COVID-19 pandemic does not well trigger the clause, they may invoke force majeure pursuant to Article 153 of the *General Principles of the Civil Law of PRC(1986)*, Article 117 of the *Contract Law of PRC (1999)* and Article 180 of the *General Provisions of the Civil Law*

of PRC(2017). Besides, while performance is still possible but is excessively onerous for the affected party, the affected party may request a Chinese court to modify or terminate the contract relying on the "change in circumstances" doctrine.

On 20 April 2020 and 15 May 2020, the Supreme People's Court (**SPC**) issued the *Guiding Opinions on the Proper Handling of Civil Cases Involving COVID-19 Pandemic in Accordance with the Law (1) and (2)* (the "**Guiding Opinions**"). In the Guiding Opinions, the SPC reiterates that *force majeure* and "change in circumstances" shall be properly assessed in a context-specific basis and in each case the Chinese court shall consider the totality of circumstances required under Chinese law.

II. FORCE MAJEURE

Under Chinese law, the COVID-19 pandemic may be deemed as a *force majeure* event when (1) the consequences caused by the COVID-19 pandemic are beyond the affected party's reasonable control; (2) the COVID-19 pandemic or its subsequent impacts lead to delays or failure of performance; (3) the adverse impacts are not attributed to either party; and (4) the affected party has taken proper measures to mitigate the adverse impacts, including but not limited to timely informing the other party to the contract of the occurrence of such *force majeure* event. The said legal elements can be reduced to three requirements: foreseeability, causality and accountability.



First, "*foreseeability*": Chinese courts will consider whether the COVID-19 pandemic and its subsequent impacts can be reasonably foreseen by the affected party. The timing of the conclusion of the contract is considered in some court judgments. Reference can be made to court judgements during the SARS outbreak in 2002/2003. In a case where the parties stipulated to limit the construction project to particular specifications after the SARS broke out in China, the court found that the adverse impact was foreseeable since the stipulation was made in response to the SARS outbreak, resulting in no establishment of *force majeure* there. As such, results may vary if the contract was concluded at different stages during the COVID-19 pandemic.

The COVID-19 pandemic may be considered as an inherent commercial risk to certain industries. In practice, Chinese courts considered that suppliers in the poultry industry should have assumed the risk of bird flu outbreak, and as such, the bird flu situation did not constitute a *force majeure* event. [1]Similarly, some contracts may have assumed the risk of the COVID-19 outbreak, such as insurance contracts where "epidemic"/ "pandemic" has been stipulated as an insured event, or futures contracts that speculate the price fluctuation caused by the COVID-19 pandemic. In such cases, the parties have fully anticipated the consequences of disease such as the COVID-19 pandemic and should have allocated the risk between the parties in the contract accordingly.

Second, "*causality*": the COVID-19 pandemic alone does not automatically constitute a *force majeure* event. The affected party must bear the burden of proving that specific obstacles due to the COVID-19 pandemic have caused the prevention, delay or hinderance of its performance of contractual obligations. That said, if the control measures cannot materially hinder performance, such difficulty would not be deemed as a *force majeure* event.

It is usually insufficient for the affected party to suggest that a general government restriction constitute a *force majeure* event. In a dispute arising from a construction contract during the SARS outbreak, the contractor contended that the control measures had restricted its hire of migrant workers, resulting in its delay of handing over the project to the owner. The court found that the local government had published a notice prohibiting the hiring of migrant workers, and most of workers hired by the contractor were indeed migrants from other provinces. Accordingly, the court found that

[1] See Fuzhou Intermediate People's Court [2017] Min Civil 01 Final Judgment No. 4464, Guilin Intermediate People's Court [2018] Gui 03 Final Civil Judgement No. 93.

the alleged *force majeure* event was sufficient to excuse delay of performance. [2] There are also some courts that accept social impacts as sufficient grounds to hinder performance. Reference can be made to a case during the MERS outbreak, where the court found that the panic caused by the MERS outbreak in China hindered the performance of contract relating to travels from China to South Korea. [3]

In addition, if there are any other reasonable alternatives for the affected party to adopt in furthering its performance of the contract, the court will not exempt the affected party's liability of non-performance. For instance, even if the local government in China has restricted access to a particular receiving port due to the COVID-19 pandemic, as long as there are alternative ports for the purchaser to take delivery of goods, it can hardly be said that the COVID-19 pandemic is the cause of the purchaser's failure to take delivery of such goods. Particularly in this booming age of e-commerce, parties no longer have to rely on physical presences, such as bank branches, to make payments or transact businesses. Many contractual obligations can be performed through online channels.

Third, "*accountability*": if the affected party has wrongfully breached the contract in the first place, the COVID-19 pandemic and its subsequent impacts should not save it from the contractual liability. The affected party is required to take reasonable steps to mitigate any damages, and otherwise it is accountable for losses that could have been prevented. The affected party should timely notify the other party of the occurrence and impact of the COVID-19 pandemic so as to prepare the counterparty to weather consequences of non-performance of the contract and enable it to discover any alternative solutions.

Where the COVID-19 pandemic can be deemed a force majeure event under the above requirements, the affected party may be fully or partially excused from contractual obligations. If performance of contractual obligations only becomes temporarily impossible, the affected party may be exempted from delay of performance but may not be waived of performance. If performance becomes permanently impossible, the affected party may seek to terminate the contract, as the purpose of the contract cannot be accomplished due to the *force majeure* event.[4]

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[2] See Sanya Intermediate People's Court [2005] Sanya Civil 1 Final Judgment No.79.

[3] See Yinchuan Intermediate People's Court [2018] Ning Civil 01 Civil Supervision No. 71.

[4] Section 1, Article 94 of the *Contract Law of PRC (1999)*.

III. CHANGE IN CIRCUMSTANCES

In addition to the *force majeure* doctrine, the affected party may invoke "change in circumstances" doctrine when the basis on which the contract was entered into has been materially altered by the COVID-19 pandemic. Article 26 of *Judicial Interpretation II of the PRC Contract Law* addresses the "change in circumstances" doctrine and grants exemption to contractual parties that come across unforeseeable difficulties such as abrupt surge of costs or significant social and economic changes. The latest draft of the *Civil Code of PRC* incorporates this doctrine in Article 533, which further provides that the affected party may initiate a re-negotiation if a material change occurs to the basis of the contract. Failing an agreement, the affected party may ask a court or an arbitral tribunal to modify or terminate the contract by initiating litigation or arbitration.

However, such exemption of contractual liability could be granted under very limited circumstances. According to Chinese law, the "change in circumstances" doctrine applies if (i) the basis on which the contract is entered into has been materially altered; (ii) such change cannot be foreseen at the time of conclusion of the contract; (iii) such change is not a commercial risk or *force majeure*, and (iv) further performance will be manifestly unfair to the affected party or cannot achieve the purpose of the contact. Compared to *force majeure*, the "change in circumstances" does not require the change to be "unavoidable" or "insurmountable". The focus of "change in circumstances" compared with *force majeure* rests in (i) whether the COVID-19 pandemic and its subsequent impacts have materially altered the basis of the contract and (ii) whether further performance will be manifestly unfair to the affected party.

First, the COVID-19 pandemic and its consequences should constitute significant changes to the basis of the contract. A typical example is that performance under the commercial lease agreement has been affected by the COVID-19 pandemic. When the stores are forced to shut down due to the control measures, their tenants can no longer make money from the commercial premises. As such, the "change in circumstances" doctrine likely applies because the COVID-19 pandemic has caused a significant disproportion between the parties' performances.

However, if the control measures do not require the tenants to shut down the stores, the mere occurrence of the COVID-19 pandemic is usually insufficient to alter the basis of the contract. Reference can be made to a commercial lease case during the SARS outbreak, where the court found that the tenant closed the store for business considerations instead of government requirements. As such, the court did not support the "change in circumstances" doctrine.[5]

Second, to establish the "change in circumstances" doctrine, it should be demonstrated that continuous performance would unreasonably burden the affected party. The standard of "manifestly unfair" depends on a totality of circumstances. The Chinese court may consider the parties' respective capacity of risk tolerance from a reasonable person's perspective, looking into how much profit the affected party may make under the contract and whether such profit can justify the risk the court may ask it to take. For instance, whilst the production costs have significantly increased due to the COVID-19 pandemic, the court is likely to accept the "change in circumstances" doctrine if there is a significant disproportion between the parties' performances. Otherwise, the price change will be deemed as a commercial risk that should be tolerated by the affected party.

If the COVID-19 pandemic qualifies as "change in circumstances", the parties are encouraged to first resolve the disproportion through re-negotiation pursuant to the latest draft of the *Civil Code of PRC*. As mentioned, the Chinese court is slow to base on the "change in circumstances" doctrine to terminate a contract. If the parties fail to reach a new agreement against the change in circumstances, the Chinese court would be inclined to modify the contract rather than terminate it.

[5] Guangxi High People's Court (2007) Gui Civil 4 Final Trial No.1.

China Law Updates

SPC Issued Guidelines on Force Majeure Claims and Contractual Disputes arising out of COVID-19 Cases

On 20 April 2020 and 15 May 2020, the Supreme People's Court ("**SPC**") respectively published *Guiding Opinions on the Proper Handling of Civil Cases Involving COVID-19 Pandemic in Accordance with the Law (1)* and *(2)* (the "**Guiding Opinions**"), providing guidance on frequently risen issues related to the COVID-19 pandemic, including, *inter alia*: (i) the application of *force majeure* doctrine and (ii) the principles to be taken into account when dealing with contractual disputes.

The *force majeure* doctrine is recognised under Article 117 of *the Contract Law of the PRC*, which exempts a non-performing party from its contractual liability in case of *force majeure* events. According to *the Guiding Opinions*, Chinese courts are required to strictly assess relevant standards in determining whether to apply the force majeure doctrine. It is further emphasised that the party claiming exemption due to *force majeure* events shall bear the burden of proving the causality between the force majeure event and its failure to perform contractual obligations.

In *the Guiding Opinions*, the SPC points out that, when dealing with contractual disputes related to the COVID-19 pandemic, the court shall follow three principles: (i) where the pandemic directly caused the performance to be

impossible, the court shall apply the *force majeure* doctrine subject to the extent of impacts of the pandemic; (ii) where the pandemic only made the contractual performance more difficult, the court shall not uphold the parties' claim of terminating the contract on the sole ground of difficulties in performance, and where further performance of the contract will be manifestly unfair to one party, the court may declare to modify the contract at the request of the party adversely affected according to the change in circumstances doctrine; and (iii) the court shall consider the varied impacts of the pandemic on different regions, industries and consider any government subsidies, tax relief or other types of funding and debt relief granted to the parties.

The Guiding Opinions provides further specifications on the performance of sale and purchase contracts. The SPC notes that where the pandemic or the prevention measures against the pandemic has caused the costs of performing the contract to significantly increase or the price of the product to significantly decrease, so as to render the contract manifestly unfair to one party, the court shall adjust the contract price based on the fairness principle and the specific facts of the case. Where the pandemic or the prevention measures have rendered it impossible to perform the contract within the time limit previously stipulated by the contract, the court shall adjust the time limit of the contract based on the fairness principle and in light of the specific facts of the case. If the contract has already been amended by adjusting the contract price or the time limit of performance, the court shall not uphold one party's claim to find the other party liable for breach of the contract.

CIETAC Issued Guidelines on Proceeding with Arbitration Actively and Properly during the COVID-19 Pandemic

On 28 April 2020, China International Economic and Trade Arbitration Commission ("**CIETAC**") issued *Guidelines on Proceeding with Arbitration Actively and Properly during the COVID-19 Pandemic (Trial)* (the "**Guidelines**"), effective from 1 May 2020.

In the Guidelines, it is emphasised that the tribunal's duty to proceed with arbitration fairly and efficiently as well as the parties' duty to proceed with the arbitration in good faith shall not be affected by the pandemic. Meanwhile, Article 2 of *the Guidelines* provides specific measures for the parties and arbitral tribunals to proceed with arbitration during the pandemic, for instance: (i) encouraging the parties to file arbitration applications online and to submit and receive arbitration documents via email, and (ii)

considering virtual hearings via CIETAC smart oral hearing platform. In this respect, CIETAC issues *Provisions on Virtual Hearings (Trial)* annexed to the Guidelines, regulating the procedure of virtual hearings, in order to ensure the efficiency and confidentiality of virtual hearings.

BAC Issued Guidelines for Virtual Hearings in Response to COVID-19 Pandemic

On 8 May 2020, Beijing Arbitration Commission ("**BAC**") issued the *BAC/BIAC Working Guidelines for Virtual Hearings (Trial)* (the "**Working Guidelines**"), which shall be applicable during the pandemic prevention and control period. *The Working Guidelines* consist of three parts, namely: (i) the definition and scope of application of virtual hearings; (ii) the conduct of virtual hearings; and (iii) the diagram of an example virtual hearing. Article 3 of *the Working Guidelines* provides the situations where virtual hearings are not appropriate, e.g., the matter in dispute is related to state secrets, commercial secrets or otherwise demands a high degree of confidentiality. Part two of *the Working Guidelines* provides guidance for the parties and arbitral tribunals on how to proceed with virtual hearings, including choice of appropriate online platforms, pre-hearing preparation, and the dos and don'ts during virtual hearings. In addition, the BIAC provided a confidentiality agreement template in the annex to *the Working Guidelines* for the reference of participants of the hearing.

HKIAC Released Case Statistics for 2019

On 30 March 2020, Hong Kong International Arbitration Centre ("**HKIAC**") released its case statistics for 2019. The statistics show that in 2019, HKIAC received a total of 503 cases, of which 308 were arbitrations, 12 were mediations, 182 were domain name disputes and 1 was adjudication. 80.9% of all arbitrations submitted to HKIAC in 2019 were international in nature, i.e. at least one party was not from Hong Kong. The total amount in dispute in all arbitration cases reached HK$36.4 billion (approximately US$4.7 billion), representing a roughly 30% decrease from HK$52.2 billion in 2018.

Moreover, following the effectiveness of the Hong Kong-Mainland China arrangement on interim measures in October 2019, HKIAC processed a total of 13 applications made to Mainland Chinese courts seeking to preserve assets or evidence in Mainland China, which amount to approximately US$798 million in total. According to HKIAC, among all parties seeking interim measures in Mainland, 40% of them are from Mainland whilst 60% are from Hong Kong, Switzerland, Singapore, Samoa, and the British Virgin Islands.

Taiwan Court Recognised an Arbitral Award of CIETAC

On 15 April 2020, the Taiwan Hsinchu District Court issued a judgement recognising an arbitral award of CIETAC. The underlying dispute involved Fujian Zhaoyuan Photoelectric ("**Zhaoyuan**"), a mainland-Taiwan joint venture and JetEazy, a Taiwanese company.

The parties entered into a purchasing contract in April 2018. Zhaoyuan terminated the contract in May 2018 due to several product quality issues, and the parties commenced negotiation about refund and compensation. After JetEazy repeatedly ignored Zhaoyuan's demands for refund and compensation, Zhaoyuan applied to CIETAC pursuant to the arbitration clause of the contract. On 22 November 2019, the Tribunal issued and CITEAC confirmed an arbitral award in favour of Zhaoyuan's claims. The Taiwan Hsinchu District Court recognised the arbitral award, holding that it is not contrary to the public order or good morals of the Taiwan region.

This is the second instance where a CIETAC arbitral award was reviewed by a Taiwanese Court. In March 2019, another local Taiwan court rejected the request to recognise an award issued by CIETAC on the ground that the respondent had not been properly served with arbitration documents and therefore enforcing such award would violate the public policy of the Taiwan region.