



Hong Kong

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## COVID-19 AND FORCE MAJEURE: WHAT YOU SHOULD KNOW

Corona virus or COVID-19 is now known to the world over and has been the headline of most news cycles for the last two months. It has been a prevailing topic of conversation and now has become the debate focus of the corporate and commercial world.

COVID-19 has impacted industries across the spectrum. The quick development, spread and uncertainty of COVID-19 has triggered a number of governments across the world to implement emergency measures in an effort to contain the spread of COVID-19. This has resulted in the forced closure of factories, compulsory quarantine, grounding of flights and forced 'work from home' procedures being implemented by employers, especially in the People's Republic of China (the "PRC"). These disruptions have exposed parties to potential liability for failure to perform at all or timeously their duties pursuant to agreements entered into. It is within this context that we will explore whether or not COVID-19 can constitute force majeure under an agreement.

It is worth noting that on 30 January 2020, the World Health Organisation (WHO) declared that COVID-19 was a public health emergency of international concern.<sup>1</sup>

### 1. Force Majeure Clauses

Force majeure is a French phrase which directly translates to superior force. In Latin, a similar phrase, casus fortuitus means a fortuitous case or an uncontrollable accident an act of God.

Generally, force majeure in English common law is understood to mean an event or circumstance that occurs and which prevents one (or both) parties to an agreement from fulfilling their obligations under the agreement. Relief provided by a force majeure clause is usually in the form of a suspension of obligations under the agreement, an extension of timeframes or alternatively, it may afford the party relying on the force majeure clause the right to terminate the agreement.

The language used in a force majeure clause in most common law jurisdictions is extremely important as it will dictate when and what relief is available. For example, will relief be available when performance is rendered impossible or will relief be available simply when performance becomes more onerous or is delayed. The former, being a much higher threshold.

Further, the force majeure clause may require that a party wishing to rely on it, give notice to the other party or take certain steps before it may invoke the clause.

### 2. Force Majeure in Hong Kong

Hong Kong has a common law legal system and as such, there is no doctrine of force majeure. Practically what this means is that there is no statutory or precise definition of force majeure. Therefore, force majeure is subject to the common law principles and standard rules of contractual interpretation. For instance, whether or not a party has a right to invoke a force majeure clause in an agreement, will depend on the construction and interpretation of the force majeure clause in the relevant agreement. As such, to understand the scope of a force majeure clause, one must understand the following:

<sup>1</sup> <https://www.who.int/emergencies/diseases/novel-coronavirus-2019/events-as-they-happen>

- a) definition of force majeure i.e., what events or circumstances will fall within the scope of the force majeure clause?;
- b) relief provided for by the force majeure clause, i.e., will relief be available when performance is rendered impossible or will relief be available simply when performance becomes more onerous or is delayed?; and
- c) does the force majeure clause require any positive steps to be taken by the party seeking to rely on the clause, i.e., is written notice required, or does the party have to mitigate any loss?.

Once the aforementioned is understood, in the context of COVID-19, a party wishing to rely on a force majeure clause must generally be in a position to demonstrate:

- a) that COVID-19 falls within the definition of the force majeure clause;
- b) as a result of COVID-19, it was prevented, hindered or delayed (the threshold here will depend on the precise language used) in performing its obligations under the agreement; and
- c) that the steps required to enforce the force majeure clause have been taken (where applicable).

As there is no statutory or precise definition of force majeure in Hong Kong, the language used in each instance will be vitally important with precedent guiding a court in the interpretation and effect thereof.

In light of the current circumstances, before entering into any new agreements, it is advisable that the parties include a clause in their agreements which deals with a possible escalation of the current outbreak. Given that COVID-19 is now a known and foreseeable event, it will be unlikely that any party entering into an agreement now will be able to successfully rely on COVID-19 being a force majeure event as it is arguable that a party entering into an agreement now should have taken steps to mitigate against the potential impact of COVID-19.

Importantly, if an agreement does not contain a force majeure clause, a Court in Hong Kong will not automatically read into an agreement a force majeure clause. This is in contrast to the approach in the PRC.

The emergence of COVID-19 has evoked memories of the Severe Acute Respiratory Syndrome (“SARS”) epidemic which adversely affected Hong Kong in 2003. Many have drawn parallels between COVID-19 and SARS in an attempt to ensure that Hong Kong has learned its lesson in dealing with epidemics and does not make the same mistakes twice. It is within the common law doctrine of ‘frustration’ that we can draw another parallel. In the case *Li Ching Wing v Xuan Yi Xiong*<sup>2</sup>, as a result of the outbreak of SARS in the estate within which the tenant resided, the tenant was subject to a mandatory 10 day isolation period. The tenant attempted to rely on the doctrine of frustration to terminate the lease. However, the Court rejected the tenant’s argument and explained that 10 (ten) days of a two year lease was insignificant. Although the Court acknowledged that it was at least arguable that SARS was an unforeseen event, such event in these circumstances did not in the opinion of the Court “significantly change the nature of the outstanding contractual rights or obligations from what the parties could reasonably have contemplated at the time of execution of the tenancy agreement.”

The doctrine of frustration may provide an alternative avenue to pursue if force majeure is not an option. However, the doctrine of frustration has limited applicability and successful cases are rare. The doctrine of frustration requires that (a) whether the subject matter of the contract or the means of performance have been destroyed such that performance is rendered objectively impossible, and (b) whether the central purpose of the contract has been frustrated or the contract has become radically different from what was contemplated by the parties at the time when it was agreed and therefore physically or commercially impossible to fulfill.

### 3. Force Majeure in the PRC

Unlike Hong Kong, the PRC has a force majeure doctrine under Article 180 of the PRC General Rules on the Civil Law and Article 117 of the PRC Contract Law (the “Doctrine”). Under the aforementioned Articles, force majeure is defined as an objective event or situation which is unforeseeable, unavoidable and insurmountable. In the PRC, if an agreement is silent on force majeure, the Doctrine will apply automatically. Again, this is in contrast to the position in Hong Kong and other common law jurisdictions such as the United Kingdom.

On 10 February 2020, the spokesperson of the Legislative Affairs Commission of the National People’s Congress Standing Committee made clear that the measures implemented by the PRC Government to contain COVID-19 can constitute an

<sup>2</sup> [2004] 1 HKLRD 754.

unforeseeable, unavoidable and insurmountable force majeure event, if performance under the agreement is prevented as a result of those containment measures. In addition, the China Council for The Promotion of International Trade (“CCPIT”) which is officially accredited with the Commerce of Industry announced that it would offer force majeure certificates to PRC companies which have been impacted by and are struggling to cope with COVID-19.

It has been reported that a record number of force majeure certificates have been issued in the PRC as industry begins counting the costs of the impact of COVID-19. The Financial Times has reported that as of 21 February 2020, the CCPIT had issued 3,325 force majeure certificates covering contracts with a combined value of USD38.5 billion.<sup>3</sup>

Importantly, the force majeure certificates that have been issued by the CCPIT serve only as evidence of certain objective circumstances that have occurred and which have impacted business such as governmental restrictions on travel or working arrangements. Ironically, these force majeure certificates do not directly use the language of ‘force majeure.’ Therefore, should a party in the PRC wish to rely on a force majeure certificate issued by the CCPIT to minimize its liability for non-performance under an agreement, that party must be in a position to present objective evidence to support its case to prove that as a result of the anti-epidemic measures in place in the PRC, it was unable to discharge its obligations under the agreement.

#### 4. A Comparison of the Application of the Doctrine of Force Majeure in Hong Kong and the PRC

The case of *Sun Wah Oil & Cereals Ltd. V Gee Tai Trading Co.*<sup>4</sup> Ltd. was heard in the Hong Kong Court of Appeal in 1993. In this case, a force majeure/arbitration clause was included in an agreement which read “Force majeure/arbitration: standard terms to apply.” The Court in its discussion noted that it was common ground that the force majeure/arbitration clause was meaningless and that there are no standard terms which are applicable to the phrase ‘standard terms apply’ in the context of force majeure and arbitration. This approach by the Hong Kong Court of Appeal highlights the distinction between the approach in the PRC where the Doctrine will automatically apply to agreements whereas in Hong Kong, this is not so. The Court of Appeal in this instance severed the clause from the agreement.

<sup>3</sup> <https://www.ft.com/content/bca84ad8-5860-11ea-a528-dd0f971febbc>

<sup>4</sup> [1993] HKC 132.

#### 5. Force Majeure and Disclosure for Publicly Listed Companies

The statutory regime governing listed companies’ disclosure of price sensitive information (referred to in the legislation as “**Inside Information**”) is set out in Part XIVA of the Securities and Futures Ordinance (“**SFO**”). The regime creates a statutory obligation on listed companies to disclose Inside Information to the public, as soon as reasonably practicable after Inside Information has come to their knowledge.

Listed companies must be reminded that should they be aware of any potential exposure as a result of COVID-19 such as a force majeure event, which information is considered to be Inside Information, they ought to make the necessary disclosures under Part XIVA of the SFO.

Listing Rules 2.03(2) and 2.13(2) (Growth Enterprise Market (“**GEM**”) Rules 2.06(2) and 17.56(2)) require that investors are provided with sufficient information to enable them to make an informed decision of the listed issuer and that such information must be accurate and complete in all material respects and not be misleading or deceptive. Material facts should not be omitted and favourable possibilities should not be presented as more probable than they are. It is within this context that listing applicants wishing to list on either the Main Board or the GEM should consider including in the risk factors section of its prospectus the potential impacts that COVID-19 may have on the listing applicant.

#### 6. Steps to Take

If you are concerned that force majeure may impact you, we recommend proactivity. You should review your agreements and look for the following:

- a) Does COVID-19 fall within the definition of a force majeure event?
- b) What is the threshold of non-performance that may trigger a party to invoke the force majeure clause i.e. will a mere delay in performance allow a party to invoke the clause?
- c) If you wish to rely on the clause, what steps must you take before you can invoke the clause?
- d) Do you need to take active measures to mitigate against the loss that may be caused by the force majeure event?

Consider including in the force majeure clause of new agreements language which will cover epidemics/pandemics and diseases. However, as explained, COVID-19 is now known to us which makes it unlikely that new force majeure clauses entered into now which specifically cover COVID-19 as a force majeure event will withstand a challenge should a party attempt to rely on COVID-19 as a force majeure event. Having said that, as the longevity and effects of COVID-19 are still unknown, it is advisable that parties entering into new agreements include clauses which will govern the relationship between the parties if there is an escalation of COVID-19. This is particularly so for parties in the manufacturing or hospitality industries where we continue to see interruptions to manufacturing, tourism, sporting events, trade shows and conferences.

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