

The thing about ...

Robert Lewis

Recently, ASIAN-MENA COUNSEL'S Patrick Dransfield photographed and talked to Zhong Lun and docQbot's Robert Lewis in Beijing and put to him a series of questions on behalf of the In-House Community.

Photo: Patrick Dransfield

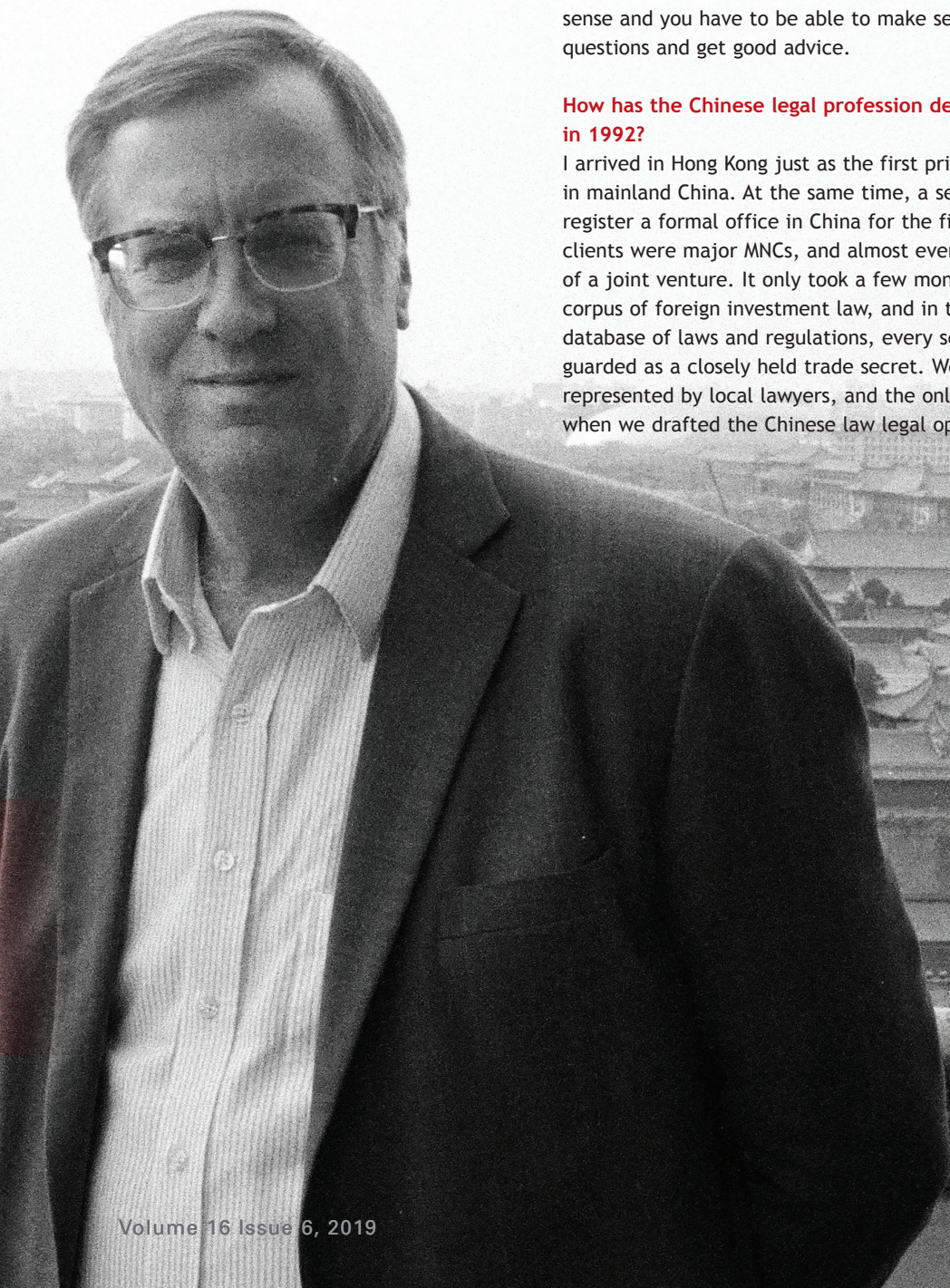
Having worked in top US, UK and China law firms, and also as Asia general counsel for Nortel, you are in a unique position to comment on the China market. How should foreigners approach investment in China?

When I first came to China more than 25 years ago, it was common for MNCs [multinational corporations] to think they had to set aside traditional western deal-structuring concepts in order to adapt to the “China way” of doing things, and a lot of internal and external business advisers worked hard to create a mysterious (and even in many cases an irrational) aura around the China market in order to preserve their own position as an indispensable adviser. An inordinate number of deals cratered as a result.

China deals need to make good business sense in the traditional western way while still being adapted to local market conditions. China has changed dramatically over the last two-plus decades, and while things are not quite as mysterious as they once were, there are still unique (and sometimes still not completely rational) characteristics. So the bottom line advice is be sensible – the deal has to make sense and you have to be able to make sense of China. The key is to ask good questions and get good advice.

How has the Chinese legal profession developed since your first arrival in China in 1992?

I arrived in Hong Kong just as the first private domestic law firms were being set up in mainland China. At the same time, a select few foreign law firms were able to register a formal office in China for the first time. In those early days, the only clients were major MNCs, and almost every foreign investment had to take the form of a joint venture. It only took a few months to get your arms around the entire corpus of foreign investment law, and in the absence of a centralised public database of laws and regulations, every scrap of official notice or response was guarded as a closely held trade secret. We never saw Chinese clients being represented by local lawyers, and the only time we engaged with local lawyers was when we drafted the Chinese law legal opinions for the Chinese lawyers to sign.



By 2000 the Chinese firms had already started to emerge to take more and more traditional FDI [foreign direct investment] work from MNC clients, but the foreign firms maintained a substantial advantage in terms of inbound M&A and higher end FDI work for MNCs. But that advantage has, in my opinion, long since eroded. In the aftermath of the global financial crisis, the foreign firms retrenched and have for the most part only maintained status quo in terms of scope and scale over the last decade, while the Chinese firms have experienced explosive growth.

In 2010 I voted with my feet and became the first senior foreign lawyer to make the move from a major international law firm to join a leading Chinese firm. The only difference between the work I do now at Zhong Lun and what I did at my prior international law firms is that I have access to much broader and deeper expertise on my current platform.

You co-founded the China Going Global Think Tank (CGGT) and are a special adviser to the law and policy bureau of the State-owned Assets Supervision and Administration Commission – could you share with us the most common problems facing Chinese outbound investment?

I actually wrote a book about this, which was published in Chinese in late 2017. I focused on the 70% of the outbound deals that are low- or mid-cap deals, usually undertaken by private companies which are doing their first few deals outside of China. In the book I listed 30 common problems that many such Chinese companies encounter as they invest abroad, but if I had to select the top five it would probably include the following:

1. Chinese companies in this category are typically too opportunistic and insufficiently strategic in their approach;
2. they tend not to be sufficiently familiar with international deal structures;
3. they don't like to pay for professional advisers and then even when they do too often they do not want to take advice;
4. they often have too many naive assumptions, principally assuming that whatever worked inside China will work outside China; and
5. overall there are a myriad of communication and culture gaps with the other side, which often simply takes the form of not speaking the same deal language as their foreign counterparts.

All of this engenders misunderstandings and mistrust, which kills deals, since above all else sellers demand deal certainty, the one thing too many Chinese outbound investors cannot give. As a result, many foreign counterparties will decline to engage with many of these Chinese investors or if they do will



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do so only if the Chinese side offers a premium. Hence, the origins (at least in part) of the much discussed “China premium.”

The problems are quite serious but ultimately all surmountable. As with the Japanese, who encountered many of the same problems in the early stages of their international expansion, it will take a generation. So the world is on notice – once the Chinese figure it out, they will be an even more dominant player on the international stage.

CGGT takes a multi-disciplinary approach to help solve issues relating to outbound investment – has this shaped the way that you see the practice of law developing as a team sport?

Part of the rationale for the multi-disciplinary nature of the CGGT was born of my frustration with getting the attention of decision makers in Chinese companies – if I talked about “legal risk” they would immediately switch off, thinking that legal issues were for the in-house lawyers and had nothing to do with them. On the one hand, I recognised that as a lawyer I had to be better about framing issues in commercial terms that business people would understand and not just talk as I would to other lawyers. This is reminiscent of the traditional Chinese proverb about



Photo: Patrick Dransfield

technology shaping the legal industry in China, and beyond? What do you see as some of the benefits – and also some of the risks?

We are at an important inflection point in the legal profession in terms of adoption of technology. We are among the last of the professions to hold on to the more traditional labour-intensive ways of doing things. Part of that is because the technology was not quite ready but perhaps it was more the case that we as lawyers have not been ready to embrace change. The western hourly rate model provides few incentives to improve efficiencies, but because the China legal market for the most part works on a fixed-fee basis, Chinese lawyers should be the earliest and most enthusiastic adopters of legal tech. The rationale is quite simple – when the client pays hourly rates, the risk of lawyer inefficiency is on the client (hence the critical role of in-house counsel to monitor outside counsel closely), but when the client pays on a fixed-fee basis, the risk of inefficiency falls squarely on the outside lawyer.

The outside lawyer obviously benefits from improved efficiencies in such a fixed-fee environment, but the in-house counsel does as well because he or she can ask for a reduced fixed-fee to share in the cost savings arising from the technology-assisted efficiencies. So in-house counsel should be requiring outside firms to adopt more legal tech solutions in order to provide better quality work product at a more competitive price.

But the benefits of the in-house applications of legal tech are perhaps even more compelling as legal tech solutions will free up in-house counsel from a tremendous amount of mind-numbing repetitive lower-end legal work so that they can focus more on higher-end strategic work. This will raise satisfaction levels on both the part of the in-house legal counsel and on the part of the in-house clients, who will more readily recognise the contributions of the in-house legal team.

At docQbot we are focusing on two fundamental and complementary legal tech tools – automated bilingual contract generation (using HotDocs) and automated English-language contract review (using LegalSifter). Our automated contract drafting tool was originally designed with the Chinese outbound investor in mind, but it works equally as well for FDI and even domestic transactions for foreign-invested enterprises [FIEs] in China, all of which need English and Chinese contracts.

One thing we have learned is that legal tech tools need both strong tech and strong knowhow content. We work with leading technology partners and we bring the content that meets international standards while still conforming to local best practices in China. We are still at the pre-launch stage but already have users all across China.

the rooster talking with the goose – they don't speak the same language. So we decided that we would be better served if we bundled our "legal risk" issues together with business strategy and finance and tax issues, which might more naturally attract the attention of the senior management team.

To a large extent, that vision has been realised – the CGGT has more than 35,000 followers on its public WeChat account, 80% of whom are senior business managers in Chinese companies, and recently we were named by the State Information Centre as a top 10 private thinktank for the Belt and Road Initiative. We also work with many top international and domestic investment banks, accounting firms, risk management consultants, law firms and other professional advisory firms across a wide range of specialisms.

The ironic thing is that it turns out that all of the other professional advisers felt the same need to be able to communicate their value proposition to senior management of Chinese companies in order to be able to be brought in earlier in the process so as to help avoid common problems. So in some respects we are all in the same boat.

As a co-founder in the legal tech platform docQbot, could you please comment on how you see

We think this will help accelerate the pace of change in legal tech adoption in China, and looking out another 10 to 20 years, we expect that legal tech will completely change the landscape of the legal profession in China. It is an exciting time.

You said at the Beijing In-House Congress in March that the new Foreign Investment law potentially ushers in a second golden age for FDI work over the next decade. Please share your vision.

The immediate catalyst for the recently adopted Foreign Investment Law (FIL) is the US-China trade talks. The new FIL is essentially a high-level statement of policy in order to codify commitments by the Chinese side to open up further, to strengthen the legal regime, principally in terms of IP protection and finally (and perhaps most importantly) to provide national treatment for foreign companies in China.

Before the new FIL takes effect on January 1 2020, quite a few additional steps will need to be taken, including not only the adoption of implementation regulations to fill in the not insignificant gaps in the FIL, but also the issuance of a new negative list specifying industry sectors that will be newly opened to increased foreign investment. Much of the focus in this regard is correctly placed on the services sector, and two areas within the services sector which in my opinion are ripe for further opening up are internet-related business and legal services. The market position of the domestic players in these two subsectors are already essentially unassailable, so further opening will not change the overall market dynamics but will give welcome new opportunities for foreign players.

However, this alone would not be enough to ignite a second wave of heightened FDI. The key driver will be the implementation of the principle of national treatment. Although not yet announced, it is my personal assessment that as part of the new sets of rules, the thin-capital rules and restrictions on use of forex capital contributions for downstream investments, which apply only to FIEs and not to domestic companies, will also need to be repealed. These two changes will open up a massive restructuring of foreign investments in China to allow a much more level playing field in China.

The final factor is the pending changes in corporate governance for FIEs. These have always been subject to the now almost archaic laws that were set up 30 years ago when China was just emerging from a planned-economy system. These old-style investment vehicles have proved to be stable and sustainable for the most part, but are still much too cumbersome in terms of actual operation. Upon the effectiveness of the new FIL, these old laws will be repealed and all FIEs will fall under the Company Law,

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which provides significant additional flexibility in terms of corporate governance, principally in terms of reduced levels of minority shareholder protections.

The one element of the new FIL that is not getting sufficient attention in my view is the requirement that within five years after the effectiveness of the new law, all FIEs will be required to convert into LLCs under the Company Law. For wholly-owned subsidiaries of foreign companies (referred to as WFOEs in China), this should be a relatively straightforward administrative exercise (so far as any administrative matter in China can be considered straightforward!), but for Sino-foreign joint ventures, this will entail a complete reworking of the constitutional documents. The old-style equity joint venture contracts were drafted to meet the soon-to-be defunct and often quirky requirements of the equity joint venture law, so those will all be consigned to the dustbin, to be replaced by a more international style shareholders agreement, which will of necessity need to be amended to reflect the changed corporate governance provisions that will now apply under the Company Law.

As we all know, once you start to make some changes to a document, the flood gates are opened and every irritant from the prior years of operation will all surface, begging to be addressed. So this will be a headache for in-house counsel and a boon for outside counsel as the new FIL eventually triggers a massive renegotiation of the joint venture contracts for 120,000-plus joint ventures all across China over a five-year period.

All of these points taken together should, I think, qualify as a basis for a second golden age of FDI in China!

What is your hinterland?

I was born and raised in suburban California and always had an unreasonable fear of urban environments growing up, so it is still surprising to me that I am now most content if you were to drop me in the middle of any big city in China or indeed almost anywhere in the world and just let me wander the streets, taking in the rhythm and pace of city life in all its varieties and complexities. Each city is in many respects a living museum, a tableau of everyday life of real people. I find it to be a never-ending delight.