

## Finding Your Groove In Chinese Dealmaking

By **Kerry Houghton and Kai Wang** (January 25, 2018, 1:46 PM EST)

The role of law firms and outside counsel in China is evolving rapidly. Nowhere is this more apparent than in the realm of multinational business ventures. Responding to the enormous growth and expansion of the Chinese economy and the globalization of companies like Alibaba, HNA, Anbang and WeChat, elite Chinese law firms (often referred to as Red Circle firms) have stepped up their games.

International law firms with offices in China have taken note and are actively trying to respond and adapt to a dynamic marketplace, as we saw with the merger of Dentons and Dacheng, which gave birth to the world's largest law firm. In-house lawyers at multinational corporations operating in China are the main beneficiaries of this trend, as the quality and efficiency of outside legal advice in China have improved markedly in just the past few years. This trend is likely to continue.

What does this mean for internal and external business lawyers advising MNCs and large enterprises on Chinese deals? They must recruit, hire and retain people with not only conventional legal skills but, more importantly, a strong capacity for empathy, because it is an essential quality in one's ability to adapt to change and embrace innovation. They must build genuine relationships with co-counsel and clients so they can advise from within, rather than pontificating from the outside. The best business lawyers add enormous value in deal-making if they can make the transition from "hired gun" or "compliance verifier" to strategic partner. There has never been a bigger opportunity in China to do this than right now.



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### Emergence of Red Circle Firms

Not long ago, even the largest domestic firms in China were perceived as "local counsel" on major deals like MNC joint ventures with local partners and large-scale inbound investments. Now, the Red Circle firms are competing successfully for lead counsel roles and they are doing so because they offer a compelling service. They are focused on delivering practical, solution-driven, real-time advice rather than lengthy memos and somewhat arcane formalism. The business, legal and regulatory landscape in China is rapidly changing. It is challenging to remain relevant and to meet the varying demands of a wide range of legal "consumers" in this complex legal marketplace. Those lawyers and law firms that have survived and excelled in this environment are certainly worth their weight in gold.

This trend should cause concern among international law firms in China because historically, MNCs engaged international firms in Beijing, Shanghai and Hong Kong to provide holistic, strategic guidance to help the business teams interpret and manage the more technical advice provided by local counsel. But this is no longer the case.

What's driving this evolution of the legal marketplace in China? Rapid globalization of the Chinese economy, huge growth in foreign direct investment, expansion of outbound investment by Chinese companies, and, most relevant perhaps, the migration of well-trained, highly skilled and bilingual legal talent from international firms to China's domestic law firms. In addition, there is increasing complexity in the regulatory landscape in China, with compliance, data privacy, antitrust, product liability and intellectual property among the rapidly changing areas of law. This is forcing counsel to develop and provide more integrated vantage points to effectively counsel businesses. The stakes are higher today than a decade ago and the ability to provide comprehensive advice is no easy task. Demand for compliance expertise is a particularly strong trend in response to increased oversight activity by government agencies. "Foreign companies in China are getting increasingly jumpy about a spate of antitrust and corruption investigations by Chinese authorities and are hiring lawyers to make sure their operations comply with the law."<sup>[1]</sup>

### Discovering Empathy

Microsoft CEO Satya Nadella views empathy as a key driver of innovation as well as a necessary quality for a successful leader. "Empathy makes you a better innovator," said Nadella. "If I look at the most successful products we have created, it comes with that ability to meet the unmet, unarticulated needs of customers."<sup>[2]</sup>

This is also true for the legal market. The ability to empathize is vital for both in-house and outside lawyers who service clients or deal with counterparts coming from a different legal culture. Having the ability to understand the needs of the client (as seen from the client's perspective) is essential, even when the client does not fully understand his or her own needs. This goes beyond just feeling their pain and seeing their challenges. It means sitting down with the business team and learning how they perceive and assess specific risks and opportunities.

Even when everyone in a room is looking at the same information, each individual often sees different implications depending on their roles and experience. "People perceive things differently. We choose to select different aspects of a message to focus our attention based on what interests us, what is familiar to us, or what we consider important."<sup>[3]</sup>

Empathy facilitates trust, trust leads to transparency, and transparency leads to optimal legal and regulatory advice and decision-making. The "empathic lawyer" might have been an oxymoron years ago, but it is now the gold standard in elite legal practices. "You cannot take even one of the most successful business models and transplant it into new contexts. You need to have the humbleness to build empathy and understand the 'job to be done' for the customers in their context."<sup>[4]</sup>

### Strengthening Law Firm/In-House Counsel Partnerships

We have seen a substantial increase in the talent and capacity of Chinese law firms to step into the shoes of their multinational clients. In most cases, those clients are also represented by in-house counsel. A genuine connection between outside and inside lawyers is where we see the biggest opportunity for the kind of creativity that leads to practical solutions and successful deal negotiations.

When in-house counsel partners with outside lawyers by bringing them into the mindset and culture of the business, the resulting work product is far superior to what is produced in a more transactional relationship. This is critically important in establishing and building complex relationships between MNCs and Chinese partners. JVs are particularly tricky to navigate, and the best ideas can be lost in poorly conceived ventures between partners who do not understand each other or who do not have a shared vision of success.

### Cultural Awareness

While it is axiomatic that understanding cultural context and nuance is an essential component to any company's compliance program, this capacity is also critical to high-stakes deal-making and negotiations. Cultural exchange requires going beyond the obligatory client dinners or hiring bilingual lawyers. The best deal lawyers in China have an insider's perspective on local history, judicial systems, regulatory structure, national policy goals, consumer preferences, and a deep understanding of the relationship dynamics between or among the various parties and the internal corporate culture of a given client.

The most successful deals in China are those negotiated from a deep understanding of the shared and distinct goals and objectives of each partner. This is possible when a deep well of trust is developed by investing the time to gain that understanding.

For example, our team's biggest challenge and top priority in building our in-house team at Starwood Hotels & Resorts Worldwide in greater China was finding the right talent with the attributes we valued and who could learn the practical skills by doing the work. We spent an incredible amount of time recruiting and attracting lawyers and supporting staff who had both the local knowledge and the international exposure to succeed in this new paradigm.

### Conclusion

The market for legal services in China is growing in size and complexity at a rapid pace. An enormous opportunity exists for firms and in-house counsel to take on more responsibility and to position themselves as essential strategic partners to senior executives and board members. In order to capitalize on this opportunity,

international law firms must hire and develop attorneys who understand the technical nuances of the legal landscape, appreciate the cultural idiosyncrasies, and have the sense of empathy necessary to develop genuine partnerships with their clients.

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[1] Reuters, "Rattled by investigations, foreign firms in China beef up compliance."

[2] Fortune.com, "Microsoft CEO Satya Nadella Says Empathy Makes You a Better Innovator,"

[3] Saylor.org, "Differences in Perception."

[4] Humanomics.co, "Why Foreign Retailers Stumble in China: Lack of Empathy."