

THE LEGAL SERVICE MARKET IN CHINA:
IMPLEMENTATION OF CHINA'S GATS COMMITMENTS AND
FOREIGN LEGAL SERVICES IN CHINA

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I. INTRODUCTION

This paper examines the legal service market in China, especially the market share of foreign legal service providers (FLSP), in the context of China's membership with the World Trade Organization (WTO). China joined the WTO on 11 December 2001. As part of accession commitments, China agreed to open its service market, gradually and conditionally, to its fellow WTO members under the General Agreement on Trade in Services (GATS).¹ Legal services are the very first ones to appear in China's schedule of commitments.²

China's fast growing economy relies largely on foreign investments and international trading. The involvement of foreign legal services in this regard is indispensable. Especially at the moment, language remains the major obstacle for the communication between business partners in the East and West. From a foreign investor or trading partner's perspective, it is simply too risky to leave matters of legal consequence to lawyers who do not speak the same language. Furthermore, the Chinese legal system and legal profession have not reached the level of maturity that could command the confidence of foreign investors and trading partners.

Foreign legal services are a necessary supplement to the legal services provided by Chinese legal professionals. However, they threaten to derail or at least forestall the development of the infantile Chinese legal industry with their overwhelming financial and organizational strength. A struggle between Chinese legal profession and its foreign counterparts is bound to ensue. State intervention will be vital for the survival of the Chinese legal profession. But how will the Chinese authority balance this interest with its obligations as a member of the WTO?

¹ General Agreement on Trade in Services, Apr. 15, 1994, 1869 U.N.T.S. 183 (GATS).

² The People's Republic of China Schedule of Specific Commitments, GATS/SC/135 (Feb. 14, 2002), *available at* http://docsonline.wto.org/GEN_highLightParent.asp?qu=+%28%40meta%5FSymbol+GATS%FCSC%FC%2A%29+and+%28%28+%40meta%5FTitle+China+%29+or+%28%40meta%5FCountries+China%29%29&doc=D%3A%2FDDFDDOCUMENTS%2FT%2FSCHD%2FGATS%2DSC%2FSC135%2EDOC%2EHTM&curdoc=9&popTitle=GATS%2FSC%2F135.

Four modes of supply – through which cross-border delivery of services are realized – were incorporated into GATS.³ Three of the four – Cross-border Supply, Commercial Presence, and Temporary Movement of Natural Persons – are relevant to this topic. The discussion will focus on Commercial Presence, which is the delivery of legal services through direct foreign investment. Since the delivery of legal service on aspects other than Chinese law does not rely on access to the Chinese legal service market, our discussion will be confined to legal services concerning only Chinese law. We will take a close look at the effect of the presence of FLSP on the Chinese legal service market, and the discrepancies between China's WTO commitments and their implementations in reality.

This paper is set in the context of the conclusion of China's Cultural Revolution and its subsequent adoption of the open door policy. Part II provides background information, including the development of China's legal profession alongside its economic reform. Part III examines the challenges facing the Chinese authority: on one hand, they are under the mounting pressure of globalization and its WTO obligations to liberalize its service market; and on the other, the state's interest of protecting an infant industry and the political interest of keeping the society under the tight grip of the Communist Party. Part IV examines the scope of China's GATS Commitments. Part V examines China's domestic legislative measures for the implementation of its GATS Commitments. Part VI looks at the effect of the implementations, including the current status of the legal service market, and whether or not China has delivered on its promises. Part VII looks at the unique position of legal service providers from China's Special Administrative Regions (SAR), and its implication on the future of FLSP in China. Part VIII expresses the author's opinion as to the future of China's legal reform and its legal profession as the conclusion of the paper.

II. BACKGROUND

Any legal system must be assessed within its historical and cultural context.⁴ In examining the Chinese legal system, one must take into consideration the effect of China's Cultural Revolution, because its impact continues to be seen and felt in every aspect of

³ “The four modes of supply were identified by American advocates for free service trade, now found in GATS Article I:2(a)-(d). They are: Mode 1. Cross-Border Supply; Mode 2. Consumption Abroad; Mode 3. Commercial Presence; and Mode 4. Temporary Movement of Natural Persons.” RAJ BHALA, *INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE: DOCUMENT SUPPLEMENT* 490 (3d ed. 2008).

⁴ JIANFU CHEN, *CHINESE LAW: CONTEXT AND TRANSFORMATION* 6 (2008).

public as well as private life in China. The Cultural Revolution is a period of 10 years between 1966 and 1976 where, to the extent this paper is concerned, legal scholars and professionals, along with other intellectuals, were brutally persecuted by the state sanctioned acts of the Red Guards.⁵ The Cultural Revolution practically reduced China to a lawless society and made it particularly difficult to restore law and order in the subsequent reconstruction of the nation.

As a result, legal services as a free standing profession were not commonly known to the Chinese people until the end of twentieth century. Traditionally, the legal system in China was an insignificant executive organ. Lawyers and judges were state employees who were under the duty to serve the interest of the state. In modern China, state interest is virtually indistinguishable from the interest of the ruling Communist Party.⁶ Law and the legal system were not orientated to facilitate the everyday life of the common people, but rather as an instrument to safeguard the stability and harmony of the society so as to perpetuate the control of the Communist Party.

China's recovery efforts started with the open door policy. After 10 years of failed attempts to build an ideal communist society, China's leadership finally came to realize that isolation from the global community was not in the best interest of China – a nation with a worldly ambition. Immediately after the conclusion of the Cultural Revolution, Communist China adopted the so-called Open Door policy under the leadership of Deng Xiaoping, and began its effort to rejoin the global society through economic reforms. Unexpectedly, the Open Door policy unleashed the world's potentially most powerful economy. China's economy suddenly threatened to overtake that of the United States – then and now the world's largest economy.⁷ With fast growing cross-border transactions, legal infrastructure became critically important.

Based on conventional wisdom, one would assume that two most important components of a society – its economy and its politics – would evolve concurrently as they depend upon one another. China, however, has proven that separation of economy and politics is not impossible.⁸ China's economic reforms adopted a capitalist approach, going from strictly state owned enterprises and planned economy to privatization and free trade in an open market. In order to show consistency with its socialist political ideology, China

⁵ The Red Guards were organized Chinese youth in the form of paramilitary, mobilized by the founding father of modern China Mao Ze Dong to persecute opponents in a political power struggle.

⁶ “Well, according to Peng Zhen, then Chairman of the Standing Committee of the NPC, law is an important and necessary tool for implementing Party policies” CHEN, *supra* note, at 52.

⁷ *Id.* at 621.

⁸ See discussion *infra*, where it is explained that this will be a short lived phenomenon. Without proper political structure, sustainable economy growth is impossible.

labeled its economy as a “socialist market economy with Chinese characteristics.”⁹ In other words, it implemented a capitalist style economy without the democratic political system which often comes as part of a capitalist society. China maintains a single party political system, which is sometimes labeled as a ‘democratic dictatorship.’¹⁰ As we will see in Part III, this seemingly brilliant invention of China’s Communist Party is becoming increasingly problematic in its endeavor to fulfill WTO obligations, especially in the liberalization of the legal service market.

III. THE CHALLENGES

Chinese culture is uniquely rooted in the teaching of Confucius. Law and its enforcement are traditionally seen as confrontational, hence inherently violent. They are repugnant to an orderly society where harmony and stability may be achieved by people’s adherence to the good nature of man. Coupled with profound distrust in the impartiality of the state officials, the acceptance of rule of law by the general public would be slow. However, China’s WTO obligations to implement its GATS Commitments and open its legal service market left it no choice but to embark on a journey of legal reform.

Factors and considerations that must be taken into account in deciding what measures to take for the reform are pulling in two opposite directions. From China’s perspective, on the one hand, it has to recognize the fact that foreign capital is often accompanied by legal advisers for the protection of the investors’ economic interests. Legal services themselves have their own economic value, hence exchange of legal services can be an additional source of income for China. More importantly, liberalizing the legal service market is an act in conformity with its effort to further integrate itself into the global society. However, on the other hand, inviting foreign legal services into China also invites foreign underlying ideologies which Chinese authority perceives as threatening to its political control. The Chinese authority has long endeavored to keep such information beyond the reach of China’s social media, and in turn, the Chinese public.

The challenges facing the Chinese authority are multifold. Tensions between protectionism and liberalization are at the top of the list. Due to the short history of modern China and the disruption of the Cultural Revolution, the legal profession is still in its infancy. State intervention is needed to safeguard against sophisticated

⁹ Guiguo Wang, *China’s FTAs: Legal Characteristics and Implications*, 105 AM. J. INT’L L. 493, 494 (2011).

¹⁰ Evan Osnos, *A Dictatorship Without A Dictator*, NEW YORKER, Jan. 18, 2011, <http://www.newyorker.com/online/blogs/evanosnos/2011/01/a-dictatorship-without-a-dictator.html>.

foreign competitors. However, WTO obligations require member states to provide a level playing field which requires the state to refrain from any form of intervention. Although under the WTO regime, the scope of market access in the service sector is left for the member states to decide themselves, the WTO's expectation of liberalization is loud and clear.

The concern of national security is especially problematic. Western-style, especially American-style, litigation emphasizes creative thinking, critical analysis and readiness to challenge authority. These characteristics do not fit well with Chinese style governance. In western democratic countries, the concept of national security is normally narrowly defined in order to facilitate free flow of information. In China, to the contrary, any matter which potentially threatens the stability of the society or the political power of the Communist Party may be dealt with under the name of national security.¹¹ This makes certain areas of economic interest potentially sensitive, such as cultural products and governmental procurement, as well as in the area of legal service where legitimacy of authority or fairness of legal procedure are issues which determine the outcome of a conflict. Legal service providers will find themselves walking the fine line between zealous representation for the interest of their clients and being accused of national security violation by the Chinese authority.

Potential loss of talent and market share to foreign competitors is also a practical concern. Once the Chinese legal service market is accessible, those foreign law firms with strong economic background will be the front runners to claim market share. Foreign investors and trading partners are likely to retain well established foreign law firms for their services for obvious reasons, such as pre-existing lawyer-client relationship and lack of language barrier. While in the meantime, China's newly established legal profession is filled with freshly qualified Chinese lawyers who, although legally qualified, may nevertheless lack international practice experience and managerial skills to compete. Foreign law firms offering a higher salary and a more prestigious portfolio of clients will undoubtedly be more attractive to young Chinese law graduates than their Chinese counterparts. In time, the market will be dominated by large foreign law firms.

Inherent inconsistency among different pieces of legislation is a constant challenge to the users of the Chinese legal system. So far, legal reforms in China are largely dictated by practical needs to

¹¹ See generally Denny Roy, *Human Rights as National Security Threat: The Case of The PRC*, 32 ISSUES AND STUDIES 65 (1996), available at <http://iir.nccu.edu.tw/attachments/journal/add/4/v32-2-4.pdf>.

facilitate economic reforms. To keep up with the fast growth of the economy, large bodies of law must be produced within short periods of time, resulting in fragmentation and ad hoc legislation. Lack of systematic legislative structure and training further contribute to inconsistency in legislations.¹²

The above are just some of the challenges and concerns that might fetter China's ability to fulfill its WTO obligations. The following Parts will discuss how China is to balance these competing interests.

IV. SCOPE OF CHINA'S GATS COMMITMENTS

Practically speaking, China's accession to WTO was not an option. Without the preferential treatment afforded through WTO membership, China was losing out on its export front. At the same time, without the participation of the world's largest exporter and consumer population, the WTO was less global than it aspired to be. The WTO needed China as much as China needed the WTO. Director-General of the WTO, Pascal Lamy, confirmed as much at the ceremony of China's 10-year membership, stating that "China has been and should remain important for WTO. WTO has been and should remain important for China."¹³

China's commitments to creating access to the legal service market is stated in Corrigendum to the Schedule of Specific Commitments.¹⁴ The Schedule focuses on legal services provided through Mode 3 – Commercial Presence, i.e. services provided through direct foreign investment.¹⁵ The manner in which FLSP are permitted to operate in China's legal service market is via representative offices.¹⁶ The scope of services permitted by FLSP is as follows:

To provide clients with consultancy on the legislation of the country / region where the lawyers of the law firm are permitted to

¹² CHEN, *supra* note, at 54.

¹³ Pascal Lamy, Dir.-Gen. of the WTO, A New Chapter in China's Reform and Opening Up to the World, (Dec. 11, 2011), available at http://www.wto.org/english/news_e/sppl_e/sppl211_e.htm.

¹⁴ The Corrigendum of the Schedule of Specific Commitments of the People's Republic of China, GATS/SC/135/Corr.1 (Feb. 20, 2003), available at <http://www.esf.be/pdfs/GATS%20UR%20Commitments/China%20Services%20Commitments%20-%20cqr%20legal%20serv.pdf>.

¹⁵ Raj Bhala, *International Trade Law: Interdisciplinary Theory and Practice* 1545-47 (2008). China places no restriction on Model 1. Cross-Border Supply, and Mode 2. Consumption Abroad; but makes no commitment on Mode 4. Temporary Movement of Natural Persons except those stated in the Horizontal Section. See also *supra* note.

¹⁶ See GATS List of Telecommunications Commitments and Exemptions - China, GATS/SC/135 (Feb. 14, 2002), available at http://www.wto.org/english/tratop_e/serv_e/telecom_e/telecom_commit_exempt_list_e.htm.

engage in lawyer's professional work, and on international conventions and practices;

To handle, when entrusted by clients or Chinese law firms, legal affairs of the country / region where the lawyers of the law firm are permitted to engage in lawyer's professional work;

To entrust, on behalf of foreign clients, Chinese law firms to deal with the Chinese legal affairs;

To enter into contracts to maintain long-term entrustment relations with Chinese law firms for legal affairs;

To provide *information on the impact of the Chinese legal environment*.

Entrustment allows the foreign representative office to directly instruct lawyers in the entrusted Chinese law firm, as agreed between both parties. Further restrictions are imposed on personnel who work in such representative offices, namely that foreign law firms may not employ Chinese practicing lawyers.¹⁷

As it appears, the description of business scope within which foreign representative offices may operate is stated in positive language: instead of general permission with exclusion in certain areas, it only allows access to enumerated areas. The rest is off limits.

An examination of China's commitments under GATS reveals a substantially limited scope for representative offices of foreign law firms to operate in the Chinese legal service market. Clause (a) and (b) address the application of foreign and international law. Clause (c) addresses the application of Chinese law. Clause (d) permits foreign law firms to form long-term contractual relationship with Chinese law firms to provide legal services jointly.¹⁸ The precise meaning of Clause (e) is unclear on its face. As it turns out, Clause (e) is the key provision that stages the battle ground for the competing sides of the market share, namely the FLSP and their Chinese counterparts.

According to Clause (a) through (c), in a typical cross border transaction between a foreign and Chinese commercial party, the foreign aspect of the transaction is to be handled by the foreign lawyers of a representative office. The Chinese aspect of the transaction is to be handled by Chinese law firms through the method of entrustment.¹⁹ That leaves us with the conclusion that issues of

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¹⁸ *Id.*

¹⁹ Clause (d) is unrelated to the allocation of market share; further analysis is thus beyond the scope of this article.

Since the discussion of this paper focus on the operation of FLSP as business entities and not individual foreign lawyers, it will not consider the possibility that individual foreign lawyers may provide legal services through the employment within Chinese law firm; in any event, such an employment arrangement is highly uncommon.

Chinese law are to be handled solely by Chinese lawyers who work in Chinese law firms. There is thus a clear line of demarcation drawn in the middle of a cross border transaction, the foreign aspect of the transaction at one end and Chinese aspect at the other. Correspondingly, foreign law firms at one end and Chinese law firms at the other.

In the eyes of many, such arbitrary allocation of business opportunities would seem unreasonably restrictive, especially in the eyes of FLSP who were otherwise planning to expand their business in this newly opened market. Thankfully, this is not the end of the story. Clause (e) permits one type of service that concerns Chinese law to be directly provided by a foreign law firm, that is: to provide information on the impact of the Chinese legal environment (Environment Clause).²⁰ However, foreign law firms are not permitted to hire practicing Chinese lawyers.²¹ Since legal certification in China is not open to foreign nationals,²² the possibility of foreign lawyers providing legal service in relation to Chinese law virtually does not exist. For a Chinese lawyer who works in a foreign law firm to provide such information, he must have foregone his right to practice. While this may seem unduly restrictive, China is far from the only GATS signatory with such provisions.²³

As discussed above, the allowance given to foreign law firms for their real participation in the Chinese legal service market is extremely limited. In the area of employment, foreign law firms may only hire, Chinese lawyers who do not practice or are willing to forego their right to practice. In the area of operations, foreign law firm may only provide, in terms of Chinese law, “information on the impact of the Chinese legal environment.” Although the Environment Clause is somewhat ambiguous, this carefully chosen terminology as the core content of the permissive Clause is unable to disguise China’s protectionist intent to preserve a significant market share for its own legal profession.

As a result of these narrowly drafted Commitment Clauses, the application of Chinese law is almost exclusively the domain of

²⁰ The Environment Clause reads, in relevant portion:

Article 33. When providing information concerning the impact of the Chinese legal environment in accordance with subparagraph (5) of Article 15 of the Administrative Regulation, representative offices and their representatives *may not provide specific views or conclusions on the application of Chinese law*.

²¹ *Id.*

²² Guojia Sifa Kaoshi Shishi Banfa (国家司法考试实施办法) [Regulations on National Judicial Examination] (promulgated by St. M. J., Aug. 14, 2008, effective Aug. 14, 2008) art. 15(1), http://www.moj.gov.cn/index/content/2008-08/14/content_923571.htm?node=7337 (China) (stating that examinees of the National Judicial Examination must be of Chinese nationality).

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¹ PHILIP RAWORTH, INTERNATIONAL REGULATION OF TRADE IN SERVICES § 36 ¶ 55 (2012).

practicing Chinese lawyers. Since foreign law firms may not employ Chinese practicing lawyer, this means that a foreign client with an issue of substantive Chinese law will have to engage a Chinese law firm for advice either directly or via a foreign representative office through the Entrustment Clause. Either way, the profit of such services is guaranteed to go to the Chinese law firm.

Balancing competing interests is never an easy task. China wants to show the WTO that it is fulfilling its membership obligations by opening its legal service market, while simultaneously withholding access to this market by imposing stringent conditions on foreign law firms so as to keep a significant share of the market beyond the reach of foreign competitors. China's sincerity to truly open its market is questionable. The permitted scope of operation is so disproportionate that it falls short of the expectations of the FLSP. Not only did the official allocation of market share fail to guide the FLSP to enter into the market smoothly as it was supposed to, but it also incited a war between foreign and Chinese legal service providers.²⁴ The ambiguity of the Environment Clause became the perfect battle ground.

V. DOMESTIC LEGISLATION ON LEGAL PROFESSION

A. A brief history on the modern Chinese legal profession

Demand for a functioning and identifiable legal system came unsurprisingly with the economic reforms. As discussed above, the absence of law and a robust legal system at the beginning of the Open Door policy posed a serious challenge to Chinese economic reform ambitions. Although the legal profession had started to reform, it did not develop at the same pace as did China's economy. This is because China's unique socialist ideology and the existing political structure predetermined that the accompanying legal reforms will be at odds with its plan to rejoin the global community.

For most of the first two decades, the development of China's legal profession, being fundamental for its continuing growth, was unimpressive to countries that had well established and mature legal systems. Traditionally in China, lawyers were perceived as state officials. In 1980, the Interim Regulations of the People's Republic of China on Lawyers (the Lawyers' Law) defined Chinese lawyers as "state legal workers."²⁵ It was not until 16 years later, in 1996, when the official version of the Lawyers' Law was passed and replaced the

²⁴ See Andrew Godwin, *The Professional 'Tug of War': The Regulation of Foreign Lawyers in China, Business Scope Issues and Some Suggestions for Reform*, 33 MELB. U. L. REV. 132 (2009).

²⁵ CHEN, *supra* note, at 162.

Interim Regulations.²⁶ During those 16 years, the All-China Lawyers' Association was established, the licensing examination for lawyers was introduced,²⁷ and the first law firm was established in Shanghai.²⁸

The first Lawyers' Law redefined Chinese lawyers as legal professionals whose service, for the first time in Chinese history, are made generally available for the protection of private interests.²⁹ China's legal profession did not actually take off until the late 1980s, when China had only a few dozen of state-owned law firms and several hundred lawyers.³⁰ Today, China claims to have a legal community of staggering 600,000 members.³¹

B. Initial legislation implementing GATS Commitments

China's GATS Commitments are neither directly applicable nor have the "self-executing effect" domestically.³² Domestic legislation implementing these Commitments is necessary for their implementation. The first implementing legislation is the Regulations on Administration of Foreign Law Firms' Representative Offices in China (Administrative Regulations) in 2001.³³

²⁶ See *Lüshi Fa* (律师法) [Lawyers Law] (promulgated by the Nat'l People's Cong., May 15, 1996, effective Jan. 1, 1997), and *Quanguo Renmin Daibiao Dahui Changwu Weiyuanhui guanyu Xiugai Zhonghua Renmin Gongheguo Lüshi Fa de Jueding* (全国人大常委会关于修改《中华人民共和国律师法的决定》) [The Decision on Amending Lawyers Law] (promulgated by the Standing Comm., Nat'l People's Cong., Dec. 29, 2001, effective Jan. 1, 2002) (Lawinfochina) (China).

²⁷ Weng Li, *Philosophical Influences on Contemporary Chinese Law*, 6 IND. INT'L & COMP. L. REV. 327, 328 (1996).

²⁸ Joseph W. Dellapenna, *The Role of Legal Rhetoric in the Failure of Democratic Change in China*, 2 BUFF. J. INT'L L. 231, 252 (1996).

²⁹ Melissa S. Hung, *Obstacles to Self-Actualization in Chinese Legal Practice*, 48 SANTA CLARA L. REV. 213, 218-19 (2008).

³⁰ CHEN, *supra* note, at 162.

³¹ Roderick O'Brien, *China Law: Towards a Legal Professional Community in China*, 41 H.K.L.J. 573, 574 (2011).

³² Jane J. Heller, *China's New Foreign Law Firm Regulations: A Step in the Wrong Direction*, 12 PAC. RIM L. & POL'Y J. 751, 766 (2003).

³³ Regulations on Administration of Foreign Law Firms' Representative Offices in China (promulgated by the State Council, Dec. 22 2001, effective Jan. 1, 2002). The relevant portion reads as follows:

Article 15. A representative office and its representatives may only conduct the following activities that do not encompass Chinese legal affairs:

To provide clients with the consultancy on the legislation of the country where the lawyers of the law firm are permitted to engage in lawyer's professional work, and on international conventions and international practices;

To handle, when entrusted by clients or Chinese law firms, legal affairs of the country where the lawyers of the law firm are permitted to engage in lawyer's professional work;

To entrust, on behalf of foreign clients, Chinese law firms to deal with the Chinese legal affairs;

To enter into contracts to maintain long-term entrustment relations with Chinese law firms for legal affairs;

To provide information on the impact of the Chinese legal environment.

Four additions were inserted into this legislation. The additions are of great significance. They further clarify and narrow down the permissible business scope for foreign law firms.

First, China's GATS Commitments do not contain the phrase "activities encompass[ing] Chinese legal affairs."³⁴ The only language in relation to Chinese law is the Environment Clause, which mandates that foreign law firms may only provide "information on the impact of the Chinese legal environment."³⁵ As discussed above, GATS Commitments positively provides a list of activities that foreign law firms may conduct, and the only service in relation to Chinese legal affairs that may be directly provided by foreign representatives are stated in the Environment Clause. Hence, this conditional phrase of "activities encompass[ing] Chinese legal affairs" (Conditional Clause), although being placed in the general heading which governs all the subsections that follow, indeed applies only to the Environment Clause. It is generally agreed that the Conditional Clause is added to further define the scope of the Environment Clause, not expand upon it.

Having read the Conditional Clause with the Environment Clause together carefully, the only logical conclusion is that that the Conditional Clause does not only clarify the Environment Clause, but also narrows down its scope. The word "environment" is a broad concept. It is defined in Merriam Webster as: "the circumstances, objects, or conditions by which one is surrounded; or the aggregate of social and cultural conditions that influence the life of an individual or community."³⁶ The ambiguity of the word "environment" lies in its all-inclusive nature while as well as its lack of clearly identifiable substance.

The Conditional Clause excludes an identifiable area of service, that is the "activities encompass[ing] Chinese legal affairs," from the all-inclusive and wide-ranging coverage of the word "environment." This exclusion is significant. Legal activities encompassing Chinese legal affairs constitute the core area of services that the Chinese legal service market provides, including legal advice on the application of

Representative offices may directly instruct lawyers in the entrusted Chinese law firms, as agreed between both parties.

A representative office and its representatives shall *not conduct any legal service activities or other for-profit activities other than those set forth in the first paragraph and the second paragraph of this Article.*

Article 16. A representative office shall not employ Chinese practitioner lawyers; its *support staff employed shall not provide legal services to clients.*

³⁴ GATS, *supra* note, at 2.

³⁵ *See id.*

³⁶ *Definition of environment*, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/environment> (last visited Dec. 15, 2012).

substantive Chinese law. Such heavy-handed exclusion is analogous to prohibiting a practicing doctor from prescribing medicine to his patients. This means, in a typical cross-border transaction, a foreign law firm may not provide service on the Chinese aspect of the transaction.

Second, the GATS Commitments use the word “international” as an adjective immediately preceding the nouns “conventions and practices” as permissible activities. The Administrative Regulations inserted an additional “international” immediately before the word “practice.”³⁷ This addition clearly reveals the legislative intention to prevent potential misinterpretation of the scope of the word “practice.” As a result, no one can now argue that the word “practices” permits activities beyond the scope of “international.” It is an act of extra caution.

Third, the GATS Commitments use general language that foreign law firms “can engage in profit-making activities.”³⁸ The scope of profit-making activities includes all the activities enumerated in the Commitments, including (in simple language): 1) consultancy on foreign and international law; 2) legal advice on foreign legal affairs; 3) engaging in Chinese law firms for legal advice on Chinese law; 4) establishing long-term relationship with Chinese law firm; and 5) providing information on the impact of Chinese legal environment.

However, the scope of profitable activities is drastically reduced by the Administrative Regulations to the extent that it now only includes the first two categories, namely 1) consultancy on foreign and international law; and 2) legal advice on foreign legal affairs (Profit Clause).³⁹ Anything else, such as advice on matters concerning Chinese law, even if provided by Chinese law firms and incorporated into the work of foreign law firms as part of a whole package, is now disallowed. Similarly, information on the impact of Chinese legal environment is no longer allowed. The Profit Clause thus effectively eliminates the incentive for foreign law firms to wage a war against Chinese law firms on the Environment Clause as anticipated.

Lastly, in addition to the prohibition that foreign law firms may not employ Chinese practicing lawyers as found in GATS Commitments, the Administrative Regulations further provide that even Chinese supporting staff in foreign law firms may not provide legal services to clients.⁴⁰ This means that not only may a foreign

³⁷ Regulations on Administration of Foreign Law Firms’ Representative Offices in China (2001) Article 15(1), *supra* note, at 12.

³⁸ GATS, *supra* note, at 2.

³⁹ *Id.* at 13.

⁴⁰ Regulations on Administration of Foreign Law Firms’ Representative Offices in China (2001) Article 16, *supra* note, at 12.

law firm not employ practicing Chinese lawyers to advise on issues concerning Chinese law, but also that a qualified Chinese lawyer, who is willing to relinquish his right to practice and act in the capacity of a supporting staff in a foreign law firm, may not give advice on Chinese law. In other words, foreign law firms' ability to advise on Chinese law has been completely stripped away.

The collective effect of the changes made by the Administrative Regulations is obvious. Chinese authority has once again drawn a bright line between the application of foreign and international law on the one side, and Chinese law on the other; foreign law firms on the one side and Chinese law firms on the other. This makes an even larger market share for the Chinese legal profession. Since foreign law firms may not make profit from services in relation to Chinese law, any work of this nature is only profitable (and thus permissible) by Chinese law firms. As such, not only the market share is preserved exclusively for Chinese law firm, but also its profitability will not be compromised by the involvement of foreign law firms.

If the term "Chinese legal service market" is interpreted narrowly to mean legal services concerning Chinese law as opposed to the physical market where law firms of any nationality may come in and conduct business, then there is virtually no access whatsoever to the Chinese legal service market. The entire market is preserved for the benefit of the Chinese legal profession. The example below illustrates this point. Needless to say, these additional restrictions imposed by the Administrative Regulations could potentially expose China to liabilities as the result of violating its GATS Commitments. The member state where a foreign law firm is from may thus resort to the Dispute Settlement procedure and bring its grievance to the WTO against China for breach of its WTO obligations.

Consider the following hypothetical application of the Administrative Regulations in a typical cross-border transaction. In such a transaction, the foreign client needs the services of a foreign law firm to advise on its foreign end of the transaction, which concerns the law of a foreign jurisdiction. At the same time, it needs advice on the Chinese-end of the transaction, obviously concerning Chinese law. Since the foreign law firm may not advise on issues concerning Chinese law, its only recourse is to engage a Chinese law firm to provide such services. Furthermore, since the foreign law firm may not make profit from the advice of Chinese law, the services provided by the Chinese law firm independently fall outside the cost-profit calculation of the foreign law firm. But how about a profit sharing arrangement; would that be permissible? As discussed below, the answer to this question is no.

The Environment Clause has thus been limited by the Administrative Regulations. Although China would like to remove it

altogether so as to provide complete protection for its own legal profession, such removal would be an outright admission of its violation of GATS Commitments. Consequently, China's measures to further limit the market access of FLSP must still comport with its GATS Commitments in order to be defensible.

C. Further legislation implementing GATS Commitments

The Administrative Regulations are only the beginning of China's attempt to narrow the scope of its GATS Commitments. In less than a year after the Administrative Regulations became effective, a set of supplementary rules – Rules for the Implementation of the 'Regulations on Administration of Foreign Law Firms' Representative Offices in China' (Implementing Rules) – was promulgated through an Order of the Ministry of Justice.⁴¹ The Implementing Rules specify activities that constitute "Chinese legal services" – an effort purported to further clarify the scope of the business activities foreign law firms may conduct, and more importantly, to directly address the scope of the Environment Clause.

To ensure compliance, the Implementing Rules prescribe the manner in which foreign law firms must conduct their business. Article 37 compels disclosure to clients by foreign law firms of their inability in advising on Chinese law at the inception of legal services. Article 38 prohibits foreign law firms from using the title of "consultants on Chinese law" for any of their personnel, including Chinese lawyers who have been qualified to practice Chinese law immediately before their employment with the foreign law firm.

Another relevant provision is Article 39, which regulates the relationship between foreign and Chinese law firms restrictively as follows:

Article 39. A representative office and the law firm it belongs to may not conduct the following acts:

⁴¹ Ministry of Justice, Order No. 73, 4 July 2002, http://www.gov.cn/gongbao/content/2003/content_62105.htm (China) (*amended by* Ministry of Justice, Order No. 92, 2 September 2004, http://www.gov.cn/gongbao/content/2005/content_77403.htm (China)). These rules read, in relevant portion:

Article 32. The following activities shall be considered to be 'Chinese legal services' as provided in Article 15 of the Administrative Regulations:

- Participating in litigation proceedings in China in the capacity of a lawyer;
- Providing opinions or certification on specific issues concerning the application of Chinese law in contracts, agreements, articles of association or other written documents;
- Providing opinions or certification on actions or events to which Chinese law applies;
- In the capacity of an agent, expressing an opinion on the application of Chinese law in arbitration activities;
- Representing clients in undertaking registration, amendment, application and filing procedures and other procedures with Chinese government authorities or other organizations that have administrative management functions conferred on them by other laws and regulations.

Directly or indirectly investing in Chinese law firms;
Making practicing associations with Chinese law firms or Chinese lawyers that share the profits or risks.

Establishing joint offices or sending personnel to Chinese law firms to engage in legal service activities.

Managing, operating, controlling or enjoying the equal rights and interests of Chinese law firms.

This article clearly intends that the operation of Chinese law firms must be independent from the influence of foreign law firms.⁴² The converse of this is that any meaningful association between foreign and Chinese law firms is impermissible. Profit sharing in a business partnership is not permitted.

VI. THE EFFECT OF THE IMPLEMENTATION

On its face, the Implementing Rules did nothing to define the outer boundary of the Environment Clause, and thus the ambiguity remained. Instead, the Implementing Rules further *watered down* the inner content of the Environment Clause, which is the only provision that opened the door for FLSP to participate in the Chinese legal service market.

Even a cursory examination of the implementing legislation reveals that China has breached its WTO obligations. The aggregated effect of the Regulations and Rules does not merely narrow the scope of the GATS Commitments to a limited extent, but rather almost completely wipes out the ability of foreign law firms to provide legal services in relation to Chinese law. Foreign lawyers have interpreted the small room for movement under the Environment Clause to permit only newsletters and general reports for clients' marketing purposes.⁴³

The presence of FLSP in China is rendered less meaningful if they are not permitted to profit from domestic legal services. The restrictive tone of the Chinese authority has resulted in a high level of consternation.⁴⁴ In response, a meeting was held by China's Ministry of Justice to clarify the interpretation of the Regulations and Rules. Foreign lawyers were invited to the meeting.⁴⁵

Some sort of "understanding" between China's Ministry of Justice and the foreign lawyers was reached during the meeting. However, with regard to prohibitions, foreign lawyers may not provide authoritative and conclusive opinions on the application of Chinese law on particular legal issues. However, as general advice

⁴² Godwin, *supra* note, at 140.

⁴³ *Id.*

⁴⁴ *Id.* at 141.

⁴⁵ *Id.*

on issues governed by Chinese law falls within the Environment Clause, it is permissible and profitable. Specific concerns were also addressed as follows:

Foreign lawyers would not be in breach of the rules by passing on advice from Chinese lawyers in communication with clients, This is so as long as it is made it clear that the information was based on advice from Chinese lawyers.

Despite the recommendations of Chinese lawyers, the rules do not prohibit foreign lawyers from drafting documents governed by Chinese law, such as joint venture contracts.

Regardless of the effect that foreign lawyers may attribute to disclaimers inserted in their advice, the disclaimers do not allow foreign lawyers to circumvent the prohibition on providing advice on specific issues concerning the application of Chinese law.

Restrictions on the relationships between foreign law firms and local law firms do not rule out flexible fee arrangements, long-term retainer arrangements (under which the foreign firm would effectively act as the 'client') or even the sharing of resources, so long as this does not result in a 'shared-office arrangement.'⁴⁶

The Understandings sound much friendlier than the restrictive tone of the Implementing Rules. In fact, a number of inconsistencies are readily identifiable. For example, drafting of legal contracts and documents governed by Chinese law which were expressly prohibited by the Implementing Rules are now permissible; mandatory disclosure of inability to advise on Chinese law may be disregarded so that the foreign lawyer now can provide legal advice on the application of Chinese law in respect to specific legal issues; even the perceived strict prohibition on all forms of association between foreign and Chinese law firm is also relatively flexible.

However, it is worth noting that the above so-called Understandings are based on a foreign lawyer's personal notes who attended the meeting held by the Ministry of Justice. There is no evidence that the Understandings have been officially recognized.⁴⁷

The unofficial status of the Understandings did not affect foreign law firms' reliance upon it. They conceded that the essential core areas of legal practices to Chinese law firms' interests are off limit. It remains the same that representation in litigation, provision of formal legal opinions on the application of Chinese law, employment of Chinese practicing lawyers, etc., are clearly impermissible. The permissibility of other legal services is more open-ended. Permissible activities include using Chinese law firms' letterhead to provide advice on issues of Chinese law and employing legally

⁴⁶ *Id.* at 142.

⁴⁷ *Id.* at 141.

qualified Chinese lawyers as Chinese legal consultants to provide professional legal services, so long as they stay outside of exclusive areas of licensed Chinese lawyers.

With the Understandings, foreign law firms are building extensive practices and resources in China.⁴⁸ Such extensive practice is noticeably inconsistent with implementing Rules and Regulations and it is in direct competition with local Chinese lawyers. In a market where foreign products are generally regarded as economically more valuable than its local counterparts (including service products), the Chinese legal profession soon felt the pinch. There are overwhelming accusations from the Chinese legal society of foreign law firms playing “edge ball” (i.e. take advantage of grey area of the laws).⁴⁹

The phenomenon of foreign law firms openly disregarding official promulgated legislation maybe shocking to the western society who is accustomed to law and order. However it is not shocking in the context of Chinese culture. Lack of legitimacy and corruption in the government has produced an atmosphere of distrust. Circumvention of government policy is not uncommon at all levels of the Chinese society. Coupled with weak enforcement, foreign law firms certainly did not take long to assimilate into this culture. This is a culture where practical gain always outweighs one’s conscience, especially when the lawmakers and the laws do not carry much moral weight in the first place.

VII. UNIQUE POSITION OF THE SAR

A discussion about China’s legal service market and its foreign players must include one important group – legal service providers from the Special Administrative Regions (SAR) of China – Hong Kong and Macau.⁵⁰ China’s SAR occupies a unique position in its political structure. Due to their historically colonial status, Hong Kong and Macau enjoy a high level of autonomy. Mainland China has agreed to refrain from exercising its absolute control over Hong Kong and Macau to a defined extent. For example, their democratic political systems, borne from their respective colonial origins, continue in their dealings with Mainland China. Additionally, Hong Kong and Macau have traditionally had much more connection with the outside world than with Mainland China, and this somewhat remains the case today. Hence, politically as well as culturally, Hong Kong and Macau are more “Western” than “Eastern.” As a result, the

⁴⁸ *Id.* at 143.

⁴⁹ *Id.* at 150.

⁵⁰ Hong Kong was returned to China from UK in 1997; Macau was returned to China from Portugal in 1999. China’s attempt to reclaim Taiwan has not succeeded.

unique position of Hong Kong and Macau is often a testing ground for foreign policy by the Mainland Chinese authority. As such, China's policy on Hong Kong and Macau is often seen as an indicator of the direction that China is heading in.

Hong Kong and Macau's participation in the WTO is independent from Mainland China, although they are technically part of China. The relationship between SAR and Mainland China is governed by a series of Partnership Agreements. The most recent agreement is the Closer Economic Partnership Arrangements (CEPA).⁵¹

Currently, China's policy on SAR lawyers in relation to providing legal services in Mainland China is as follows:⁵²

Limited forms of association between SAR law firms and interior law firms are permissible;

Interior law firms may employ SAR lawyers;

The qualification examination is open to SAR lawyers (it is not available to foreign lawyers⁵³).

These permissions are subject to the condition that SAR lawyers may not handle matters of Mainland law and litigation. Although it is still far from total liberalization, this policy reflects a more relaxed attitude towards SAR lawyers than the current regime governing the operation of foreign law firms. FLSP thus seem to have much to look forward to in the near future.

VIII. CONCLUSION

Currently, although foreign lawyers are not permitted to practice Chinese law, they are still active in a wide variety of legal areas, such as banking, finance, commercial arbitration, property, tax, maritime law, direct investment, intellectual property, and general corporate consulting.⁵⁴ Their contribution is not limited to building a healthy competitive market. The young Chinese legal profession stands to learn from their foreign counterparts' professionalism, managerial skills, and internationally accepted code of conduct.

There is no doubt that China has made considerable progress in its legal reforms in the last three decades. However, the reforms are

⁵¹ The CEPA is a free trade agreement. There are two sets of CEPA's; one signed between Mainland China and Hong Kong, and one between Mainland China and Macau. They are regularly reviewed and supplemented. See Mainland and Hong Kong Closer Economic Partnership Arrangement, China-H.K., June 29, 2003, 2 CHINESE J. INT'L L. 640, available at http://www.tid.gov.hk/english/cepa/legaltext/cepa_legaltext.html [hereinafter H.K. CEPA]. See also Mainland and Macao Closer Economic Partnership Arrangement, China-Mac., Oct. 17, 2003, available at http://www.economia.gov.mo/public/docs/CEPA_CEPA_I/index/en/efulltext.pdf.

⁵² H.K. CEPA is being used here as representative of both SAR regions. See Annex 4 to H.K. CEPA, available at <http://www.tid.gov.hk/english/cepa/files/annex4.pdf>.

⁵³ See Regulations on National Judicial Examination, *supra* note.

⁵⁴ CHEN, *supra* note, at 165.

superficial and are limited to only specific sectors. Western legal systems are built on capitalist ideology; their laws and political structure are consistent with the notion of separation of powers, rule of law, democracy, natural justice, etc. China's reform will not be immune to these dominant influences.

So far, China's reform, albeit superficial, has been consistent with the western mode of practice. This is the result of combined forces, such as the influence of the FLSP, the pressure of globalization, and especially WTO obligations. However, its socialist nature and the supremacy of Communist Party interests are inherently at odds with the direction it is heading in. In due time, China's legal reform will reach the point where its political ideology and structure will be questioned, or the reforms will meet a dead end. Law is a mere extension of politics, after all.