



The following is a transcript of an interview with Pamir Law Group partner Nicholas V. Chen (Nick), conducted by Hanna Hasl-Kelchner (Hanna) for “The No-Nonsense Lawyer” show.

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Hanna: Hello and welcome. My name is Hanna Hasl-Kelchner and I am “The No-Nonsense Lawyer.” My guest today is Mr. Nicholas Chen, and our topic is, “The Legal Aspects of Doing Business in Greater China.” Let me first introduce Nick.

Nick is a founding partner of the Pamir Law Group. He has been traveling and working extensively in China since 1973. He was born in and educated in the United States. He holds a bachelor’s degree from Yale and a law degree from New York University. But more importantly, he is a bridge between China and the rest of the world. He has successfully completed hundreds of foreign investments into China and he has also assisted the Chinese government as well as private and state-owned enterprises in their outbound investments and cross border transactions in China and overseas. He is an arbitrator for the China International Economic Trade Arbitration Commission (CIETAC) and he splits his time between Taipei, Shanghai, and Beijing. Welcome Nick.

Nick: Thank you.

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Hanna: There have been so many things happening in China, and as Westerners, there are so many misconceptions we probably have about the country. What is the best way for an individual to get started to do business in China and the surrounding countries if an individual has no contacts in the region? By “doing business,” I mean inbound transactions from countries such as the United States or Europe into China.

Nick: Well Hanna, first let me thank you for arranging this call. Obviously in China, as in other places when one is doing business, one of the most important things is partner selection. Whether you are doing inbound investment into China, or whether you are setting up a manufacturing operation, or finding a low cost supply chain solution on your sourcing, the most important thing is to find the right partner. No amount of good lawyering or professional consulting can really help compensate for a bad partner selection.

Hanna: If you do not have any contacts over there, how would you go about finding the key players in your industry? Let’s start there.

Nick: There are many sources to find out who the key players are, and finding the right counterpart party can be different every time. There are many things that can be done such as background or industry research, and you can find consultants and lawyers who can help identify the key players.

There are consultants that do partner matching and background information search. You can do it based on an industry, or a sector of an industry. In addition, a search can be targeted at a particular company or potential counterpart party.

It is very important to get the right background information. There are several types of background information you can get in China. They are not exactly done in Bradstreet-type style, but you can certainly find shareholder information for public companies and most private companies.

You can also get capitalization, officer, and director information. With public company cases, you can get the volume of business, and information about the sector, which is commercially available.

Hanna: That is good to know. I noticed your careful use of the phrase “the counterpart party,” and making sure you have the right one, not just anybody.

I guess that also goes to the question of trust and so forth. What suggestions do you have for being able to achieve a comfort level that you found the right party?

Nick: Doing due diligence for every counterpart party is important. That might be somebody who co-invests with you, it might be somebody who is part of your supply chain who you do not have a co-investment with, and it could be a supplier or vendor of any sort. It could even be on your lawyer, accountant, or locally hired key persons. They are all parts of the value chain. The level of trust and dependability is very important, so my earlier comment about no “amount of good lawyering will save you from a bad partner or counterpart selection” holds true for this as well. There is HR due diligence as opposed to counterparty due diligence, and it is different if you are buying a target or investing in a target.

The due diligence process in China is fairly complicated just like other jurisdictions. Much of it has to do with verification of information, not verification of documentation. You need to understand the background of a person and sometimes their family. Ask where they come from, their educational background, and what are the things that are important to them. In China, go far beyond just looking at a resume. The real references, not just the paper references, need to be checked.

The same is true about a company. There is background check as I mentioned, commercial services that are available to find out the company’s background on paper. But, how are decisions made in the company? Who are the people at the table? Who are the people that are involved in the decision making that are not at the table? Who are the regulatory voices? In certain industries, regulatory voices and the environment that is around the company are important. Therefore, due diligence is often about information verification, not document verification.

Targets need to be looked at in the changing social context. Chinese society is radically different this year than five years or three years ago. It will also be very different three to five years from now. The Chinese society, the Chinese economy, the Chinese policy/political system has been evolving very rapidly over the last twenty to thirty years.

With due diligence, how do you know you can trust somebody? How do you get the information? In China, it is about what is this target today versus

yesterday versus what it will become tomorrow. I am not just investing for today. I am investing for tomorrow, and that is true about a supplier too. What are the potential problems of that supplier? If that supplier looks good this year, there might be industry issues or choke points or price pressure. This company may not be well positioned to anticipate or to adjust for those conditions as they change next year and in the future. If I do not have a good assessment of this issue, I may be planting the seeds for future supply chain problems.

A supplier may be able to help you today, but may be unable to produce the volume, quality, or price competitiveness one or two years out. This is the kind of due diligence that needs to be done to pick the key persons, partners, or counterparts to have business reliability.

It is a business trust issue, and it is not necessarily personal. It is also about their ability for capacity to do what you need them to do.

Hanna: It sounds like very good advice. I think the western-style due diligence could benefit from that as well. All too often, it's just a "hit and run," serves its purpose, but the relationships may be shorter lived. But let me ask you this, you know when investing abroad or just even doing business abroad, particularly in countries that have very different cultures from ours in the states, there seems to be a couple of hot button areas that Westerners are concerned about. They seem to boil down into six areas, one of them being property rights. There are both commercial property rights and intellectual property rights. Let's talk about the commercial ones first. How do they differ in China as compared to the United States?

Nick: Why don't I handle commercial property rights, or real estate property rights first?

Hanna: Okay.

Nick: Let me start with real property. For 50 years until today, land is essentially owned by the state. There are very small grandfathered exceptions where certain farmers may have what would be considered fee simple ownership title. However, those are the vast minority and very rare.

For our purposes, you can assume that land is owned by the state. That means that I cannot necessarily have title on the land. What we are able to get as

investors, or owners of a property, is a land use right. Essentially, the Chinese legal system has allowed private parties to register a land use right, like a leasehold.

Therefore, depending on the nature of the land and what is negotiated in the price, it might be for a few years or 5 years or 20 years or 50 years. Or, in some cases, 70 years. At the end of the leasehold, you could pay another fee. These are leasehold or land use rights that are long enough in term that they can be purchased and sold, and you can do that by contract. A foreigner can own that as well as a local person.

Hanna: So, it is not necessary to have a Chinese partner.

Nick: That is correct for most industries. For example, if I'm opening up a business in China or if I'm setting up a factory, I can pay a fee and get a land use right. I can do that as a wholly-foreign owned enterprise.

I can also do it as a joint venture with a percentage of ownership being Chinese and a percentage being foreign. It is a commercial transaction and can be documented. The land use right and the right to use the factory building can be registered. There is also public notice.

While clean-free fee title is not available as in other countries, it's only because the system is different. You essentially can get to the same place. Regarding real property, there was a national law passed in China within the last five years which provides detailed and enforceable rights to ownership.

Hanna: I know there's always this concern and you certainly addressed it as far as real property. I think that goes to maybe a fear that there will be expropriation of the property, and then where do you stand? But on the intellectual property rights and the intangibles, I think in the back of everybody's mind is this question about how much is it really going to be respected and the fear of counterfeiting. And basically "handing over the family jewels" in a situation like that.

Nick: In the area of intellectual property, it is a little more complicated. There are several levels of protection that are available to a foreign party. First, China is a signatory to all the international and multi-lateral intellectual property conventions and treaties. Therefore, Madrid, Berne, and registration of rights in China comport with all of the protections available outside the country.

The first level is where your trademark or patent is already registered somewhere, you are in a place where you are part of the treaty, and then you can get retroactive time registration rights in China.

The second level is that there are a lot of national laws on trademark, patent, copyright, and plant genetics. Patent and trademark is “first to file”, so you have to file in order to get the protection. What I think is significant about enforcement of intellectual property rights in China is that there are many, many tools available to the foreign party available in the toolbox. These run the range from administrative protections and enforcement mechanisms, to civil, to criminal, and to what we call “civil ancillary protection piggy-backed on criminal.”

Administrative protection is mostly fines. My approach in intellectual property enforcement in China is to rely on criminal protection. Criminal enforcement penalties under Chinese law include imprisonment, and the number of years of imprisonment is dependent on the monetary amount of damage that one can prove. Another possibility is to count the number of offenses – if your intellectual property is violated multiple times, an individual could get 3-7 years of imprisonment for each count.

I tend towards criminal enforcement because I believe that criminal imprisonment creates fear. Without fear, behavior is not changed. There is no preventive impact without the fear.

This is dependant on whether you are able to get the evidence, collect the evidence of the violation, and prove the damages. In my view, this is real protection because these thresholds before imprisonment are fairly low – they are in the low few thousand dollars.

In many other countries, you do not have that. There are special intellectual property courts where the judges are specially trained in intellectual property. The resources of the courts are limited so you need an experienced anti-counterfeiting or IP enforcement team to gather the evidence, build the case, make the case, and prosecute.

The number of cases has been increasing every year. People are being imprisoned and people are being closed down.

In the media, we naturally hear about the horror stories, the cases where big companies are not protected or feel they are not protected, and we remember those cases. We remember the blatant cases. But in fact, many cases of IP enforcement are being successfully prosecuted. I think that is one of the trends after China joined the WTO, the World Trade Organization, in the last 10 years. They recognize that a business environment that does not allow for protection of intellectual property limits their ability to develop their industry, to get the technology licensing, to get the trade secrets, and it will retard the development of their economy. The government understands this and has invested a great deal of energy and resources into protecting intellectual property.

However, it is not a perfect world. Every international investor or person who is going to China that does not want to buy back their own product needs to develop a strategy, a forward thinking legal and practical business strategy.

There are many particularities of doing business in China. Strategies may include registration of intellectual property and there are many places where you may choose to not register because you want to deal with it as a trade secret. With trade secrets, you need to think about how you will handle the information, access, and internal documentation. Considerations to help a judge deem if information is a trade secret include how the factory is run and who has access to the facilities.

Hanna: And that's not different than how we handle it in the states.

Nick: That's right.

Hanna: It's nice to see some similarities and a sense of increased enforcement, and I think that helps create a comfort level. Let's talk about contracts, a third area that raises concern. So much is written about the value of relationships, and you have pointed out that it is part of the due diligence process, so you get to know these people, and not just where they have been to school. You know their families and what are they interested in.

It's just a whole wider web that is cast and I am just wondering as far as contracts, are they really just mere formalities that are trumped by personal relationships? Or, when negotiating them, are there certain hot button issues that Westerners need to avoid so to as to make them more binding?

Nick: That is a complicated question.

Hanna: Let's break it up then.

Nick: OK. Generally, contracts are enforceable in China. There is a law called a foreign economic contract law which governs and provides for enforcement of contracts between a foreign party and a Chinese domestic party. Essentially, as long as the negotiated terms are at arm's length, between two willing parties, and not against public policy (meaning that nothing illegal is being promoted), the courts in China will generally enforce those terms. That is the general rule.

You ask whether contract terms are mere formalities, and they are not. You asked whether they would be trumped by personal relationships, and the general answer is no. The exception, and everyone should think of it as an exception, is that there is local protectionism. In certain places... I would not say that the court system is uniformly well-developed throughout the country. If I were in a remote area, I might expect personal relationships between the court system and the business-side. China has not yet developed what we call an independent judiciary, which is completely divorced from the government or the political party system. It would be naïve to say that there is an independent judiciary. That is not a criticism, but merely an observation of reality.

Having said that, when structuring a contract, there may be hot buttons that Westerners should be aware of and think about. For example, many international companies operating in China decide to opt for arbitration. These are run by professional international or Chinese international arbitration commissions which are not tied to the government or the judiciary.

In your introduction, you mentioned that I was an arbitrator at CIETAC (Chinese International Economic and Trade Arbitration Commission). There are many other arbitral commissions such as Stockholm, ICC, or UNCITRAL. You might also use American Arbitration or Hong Kong. These are all professionally run by international arbitrators. Each party picks their arbitrator and the arbitrators then pick another member for a total panel of three.

This involves cost and time, and it may or may not be workable depending on the size of the situation. For a smaller budget, you might use a mediation

process. In many cases, however, the court system does work.

For example, specialty courts and specialty judges are familiar with some of the complex issues in intellectual property. When thinking about available dispute mechanisms to enforce contracts, there might be things that I would want a China experienced lawyer or legal team to look at.

For example, in your hometown in the United States, a lawyer might be very familiar with the U.S. court system. It would be quite natural for that lawyer or legal team to assume that their choice of law should be US or US State, and the jurisdiction would be the court of their hometown.

The practical problem is that judgments issued in the United States on paper are enforceable in China and vice versa. But in practice, a final and binding judgment issued by a U.S. court would go through a system called Letters Rogatory. One would make an application, take the final judgment, send it to the U.S. Department of State, who would then send it on to the Ministry of Foreign Affairs in China. They would then notify the Chinese court to enforce the judgment. That is what exists on paper. Unfortunately, in reality, that never happens.

The problem is essentially a lack of a remedy unless the Chinese counterpart party has assets in the United States you can enforce against. In reality, you could not use that judgment to seize assets in China to satisfy the judgment. You would wind up in a Chinese court litigating again.

For arbitration, China is a signatory to the New York Convention and a final and binding decision in a foreign arbitration or in a Chinese arbitration, would be mandatory under law for a court to enforce.

That is why many international companies will opt for international or CIETAC arbitration. Those who are more knowledgeable about China have also chosen Chinese court. In truth, I did an informal discussion with a clerk at the Supreme People's Court in Beijing a few years ago, and in cases involving a Chinese party and a foreign party, *the foreign party won more than half the time.*

That's not a guarantee that you will win, but obviously if one believed that the Chinese court system was completely anti-foreign, then foreign parties should lose more than half the time. Therefore, I think contracts *can* generally

be enforceable in China, and they *will* be enforced.

At the beginning of a transaction, when drafting a contract, you need to think about variables such as enforcement, size, where, and how. A boilerplate clause used for the last 20 years by a company in Michigan is not automatically enforceable in China. To make that assumption would be stupid.

Hanna: Fair enough. Let me move to regulatory enforcement, another “hot button” area, particularly if you are buying from a Chinese counterpart. I think this is number four.

We have seen the scandals in the headlines about food, the milk scandal, or the lead paint that has caused millions of toys to be recalled and probably ruined the holiday for a few of them. What is the regulatory climate? Has enforcement stepped up? What do you see as the government’s perspective on that?

Nick: Let me put this in perspective. Thirty years ago, China was in the Cultural Revolution. It was truly ruled by man and ruled by fiat. There was not rule by law. There were no laws. And at the end of the 70s and in the 80s, China reestablished a rule of law. They reestablished a legislature that passed laws.

Many of those laws were based on international research comparisons with the developed world and legal systems in the developing world. They promulgated many “big” laws, as I call them. In addition, they passed regulations to interpret, enforce, and establish institutions that implement the enforcement of those laws. China is in the first 20/30 years of that process. There has been tremendous progress, but frankly, there is also room for improvement.

Let’s take the area of food quality and product safety. The milk scandal, the lead paint in toys scandal, and the pet food scandal, were all within the last few years and received worldwide attention.

There is a pending case on dry board, drywall, and construction materials from Chinese companies exporting these materials around the world including to the United States. All of these issues had massive negative impact on the Chinese economy and not just in the toy, food, pet food, and construction sectors.

It created a wide trickle-down effect which slowed export sales of Chinese-made products, because it generated a general taint and worry about quality, which impacts the Chinese government's view on the enforcement of regulations in place.

The milk scandal affected the entire supply chain. It impacted the international distribution and sales chain, and it also impacted domestic consumption, which dropped essentially to near zero, because Chinese babies and Chinese consumers were being negatively impacted. The government position has been for consumer safety. The outcry from the consumer sector in China has actually been louder than abroad from the international consumer.

Obviously, the media coverage in the United States, for example, is focusing significantly on the international consumer protection voices. However, the Chinese consumer voices were certainly louder.

In the case of food safety, the Chinese equivalent to the United States Food and Drug Administration did a complete review and overhaul of the regulatory system. For both pharmaceuticals and food, they had a complete review of the standards.

They had applicable safety standards on the scientific level. They had a complete review of the enforcement mechanisms not only on paper, but on how they really worked. In the milk scandal, the end result, which is probably not widely reported in the United States, has been that death sentences were issued for some who were responsible. Irresponsible government officials were convicted after investigation and judicial proceedings and were found to have taken bribes, done cover ups, and other behavior which was not acceptable and consistent with Chinese law. That's pretty serious enforcement.

In the area of pharmaceutical enforcement, there was a case where a very senior officer of the government was sentenced to death by firing squad for taking bribes and not going through the system. These are rogue and renegade government officials who are gaining personal benefit at the expense of the public. This is also serious enforcement.

The toy industry, which was involved in a scandal two years ago, did a

massive overhaul, after members of the toy industry association were decimated with the loss of overseas export markets. The industry went on the warpath and investigated every toy company, from big to small. Many licenses were revoked, and the companies were put out of business. There was self-regulation, which was commercially driven, since it was in the self-interest of the companies in those industries to clean up their act.

It would have been better if this had happened before people got hurt. In the pet food scandal, it would have been better before the dogs and the cats got adulterated food. However, as a market mechanism and a regulatory system, it is self-correcting and I think that is good news.

Hanna: That is good news. We have two more hot button issues, and this time they are going to get a little bit juicier.

Nick: Okay.

Hanna: Bribery and then kidnapping.

Nick: Oh, great.

Hanna: Bribery is one of those things, and you mentioned about corruption and corrupt government officials, and at least the ones that get caught and convicted face very serious penalties if not their life.

For someone coming into the country to do a transaction, how should they handle a request for a bribe?

At this point, they may have a lot invested already in terms of time and research, and say for example, there is a bureaucrat somehow key in the decision making process. Without this bureaucrat's cooperation, all the time, money, and investment could just be gone in a flash. How do you recommend somebody handle that?

Nick: I recently returned from delivering a talk in Shanghai to China's anti-corruption and anti-bribery summit.

The summit is held every year and it is composed of international and Chinese experts. The common message of all of the presenters, whether they were government, private sector, lawyers, business experts, is that the best

practice with anti-corruption and anti-bribery is “a zero-tolerance response. “

What do I mean by that? Most companies and most company general counsels know that it is illegal for U.S. companies to pay a bribe. When I say a bribe, I don't necessarily mean only cash bribes, but it can be any kind of benefit.

The Foreign Corrupt Practices Act (FCPA) in the United States has a small exception to use a bribe to facilitate speedier decision, but not to change the nature of the decision. In an administrative facilitating, that is allowed, but generally, you cannot give any kind of broadly defined benefit to anybody who is close to a government official, who is a government official, or who is a “white glove” or proxy for a government official of a foreign government.

That includes a state owned company or a state invested company. It is illegal in the United States, and it is even more illegal in China. If somebody asks for that, you can cite Chinese law. The penalties are more severe in China; we are talking about imprisonment and possible death.

Even on an administrative level, I had a situation several years ago where a company in Guangzhou needed a permit for a water theme park. Their permit was held up. It was fairly clear to him that they were expecting a payment to issue that permit, and it was not a question of speed as they were essentially holding it hostage.

He asked me what to do and I said, “Look, why don't you leave it to me?”

I had a short conversation with the official in charge, and I cited the Administrative Procedure Act, which makes the official personally liable for the damages if I lost the business or if I lost the investment. If I had a penalty or if my client had a penalty, I would charge him in his individual capacity.

This goes far beyond the Administrative Procedure Act in the United States, where you can charge an official for taking actions that can be considered “arbitrary and capricious.”

I also made a citation to the criminal code and the penalties. Of course, I was very nice. I said, “Well, I could be mistaken. It's probably me as a foreigner not understanding your legal system, but there are these several provisions. Please take it under advisement and let me know what your thoughts are.”

The following day, this official and his boss came to see me and said there must have been a misunderstanding. I said of course, it must have been on my side, it was my misunderstanding. Of course, the permit came down immediately.

I essentially turned the tables on the guy, and I let him know that if he continued to do this, I would report him. I didn't say it blatantly, and I did it in a soft, understated way. They clearly got the message that I didn't misunderstand. In that situation, there was a good result, and the permit came down.

There were situations where the permits did not come down. Whether the client was willing to put the foot to the floor and step on the gas or not, is the client's decision, and in some cases, they walked away from the deal.

They walked away from the situation because it is very similar to my earlier comments about knowing your partners, doing the due diligence, and having a degree of comfort and trust in a situation. In those cases, the client would say, "I'm not comfortable with this level of discomfort now, and what could it be in the future? If I made a business decision now and encouraged this behavior, I would be providing illicit and illegal benefit to someone. It would be like giving drugs to a drug addict." Some decided that this was not a good situation and that the government regulator, partner or the counterpart was not reliable. They decided to take their business, investment, and their factory to another place.

Bribery and corruption exists everywhere, including China. However, it is not uniform across the board where all places are corrupt or have bribery. That would be the wrong assumption. Having said that, as an individual investor or trader, one must always protect against the worst.

Hanna: Absolutely. And it is good to have a tactic as you suggested in order to counteract that and achieve the result that you are really looking for. Certainly, it does speak volumes about the party that you are dealing with.

Let's talk about the more personal subject of kidnapping. It is one thing to have somebody hold you up for money, as it is just money. If somebody is actually taking somebody hostage in a kidnapping situation, there is personal safety at risk. It is no longer just about cold cash. How prominent is that?

Nick: I would say that it is certainly the exception rather than the rule. Kidnapping is a violent crime, and criminal enforcement in China has massive consequences such as long imprisonments, hard labor and capital punishment. The court system, the criminal justice system, the police, the prosecutors, and the criminal judges work well.

It is the exception rather than the rule, and having said that, there are many companies that look at personal safety and security as part of their due diligence, depending on where the company is setting up its operation.

That is an issue on the checklist, whether you are in a coastal city like Shanghai, or whether you are in the interior. Depending on what industry you are in and the nature of the trade secrets or the intellectual property, China has been in the news in certain situations where industrial espionage is an issue.

We see cases where certain interests in the Chinese state-owned enterprise sector have used accusations of stealing state secrets to seize and illegally hold representatives of foreign companies in China as political and business leverage. There are many prominent cases where this happens every year.

Some companies have security response teams, security officers, and security strategies in place for the safety of their personnel and intellectual property. I do not believe that it is used or necessary at all times. But, I would be naïve to say that it is not necessary sometimes.

This is not to be alarmist, over-emphasize, or misrepresent that China is not a place that is suitable for normal business across the border. However, it is something that is on the checklist, and every company must determine what level of risk and level of prevention and precaution need to be applied for their situation. There are commercial services and bodyguard companies, both available internationally and domestically.

I had a case where an international executive team went into a company that was pre-IPO to help launch it, and found financial information subsequent to IPO where things were covered up or misrepresented. The international team wanted to disclose and prevent it, but the Chinese management was opposed to that. I availed myself of commercially available protection services to negotiate the exits of the international team, and their ongoing safety. These are realities you sometimes have to face as business and legal advisors to

companies and corporate management teams.

Hanna: So we put it on the checklist, we address it, we contain it, and we keep doing business.

Nick: Correct.

Hanna: Okay, let me flip the tables a little bit. Up until now, we have been talking about western fears, perceptions, and misperceptions about what somebody who is unfamiliar with greater China may have heard about what it is like to do business there; The property concerns, whether it is real property and intellectual property; contract concerns; and regulatory enforcement. There is bribery and kidnapping, and like you said, it exists. However, there are ways to manage, contain, and be smart about it in terms of managing the risk. That's from the Western side looking in.

After all of the years that you have been working in China and dealing with China, looking through your eyes out back to the Western world, what are the most common mistakes you particularly see U.S. companies making when they first try to do business in China?

Nick: I have been coming and going between China and the United States for 35 years, and I have seen many different kinds of mistakes, and many of them get repeated. I'll just pick a few of them.

I think the biggest mistake, and it really is the biggest mistake because it leads to all of the other mistakes, is making cultural mistakes.

Foreign parties, wherever they are from, whether it be Europe, the United States, or Japan, often look at a situation through their own prism, through their own eyes, through their own culture. They do not necessarily know that they're doing it.

I call it "cultural Rashomon," and I borrow the term "Rashomon" from the movie that Akira Kurosawa made many years ago, which was about a crime scene, and different people looking at the same set of facts and circumstances reached completely different conclusions. They saw the situation differently, based on who they were. Similarly, in a cross-border transaction, whether with China, Africa, or anywhere else, we have two different business and ethnic cultures. One has to look at it from more than one's own

perspective.

I often use an example I call “Yes or No?” Basically, I put 20 expressions on the wall for a company’s executive team. I ask whether a certain response from the Chinese side means “Yes” or “No,” and different people will put their hands up. I go through the twenty expressions and the truth is that in each case, half the room says it means a “Yes” and the other half thinks it is a “No.”

Another example I give is smiling. When you (a Westerner) see a Chinese person smiling, you would automatically assume that the person was happy. You would likely proceed on, based on that assumption. However, in a Chinese, or an Asian context, the smile might mean embarrassment. It might be a cover-up for anger or disappointment, as saying “no” is considered impolite.

There are many other common mistakes that foreigners make in China. The biggest one is not protecting your intellectual property. You need to have a strategy in advance for the worst-case scenario, and know how to prevent it.

Another is partner selection. Again, no amount of good lawyering will save you from bad partner selection. If you select a bad vendor, a bad supplier, a bad lawyer, or a bad business partner, you are going to be playing a very American game for a very long time. That American game is called “catch-up.” You will have laid the seeds for more problems. Therefore, instead of making the business, you will be making excuses and remedies, and that is not a good thing to do.

The other mistake that people often forget to think about is whether there is an economically viable business. Oftentimes, there is a romanticism about China. People say they are going to the “biggest market,” or the “fastest growing market.” These statements may be true, but they are macro issues, and business is made at the micro level. The relevant questions are – does something make economic sense? Can we do it and make a profit?

Another mistake that foreigners often make is assuming that they can use an older technology, an older model, or an older product. The truth is they are wrong. In the Chinese market, the Chinese competitor will be very price competitive. You need to have your best product out there for the best possible price.

The competition will be virulent, and the assumption that it is a backwards developing market is wrong. International companies often use China as a platform to lower their costs, and not only to secure the Chinese market, but to also compete at a better price point internationally.

Do not go to China with your second best. Go to China with your best product and your best quality of service. Otherwise, you will be playing catch up.

Hanna: So you have answered the flipside as to what they can do to improve it. In other words, go with your best product and your best quality. What advice would you give on the cultural front so that people are not the “ugly Americans?”

Nick: I think that you need a team that is “China capable”. Many successful companies have brilliant management teams, and they have good external service providers. They also have good lawyers and accountants. They are going to need practical advice about the China business environment. They should supplement their existing capabilities with professionals and teams that have a proven track record in China and are not just uni-faceted.

If you find an accountant that is going to help you, make sure that they understand not only China accounting rules, but China’s business culture, and they have a track record of success. This is the same advice for the lawyer.

I came out of big, multi-national, international law firms. Many of them are able to move fast with a broad range of capabilities. However, in China, if you have an eye problem, you want an eye doctor. If you have a heart problem, you want a heart doctor.

You do not want the heart doctor doing your eyes and the eye doctor doing your heart. You need to have a China-capable, field-capable, proven-track-record team. One of the most important ways in which a no-nonsense lawyer can help a foreign company is to help build their business, help spot problems in advance, and help build and develop business relationships that go smoothly in China, as well as doing the accounting or doing legal documentation. These are all important.

However, if you cannot understand what is happening across, behind, around,

or at the table, then you are going to be in trouble and you are going to be at a disadvantage.

There is no such thing as a friend or a relative at a poker table, and it is the same for business. You need to structure a deal with the best team possible. You train and prepare for it. It does not end when you sign the contract, as it only begins then.

Your due diligence does not end when you put your money in. It only begins and continues, and it is especially important after you do the deal, after you sign the contract, after you put your people on the ground after you put your money, after you position people and intellectual property in China.

That is when you need the due diligence. That is when you need the professional team. It is not before you do the deal – it is “during the deal” and “after the deal.” “During the deal” means after you sign the contract and when you start to implement. Those are the most important things that an international party can do to protect their business in interest in China no matter how big or how small it is. You need to do the homework and do it every day. China is changing very rapidly.

Hanna: Speaking of changes, what changes do you see coming down the pike, and how they might benefit business investors?

Nick: We are 30 years away from a period that was very dark in China’s history, where you had social unrest and a very heavy hand to preserve stability. If one looked at that period and you went to an American or international company to ask if this was an environment you would want to invest in, the answer would have probably been, “I think I’ll find somewhere else.”

In the subsequent 30 years, what you have seen is an unprecedented evolution, an unprecedented level of international investment in China, where you’re talking on the average, over the last 20 years, about \$50-some billion of direct foreign investment into China every year.

That is quite amazing. That is several billion dollars of investment arriving every month for the last 20 years. There has been a massive transformation of Chinese society, the Chinese economy, the standard of living, and the consumer tastes of what they expect and want in their lives. That is over the last 30 years, and at that pace, the velocity of change and the trajectory of that

change have been nothing short of phenomenal.

Where will we be 30 years going out? Where will China be in just a decade, in 2020? You know we are going to see massive demographic changes where you see massive urbanization. The countryside is urbanizing, and second tier and third tier cities are rising.

When I talk about second tier and third tier cities, I am talking about populations. There are many first tier cities in China, which are cities with over 20 million people. That is mind-boggling.

New York City has about 7-8 million people. Shanghai has three times that population. Second tier cities have 10 million people, and New York City would be a third tier city in terms of size.

Hanna: Oh, please do not tell New York that.

Nick: As a New Yorker, we must face reality. You are talking about a totally different world.

There is a rising level of consumer expectation, and hopefully this government needs to increase their purchasing power. This is the rise of a consumer society that is of a size and order of magnitude that will be hard to imagine. There are more internet users and people learning English in China than in America. There are over 300 million people today learning English in China at some level. There are about 300 million Americans on the planet. That number is only rising in China. The court system and legal system will continue to evolve.

Consumption for leisure as well as daily products will continue to evolve. The only places where Michigan-based auto companies have any growth at all is China. Ironically, they are doing very well in China because of the rise of the Chinese consumer. The Chinese market is becoming bigger, and therefore, is a target for U.S. manufacturers, exporters, products, and services.

You will see more and more Chinese students, scholars, and professors involved in educational, cultural and scientific exchanges with the rest of the world. You will see more and more Chinese tourists traveling overseas to spend their money. These are things that are happening now. The scales will change. The Taiwan-China cross-straits environment is starting to normalize.

You are seeing more cultural and business exchanges. You are seeing acquisitions by Chinese companies in the United States, in the third world, and in the second world. We are often seeing that pattern. Ten years ago, that was a very small amount of business. Now, you are talking tens of billions of dollars. The Chinese are participating. They are sometimes winning and sometimes losing in these international bid situations. In many ways, the changes are not imaginable yet. We can, however, see the writing on the wall.

Hanna: It looks like everybody is going to benefit, including both the consumer and all of the companies that will have an opportunity to feed that demand.

Nick: One would hope so. But, the truth is that there will be winners and there will be losers. Those who take note of the things we said and prepare and do their homework every day will be winners. However, there will still be those who will make assumptions that smiles mean that a person is happy.

I once heard a joke, which is relevant for U.S. businesses. The joke was, “Nick, what do you call somebody that knows three languages?” The answer was trilingual. “What do you call somebody that knows two languages?” The answer was bilingual. “What do you call the person that only knows one language?” American.

And of course, that was not just linguistically. It was a way of thinking. The world has become multi-polar, and it has become multi-cultural and globalized. That is also true in America’s cities, neighborhoods, countryside, and our economy. It is truly a much smaller place.

Hanna: So the message is: wake up America.

Nick: Wake up America. Good Morning America.

Hanna: Good morning, good afternoon, don’t close your eyes.

Nick: That’s right, that’s right.

Hanna: Well, we’re running out of time here. Do you have any final comments or thoughts that you would like to leave the audience with today?

Nick: Yes. When you are doing business across a border, that might be from one state to another, or it might be just cross-town. It might be between company

A and company B as well as between a foreign company and China. Those are all cross-border situations.

My parting thought is this. What we learned when we were little kids applies especially in China. When you get to the corner to cross the street (or a border), – you always look all ways. You look left, you look right. You look to the front, and you look to the back. That is as important as doing your homework.

The other thing we learned as children was to hold hands with an adult. Hold hands with somebody who has crossed the street before. Get a bodyguard. Get a tour guide. Get a traffic cop. Hold hands.

Your parents told you that when you were a little kid, and it was good advice. It is still good advice in business. Get a China-capable lawyer. Get a China-capable professional team that knows where the risks are. When doing international business, please do not forget what your parents taught you. Do not become road kill. Those are my parting thoughts.

Hanna: Touché. Again, my guest today, Nicholas Chen, partner in the Pamir Law Group. A lot of practical and sound advice certainly based on many years of experience. Thank you so much for your time.

Nick: My pleasure. Thanks for having me. And I look forward to seeing you soon.

Hanna: Thank you so much.